

Horizon Technology Finance Corp  
Form 10-K  
March 08, 2016

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**Form 10-K**

(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: 814-00802**

**HORIZON TECHNOLOGY FINANCE CORPORATION**

*(Exact name of registrant as specified in its charter)*

**DELAWARE 27-2114934**

*(I.R.S.*

*(State or other jurisdiction of Employer*

*incorporation or organization) Identification  
No.)*

**312 Farmington Avenue,  
Farmington, CT**

**06032**

*(Address of principal executive  
offices) (Zip Code)*

**Registrant's telephone number, including area code (860) 676-8654**

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

<b>Title of Each Class</b>	<b>Name of Each Exchange on Which Registered</b>
Common Stock, par value \$0.001 per share	The NASDAQ Stock Market LLC
7.375% Senior Notes due 2019	The New York Stock Exchange

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

**None**

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 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 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, or a non-accelerated filer. See definition of "accelerated filer" and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller Reporting Company   
(Do not check if a 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 aggregate market value of common stock held by non-affiliates of the Registrant on June 30, 2015 based on the closing price on that date of \$12.68 on the Nasdaq Global Select Market was \$146.1 million. For the purposes of calculating this amount only, all directors and executive officers of the Registrant have been treated as affiliates. There were 11,538,984 shares of the Registrant's common stock outstanding as of March 1, 2016.

Documents Incorporated by Reference: Portions of the Registrant's Proxy Statement relating to the Registrant's 2016 Annual Meeting of Stockholders to be filed not later than 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K are incorporated by reference into Part III of this Annual Report on Form 10-K.

**HORIZON TECHNOLOGY FINANCE CORPORATION**

**FORM 10-K**

**FOR THE YEAR ENDED DECEMBER 31, 2015**

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## **PART I**

*In this annual report on Form 10-K, except where the context suggests otherwise, the terms:*

“we,” “us,” “our” “the Company” and “Horizon Technology Finance” refer to Horizon Technology Finance Corporation, a Delaware corporation, and its consolidated subsidiaries;

The “Advisor” and the “Administrator” refer to Horizon Technology Finance Management LLC, a Delaware limited liability company;

“Credit II” refers to Horizon Credit II LLC, a Delaware limited liability company, which is a special purpose bankruptcy remote entity and our direct subsidiary;

· “Key” refers to KeyBank National Association and “Key Facility” refers to the revolving credit facility with Key;

· “2019 Notes” refers to our \$33 million aggregate principal amount of 7.375% senior unsecured notes due 2019;

“Term Loan Facility” refers to a term loan credit facility we entered into with Fortress Credit Co LLC on August 23, 2012 that was terminated on June 17, 2014;

· “2013-1 Securitization” refers to the \$189.3 million securitization of secured loans we completed on June 28, 2013;

“Asset-Backed Notes” refers to our \$90 million aggregate principal amount of fixed-rate asset-backed notes issued in conjunction with the 2013-1 Securitization; and

· The “2013-1 Trust” refers to Horizon Funding Trust 2013-1, a Delaware trust.

*Some of the statements in this annual report on Form 10-K constitute forward-looking statements which apply to both us and our consolidated subsidiaries and relate to future events, future performance or financial condition. The forward-looking statements involve risks and uncertainties for both us and our consolidated subsidiaries and actual results could differ materially from those projected in the forward-looking statements for any reason, including those factors described in “Item 1A.—Risk Factors” and elsewhere in this annual report on Form 10-K.*

### **Item 1. Business**

## General

We are a specialty finance company that lends to and invests in development-stage companies in the technology, life science, healthcare information and services and cleantech industries, which we refer to collectively as our “Target Industries.” Our investment objective is to generate current income from the debt investments we make and capital appreciation from the warrants we receive when making such debt investments. We are focused on making secured debt investments, which we refer to as “Venture Loans,” to venture capital backed companies in our Target Industries, which we refer to as “Venture Lending.” We also selectively provide Venture Loans to publicly traded companies in our Target Industries. Our debt investments are typically secured by first liens or first liens behind a revolving line of credit, or “Senior Term Loans.” Venture Lending is typically characterized by (1) the making of a secured debt investment after a venture capital or equity investment in the portfolio company has been made, which investment provides a source of cash to fund the portfolio company’s debt service obligations under the Venture Loan, (2) the senior priority of the Venture Loan which requires repayment of the Venture Loan prior to the equity investors realizing a return on their capital, (3) the relatively rapid amortization of the Venture Loan and (4) the lender’s receipt of warrants or other success fees with the making of the Venture Loan.

We are an externally managed, closed-end, non-diversified management investment company that has elected to be regulated as a business development company, or BDC, under the Investment Company Act of 1940, as amended, or the 1940 Act. In addition, for U.S. federal income tax purposes, we have elected to be treated as a regulated investment company, or RIC, under Subchapter M of the Internal Revenue Code of 1986, as amended, or the Code. As a BDC, we are required to comply with regulatory requirements, including limitations on our use of debt. We are permitted to, and expect to, finance our investments through borrowings. However, as a BDC, we are only generally allowed to borrow amounts such that our asset coverage, as defined in the 1940 Act, equals at least 200% after such borrowing. The amount of leverage that we employ depends on our assessment of market conditions and other factors at the time of any proposed borrowing. As a RIC, we generally do not have to pay corporate-level federal income taxes on our investment company taxable income and our net capital gain that we distribute to our stockholders as long as we meet certain source-of-income, distribution, asset diversification and other requirements.

Compass Horizon Funding Company LLC, or Compass Horizon, our predecessor company, commenced operations in March 2008. We were formed in March 2010 for the purpose of acquiring Compass Horizon and continuing its business as a public entity.

From our inception through December 31, 2015, we funded 138 portfolio companies and invested \$780.0 million in debt investments. As of December 31, 2015, our debt investment portfolio consisted of 52 debt investments with an aggregate fair value balance of \$242.2 million. As of December 31, 2015, 97.8%, or \$236.9 million, of our debt investment portfolio at fair value consisted of Senior Term Loans. As of December 31, 2015, 18.6%, or \$45.1 million, of our total debt investment portfolio at fair value was held through our 2013-1 Securitization. As of December 31, 2015, our net assets were \$159.8 million and all of our debt investments were secured by all or a portion of the tangible and intangible assets of the applicable portfolio company. The debt investments in our portfolio are generally not rated by any rating agency. If the individual debt investments in our portfolio were rated, they would be rated below “investment grade” because they are subject to many risks, including volatility, intense competition, short product life cycles and periodic downturns.

For the year ended December 31, 2015, our debt investment portfolio had a dollar-weighted annualized yield of 14.2% (excluding any yield from warrants). The warrants we receive from time to time when making loans to portfolio companies are excluded from the calculation of our dollar-weighted annualized yield because such warrants do not generate any yield since we do not receive dividends or other payments in respect of our outstanding warrants. We calculate the yield on dollar-weighted average debt investments for any period measured as (1) total investment income during the period divided by (2) the average of the fair value of debt investments outstanding on (a) the last day of the calendar month immediately preceding the first day of the period and (b) the last day of each calendar month during the period. The dollar-weighted annualized yield represents the portfolio yield and will be higher than what investors will realize because it does not reflect our expenses or any sales load paid by investors. As of December 31, 2015, our debt investments had a dollar-weighted average term of 44 months from inception and a dollar-weighted average remaining term of 32 months. As of December 31, 2015, substantially all of our debt investments had an original committed principal amount of between \$2 million and \$12 million, repayment terms of between 11 and 48 months and bore current pay interest at annual interest rates of between 9% and 13%.

For the year ended December 31, 2015, our total return based on market value was (6.3)%. Total return based on market value is calculated as (x) the sum of (i) the closing sales price of our common stock on the last day of the period plus (ii) distributions paid per share during the period, less (iii) the closing sales price of our common stock on the first day of the period, divided by (y) the closing sales price of our common stock on the first day of the period.

In addition to our debt investments, as of December 31, 2015, we held warrants to purchase stock in 83 portfolio companies, equity positions in six portfolio companies and success fee arrangements in ten portfolio companies.



Our investment activities, and our day-to-day operations, are managed by our Advisor and supervised by our board of directors, or the Board, of which a majority of the members are independent of us. Under an amended and restated investment management agreement, or the Investment Management Agreement, we have agreed to pay our Advisor a base management fee and an incentive fee for its advisory services to us. We have also entered into an administration agreement, or the Administration Agreement, with our Advisor under which we have agreed to reimburse our Advisor for our allocable portion of overhead and other expenses incurred by our Advisor in performing its obligations under the Administration Agreement.

Our common stock began trading October 29, 2010 and is currently traded on the NASDAQ Global Select Market under the symbol “HRZN”.

### **Information available**

Our principal executive office is located at 312 Farmington Avenue, Farmington, Connecticut 06032, our telephone number is (860) 676-8654, and our internet address is [www.horizontechfinance.com](http://www.horizontechfinance.com). We make available, free of charge, on our website our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports as soon as reasonably practicable after we electronically file such material with, or furnish it to, the U.S. Securities and Exchange Commission, or the SEC. Information contained on our website is not incorporated by reference into this annual report on Form 10-K and you should not consider information contained on our website to be part of this annual report on Form 10-K or any other report we file with the SEC.

## **Our advisor**

Our investment activities are managed by our Advisor, and we expect to continue to benefit from our Advisor's ability to identify attractive investment opportunities, conduct diligence on and value prospective investments, negotiate investments and manage our diversified portfolio of investments. In addition to the experience gained from the years that they have worked together both at our Advisor and prior to the formation of our Advisor, the members of our investment team have broad lending backgrounds, with substantial experience at a variety of commercial finance companies, technology banks and private debt funds, and have developed a broad network of contacts within the venture capital and private equity community. This network of contacts provides a principal source of investment opportunities.

Our Advisor is led by five senior managers including Robert D. Pomeroy, Jr., our Chief Executive Officer, Gerald A. Michaud, our President, Christopher M. Mathieu, our Senior Vice President and Chief Financial Officer, John C. Bombara, our Senior Vice President, General Counsel and Chief Compliance Officer, and Daniel S. Devorsetz, our Senior Vice President and Chief Investment Officer.

## **Our strategy**

Our investment objective is to maximize our investment portfolio's total return by generating current income from the debt investments we make and capital appreciation from the warrants we receive when making such debt investments. To further implement our business strategy, we expect our Advisor to continue to employ the following core strategies:

*Structured investments in the venture capital and private equity markets.* We make loans to development-stage companies within our Target Industries typically in the form of secured loans. The secured debt structure provides a lower risk strategy, as compared to equity investments, to participate in the emerging technology markets because the debt structures we typically utilize provide collateral against the downside risk of loss, provide return of capital in a much shorter timeframe through current-pay interest and amortization of principal and have a senior position to equity in the borrower's capital structure in the case of insolvency, wind down or bankruptcy. Unlike venture capital and private equity investments, our investment returns and return of our capital do not require equity investment exits such as mergers and acquisitions or initial public offerings. Instead, we receive returns on our debt investments primarily through regularly scheduled payments of principal and interest and, if necessary, liquidation of the collateral supporting the debt investment upon a default. Only the potential gains from warrants depend upon equity investments exits.

*“Enterprise value” lending.* We and our Advisor take an enterprise value approach to the loan structuring and underwriting process. Enterprise value includes the implied valuation based upon recent equity capital invested as

well as the intrinsic value of the applicable portfolio company's particular technology, service or customer base. We secure our lien position against the enterprise value of each portfolio company.

*Creative products with attractive risk-adjusted pricing.* Each of our existing and prospective portfolio companies has its own unique funding needs for the capital provided from the proceeds of our Venture Loans. These funding needs include funds for additional development "runways," funds to hire or retain sales staff or funds to invest in research and development in order to reach important technical milestones in advance of raising additional equity. Our loans include current-pay interest, commitment fees, end-of-term payments, or ETPs, pre-payment fees, success fees and non-utilization fees. We believe we have developed pricing tools, structuring techniques and valuation metrics that satisfy our portfolio companies' financing requirements while mitigating risk and maximizing returns on our investments.

*Opportunity for enhanced returns.* To enhance our debt investment portfolio returns, in addition to interest and fees, we obtain warrants to purchase the equity of our portfolio companies as additional consideration for making debt investments. The warrants we obtain generally include a "cashless exercise" provision to allow us to exercise these rights without requiring us to make any additional cash investment. Obtaining warrants in our portfolio companies has allowed us to participate in the equity appreciation of our portfolio companies, which we expect will enable us to generate higher returns for our investors.

*Direct origination.* We originate transactions directly with technology, life science, healthcare information and services and cleantech companies. These transactions are referred to our Advisor from a number of sources, including referrals from, or direct solicitation of, venture capital and private equity firms, portfolio company management teams, legal firms, accounting firms, investment banks and other lenders that represent companies within our Target Industries. Our Advisor has been the sole or lead originator in substantially all transactions in which the funds it manages have invested.

*Disciplined and balanced underwriting and portfolio management.* We use a disciplined underwriting process that includes obtaining information validation from multiple sources, extensive knowledge of our Target Industries, comparable industry valuation metrics and sophisticated financial analysis related to development-stage companies. Our Advisor's due diligence on investment prospects includes obtaining and evaluating information on the prospective portfolio company's technology, market opportunity, management team, fund raising history, investor support, valuation considerations, financial condition and projections. We seek to balance our investment portfolio to reduce the risk of down market cycles associated with any particular industry or sector, development-stage or geographic area. Our Advisor employs a "hands on" approach to portfolio management requiring private portfolio companies to provide monthly financial information and to participate in regular updates on performance and future plans.

*Use of leverage.* We use leverage to increase returns on equity through our Key Facility, our 2019 Notes and our 2013-1 Securitization. See "Item 7 — Management's Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and capital resources" for additional information about our use of leverage. In addition, we may issue additional debt securities or preferred stock in one or more series in the future.

## **Market opportunity**

We focus our investments primarily in four key industries of the emerging technology market: technology, life science, healthcare information and services and cleantech. The technology sectors we focus on include communications, networking, data storage, software, cloud computing, semiconductor, power management, internet and media and consumer-related technologies. The life science sectors we focus on include biotechnology, drug delivery, bioinformatics and medical devices. The healthcare information and services sectors we focus on include diagnostics, medical record services and software and other healthcare related services and technologies that improve efficiency and quality of administered healthcare. The cleantech sectors we focus on include alternative energy, water purification, energy efficiency, green building materials and waste recycling. We refer to all of these companies as "technology-related" companies and intend, under normal market conditions, to invest at least 80% of the value of our total assets in such businesses.

We believe that Venture Lending has the potential to achieve enhanced returns that are attractive notwithstanding the high degree of risk associated with lending to development-stage companies. Potential benefits include:

-

interest rates that typically exceed rates that would be available to portfolio companies if they could borrow in traditional commercial financing transactions;

the debt investment support provided by cash proceeds from equity capital invested by venture capital and private equity firms;

- relatively rapid amortization of principal;
- senior ranking to equity and collateralization of debt investments to minimize potential loss of capital; and
- potential equity appreciation through warrants.

We believe that Venture Lending also provides an attractive financing source for portfolio companies, their management teams and their equity capital investors, as it:

- is typically less dilutive to the equity holders than additional equity financing;

extends the time period during which a portfolio company can operate before seeking additional equity capital or pursuing a sale transaction or other liquidity event; and

- allows portfolio companies to better match cash sources with uses.

## **Competitive strengths**

We believe that we, together with our Advisor, possess significant competitive strengths, including:

*Consistently execute commitments and close transactions.* Our Advisor and its senior management and investment professionals have an extensive track record of originating, underwriting and managing Venture Loans. Our Advisor and its predecessor have directly originated, underwritten and managed Venture Loans with an aggregate original principal amount over \$1.2 billion to more than 200 companies since operations commenced in 2004.

*Robust direct origination capabilities.* Our Advisor's managing directors each has significant experience originating Venture Loans in our Target Industries. This experience has given each managing director a deep knowledge of our Target Industries and an extensive base of transaction sources and references.

*Highly experienced and cohesive management team.* Our Advisor has had the same senior management team of experienced professionals since its inception. This consistency allows companies, their management teams and their investors to rely on consistent and predictable service, loan products and terms and underwriting standards.

*Relationships with venture capital and private equity investors.* Our Advisor has developed strong relationships with venture capital and private equity firms and their partners.

*Well-known brand name.* Our Advisor has originated Venture Loans to more than 200 companies in our Target Industries under the "Horizon Technology Finance" brand.

## **Competition**

We compete to provide financing to development-stage companies in our Target Industries with a number of investment funds and other BDCs, as well as traditional financial services companies such as commercial banks and other financing sources. Some of our competitors are larger and have greater financial and other resources than we do. We believe we compete effectively with these entities primarily on the basis of the experience, industry knowledge and contacts of our Advisor's investment professionals, its responsiveness and efficient investment analysis and decision-making processes, its creative financing products and its customized investment terms. We do not intend to compete primarily on the interest rates we offer and believe that some competitors make loans with rates that are comparable or lower than our rates. For additional information concerning our competitive position and competitive risks, see "Item 1A — Risk Factors — Risks related to our business and structure — We operate in a highly competitive market for investment opportunities, and if we are not able to compete effectively, our business, results of operations and financial condition may be adversely affected and the value of your investment in us could decline."

### **Investment criteria**

We seek to invest in companies that are diversified by their stage of development, their Target Industries and sectors of Target Industries and their geographical location, as well as by the venture capital and private equity sponsors that support our portfolio companies. While we invest in companies at various stages of development, we require that prospective portfolio companies be beyond the seed stage of development and have received at least their first round of venture capital or private equity financing before we will consider making an investment. We expect a prospective portfolio company to demonstrate its ability to advance technology and increase its value over time.

We have identified several criteria that we believe have proven, and will prove, important in achieving our investment objective. These criteria provide general guidelines for our investment decisions. However, we caution you that not all of these criteria are met by each portfolio company in which we choose to invest.

*Management.* Our portfolio companies are generally led by experienced management that has in-market expertise in the Target Industry in which the company operates, as well as extensive experience with development-stage companies. The adequacy and completeness of the management team is assessed relative to the stage of development and the challenges facing the potential portfolio company.

*Continuing support from one or more venture capital and private equity investors.* We typically invest in companies in which one or more established venture capital and private equity investors have previously invested and continue to make a contribution to the management of the business. We believe that established venture capital and private equity investors can serve as a committed partner and will assist their portfolio companies and their management teams in creating value. We take into consideration the total amount raised by the company, the valuation history, investor reserves for future investment and the expected timing and milestones to the next equity round financing.

*Operating plan and cash resources.* We generally require that a prospective portfolio company, in addition to having sufficient access to capital to support leverage, demonstrate an operating plan capable of generating cash flows or the ability to raise the additional capital necessary to cover its operating expenses and service its debt. Our review of the operating plan will take into consideration existing cash, cash burn, cash runway and the milestones necessary for the company to achieve cash flow positive operations or to access additional equity from the investors.

*Enterprise and technology value.* We expect that the enterprise value of a prospective portfolio company should substantially exceed the principal balance of debt borrowed by the company. Enterprise value includes the implied valuation based upon recent equity capital invested as well as the intrinsic value of the company's particular technology, service or customer base.

*Market opportunity and exit strategy.* We seek portfolio companies that are addressing large market opportunities that capitalize on their competitive advantages. Competitive advantages may include unique technology, protected intellectual property, superior clinical results or significant market traction. As part of our investment analysis, we typically also consider potential realization of our warrants through merger, acquisition or initial public offering based upon comparable exits in the company's Target Industry.

## **Investment process**

Our Board has delegated authority for all investment decisions to our Advisor. Our Advisor, in turn, has created an integrated approach to the loan origination, underwriting, approval and documentation process that we believe effectively combines the skills of our Advisor's professionals. This process allows our Advisor to achieve an efficient and timely closing of an investment from the initial contact with a prospective portfolio company through the investment decision, close of documentation and funding of the investment, while ensuring that our Advisor's rigorous underwriting standards are consistently maintained. We believe that the high level of involvement by our Advisor's staff in the various phases of the investment process allows us to minimize the credit risk while delivering superior service to our portfolio companies.



*Origination.* Our Advisor's loan origination process begins with its industry-focused regional managing directors who are responsible for identifying, contacting and screening prospects. These managing directors meet with key decision makers and deal referral sources such as venture capital and private equity firms and management teams, legal firms, accounting firms, investment banks and other lenders to source prospective portfolio companies. We believe our brand name and management team are well known within the Venture Lending community, as well as by many repeat entrepreneurs and board members of prospective portfolio companies. These broad relationships, which reach across the Venture Lending industry, give rise to a significant portion of our Advisor's deal origination.

The responsible managing director of our Advisor obtains review materials from the prospective portfolio company and from those materials, as well as other available information, determines whether it is appropriate for our Advisor to issue a non-binding term sheet. The managing director bases this decision to proceed on his or her experience, the competitive environment and the prospective portfolio company's needs and also seeks the counsel of our Advisor's senior management and investment team.

*Term sheet.* If the managing director determines, after review and consultation with senior management, that the potential transaction meets our Advisor's initial credit standards, our Advisor will issue a non-binding term sheet to the prospective portfolio company.

The terms of the transaction are tailored to a prospective portfolio company's specific funding needs while taking into consideration market dynamics, the quality of the management team, the venture capital and private equity investors involved and applicable credit criteria, which may include the prospective portfolio company's existing cash resources, the development of its technology and the anticipated timing for the next round of equity financing.

*Underwriting.* Once the term sheet has been negotiated and executed and the prospective portfolio company has remitted a good faith deposit, we request additional due diligence materials from the prospective portfolio company and arrange for a due diligence visit.

*Due diligence.* The due diligence process includes a formal visit to the prospective portfolio company's location and interviews with the prospective portfolio company's senior management team. The process includes obtaining and analyzing information from independent third parties that have knowledge of the prospective portfolio company's business, including, to the extent available analysts that follow the technology market, thought leaders in our Target Industries and important customers or partners, if any. Outside sources of information are reviewed, including industry publications, scientific and market articles, Internet publications, publicly available information on competitors or competing technologies and information known to our Advisor's investment team from their experience in the technology markets.

A key element of the due diligence process is interviewing key existing investors in the prospective portfolio company, who are often also members of the prospective portfolio company's board of directors. While these board members and/or investors are not independent sources of information, their support for management and willingness to support the prospective portfolio company's further development are critical elements of our decision making process.

*Investment memorandum.* Upon completion of the due diligence process and review and analysis of all of the information provided by the prospective portfolio company and obtained externally, our Advisor's assigned credit officer prepares an investment memorandum for review and approval. The investment memorandum is reviewed by our Advisor's Chief Investment Officer and submitted to our Advisor's investment committee for approval.

*Investment committee.* Our Advisor's investment committee is responsible for overall credit policy, portfolio management, approval of all investments, portfolio monitoring and reporting and managing of problem accounts. The committee interacts with the entire staff of our Advisor to review potential transactions and deal flow. This interaction of cross-functional members of our Advisor's staff assures efficient transaction sourcing, negotiating and underwriting throughout the transaction process. Portfolio performance and current market conditions are reviewed and discussed by the investment committee on a regular basis to assure that transaction structures and terms are consistent and current.

*Loan closing and funding.* Approved investments are documented and closed by our Advisor's in-house legal and loan administration staff. Loan documentation is based upon standard templates created by our Advisor and is customized for each transaction to reflect the specific deal terms. The transaction documents typically include a loan and security agreement, warrant agreement and applicable perfection documents, including applicable Uniform Commercial Code, or UCC, financing statements and, as applicable, may also include a landlord agreement, patent and trademark security grants, a subordination agreement and other standard agreements for commercial loans in the Venture Lending industry. Funding requires final approval by our Advisor's General Counsel, Chief Executive Officer or President, Chief Financial Officer and Chief Investment Officer.

*Portfolio management and reporting.* Our Advisor maintains a "hands on" approach to maintain communication with our portfolio companies. At least quarterly, our Advisor contacts our portfolio companies for operational and financial updates by phone and performs reviews. Our Advisor may contact portfolio companies deemed to have greater credit risk on a monthly basis. Our Advisor requires all private companies to provide financial statements. For public companies, our Advisor typically relies on publicly reported quarterly financials. This allows our Advisor to identify any unexpected developments in the financial performance or condition of our portfolio company.

Our Advisor has developed a proprietary internal credit rating system to analyze the quality of our debt investments. Using this system, our Advisor analyzes and then rates the credit risk within the portfolio on a monthly basis. Each portfolio company is rated on a 1 through 4 scale, with 3 representing the rating for a standard level of risk. A rating of 4 represents an improved and better credit quality. A rating of 2 or 1 represents a deteriorating credit quality and increasing risk. Newly funded investments are typically assigned a rating of 3, unless extraordinary circumstances require otherwise. These investment ratings are generated internally by our Advisor, and we cannot guarantee that others would assign the same ratings to our portfolio investments or similar portfolio investments.

Our Advisor closely monitors portfolio companies rated a 1 or 2 for adverse developments. In addition, our Advisor maintains regular contact with the management, board of directors and major equity holders of these portfolio companies in order to discuss strategic initiatives to correct the deterioration of the portfolio company.

The following table describes each rating level:

#### Rating

4 The portfolio company has performed in excess of our expectations at the time of initial underwriting as demonstrated by exceeding revenue milestones, clinical milestones or other operating metrics or as a result of raising capital well in excess of our underwriting assumptions. Generally the portfolio company displays one or more of the following: its enterprise value greatly exceeds our loan balance; it has achieved cash flow positive operations or has sufficient cash resources to cover the remaining balance of the loan; there is strong potential for warrant gains from our warrants; and there is a high likelihood that the borrower will receive favorable future financing to support operations. Loans rated 4 are the lowest risk profile in our portfolio, and there is no expected risk of principal loss.

3 The portfolio company has performed to our expectations at the time of initial underwriting as demonstrated by meeting revenue milestones, clinical milestones or other operating metrics. It has raised, or is expected to raise, capital consistent with our underwriting assumptions. Generally the portfolio company displays one or more of the following: its enterprise value comfortably exceeds our loan balance; it has sufficient cash resources to operate according to its plan; it is expected to raise additional capital as needed; and there continues to be potential for warrant gains from our warrants. New loans are typically rated 3 when approved and thereafter 3-rated loans represent a standard risk profile, with no loss currently expected.

2 The portfolio company has performed below our expectations at underwriting as demonstrated by missing revenue milestones, delayed clinical progress or otherwise failing to meet projected operating metrics. It may have raised capital in support of the poorer performance but generally on less favorable terms than originally contemplated at the time of underwriting. Generally the portfolio company displays one or more of the following: its enterprise value exceeds our loan balance but at a lower multiple than originally expected; it has sufficient cash to operate according to its plan but liquidity may be tight; and it is planning to raise additional capital but there is uncertainty and the potential for warrant gains from our warrants are possible, but unlikely. Loans rated 2 represent an increased level of risk. While no loss is currently anticipated for a 2-rated loan, there is potential for future loss of principal.

1 The portfolio company has performed well below plan as demonstrated by materially missing revenue milestones, delayed or failed clinical progress or otherwise failing to meet operating metrics. The portfolio company has not raised sufficient capital to operate effectively or retire its debt obligation to us. Generally the portfolio company displays one or more of the following: its enterprise value may not exceed our loan balance; it has insufficient cash to operate according to its plan and liquidity may be tight; and there are uncertain plans to raise additional capital or the portfolio company is being sold under distressed conditions. There is no potential for warrant gains from our warrants. Loans rated 1 are generally put on non-accrual status and represent a high degree of risk of loss.

For a discussion of the ratings of our existing portfolio, see “Item 7 — Management’s Discussion and Analysis of Financial Condition and Results of Operations — Debt investment asset quality.”

**Managerial assistance**

As a BDC, we offer, through our Advisor, and must provide upon request, managerial assistance to certain of our portfolio companies. This assistance may involve monitoring the operations of the portfolio companies, participating in board of directors and management meetings, consulting with and advising officers of portfolio companies and providing other organizational and financial guidance.

Although we may receive fees for these services, pursuant to the Administration Agreement, we will reimburse our Advisor for its expenses related to providing such services on our behalf.

## **Employees**

We do not have any employees. Each of our executive officers is an employee of our Advisor. Our day-to-day investment operations are managed by our Advisor. We reimburse our Advisor for our allocable portion of expenses incurred by it in performing its obligations under the Administration Agreement, as our Administrator, including our allocable portion of the cost of our Chief Financial Officer and Chief Compliance Officer and their respective staffs.

## **Investment Management Agreement**

Under the terms of the Investment Management Agreement, our Advisor:

- determines the composition of our portfolio, the nature and timing of the changes to our portfolio and the manner of implementing such changes;
- identifies, evaluates and negotiates the structure of the investments we make (including performing due diligence on our prospective portfolio companies); and
- closes, monitors and administers the investments we make, including the exercise of any voting or consent rights.

Our Advisor's services under the Investment Management Agreement are not exclusive, and it is free to furnish similar services to other entities so long as its services to us are not impaired.

## **Investment advisory fees**

Pursuant to our Investment Management Agreement, we pay our Advisor a fee for investment advisory and management services consisting of a base management fee and an incentive fee.

*Base management fee.* The base management fee, payable monthly in arrears, is calculated at an annual rate of 2.00% of (i) our gross assets less (ii) cash and cash equivalents. For purposes of calculating the base management fee, the term “gross assets” includes any assets acquired with the proceeds of leverage.

The Advisor agreed to waive the base management fee relating to the proceeds raised in a public offering of our common stock that closed on March 24, 2015, to the extent such fee is not otherwise waived and regardless of the application of the proceeds raised, until the earlier to occur of (i) March 31, 2016 or (ii) the last day of the second consecutive calendar quarter in which our net investment income exceeds distributions declared on shares of our common stock for the applicable quarter. As of December 31, 2015, condition (ii) above has been met, as our net investment income exceeded distributions declared for the quarters ended September 30, 2015 and December 31, 2015, and our Advisor is not obligated to waive the base management fee with respect to such offering proceeds for any future quarter.

*Incentive fee.* The incentive fee has two parts, as follows:

The first part, which is subject to the Incentive Fee Cap and Deferral Mechanism, as defined below, is calculated and payable quarterly in arrears based on our Pre-Incentive Fee Net Investment Income for the immediately preceding calendar quarter. For this purpose, “Pre-Incentive Fee Net Investment Income” means interest income, dividend income and any other income (including any other fees (other than fees for providing managerial assistance), such as commitment, origination, structuring, diligence and consulting fees or other fees received from portfolio companies) accrued during the calendar quarter, minus operating expenses for the quarter (including the base management fee, expenses payable under the Administration Agreement and any interest expense and any dividends paid on any issued and outstanding preferred stock, but excluding the incentive fee). Pre-Incentive Fee Net Investment Income includes, in the case of investments with a deferred interest feature (such as original issue discount, debt instruments with payment-in-kind interest and zero coupon securities), accrued income we have not yet received in cash. The incentive fee with respect to the Pre-Incentive Fee Net Investment Income is 20.00% of the amount, if any, by which the Pre-Incentive Fee Net Investment Income for the immediately preceding calendar quarter, expressed as a rate of return on the value of our net assets at the end of such quarter, exceeds a 1.75% (which is 7.00% annualized) hurdle rate and a “catch-up” provision. Under this provision, in any calendar quarter, the Advisor receives no incentive fee until the Pre-Incentive Fee Net Investment Income equals the hurdle rate of 1.75%, but then receives, as a “catch-up,” 100.00% of the Pre-Incentive Fee Net Investment Income with respect to that portion of such Pre-Incentive Fee Net Investment Income, if any, that exceeds the hurdle rate but is less than 2.1875%. The effect of this “catch-up” provision is that, if Pre-Incentive Fee Net Investment Income exceeds 2.1875% in any calendar quarter, the Advisor will receive 20.00% of the Pre-Incentive Fee Net Investment Income as if the hurdle rate did not apply.

Pre-Incentive Fee Net Investment Income does not include any realized capital gains, realized capital losses or unrealized capital appreciation or depreciation. Because of the structure of the incentive fee, it is possible that we may pay an incentive fee in a quarter in which we incur a loss. For example, if we receive Pre-Incentive Fee Net Investment Income in excess of the quarterly minimum hurdle rate, we will pay the applicable incentive fee up to the Incentive Fee Cap, defined below, even if we have incurred a loss in that quarter due to realized and unrealized capital losses. Our net investment income used to calculate this part of the incentive fee is also included in the amount of our gross assets used to calculate the 2.00% base management fee. These calculations are appropriately prorated for any period of less than three months and adjusted for any share issuances or repurchases during the applicable quarter.

Commencing with the calendar quarter beginning July 1, 2014, the incentive fee on Pre-Incentive Fee Net Investment Income is subject to a fee cap and deferral mechanism which is determined based upon a look-back period of up to three years and is expensed when incurred. For this purpose, the Incentive Fee Look-back Period commenced on July 1, 2014 and increases by one quarter in length at the end of each calendar quarter until June 30, 2017, after which time, the Incentive Fee Look-back Period will include the relevant calendar quarter and the 11 preceding full calendar quarters. Each quarterly incentive fee payable on Pre-Incentive Fee Net Investment Income is subject to a cap (the “Incentive Fee Cap”) and a deferral mechanism through which the Advisor may recoup a portion of such deferred incentive fees (collectively, the “Incentive Fee Cap and Deferral Mechanism”). The Incentive Fee Cap is equal to (a) 20.00% of Cumulative Pre-Incentive Fee Net Return (as defined below) during the Incentive Fee Look-back Period less (b) cumulative incentive fees of any kind paid to the Advisor during the Incentive Fee Look-back Period. To the extent the Incentive Fee Cap is zero or a negative value in any calendar quarter, we will not pay an incentive fee on Pre-Incentive Fee Net Investment Income to the Advisor in that quarter. To the extent that the payment of incentive fees on Pre-Incentive Fee Net Investment Income is limited by the Incentive Fee Cap, the payment of such fees will be deferred and paid in subsequent calendar quarters up to three years after their date of deferment, subject to certain limitations, which are set forth in the Investment Management Agreement. We only pay incentive fees on Pre-Incentive Fee Net Investment Income to the extent allowed by the Incentive Fee Cap and Deferral Mechanism. “Cumulative Pre-Incentive Fee Net Return” during any Incentive Fee Look-back Period means the sum of (a) Pre-Incentive Fee Net Investment Income and the base management fee for each calendar quarter during the Incentive Fee Look-back Period and (b) the sum of cumulative realized capital gains and losses, cumulative unrealized capital appreciation and cumulative unrealized capital depreciation during the applicable Incentive Fee Look-back Period.

The following is a graphical representation of the calculation of the income-related portion of the incentive fee:

#### **Quarterly incentive fee based on Net Investment Income**

#### **Pre-Incentive Fee Net Investment Income (expressed as a percentage of the value of net assets)**



**Percentage of Pre-Incentive Fee Net Investment Income allocated to first part of incentive fee**

The second part of the incentive fee is determined and payable in arrears as of the end of each calendar year (or upon termination of the Investment Management Agreement, as of the termination date), and equals 20.00% of our realized capital gains, if any, on a cumulative basis from the date of our election to be a BDC through the end of each calendar year, computed net of all realized capital losses and unrealized capital depreciation on a cumulative basis, less all previous amounts paid in respect of the capital gain incentive fee.

**Examples of incentive fee calculation**

**Example 1: Income related portion of incentive fee before total return requirement calculation for each fiscal quarter**

*Alternative 1*

**Assumptions:**

Investment income (including interest, distributions, fees, etc.) = 1.25%

Hurdle rate<sup>(1)</sup> = 1.75%

Management fee<sup>(2)</sup> = 0.50%

Other expenses (legal, accounting, custodian, transfer agent, etc.)<sup>(3)</sup> = 0.20%

Pre-Incentive Fee Net Investment Income (investment income - (management fee + other expenses)) = 0.55%

Pre-Incentive Fee Net Investment Income does not exceed hurdle rate; therefore, there is no income-related incentive fee.

*Alternative 2*

**Assumptions:**

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Investment income (including interest, distributions, fees, etc.) = 2.80%

Hurdle rate<sup>(1)</sup> = 1.75%

Management fee<sup>(2)</sup> = 0.50%

Other expenses (legal, accounting, custodian, transfer agent, etc.)<sup>(3)</sup> = 0.20%

Pre-Incentive Fee Net Investment Income (investment income - (management fee + other expenses)) = 2.10%

Incentive fee = 100.00% × Pre-Incentive Fee Net Investment Income (subject to “catch-up”<sup>(4)</sup>)

= 100.00% × (2.10% - 1.75%)

= 0.35%

Pre-Incentive Fee Net Investment Income exceeds the hurdle rate, but does not fully satisfy the “catch-up” provision; therefore, the income related portion of the incentive fee is 0.35%.

*Alternative 3*

Assumptions:

Investment income (including interest, distributions, fees, etc.) = 3.00%

Hurdle rate<sup>(1)</sup> = 1.75%

Management fee<sup>(2)</sup> = 0.50%

Other expenses (legal, accounting, custodian, transfer agent, etc.)<sup>(3)</sup> = 0.20%

Pre-Incentive Fee Net Investment Income (investment income - (management fee + other expenses)) = 2.30%

Incentive fee = 100.00% × Pre-Incentive Fee Net Investment Income (subject to “catch-up”<sup>(4)</sup>)

Incentive fee = 100.00% × “catch-up” + (20.00% × (Pre-Incentive Fee Net Investment Income - 2.1875%))

Catch up = 2.1875% - 1.75%

= 0.4375%

$$\text{Incentive fee} = (100.00\% \times 0.4375\%) + (20.00\% \times (2.30\% - 2.1875\%))$$

$$= 0.4375\% + (20.00\% \times 0.1125\%)$$

$$= 0.4375\% + 0.0225\%$$

$$= 0.46\%$$

Pre-Incentive Fee Net Investment Income exceeds the hurdle rate and fully satisfies the “catch-up” provision; therefore, the income related portion of the incentive fee is 0.46%.

- (1) Represents 7.00% annualized hurdle rate.
- (2) Represents 2.00% annualized base management fee.
- (3) Excludes organizational and offering expenses.

The “catch-up” provision is intended to provide our Advisor with an incentive fee of 20.00% on all Pre-Incentive (4) Fee Net Investment Income as if a hurdle rate did not apply when our net investment income exceeds 2.1875% in any fiscal quarter.

Example 2: Income related portion of incentive fee after total return requirement calculation for each fiscal quarter

*Alternative 1*

Assumptions:

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Investment income (including interest, distributions, fees, etc.) = 1.25%

Hurdle rate<sup>(1)</sup> = 1.75%

Management fee<sup>(2)</sup> = 0.50%

Other expenses (legal, accounting, custodian, transfer agent, etc.)<sup>(3)</sup> = 0.20%

Pre-Incentive Fee Net Investment Income (investment income - (management fee + other expenses)) = 0.55%

Pre-Incentive Fee Net Investment Income does not exceed hurdle rate; therefore, there is no income-related incentive fee.

Cumulative incentive compensation accrued and/or paid since July 1, 2014 = \$9,000,000

20.0% of cumulative net increase in net assets resulting from operations since July 1, 2014 = \$8,000,000

Although our Pre-Incentive Fee Net Investment Income exceeds the hurdle rate of 1.75% (as shown in Alternative 3 of Example 1 above), no incentive fee is payable because 20.0% of the cumulative net increase in net assets resulting from operations since July 1, 2014 did not exceed the cumulative income and capital gains incentive fees accrued and/or paid since July 1, 2014.

*Alternative 2*

Assumptions:

Investment income (including interest, distributions, fees, etc.) = 2.80%

Hurdle rate<sup>(1)</sup> = 1.75%

Management fee<sup>(2)</sup> = 0.50%

Other expenses (legal, accounting, custodian, transfer agent, etc.)<sup>(3)</sup> = 0.20%

Pre-Incentive Fee Net Investment Income (investment income - (management fee + other expenses)) = 2.10%

Incentive fee = 100.00% × Pre-Incentive Fee Net Investment Income (subject to “catch-up”<sup>(4)</sup>)

$$=100.00\% \times (2.10\% - 1.75\%)$$

$$= 0.35\%$$

Pre-Incentive Fee Net Investment Income exceeds the hurdle rate, but does not fully satisfy the “catch-up” provision; therefore, the income related portion of the incentive fee is 0.35%.

Cumulative incentive compensation accrued and/or paid since July 1, 2014 = \$9,000,000

20.0% of cumulative net increase in net assets resulting from operations since July 1, 2014 = \$10,000,000

Because our Pre-Incentive Fee Net Investment Income exceeds the hurdle rate of 1.75% and because 20.0% of the cumulative net increase in net assets resulting from operations since July 1, 2014 exceeds the cumulative income and capital gains incentive fees accrued and/or paid since July 1, 2014, an incentive fee would be payable, as shown in Alternative 3 of Example 1 above.

- (1) Represents 7.00% annualized hurdle rate.
- (2) Represents 2.00% annualized base management fee.
- (3) Excludes organizational and offering expenses.

The “catch-up” provision is intended to provide our Advisor with an incentive fee of 20.00% on all Pre-Incentive Fee Net Investment Income as if a hurdle rate did not apply when our net investment income exceeds 2.1875% in any fiscal quarter.

Example 3: Capital gains portion of incentive fee

*Alternative 1*



Assumptions:

Year 1: \$20 million investment made in Company A (“Investment A”), and \$30 million investment made in Company B (“Investment B”)

Year 2: Investment A sold for \$50 million and fair market value (“FMV”) of Investment B determined to be \$32 million

Year 3: FMV of Investment B determined to be \$25 million

Year 4: Investment B sold for \$31 million

The capital gains portion of the incentive fee, if any, would be:

Year 1: None (No sales transaction)

Year 2: Capital gains incentive fee of \$6 million (\$30 million realized capital gains on sale of Investment A multiplied by 20%)

Year 3: None; \$5 million ((20% multiplied by (\$30 million cumulative capital gains less \$5 million cumulative capital depreciation)) less \$6 million (previous capital gains fee paid in Year 2))

Year 4: Capital gains incentive fee of \$200,000; \$6.2 million ((\$31 million cumulative realized capital gains multiplied by 20%) less \$6 million (capital gains incentive fee taken in Year 2))

*Alternative 2*

Assumptions:

Year 1: \$20 million investment made in Company A (“Investment A”), \$30 million investment made in Company B (“Investment B”) and \$25 million investment made in Company C (“Investment C”)

Year 2: Investment A sold for \$50 million, FMV of Investment B determined to be \$25 million and FMV of Investment C determined to be \$25 million

Year 3: FMV of Investment B determined to be \$27 million and Investment C sold for \$30 million

Year 4: FMV of Investment B determined to be \$35 million

Year 5: Investment B sold for \$20 million

The capital gains incentive fee, if any, would be:

Year 1: None (no sales transaction)

Year 2: \$5 million capital gains incentive fee (20% multiplied by \$25 million (\$30 million realized capital gains on Investment A less unrealized capital depreciation on Investment B))

Year 3: \$1.4 million capital gains incentive fee<sup>(1)</sup> (\$6.4 million (20% multiplied by \$32 million (\$35 million cumulative realized capital gains less \$3 million unrealized capital depreciation)) less \$5 million capital gains incentive fee received in Year 2

Year 4: None (no sales transaction)

Year 5: None (\$5 million (20% multiplied by \$25 million (cumulative realized capital gains of \$35 million less realized capital losses of \$10 million)) less \$6.4 million cumulative capital gains incentive fee paid in Year 2 and Year 3<sup>(2)</sup>

The hypothetical amounts of returns shown are based on a percentage of our total net assets and assume no leverage. There is no guarantee that positive returns will be realized and actual returns may vary from those shown in this example.

As illustrated in Year 3 of Alternative 1 above, if we were to be wound up on a date other than our fiscal year end (1) of any year, we may have paid aggregate capital gains incentive fees that are more than the amount of such fees that would be payable if we had been wound up on its fiscal year end of such year.

As noted above, it is possible that the cumulative aggregate capital gains fee received by our Advisor (2) (\$6.4 million) is effectively greater than \$5 million (20.00% of cumulative aggregate realized capital gains less net realized capital losses or net unrealized depreciation (\$25 million)).

### Payment of our expenses

All investment professionals and staff of our Advisor, when and to the extent engaged in providing investment advisory and management services, and the compensation and routine overhead expenses of its personnel allocable to such services, are provided and paid for by our Advisor. We bear all other costs and expenses of our operations and transactions, including those relating to:

- our organization;
- calculating our net asset value (including the cost and expenses of any independent valuation firms);

expenses, including travel expense, incurred by our Advisor or payable to third parties performing due diligence on prospective portfolio companies, monitoring our investments and, if necessary, enforcing our rights;

- interest payable on debt, if any, incurred to finance our investments;
- the costs of all future offerings and repurchases of our common stock and other securities, if any;
  - the base management fee and any incentive fee;
  - distributions on our shares;
  - administration fees payable under the Administration Agreement;

the allocated costs incurred by our Advisor as our Administrator in providing managerial assistance to those portfolio companies that request it;

- amounts payable to third parties relating to, or associated with, making investments;

transfer agent and custodial fees;

- registration fees;
- listing fees;
- fees and expenses associated with marketing efforts;
- taxes;
- independent director fees and expenses;
- brokerage commissions;
- costs of preparing and filing reports or other documents with the SEC;
- the costs of any reports, proxy statements or other notices to our stockholders, including printing costs;
- the fidelity bond;
- directors and officers/errors and omissions liability insurance, and any other insurance premiums;
- indemnification payments;
- direct costs and expenses of administration, including audit and legal costs; and

all other expenses incurred by us or the Administrator in connection with administering our business, such as the allocable portion of overhead under the Administration Agreement, including rent, the fees and expenses associated with performing compliance functions and our allocable portion of the costs of compensation and related expenses of our Chief Financial Officer and Chief Compliance Officer and their respective staffs.

Generally, our expenses are expensed as incurred in accordance with U.S. generally accepted accounting principles, or GAAP. To the extent we incur costs that should be capitalized and amortized into expense we also do so in accordance with GAAP, which may include amortizing such amount on a straight line basis over the life of the asset

or the life of the services or product being performed or provided.

### **Limitation of liability and indemnification**

The Investment Management Agreement provides that our Advisor and its officers, managers, partners, agents, employees, controlling persons and any other person or entity affiliated with our Advisor are not liable to us for any act or omission by it in the supervision or management of our investment activities or for any loss sustained by us except for acts or omissions constituting willful misfeasance, bad faith, gross negligence or reckless disregard of its obligations under the Investment Management Agreement. The Investment Management Agreement also provides for indemnification by us of our Advisor and its officers, managers, partners, agents, employees, controlling persons and any other person or entity affiliated with our Advisor for liabilities incurred by them in connection with their services to us (including any liabilities associated with an action or suit by or in the right of us or our stockholders), but excluding liabilities for acts or omissions constituting willful misfeasance, bad faith or gross negligence or reckless disregard of their duties under the Investment Management Agreement subject to certain conditions.

### **Board approval of the Investment Management Agreement**

Our Board held an in-person meeting on July 29, 2015, at which it considered and reapproved our Investment Management Agreement for an additional 12-month period. In its consideration of the Investment Management Agreement, our Board focused on information it had received relating to (a) the nature, quality and extent of the advisory and other services to be provided to us by our Advisor; (b) comparative data with respect to advisory fees or similar expenses paid by other BDCs with similar investment objectives; (c) our projected expenses and expense ratio compared to BDCs with similar investment objectives; (d) any existing and potential sources of indirect income to our Advisor or the Administrator from their relationships with us and the profitability of those relationships; (e) information about the services to be performed and the personnel performing such services under the Investment Management Agreement; (f) the organizational capability and financial condition of our Advisor and its affiliates; (g) our Advisor's practices regarding the selection and compensation of brokers that may execute our portfolio transactions and the brokers' provision of brokerage and research services to our Advisor; and (h) the possibility of obtaining similar services from other third party service providers or through an internally managed structure.

Based on the information reviewed and its discussions related thereto, our Board, including a majority of the directors who are not interested persons of us, concluded that the investment management fee rates were reasonable in relation to the services to be provided.

### **Duration and termination**

The Investment Management Agreement was reapproved by our Board on July 29, 2015. Unless terminated earlier as described below, it will continue in effect from year to year thereafter if approved annually by our Board including a majority of our directors who are not interested persons or by the affirmative vote of the holders of a majority of our outstanding voting securities and a majority of our directors who are not interested persons. The Investment Management Agreement will automatically terminate in the event of its assignment. The Investment Management Agreement may be terminated by either party without penalty by delivering notice of termination upon not more than 60 days' written notice to the other party. See "Item 1A — Risk Factors — Risks related to our business and structure — Our Advisor can resign on 60 days' notice, and we may not be able to find a suitable replacement within that time, resulting in a disruption in our operations that could adversely affect our business, results of operations or financial condition."

### **Administration Agreement**

The Administration Agreement was considered and reapproved by our Board on July 29, 2015. Under the Administration Agreement, the Administrator furnishes us with office facilities and equipment, provides us clerical, bookkeeping and record keeping services at such facilities and provides us with other administrative services necessary to conduct our day-to-day operations. We reimburse the Administrator for our allocable portion of overhead and other expenses incurred by the Administrator in performing its obligations under the Administration Agreement, including rent, the fees and expenses associated with performing compliance functions and our allocable portion of the costs of compensation and related expenses of our Chief Financial Officer and Chief Compliance Officer and their respective staffs.

### **License agreement**

We have entered into a license agreement with Horizon Technology Finance, LLC, or HTF, pursuant to which we were granted a non-exclusive, royalty-free right and license to use the service mark "Horizon Technology Finance." Under this agreement, we have a right to use the "Horizon Technology Finance" service mark for so long as the Investment Management Agreement with our Advisor is in effect. Other than with respect to this limited license, we have no legal right to the "Horizon Technology Finance" service mark.



## Regulation

We have elected to be regulated as a BDC under the 1940 Act and elected to be treated as a RIC under Subchapter M of the Code. As with other companies regulated by the 1940 Act, a BDC must adhere to certain substantive regulatory requirements. The 1940 Act contains prohibitions and restrictions relating to transactions between BDCs and their affiliates (including any investment advisers or sub-advisers), principal underwriters and affiliates of those affiliates or underwriters and requires that a majority of the directors be persons other than “interested persons,” as that term is defined in the 1940 Act. In addition, the 1940 Act provides that we may not change the nature of our business so as to cease to be, or to withdraw our election as, a BDC unless approved by “a majority of our outstanding voting securities” as defined in the 1940 Act. A majority of the outstanding voting securities of a company is defined under the 1940 Act as the lesser of: (1) 67% or more of such company’s shares present at a meeting if more than 50% of the outstanding shares of such company are present or represented by proxy or (2) more than 50% of the outstanding shares of such company. Our bylaws provide for the calling of a special meeting of stockholders at which such action could be considered upon written notice of not less than ten or more than sixty days before the date of such meeting.

We may invest up to 100% of our assets in securities acquired directly from issuers in privately negotiated transactions. With respect to such securities, we may, for the purpose of public resale, be deemed an “underwriter” as that term is defined in the Securities Act of 1933, as amended, or the Securities Act. We do not intend to acquire securities issued by any investment company that exceed the limits imposed by the 1940 Act. Under these limits, except for registered money market funds, we generally cannot acquire more than 3% of the voting stock of any investment company, invest more than 5% of the value of our total assets in the securities of one investment company or invest more than 10% of the value of our total assets in the securities of more than one investment company. With regard to that portion of our portfolio invested in securities issued by investment companies, it should be noted that such investments might subject our stockholders to additional expenses. None of our investment policies are fundamental and any may be changed without stockholder approval.

We may also be prohibited under the 1940 Act from knowingly participating in certain transactions with our affiliates without the prior approval of our directors who are not interested persons and, in some cases, prior approval by the SEC. For example, under the 1940 Act, absent receipt of exemptive relief from the SEC, we and our affiliates may be precluded from co-investing in private placements of securities. As a result of one or more of these situations, we may not be able to invest as much as we otherwise would in certain investments or may not be able to liquidate a position as quickly.

We expect to be periodically examined by the SEC for compliance with the 1940 Act.

We are required to provide and maintain a bond issued by a reputable fidelity insurance company to protect us against larceny and embezzlement. Furthermore, as a BDC, we are prohibited from protecting any director or officer against any liability to us or our stockholders arising from willful misfeasance, bad faith, gross negligence or reckless disregard of the duties involved in the conduct of such person's office.

We and our Advisor have adopted and implemented written policies and procedures reasonably designed to prevent violation of the federal securities laws and review these policies and procedures annually for their adequacy and the effectiveness of their implementation. We and our Advisor have designated a chief compliance officer to be responsible for administering the policies and procedures.

### *Qualifying assets*

Under the 1940 Act, a BDC may not acquire any asset other than assets of the type listed in section 55(a) of the 1940 Act, which are referred to as qualifying assets, unless, at the time the acquisition is made, qualifying assets represent at least 70% of the company's total assets. The principal categories of qualifying assets relevant to our proposed business are the following:

Securities purchased in transactions not involving any public offering from the issuer of such securities, which issuer (subject to certain limited exceptions) is an eligible portfolio company, or from any person who is, or has been during the preceding 13 months, an affiliated person of an eligible portfolio company, or from any other person, subject to such rules as may be prescribed by the SEC. An eligible portfolio company is defined in the 1940 Act as any issuer which:

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

is not an investment company (other than a small business investment company wholly owned by the BDC) or a company that would be an investment company but for certain exclusions under the 1940 Act; and

- satisfies any of the following:

has a market capitalization of less than \$250 million or does not have any class of securities listed on a national securities exchange;

is controlled by a BDC or a group of companies including a BDC, the BDC actually exercises a controlling influence over the management or policies of the eligible portfolio company, and, as a result thereof, the BDC has an affiliated person who is a director of the eligible portfolio company; or

is a small and solvent company having total assets of not more than \$4 million and capital and surplus of not less than \$2 million.

- Securities of any eligible portfolio company which we control.

Securities purchased in a private transaction from a U.S. issuer that is not an investment company or from an affiliated person of the issuer, or in transactions incident thereto, if the issuer is in bankruptcy and subject to reorganization or if the issuer, immediately prior to the purchase of its securities was unable to meet its obligations as they came due without material assistance other than conventional lending or financing arrangements.

• Securities of an eligible portfolio company purchased from any person in a private transaction if there is no ready market for such securities and we already own 60% of the outstanding equity of the eligible portfolio company.

• Securities received in exchange for or distributed on or with respect to securities described above, or pursuant to the exercise of warrants or rights relating to such securities.

• Cash, cash equivalents, U.S. Government securities or high-quality debt securities maturing in one year or less from the time of investment.

The regulations defining qualifying assets may change over time. We may adjust our investment focus as needed to comply with and/or take advantage of any regulatory, legislative, administrative or judicial actions in this area.

#### ***Managerial assistance to portfolio companies***

A BDC must have been organized and have its principal place of business in the United States and must be operated for the purpose of making investments in the types of securities described in “— Qualifying assets.” However, in order to count portfolio securities as qualifying assets for the purpose of the 70% test, the BDC must either control the issuer of the securities or must offer to make available to the issuer of the securities (other than small and solvent companies described above) significant managerial assistance. Where the BDC purchases such securities in conjunction with one or more other persons acting together, the BDC will satisfy this test if one of the other persons in the group makes available such managerial assistance. Making available managerial assistance means, among other things, any arrangement whereby the BDC, through its directors, officers or employees, offers to provide, and, if accepted, does so provide, significant guidance and counsel concerning the management, operations or business objectives and policies of a portfolio company.

#### ***Issuance of additional shares***

We are not generally able to issue and sell our common stock at a price below net asset value per share. We may, however, issue and sell our common stock at a price below the current net asset value of the common stock, or issue and sell warrants, options or rights to acquire such common stock at a price below the current net asset value of the common stock if our Board determines that such sale is in our best interest and in the best interests of our stockholders, and our stockholders have approved our policy and practice of making such sales within the preceding 12 months. In any such case, the price at which our securities are to be issued and sold may not be less than a price which, in the determination of our Board, closely approximates the market value of such securities. Our stockholder approval to sell shares of our common stock below its net asset value expired on January 21, 2016. We intend to seek approval from our stockholders to offer shares of our common stock below its net asset value in the future.

*Temporary investments*

Pending investment in other types of “qualifying assets,” as described above, our investments may consist of cash, cash equivalents, U.S. Government securities or high-quality debt securities maturing in one year or less from the time of investment, which we refer to, collectively, as temporary investments, so that 70% of our assets are qualifying assets. Typically, we invest in highly rated commercial paper, U.S. Government agency notes, U.S. Treasury bills or in repurchase agreements relating to such securities that are fully collateralized by cash or securities issued by the U.S. Government or its agencies. A repurchase agreement involves the purchase by an investor, such as us, of a specified security and the simultaneous agreement by the seller to repurchase it at an agreed-upon future date and at a price which is greater than the purchase price by an amount that reflects an agreed-upon interest rate. There is no percentage restriction on the proportion of our assets that may be invested in such repurchase agreements. However, subject to certain exceptions, if more than 25% of our total assets constitute repurchase agreements from a single counterparty, we generally would not meet the diversification tests in order to qualify as a RIC for federal income tax purposes. Thus, we do not intend to enter into repurchase agreements with a single counterparty in excess of this limit. Our Advisor monitors the creditworthiness of the counterparties with which we enter into repurchase agreement transactions.

***Senior securities; derivative securities***

We are permitted, under specified conditions, to issue multiple classes of indebtedness and one class of stock senior to our common stock if our asset coverage, as defined in the 1940 Act, is at least equal to 200% immediately after each such issuance. In addition, while any senior securities are outstanding, we must make provisions to prohibit any distribution to our stockholders or the repurchase of such securities or shares unless we meet the applicable asset coverage requirement at the time of the distribution or repurchase. We may also borrow amounts up to 5% of the value of our total assets for temporary purposes without regard to asset coverage. For a discussion of the risks associated with leverage, see “Item 1A — Risk Factors — Risks related to our business and structure — We borrow money, which magnifies the potential for gain or loss on amounts invested and may increase the risk of investing in us.”

The 1940 Act also limits the amount of warrants, options and rights to common stock that we may issue and the terms of such securities.

***Code of ethics***

We and our Advisor have each adopted a code of ethics pursuant to Rule 17j-1 under the 1940 Act and Rule 204A-1 under the Investment Advisers Act of 1940, as amended, or the Advisers Act, respectively, that establishes procedures for personal investments and restricts certain personal securities transactions. Personnel subject to each code may invest in securities for their personal investment accounts, including securities that may be purchased or held by us, so long as such investments are made in accordance with the code’s requirements. You may read and copy the code of ethics at the SEC’s Public Reference Room in Washington, D.C. You may obtain information on the operation of the Public Reference Room by calling the SEC at (202) 942-8090. In addition, each code of ethics is attached as an exhibit to our Pre-effective Amendment No. 3 to the registration statement on Form N-2 (File No. 333-165570 filed with the SEC on July 19, 2010 as Exhibits (r)(1) and (r)(2)), which is available on the SEC’s Internet site at [www.sec.gov](http://www.sec.gov). You may also obtain copies of the code of ethics, after paying a duplicating fee, by electronic request at the following e-mail address: [publicinfo@sec.gov](mailto:publicinfo@sec.gov), or by writing the SEC’s Public Reference Section, Washington, D.C. 20549-0102.

***Proxy voting policies and procedures***

We have delegated our proxy voting responsibility to our Advisor. The proxy voting policies and procedures of our Advisor are set forth below. The guidelines are reviewed periodically by our Advisor and our independent directors and, accordingly, are subject to change.

*Introduction*

Our Advisor is registered with the SEC as an investment adviser under the Advisers Act. As an investment adviser registered under the Advisers Act, our Advisor has fiduciary duties to us. As part of this duty, our Advisor recognizes that it must vote client securities in a timely manner free of conflicts of interest and in our best interests and the best interests of our stockholders. Our Advisor's proxy voting policies and procedures have been formulated to ensure decision-making is consistent with these fiduciary duties.

These policies and procedures for voting proxies are intended to comply with Section 206 of, and Rule 206(4)-6 under, the Advisers Act.

*Proxy policies*

Our Advisor votes proxies relating to our portfolio securities in what our Advisor perceives to be the best interest of our stockholders. Our Advisor reviews on a case-by-case basis each proposal submitted to a stockholder vote to determine its effect on the portfolio securities held by us. Although our Advisor generally votes against proposals that may have a negative effect on our portfolio securities, our Advisor may vote for such a proposal if there exist compelling long-term reasons to do so.

Our Advisor's proxy voting decisions are made by those senior officers who are responsible for monitoring each of our investments. To ensure that a vote is not the product of a conflict of interest, our Advisor requires that (1) anyone involved in the decision-making process disclose to our Chief Compliance Officer any potential conflict that he or she is aware of and any contact that he or she has had with any interested party regarding a proxy vote and (2) employees involved in the decision-making process or vote administration are prohibited from revealing how we intend to vote on a proposal in order to reduce any attempted influence from interested parties.

*Proxy voting records*

You may obtain information about how we voted proxies by making a written request for proxy voting information to: Chief Compliance Officer, Horizon Technology Finance Corporation, 312 Farmington Avenue, Farmington, Connecticut 06032 or by calling (860) 676-8654.

*Sarbanes-Oxley Act of 2002*

The Sarbanes-Oxley Act of 2002, or the Sarbanes-Oxley Act, imposes a wide variety of regulatory requirements on publicly held companies and their insiders. Many of these requirements affect us. For example:

pursuant to Rule 13a-14 under the Securities Exchange Act of 1934, as amended, or the Exchange Act, our principal executive officer and principal financial officer must certify the accuracy of the financial statements contained in our periodic reports;

pursuant to Item 307 under Regulation S-K, our periodic reports must disclose our conclusions about the effectiveness of our disclosure controls and procedures;

pursuant to Rule 13a-15 under the Exchange Act, our management must prepare an annual report regarding its assessment of our internal control over financial reporting, which must be audited by our independent registered public accounting firm; and

pursuant to Item 308 of Regulation S-K and Rule 13a-15 under the Exchange Act, our periodic reports must disclose whether there were significant changes in our internal controls over financial reporting or in other factors that could significantly affect these controls subsequent to the date of their evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

The Sarbanes-Oxley Act requires us to review our current policies and procedures to determine whether we comply with the Sarbanes-Oxley Act and the regulations promulgated thereunder. We will continue to monitor our compliance with all regulations under the Sarbanes-Oxley Act and intend to take actions necessary to ensure that we are in compliance therewith.

*NASDAQ Global Select Market corporate governance regulations*



NASDAQ has adopted corporate governance regulations with which listed companies must comply. We intend to be in compliance with these corporate governance listing standards. We intend to monitor our compliance with all future listing standards and to take all necessary actions to ensure that we are in compliance therewith.

### *Privacy principles*

We are committed to maintaining the privacy of stockholders and to safeguarding our non-public personal information. The following information is provided to help you understand what personal information we collect, how we protect that information and why, in certain cases, we may share information with select other parties.

Generally, we do not receive any nonpublic personal information relating to our stockholders, although certain nonpublic personal information of our stockholders may become available to us. We do not disclose any nonpublic personal information about our stockholders or former stockholders, except as permitted by law or as is necessary in order to service stockholder accounts (for example, to a transfer agent or third party administrator).

We restrict access to nonpublic personal information about our stockholders to our Advisor's employees with a legitimate business need for the information. We maintain physical, electronic and procedural safeguards designed to protect the nonpublic personal information of our stockholders.

### *Election to be taxed as a RIC*

We have elected to be taxed, and intend to qualify annually to maintain our election to be taxed, as a RIC under Subchapter M of the Code. To maintain our RIC status, we must, among other requirements, meet certain source-of-income and quarterly asset diversification requirements (as described below). We also must distribute dividends each tax year of an amount generally at least equal to 90% of the sum of our ordinary income and our realized net short-term capital gains (i.e. net short-term capital gains in excess of net long term losses), or investment company taxable income, if any, out of the assets legally available for distribution, which we refer to as the "Annual Distribution Requirement." Although not required for us to maintain our RIC tax status, in order to preclude the imposition of a 4% nondeductible federal excise tax imposed on RICs, we are required to distribute dividends in respect of each calendar year of an amount generally at least equal to the sum of (1) 98% of our ordinary income (taking into account certain deferrals and elections) for the calendar year, (2) 98.2% of the excess of our capital gains over our capital losses, or capital gain net income (adjusted for certain ordinary losses) for the one-year period ending on October 31 of the calendar year and (3) any ordinary income and net capital gains for preceding years that were not distributed during such years and on which we previously did not pay U.S. federal corporate income tax, or the Excise Tax Avoidance Requirement. In addition, although we may distribute realized net capital gains (i.e., net long-term capital gains in excess of short-term capital losses), if any, at least annually out of the assets legally available for such distributions, we may decide to retain such net capital gains or ordinary income to provide us with additional liquidity.

In order to qualify as a RIC for federal income tax purposes under Section 851(a) of the Code, we must:

- maintain an election to be treated as a BDC under the 1940 Act at all times during each tax year;
- meet any applicable securities law requirements, including capital structure requirements;

derive in each tax year at least 90% of our gross income from dividends, interest, payments with respect to certain securities loans, gains from the sale of stock or other securities, net income from certain qualified publicly traded partnerships or other income derived with respect to our business of investing in such stock or securities, or the Qualifying Income Test; and

- diversify our holdings so that at the end of each quarter of the tax year:

at least 50% of the value of our assets consists of cash, cash equivalents, U.S. government securities, securities of other RICs, and other securities if such other securities of any one issuer neither represent more than 5% of the value of our assets nor more than 10% of the outstanding voting securities of the issuer; and

no more than 25% of the value of our assets is invested in the securities, other than U.S. government securities or securities of other RICs, of one issuer or of two or more issuers that are controlled, as determined under applicable tax rules, by us and that are engaged in the same or similar or related trades or businesses or in certain qualified publicly traded partnerships, or the Diversification Tests.

### ***Taxation as a RIC***

If we qualify as a RIC under Section 851(a) of the Code, and satisfy the Annual Distribution Requirement, then we are not be subject to federal income tax on the portion of our investment company taxable income as well as any net capital gain (i.e., realized net long-term capital gains in excess of realized net short-term capital losses) we distribute as dividends to stockholders. We may retain for investment all or a portion of our net capital gain. However, if we retain any investment company taxable income or net capital gains, and satisfy the Annual Distribution Requirement, we will be subject to tax at regular corporate rates on any amounts retained. If we fail to qualify as a RIC for a period greater than two consecutive tax years, to qualify as a RIC in a subsequent tax year, we may be subject to regular corporate rates on any net built-in gains with respect to certain of our assets (that is, the excess of the aggregate gains, including items of income, over aggregate losses that would have been realized with respect to such assets if we had sold the property at fair market value at the end of the tax year) that we elect to recognize on requalification or when recognized over the next five tax years.

We may be required to recognize taxable income in circumstances in which we do not receive cash. For example, if we hold debt obligations that are treated under applicable tax rules as having original issue discount (such as debt instruments with payment in kind interest or, in certain cases, increasing interest rates or issued with warrants), we must include in income each tax year a portion of the original issue discount that accrues over the life of the

obligation, regardless of whether cash representing such income is received by us in the same tax year. Because any original issue discount accrued will be included in our investment company taxable income for the tax year of accrual, we may be required to make a distribution to our stockholders in order to satisfy the Annual Distribution Requirement or the Excise Tax Avoidance Requirement, even though we will not have received any corresponding cash amount.

Gain or loss realized by us from warrants acquired by us as well as any loss attributable to the lapse of such warrants generally will be treated as capital gain or loss. Such gain or loss generally will be long-term or short-term, depending on how long we held a particular warrant.

Although we do not presently expect to do so, we are authorized to borrow funds and to sell assets in order to satisfy distribution requirements. However, under the 1940 Act, we are not permitted to make distributions to our stockholders while our debt obligations and other senior securities are outstanding unless certain “asset coverage” tests are met. Moreover, our ability to dispose of assets to meet our distribution requirements may be limited by (1) the illiquid nature of our portfolio and/or (2) other requirements relating to our status as a RIC, including the Diversification Tests. If we dispose of assets in order to meet the Annual Distribution Requirement or the Excise Tax Avoidance Requirement, we may make such dispositions at times that, from an investment standpoint, are not advantageous.

### *Failure to qualify as a RIC*

If we fail to satisfy the Annual Distribution Requirement or fail to qualify as a RIC in any tax year, assuming we do not qualify for or take advantage of certain remedial provisions, we will be subject to tax in that year on all of our taxable income, regardless of whether we make any distributions to our stockholders. In that case, all of our income will be subject to corporate-level federal income tax, reducing the amount available to be distributed to our stockholders. In contrast, assuming we qualify as a RIC, our corporate-level federal income tax liability should be substantially reduced or eliminated. See “—Election to be taxed as a RIC” above.

If we are unable to maintain our status as a RIC, we would be subject to tax on all of our taxable income at regular corporate rates. We would not be able to deduct distributions to stockholders, nor would they be required to be made. Distributions would generally be taxable to our stockholders as ordinary distribution income eligible for the 15% or 20% maximum rate to the extent of our current and accumulated earnings and profits. Subject to certain limitations under the Code, dividends paid by us to certain corporate distributees would be eligible for the dividends received deduction. Distributions in excess of our current and accumulated earnings and profits would be treated first as a return of capital to the extent of the stockholder’s tax basis in our common stock, and any remaining distributions would be treated as a capital gain.

**Item 1A. Risk Factors**

*Investing in our securities involves a high degree of risk. In addition to the other information contained in this annual report on Form 10-K, you should consider carefully the following information before making an investment in our securities. The risks set out below are not the only risks we face. If any of the following events occur, our business, financial condition and results of operations could be materially and adversely affected. In such case, our net asset value, or NAV, per share and the trading price of our common stock could decline, and you may lose part or all of your investment.*

**Risks related to our business and structure**

*We are dependent upon key personnel of our Advisor and our Advisor's ability to hire and retain qualified personnel.*

We do not have any employees and are dependent upon the members of our Advisor's senior management, as well as other key personnel for the identification, evaluation, final selection, structuring, closing and monitoring of our investments. These employees have critical industry experience and relationships that we rely on to implement our business plan to originate Venture Loans in our Target Industries. Our future success depends on the continued service of the senior members of our Advisor's management team. If our Advisor were to lose the services of any of the senior members of our Advisor's management team, we may not be able to operate our business as we expect, and our ability to compete could be harmed, either of which could cause our business, results of operations or financial condition to suffer. In addition, if more than one of Mr. Pomeroy, Mr. Michaud or Mr. Mathieu, our Chief Financial Officer, cease to be actively involved with us or our Advisor, and are not replaced by individuals satisfactory to Key within 90 days, Key could, absent a waiver or cure, demand repayment of any outstanding obligations under the Key Facility.

Our future success also depends, in part, on our Advisor's ability to identify, attract and retain sufficient numbers of highly skilled employees. If our Advisor is not successful in identifying, attracting and retaining such employees, we may not be able to operate our business as we expect. In addition, our Advisor may in the future manage investment funds with investment objectives similar to ours thereby diverting the time and attention of its investment professionals that we rely on to implement our business plan.

*Our Advisor may change or be restructured.*

We cannot assure you that the Advisor will remain our investment adviser or that we will continue to have access to our Advisor's investment professionals or its relationships. We would be required to obtain shareholder approval for a new investment management agreement in the event that (1) the Advisor resigns as our investment adviser or (2) a change of control or deemed change of control of the Advisor occurs. We cannot provide assurance that a new investment management agreement or new investment adviser would provide the same or equivalent services on the same or on as favorable of terms as the Investment Management Agreement or the Advisor.

***We operate in a highly competitive market for investment opportunities, and if we are not able to compete effectively, our business, results of operations and financial condition may be adversely affected and the value of your investment in us could decline.***

We compete for investments with a number of investment funds and other BDCs, as well as traditional financial services companies such as commercial banks and other financing sources. Some of our competitors are larger and have greater financial, technical, marketing and other resources than we have. For example, some competitors may have a lower cost of funds and access to funding sources that are not available to us. This may enable these competitors to make commercial loans with interest rates that are comparable to, or lower than, the rates we typically offer. We may lose prospective portfolio companies if we do not match our competitors' pricing, terms and structure. If we do match our competitors' pricing, terms or structure, we may experience decreased net interest income and increased risk of credit losses. In addition, some of our competitors may have higher risk tolerances or different risk assessments, which could allow them to consider a wider variety of investments, establish more relationships than us and build their market shares. Furthermore, many of our competitors are not subject to the regulatory restrictions that the 1940 Act imposes on us as a BDC or that the Code imposes on us as a RIC. If we are not able to compete effectively, we may not be able to identify and take advantage of attractive investment opportunities that we identify and may not be able to fully invest our available capital. If this occurs, our business, financial condition and results of operations could be materially adversely affected.

*We borrow money, which magnifies the potential for gain or loss on amounts invested and may increase the risk of investing in us.*

Leverage is generally considered a speculative investment technique, and we intend to continue to borrow money as part of our business plan. The use of leverage magnifies the potential for gain or loss on amounts invested and, therefore, increases the risks associated with investing in us. See “Item 7 — Management’s Discussion and Analysis of Financial Condition and Results of Operation — Liquidity and capital resources.” Lenders of senior debt securities have fixed dollar claims on our assets that are superior to the claims of our common stockholders. If the value of our assets increases, then leveraging would cause the NAV attributable to our common stock to increase more sharply than it would have had we not leveraged. However, any decrease in our income would cause net income to decline more sharply than it would have had we not leveraged. This decline could adversely affect our ability to make common stock distribution payments. In addition, because our investments may be illiquid, we may be unable to dispose of them or unable to do so at a favorable price in the event we need to do so, if we are unable to refinance any indebtedness upon maturity, and, as a result, we may suffer losses.

Our ability to service any debt that we incur depends largely on our financial performance and is subject to prevailing economic conditions and competitive pressures. Moreover, as our Advisor’s management fee is payable to our Advisor based on our gross assets, including those assets acquired through the use of leverage, our Advisor may have a financial incentive to incur leverage which may not be consistent with our stockholders’ interests. In addition, holders of our common stock bear the burden of any increase in our expenses, as a result of leverage, including any increase in the management fee payable to our Advisor.

In addition to the leverage described above, we have securitized a large portion of our debt investments to generate cash for funding new investments and may seek to securitize additional debt investments in the future. To securitize additional debt investments in the future, we may create a wholly-owned subsidiary and sell and/or contribute a pool of debt investments to such subsidiary. This could include the sale of interests in the subsidiary on a non-recourse basis to purchasers, who we would expect to be willing to accept a lower interest rate to invest in investment grade loan pools. We would retain all or a portion of the equity in any such securitized pool of loans. An inability to securitize part of our debt investments in the future could limit our ability to grow our business, fully execute our business strategy and increase our earnings. Moreover, certain types of securitization transactions may expose us to greater risk of loss than would other types of financing.

*Illustration:* The following table illustrates the effect of leverage on returns from an investment in our common stock assuming various annual returns, net of expenses. The calculations in the table below are hypothetical and actual returns may be higher or lower than those appearing in the table below:

#### **Assumed Return on Our Portfolio**



	<b>(Net of Expenses)</b>				
	-10%	-5%	0%	5%	10%
Corresponding return to stockholder(1)	-21.26%	-12.48%	-3.70%	5.09%	13.87%

(1) Assumes \$281 million in total assets, \$116 million in outstanding debt, \$160 million in net assets, and an average cost of borrowed funds of 5.10% at December 31, 2015. Actual interest payments may be different.

Based on our outstanding indebtedness of \$116 million as of December 31, 2015 and the average cost of borrowed funds of 5.10% as of that date, our investment portfolio would have been required to experience an annual return of at least 2.31% to cover annual interest payments on the outstanding debt.

***If we are unable to comply with the covenants or restrictions in the Key Facility or make payments when due thereunder, our business could be materially adversely affected.***

Our Key Facility is secured by a lien on the assets of our wholly owned subsidiary, Credit II. The breach of certain of the covenants or restrictions or our failure to make payments when due under the Key Facility, unless cured within the applicable grace period, would result in a default under the Key Facility that would permit the lender thereunder to declare all amounts outstanding to be due and payable. In such an event, we may not have sufficient assets to repay such indebtedness and the lender may exercise rights available to them, including to the extent permitted under applicable law, the seizure of such assets without adjudication.

The Key Facility also requires Credit II and our Advisor to comply with various financial covenants, including maintenance by our Advisor of a minimum tangible net worth and limitations on the value of, and modifications to, the loan collateral that secures the Key Facility. Complying with these restrictions may prevent us from taking actions that we believe would help us to grow our business or are otherwise consistent with our investment objective. These restrictions could also limit our ability to plan for or react to market conditions, meet extraordinary capital needs or otherwise restrict corporate activities, and could result in our failing to qualify as a RIC resulting in our becoming subject to corporate-level income tax. See “Item 7 — Management’s Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and capital resources” for additional information regarding our credit arrangements.

An event of default or acceleration under the Key Facility could also cause a cross-default or cross-acceleration of other debt instruments or contractual obligations, which would adversely impact our liquidity. We may not be granted waivers or amendments to the Key Facility, if for any reason we are unable to comply with the terms of the Key Facility and we may not be able to refinance the Key Facility on terms acceptable to us, or at all.

***If we are unable to obtain additional debt financing, our business could be materially adversely affected.***

We may want to obtain additional debt financing, or need to do so upon maturity of the Key Facility, Asset-Back Notes or 2019 Notes, in order to obtain funds which may be made available for investments. We may borrow under the Key Facility until August 12, 2018. After such date, we must repay the outstanding advances under the Key Facility in accordance with its terms and conditions. All outstanding advances under the Key Facility are due and payable on August 12, 2020, unless such date is extended in accordance with its terms. All outstanding amounts on our 2019 Notes are due and payable on March 15, 2019 unless redeemed prior to that date. The Asset-Backed Notes have a stated maturity of May 15, 2018. If we are unable to increase, renew or replace the Key Facility or enter into other new debt financings on commercially reasonable terms, our liquidity may be reduced significantly. In addition, if we are unable to repay amounts outstanding under any such debt financings and are declared in default or are unable to renew or refinance these debt financings, we may not be able to make new investments or operate our business in the normal course. These situations may arise due to circumstances that we may be unable to control, such as lack of access to the credit markets, a severe decline in the value of the U.S. dollar, a further economic downturn or an operational problem that affects third parties or us, and could materially damage our business.

***Our 2019 Notes are unsecured and therefore are effectively subordinated to any secured indebtedness we have currently incurred or may incur in the future.***

Our 2019 Notes are not secured by any of our assets or any of the assets of our subsidiaries. As a result, the 2019 Notes are effectively subordinated to any secured indebtedness we or our subsidiaries have currently incurred and may incur in the future (or any indebtedness that is initially unsecured to which we subsequently grant security) to the extent of the value of the assets securing such indebtedness. In any liquidation, dissolution, bankruptcy or other similar proceeding, the holders of any of our existing or future secured indebtedness and the secured indebtedness of

our subsidiaries may assert rights against the assets pledged to secure that indebtedness in order to receive full payment of their indebtedness before the assets may be used to pay other creditors, including the holders of the 2019 Notes.

***Our 2019 Notes are structurally subordinated to the indebtedness and other liabilities of our subsidiaries.***

Our 2019 Notes are obligations exclusively of Horizon Technology Finance Corporation, and not of any of our subsidiaries. None of our subsidiaries is a guarantor of the 2019 Notes and the 2019 Notes are not required to be guaranteed by any subsidiaries we may acquire or create in the future. The assets of such subsidiaries are not directly available to satisfy the claims of our creditors, including holders of the 2019 Notes.

Except to the extent we are a creditor with recognized claims against our subsidiaries, all claims of creditors (including trade creditors) and holders of preferred stock, if any, of our subsidiaries have priority over our equity interests in such subsidiaries (and therefore the claims of our creditors, including holders of the 2019 Notes) with respect to the assets of such subsidiaries. Even if we are recognized as a creditor of one or more of our subsidiaries, our claims are effectively subordinated to any security interests in the assets of any such subsidiary and to any indebtedness or other liabilities of any such subsidiary senior to our claims. Consequently, the 2019 Notes are structurally subordinated to all indebtedness and other liabilities (including trade payables) of any of our subsidiaries and any subsidiaries that we may in the future acquire or establish as financing vehicles or otherwise.

In addition, our subsidiaries may incur substantial additional indebtedness in the future, all of which would be structurally senior to the 2019 Notes.

*The indenture under which our 2019 Notes were issued contains limited protection for holders of our 2019 Notes.*

The indenture under which the 2019 Notes were issued offers limited protection to holders of the 2019 Notes. The terms of the indenture and the 2019 Notes do not restrict our or any of our subsidiaries' ability to engage in, or otherwise be a party to, a variety of corporate transactions, circumstances or events that could have a material adverse impact on investments in the 2019 Notes. In particular, the terms of the indenture and the 2019 Notes do not place any restrictions on our or our subsidiaries' ability to:

issue securities or otherwise incur additional indebtedness or other obligations, including (1) any indebtedness or other obligations that would be equal in right of payment to the 2019 Notes, (2) any indebtedness or other obligations that would be secured and therefore rank effectively senior in right of payment to the 2019 Notes to the extent of the values of the assets securing such debt, (3) indebtedness of ours that is guaranteed by one or more of our subsidiaries and which therefore is structurally senior to the 2019 Notes and (4) securities, indebtedness or obligations issued or incurred by our subsidiaries that would be senior to our equity interests in our subsidiaries and therefore rank structurally senior to the 2019 Notes with respect to the assets of our subsidiaries, in each case other than an incurrence of indebtedness or other obligation that would cause a violation of Section 18(a)(1)(A) as modified by Section 61(a)(1) of the 1940 Act or any successor provisions, whether or not we continue to be subject to such provisions of the 1940 Act, but giving effect, in either case, to any exemptive relief granted to us by the SEC (these provisions generally prohibit us from making additional borrowings, including through the issuance of additional debt or the sale of additional debt securities, unless our asset coverage, as defined in the 1940 Act, equals at least 200% after such borrowings);

pay dividends on, or purchase or redeem or make any payments in respect of capital stock or other securities ranking junior in right of payment to the 2019 Notes, including subordinated indebtedness, in each case other than dividends, purchases, redemptions or payments that would cause a violation of Section 18(a)(1)(B) as modified by Section 61(a)(1) of the 1940 Act or any successor provisions giving effect to any exemptive relief granted to us by the SEC (these provisions generally prohibit us from declaring any cash dividend or distribution upon any class of our capital stock, or purchasing any such capital stock unless our asset coverage, as defined in the 1940 Act, equals at least 200% at the time of the declaration of the dividend or distribution or the purchase and after deducting the amount of such dividend, distribution or purchase);

sell assets (other than certain limited restrictions on our ability to consolidate, merge or sell all or substantially all of our assets);

enter into transactions with affiliates;

create liens (including liens on the shares of our subsidiaries) or enter into sale and leaseback transactions;

make investments; or

- create restrictions on the payment of dividends or other amounts to us from our subsidiaries.

In addition, the indenture does not require us to offer to purchase the 2019 Notes in connection with a change of control or any other event.

Furthermore, the terms of the indenture and the 2019 Notes do not protect holders of the 2019 Notes in the event that we experience changes (including significant adverse changes) in our financial condition, results of operations or credit ratings, as they do not require that we or our subsidiaries adhere to any financial tests or ratios or specified levels of net worth, revenues, income, cash flow, or liquidity.

Our ability to recapitalize, incur additional debt and take a number of other actions that are not limited by the terms of the 2019 Notes may have important consequences for holders of the 2019 Notes, including making it more difficult for us to satisfy our obligations with respect to the 2019 Notes or negatively affecting the trading value of the 2019 Notes.

Certain of our current debt instruments include more protections for their holders than the indenture and the 2019 Notes. In addition, other debt we issue or incur in the future could contain more protections for its holders than the indenture and the 2019 Notes, including additional covenants and events of default. The issuance or incurrence of any such debt with incremental protections could affect the market for and trading levels and prices of the 2019 Notes.

***An active trading market for our 2019 Notes may not exist, which could limit holders' ability to sell our 2019 Notes or affect the market price of the 2019 Notes.***

The 2019 Notes are listed on the New York Stock Exchange, or NYSE, under the symbol "HTF". However, we cannot provide any assurances that an active trading market for the 2019 Notes will exist in the future or that you will be able to sell your 2019 Notes. Even if an active trading market does exist, the 2019 Notes may trade at a discount from their initial offering price depending on prevailing interest rates, the market for similar securities, our credit ratings, if any, general economic conditions, our financial condition, performance and prospects and other factors. To the extent an active trading market does not exist, the liquidity and trading price for the 2019 Notes may be harmed. Accordingly, you may be required to bear the financial risk of an investment in the 2019 Notes for an indefinite period of time.

***If we default on our obligations to pay our other indebtedness, we may not be able to make payments on our 2019 Notes.***

Any default under the agreements governing our indebtedness, including a default under the Key Facility or the 2013-1 Securitization, or other indebtedness to which we may be a party that is not waived by the required lenders or holders thereunder, and the remedies sought by the holders of such indebtedness could make us unable to pay principal, premium, if any, and interest on the 2019 Notes and substantially decrease the market value of the 2019 Notes. If we are unable to generate sufficient cash flow and are otherwise unable to obtain funds necessary to meet required payments of principal, premium, if any, and interest on our indebtedness, or if we otherwise fail to comply with the various covenants, including financial and operating covenants, in the instruments governing our indebtedness, we could be in default under the terms of the agreements governing such indebtedness. In the event of such default, the holders of such indebtedness could elect to declare all the funds borrowed thereunder to be due and payable, together with accrued and unpaid interest, the lender under the Key Facility and our 2013-1 Securitization or other debt we may incur in the future could elect to terminate their commitments, cease making further loans and institute foreclosure proceedings against our assets, and we could be forced into bankruptcy or liquidation. If our operating performance declines, we may in the future need to seek to obtain waivers from the required lender under the Key Facility and our 2013-1 Securitization or other debt that we may incur in the future to avoid being in default. If we breach our covenants under the Key Facility and our 2013-1 Securitization or other debt and seek a waiver, we may not be able to obtain a waiver from the required lenders or holders. If this occurs, we would be in default and our lenders or debt holders could exercise their rights as described above, and we could be forced into bankruptcy or liquidation. If we are unable to repay debt, lenders having secured obligations, including the lender under the Key Facility and our 2013-1 Securitization, could proceed against the collateral securing the debt. Because the Key Facility and our 2013-1 Securitization have, and any future credit facilities will likely have, customary cross-default provisions, if the indebtedness thereunder or under any future credit facility is accelerated, we may be unable to repay or finance the amounts due.

***We are subject to certain risks as a result of our interests in connection with the 2013-1 Securitization and our equity interest in the 2013-1 Trust.***

On June 28, 2013, in connection with the 2013-1 Securitization and the offering of the Asset-Backed Notes by the 2013-1 Trust, we sold and/or contributed to Horizon Funding 2013-1, LLC or the Trust Depositor, certain loans, or the Trust Loans, which the Trust Depositor in turn sold and/or contributed to the 2013-1 Trust in exchange for 100% of the equity interest in the 2013-1 Trust, cash proceeds and other consideration. Following these transfers, the 2013-1 Trust, and not the Trust Depositor or us, holds all of the ownership interest in the Trust Loans.

As a result of the 2013-1 Securitization, we hold, indirectly through the Trust Depositor, 100% of the equity interest of the 2013-1 Trust. As a result, we consolidate the financial statements of the Trust Depositor and the 2013-1 Trust, as well as our other subsidiaries, in our consolidated financial statements. Because each of the Trust Depositor and the 2013-1 Trust is disregarded as an entity separate from its owner for U.S. federal income tax purposes, the sale or contribution by us to the Trust Depositor, and by the Trust Depositor to the 2013-1 Trust, did not constitute a taxable event for U.S. federal income tax purposes. If the U.S. Internal Revenue Service were to take a contrary position, there could be a material adverse effect on our business, financial condition, results of operations or cash flows. Further, a failure of the 2013-1 Trust to be treated as a disregarded entity for U.S. federal income tax purposes would constitute an event of default pursuant to the indenture under the 2013-1 Securitization, upon which the trustee under the 2013-1 Securitization, or the Trustee, may, and will at the direction of a supermajority of the holders of the Asset-Backed Notes (collectively, the "Noteholders"), declare the Asset-Backed Notes to be immediately due and payable and exercise remedies under the indenture, including (i) institute proceedings for the collection of all amounts then payable on the Asset-Backed Notes or under the indenture, enforce any judgment obtained, and collect from the 2013-1 Trust and any other obligor upon the Asset-Backed Notes monies adjudged due; (ii) institute proceedings from time to time for the complete or partial foreclosure of the indenture with respect to the property of the 2013-1 Trust; (iii) exercise any remedies as a secured party under the relevant provisions of the applicable jurisdiction's UCC and take other appropriate action under applicable law to protect and enforce the rights and remedies of the Trustee and the Noteholders; or (iv) sell the property of the 2013-1 Trust or any portion thereof or rights or interest therein at one or more public or private sales called and conducted in any matter permitted by law. Any such exercise of remedies could have a material adverse effect on our business, financial condition, results of operations or cash flows.

***An event of default in connection with the 2013-1 Securitization could give rise to a cross-default under our other material indebtedness.***

The documents governing our other material indebtedness contain customary cross-default provisions that could be triggered if an event of default occurs in connection with the 2013-1 Securitization. An event of default with respect to our other indebtedness could lead to the acceleration of such indebtedness and the exercise of other remedies as provided in the documents governing such other indebtedness. This could have a material adverse effect on our business, financial condition, results of operations and cash flows and may result in our inability to make distributions sufficient to maintain our status as a RIC.

***We may not receive cash distributions in respect of our indirect ownership interest in the 2013-1 Trust.***

Apart from fees payable to us in connection with our role as servicer of the Trust Loans and the reimbursement of related amounts under the 2013-1 Securitization documents, we receive cash in connection with the 2013-1 Securitization only to the extent that the Trust Depositor receives payments in respect of its equity interest in the 2013-1 Trust. The holder of the equity interest in the 2013-1 Trust is the residual claimant on distributions, if any, made by the 2013-1 Trust after the Noteholders and other claimants have been paid in full on each payment date or upon maturity of the Asset-Backed Notes, subject to the priority of payment provisions under the 2013-1 Securitization documents. To the extent that the value of the 2013-1 Trust's portfolio of Trust Loans is reduced as a result of conditions in the credit markets (relevant in the event of a liquidation event), other macroeconomic factors, distressed or defaulted Trust Loans or the failure of individual portfolio companies to otherwise meet their obligations in respect of the Trust Loans, or for any other reason, the ability of the 2013-1 Trust to make cash distributions in respect of the Trust Depositor's equity interest would be negatively affected and, consequently, the value of the equity interest in the 2013-1 Trust would also be reduced. In the event that we fail to receive cash indirectly from the 2013-1 Trust, we could be unable to make distributions in amounts sufficient to maintain our status as a RIC or at all.

***The interests of the Noteholders may not be aligned with our interests.***

The Asset-Backed Notes are debt obligations ranking senior in right of payment to the rights of the holder of the equity interest in the 2013-1 Trust (currently the Trust Depositor, our wholly owned subsidiary), as residual claimant in respect of distributions, if any, made by the 2013-1 Trust. As such, there are circumstances in which the interests of the Noteholders may not be aligned with the interests of the holder of the equity interest in the 2013-1 Trust. For example, under the terms of the documents governing the 2013-1 Securitization, the Noteholders have the right to receive payments of principal and interest prior to the holder of the equity interest in the 2013-1 Trust.



For as long as the Asset-Backed Notes remain outstanding, the Noteholders have the right to act in certain circumstances with respect to the Trust Loans in ways that may benefit their interests but not the interests of holder of the equity interest in the 2013-1 Trust, including by exercising remedies under the documents governing the 2013-1 Securitization.

If an event of default occurs, the Noteholders will be entitled to determine the remedies to be exercised, subject to the terms of the documents governing the 2013-1 Securitization. For example, upon the occurrence of an event of default with respect to the Asset-Backed Notes, the Trustee may, and will at the direction of the holders of a supermajority of the Asset-Backed Notes, declare the principal, together with any accrued interest, of the Asset-Backed Note to be immediately due and payable. This would have the effect of accelerating the principal on such Asset-Backed Note, triggering a repayment obligation on the part of the 2013-1 Trust. The Asset-Backed Notes then outstanding will be paid in full before any further payment or distribution is made to the holder of the equity interest in 2013-1 Trust. There can be no assurance that there will be sufficient funds through collections on the Trust Loans or through the proceeds of the sale of the Trust Loans in the event of a bankruptcy or insolvency to repay in full the obligations under the Asset-Backed Notes, or to make any distribution payment to holder of the equity interest in the 2013-1 Trust.

Remedies pursued by the Noteholders could be adverse to our interests as the indirect holder of the equity interest in the 2013-1 Trust. The Noteholders have no obligation to consider any possible adverse effect on such other interests. Thus, there can be no assurance that any remedies pursued by the Noteholders will be consistent with the best interests of the Trust Depositor or that we will receive, indirectly through the Trust Depositor, any payments or distributions upon an acceleration of the Asset-Backed Notes. Any failure of the 2013-1 Trust to make distributions in respect of the equity interest that we indirectly hold through the Trust Depositor, whether as a result of an event of default and the acceleration of payments on the Asset-Backed Notes or otherwise, could have a material adverse effect on our business, financial condition, results of operations and cash flows and may result in our inability to make distributions sufficient to maintain our status as a RIC.

***Certain events related to the performance of Trust Loans could lead to the acceleration of principal payments on the Asset-Backed Notes.***

The following constitute rapid amortization events, or Rapid Amortization Events, under the documents governing the 2013-1 Securitization: (i) the aggregate outstanding principal balance of all delinquent Trust Loans, and restructured Trust Loans that would constitute delinquent Trust Loans had such Trust Loans not become restructured Trust Loans, exceeds ten percent (10%) of the aggregate outstanding principal balance of the Trust Loans for a period of three consecutive months; (ii) the aggregate outstanding principal balance of defaulted Trust Loans exceeds five percent (5%) of the initial aggregate outstanding principal balance of the Trust Loans determined as of June 28, 2013 for a period of three consecutive months; (iii) the aggregate outstanding principal balance of the Asset-Backed Notes exceeds the borrowing base (which is a percentage of the outstanding principal balance of the Trust Loans less defaulted, delinquent, ineligible, and certain restructured Trust Loans and Trust Loans to issuers that exceed given thresholds) for a period of three consecutive months; (iv) the 2013-1 Trust's pool of Trust Loans contains Trust Loans to ten or fewer obligors; and (v) the occurrence of an event of default under the documents governing the 2013-1 Securitization. After a Rapid Amortization Event has occurred, subject to the priority of payment provisions under the documents governing the 2013-1 Securitization, principal collections on the Trust Loans will be used to make accelerated payments of principal on the Asset-Backed Notes until the payment of principal balance of the Asset-Backed Notes is reduced to zero. Such an event could delay, reduce or eliminate the ability of the 2013-1 Trust to make payments or distributions in respect of the equity interest that we indirectly hold, which could have a material adverse effect on our business, financial condition, results of operations and cash flows and may result in our inability to make distributions sufficient to maintain our status as a RIC.

***We have certain repurchase obligations with respect to the Trust Loans transferred in connection with the 2013-1 Securitization.***

As part of the 2013-1 Securitization, we entered into a sale and contribution agreement and a sale and servicing agreement under which we would be required to repurchase any Trust Loan (or participation interest therein) which was sold to the 2013-1 Trust in breach of certain customary representations and warranties made by us or by the Trust Depositor with respect to such Trust Loan or the legal structure of the 2013-1 Securitization. To the extent that there is such a breach of such representations and warranties and we fail to satisfy any such repurchase obligation, the Trustee

may, on behalf of the 2013-1 Trust, bring an action against us to enforce these repurchase obligations.

***Because we distribute all or substantially all of our investment company taxable income to our stockholders, we will need additional capital to finance our growth. If additional funds are unavailable or not available on favorable terms, our ability to grow will be impaired.***

To satisfy the requirements applicable to a RIC, to avoid payment of excise taxes and to minimize or to avoid payment of corporate-level federal income taxes, we intend to distribute to our stockholders all or substantially all of our investment company taxable income and net capital gains. However, we may retain all or a portion of our net capital gains, pay applicable income taxes with respect thereto, and elect to treat such retained capital gains as deemed distributions to our stockholders. As a BDC, we generally are required to maintain coverage of total assets to total senior securities, which includes all of our borrowings and any preferred stock we may issue in the future, of at least 200%. This requirement limits the amount that we may borrow. Because we continue to need capital to grow our debt investment portfolio, this limitation may prevent us from incurring debt and require us to raise additional equity at a time when it may be disadvantageous to do so. We cannot assure you that debt and equity financing will be available to us on favorable terms, or at all, and debt financings may be restricted by the terms of any of our outstanding borrowings. In addition, as a BDC, we are limited in our ability to issue equity securities at a price below the then current NAV per share. If additional funds are not available to us, we could be forced to curtail or cease new lending and investment activities, and our NAV could decline.

***As a BDC, we generally are not able to issue our common stock at a price below the then current NAV per share without first obtaining the approval of our stockholders and our independent directors. If our common stock trades at a price below NAV per share and we do not receive such approval, our business could be materially adversely affected.***

As a BDC, we generally are not able to issue our common stock at a price below the then current NAV per share without first obtaining the approval of our stockholders and our independent directors. Stockholder approval to offer our common stock at a price below NAV per share expired in January 2016, but we may seek such approval again in the future. If our common stock trades at a price below NAV per share and we do not receive approval from our stockholders and our independent directors to issue common stock at a price below NAV per share, we cannot raise capital through the issuance of equity securities. This may limit our ability: to grow and make new investments; to attract and retain top investment professionals; to maintain deal flow and relations with top companies in our Target Industries and related entities such as venture capital and private equity sponsors; and to sustain a minimum efficient scale for a public company.

***We are subject to risks associated with the current interest rate environment that may affect our cost of capital and net investment income.***

Since the economic downturn that began in mid-2007, interest rates have remained low. Because longer-term inflationary pressure may result from the U.S. government's fiscal policies and other challenges, because of the historically low interest rate environment in which we now operate and because the Federal Reserve has ended its quantitative easing program, we will likely experience rising interest rates, rather than falling rates in the future.

Because we currently incur indebtedness to fund our investments, a portion of our income depends upon the difference between the interest rate at which we borrow funds and the interest rate at which we invest these funds. Some of our investments have fixed interest rates, while the Key Facility has a floating interest rate. As a result, a significant change in interest rates could have a material adverse effect on our net investment income. In periods of rising interest rates, our cost of funds could increase, which may reduce our net investment income. We may hedge against interest rate fluctuations by using hedging instruments such as swaps, futures, options and forward contracts, subject to applicable legal requirements, including all necessary registrations (or exemptions from registration) with the Commodity Futures Trading Commission. These activities may limit our ability to benefit from lower interest rates with respect to the hedged portfolio. Adverse developments resulting from changes in interest rates or hedging transactions or any adverse developments from our use of hedging instruments could have a material adverse effect on our business, financial condition and results of operations. In addition, we may be unable to enter into appropriate hedging transactions when desired and any hedging transactions we enter into may not be effective.

***Because many of our investments are not and typically will not be in publicly traded securities, the value of our investments may not be readily determinable, which could adversely affect the determination of our NAV.***

Our investments consist, and we expect our future investments to consist, primarily of debt investments or securities issued by privately held companies. As these investments are not publicly traded, their fair value may not be readily determinable. In addition, we are not permitted to maintain a general reserve for anticipated debt investment losses. Instead, we are required by the 1940 Act to specifically value each investment and record an unrealized gain or loss for any asset that we believe has increased or decreased in value. We value these investments on a quarterly basis, or more frequently as circumstances require, in accordance with our valuation policy and consistent with GAAP. Our Board employs an independent third-party valuation firm to assist them in arriving at the fair value of our investments. Our Board discusses valuations and determines the fair value in good faith based on the input of our Advisor and the third-party valuation firm. The factors that may be considered in fair value pricing our investments include the nature and realizable value of any collateral, the portfolio company's earnings and its ability to make payments on its indebtedness, the markets in which the portfolio company does business, comparisons to publicly traded companies, discounted cash flow and other relevant factors. Because such valuations are inherently uncertain and may be based on estimates, our determinations of fair value may differ materially from the values that would be assessed if a ready market for these securities existed. Our NAV could be adversely affected if our determinations regarding the fair value of our investments are materially higher than the values that we ultimately realize upon the disposal of these investments.

***Global capital markets could enter a period of severe disruption and instability. These conditions have historically affected and could again materially and adversely affect debt and equity capital markets in the United States and around the world and our business.***

The U.S. and global capital markets experienced extreme volatility and disruption during the economic downturn that began in mid-2007, and the U.S. economy was in a recession for several consecutive calendar quarters during the same period. This economic decline materially and adversely affected the broader financial and credit markets and has reduced the availability of debt and equity capital for the market as a whole and to financial firms, in particular. At various times, these disruptions resulted in a lack of liquidity in parts of the debt capital markets, significant write-offs in the financial services sector relating to subprime mortgages and the repricing of credit risk in the broadly syndicated market. These disruptions in the capital markets also increased the spread between the yields realized on risk-free and higher risk securities and reduced the availability of debt and equity capital for the market as a whole and financial services firms in particular. These conditions may reoccur for a prolonged period of time again or materially worsen in the future. Unfavorable economic conditions, including future recessions, also could affect our investment valuations, increase our funding costs, limit our access to the capital markets or result in a decision by lenders not to extend credit to us or our portfolio companies. We may in the future have difficulty accessing debt and equity capital on attractive terms, or at all, and a severe disruption and instability in the global financial markets or deteriorations in credit and financing conditions may cause us to reduce the volume of debt investments we originate and/or fund, adversely affect the value of our portfolio investments or otherwise have a material adverse effect on our business, financial condition, results of operations and cash flows.

***Regulations governing our operation as a BDC affect our ability to, and the way in which, we raise additional capital, which may expose us to additional risks.***

Our business plans contemplate a need for a substantial amount of capital in addition to our current amount of capital. We may obtain additional capital through the issuance of debt securities or preferred stock, and we may borrow money from banks or other financial institutions, which we refer to collectively as “senior securities,” up to the maximum amount permitted by the 1940 Act. If we issue senior securities, we would be exposed to typical risks associated with leverage, including an increased risk of loss. In addition, if we issue preferred stock, it would rank senior to common stock in our capital structure and preferred stockholders would have separate voting rights and may have rights, preferences or privileges more favorable than those of holders of our common stock.

The 1940 Act permits us to issue senior securities in amounts such that our asset coverage, as defined in the 1940 Act, equals at least 200% after each issuance of senior securities. If our asset coverage is not at least 200%, we are not permitted to pay distributions or issue additional senior securities. As a result, we may have difficulty meeting the Annual Distribution Requirement necessary to qualify for and maintain RIC tax treatment under Subchapter M of the Code. Moreover, if the value of our assets declines, we may be unable to satisfy this asset coverage test. If that happens, we may be required to liquidate a portion of our investments and repay a portion of our indebtedness at a time when we may be unable to do so or unable to do so on favorable terms.

As a BDC, we generally are not able to issue our common stock at a price below NAV per share without first obtaining the approval of our stockholders and our independent directors. Our stockholder approval expired in January 2016, but we may seek such approval again in the future. This requirement does not apply to stock issued upon the exercise of options, warrants or rights that we may issue from time to time. If we raise additional funds by issuing more common stock or senior securities convertible into, or exchangeable for, our common stock, the percentage ownership of our stockholders at that time would decrease, and you may experience dilution.

*Pending legislation may allow us to incur additional leverage.*

As a BDC, under the 1940 Act we generally are not permitted to incur indebtedness unless immediately after such borrowing we have an asset coverage for total borrowings of at least 200% (i.e., the amount of debt may not exceed 50% of the value of our assets). Legislation introduced in the U.S. House of Representatives, if eventually passed, would modify this section of the 1940 Act and, subject to stockholder approval, increase the amount of debt that BDCs may incur from 200% to 150%. As a result, we may be able to incur additional indebtedness in the future, and therefore the risk of an investment in us may increase.

*If we are unable to satisfy the requirements under the Code for qualification as a RIC, we will be subject to corporate-level federal income tax.*

To qualify as a RIC under the Code, we must meet certain source-of-income, asset diversification and distribution requirements contained in Subchapter M of the Code, as well as maintain our election to be regulated as a BDC under the 1940 Act. We must also meet the Annual Distribution Requirement (as described below) to avoid corporate-level federal income tax in that year on all of our taxable income, regardless of whether we make any distributions to our stockholders.

The Qualifying Income Test is satisfied if we derive in each tax year at least 90% of our gross income from dividends, interest (including tax-exempt interest), payments with respect to certain securities loans, gains from the sale or other disposition of stock, securities or foreign currencies, other income (including but not limited to gain from options, futures or forward contracts) derived with respect to our business of investing in stock, securities or currencies, or net income derived from interests in “qualified publicly traded partnerships.” The status of certain forms of income we receive could be subject to different interpretations under the Code and might be characterized as non-qualifying income that could cause us to fail to qualify as a RIC, assuming we do not qualify for or take advantage of certain remedial provisions, and, thus, may cause us to be subject to corporate-level federal income taxes.

To qualify as a RIC, we must also meet the Diversification Tests at the end of each calendar quarter. Failure to meet these tests may result in our having to (1) dispose of certain investments quickly; (2) raise additional capital to prevent the loss of RIC status; or (3) engage in certain remedial actions that may entail the disposition of certain investments at disadvantageous prices that could result in substantial losses, and the payment of penalties, if we qualify to take such actions. Because most of our investments are and will be in development-stage companies within our Target Industries, any such dispositions could be made at disadvantageous prices and may result in substantial losses. If we raise additional capital to satisfy the asset diversification requirements, it could take a longer time to invest such capital. During this period, we will invest in temporary investments, such as money market funds, which we expect will earn yields substantially lower than the interest income that we anticipate receiving in respect of our investments in secured and amortizing debt investments.

The Annual Distribution Requirement for a RIC is satisfied if we distribute dividends to our stockholders in each tax year of an amount generally equal to at least 90% of our investment company taxable income. If we borrow money, we may be subject to certain asset coverage requirements under the 1940 Act and loan covenants that could, under certain circumstances, restrict us from making distributions necessary to qualify as a RIC. If we are unable to obtain cash from other sources, we may fail to qualify for the federal income tax benefits allowable to a RIC, assuming we do not qualify for or take advantage of certain remedial provisions, and, thus, may be subject to corporate-level income tax.



If we were to fail to qualify for the federal income tax benefits allowable to RICs for any reason and become subject to a corporate-level federal income tax, the resulting taxes could substantially reduce our net assets, the amount of income available for distribution to our stockholders, and the actual amount of our distributions. Such a failure would have a material adverse effect on us, the NAV of our common stock and the total return, if any, obtainable from your investment in our common stock. In addition, we could be required to recognize unrealized gains, pay substantial taxes and interest and make substantial distributions before requalifying as a RIC. See “Item 1. Business—Regulation.”

***We may have difficulty paying our required distributions if we recognize taxable income before or without receiving cash.***

We may be required to recognize taxable income in circumstances in which we do not receive cash. For example, if we hold debt instruments that are treated under applicable tax rules as having original issue discount (such as debt instruments with payment-in-kind interest or, in certain cases, increasing interest rates or issued with warrants), we must include in taxable income each tax year a portion of the original issue discount that accrues over the life of the debt instrument, regardless of whether cash representing such income is received by us in the same tax year. We do not have a policy limiting our ability to invest in original issue discount instruments, including payment-in-kind debt investments. Because in certain cases we may recognize taxable income before or without receiving cash representing such income, we may have difficulty meeting the Annual Distribution Requirement.

Accordingly, we may need to sell some of our assets at times that we would not consider advantageous, raise additional debt or equity capital or forego new investment opportunities or otherwise take actions that are disadvantageous to our business (or be unable to take actions that we believe are necessary or advantageous to our business) in order to satisfy the Annual Distribution Requirement. If we are unable to obtain cash from other sources to satisfy the Annual Distribution Requirement, we may fail to qualify for the federal income tax benefits allowable to RICs and, thus, become subject to a corporate-level federal income tax on all our income. The proportion of our income, consisting of interest and fee income that resulted from the portion of original issue discount classified as such in accordance with GAAP not received in cash for the years ended December 31, 2015, 2014 and 2013 was 8.9%, 9.5% and 11.5%, respectively.

***If we make loans to borrowers or acquire loans that contain deferred payment features, such as loans providing for the payment of portions of principal and/or interest at maturity, this could increase the risk of default by our borrowers.***

Our investments with deferred payment features, such as debt investments providing for ETPs, may represent a higher credit risk than debt investments requiring payments of all principal and accrued interest at regular intervals over the life of the debt investment. For example, even if the accounting conditions for income accrual were met during the period when the obligation was outstanding, the borrower could still default when our actual collection is scheduled to occur upon maturity of the obligation. The amount of ETPs due under our investments having such a feature currently represents a small portion of the applicable borrowers' total repayment obligations under such investments. However, deferred payment arrangements increase the incremental risk that we will not receive a portion of the amount due at maturity. Additionally, because investments with a deferred payment feature may have the effect of deferring a portion of the borrower's payment obligation until maturity of the debt investment, it may be difficult for us to identify and address developing problems with borrowers in terms of their ability to repay us. Any such developments may increase the risk of default on our debt investments by borrowers.

In addition, debt investments providing for ETPs are subject to the risks associated with debt investments having original issue discount (such as debt instruments with payment-in-kind interest or, in certain cases, increasing interest rates or issued with warrants). See “—We may have difficulty paying our required distributions if we recognize taxable income before or without receiving cash.”

***The borrowing needs of our portfolio companies are unpredictable, especially during a challenging economic environment. We may not be able to meet our unfunded commitments to extend credit, which could have a material adverse effect on our business, financial condition and results of operations.***

A commitment to extend credit is a formal agreement to lend funds to our portfolio companies as long as there is no violation of any condition established under the agreement. The actual borrowing needs of our portfolio companies under these commitments have historically been lower than the contractual amount of the commitments. A significant

portion of these commitments expire without being drawn upon, and as such, the total amount of unfunded commitments does not reflect our expected future cash funding requirements. Because of the credit profile of our portfolio companies, we typically have a substantial amount of total unfunded credit commitments, which amount is not reflected on our balance sheet. The actual borrowing needs of our portfolio companies may exceed our expected funding requirements, especially during a challenging economic environment when our portfolio companies may be more dependent on our credit commitments due to the lack of available credit elsewhere, an increasing cost of credit or the limited availability of financing from venture capital firms. In addition, limited partner investors of some of our portfolio companies may fail to meet their underlying investment commitments due to liquidity or other financing issues, which may increase our portfolio companies' borrowing needs. Any failure to meet our unfunded credit commitments in accordance with the actual borrowing needs of our portfolio companies may have a material adverse effect on our business, financial condition and results of operations.

***If we do not invest a sufficient portion of our assets in qualifying assets, we could fail to qualify as a BDC or be precluded from investing according to our current business strategy.***

As a BDC, we are prohibited from acquiring any assets other than qualifying assets (as defined under the 1940 Act) unless, at the time of and after giving effect to such acquisition, at least 70% of our total assets are qualifying assets. As of December 31, 2015 and 2014, 100% of our assets were qualifying assets, and we expect that substantially all of our assets that we may acquire in the future will be qualifying assets, although we may decide to make other investments that are not qualifying assets to the extent permitted by the 1940 Act. If we acquire debt or equity securities from an issuer that has outstanding marginable securities at the time we make an investment, these acquired assets may not be treated as qualifying assets. This result is dictated by the definition of "eligible portfolio company" under the 1940 Act, which in part looks to whether a company has outstanding marginable securities. See Item 1 above, "Regulation — Qualifying assets." If we do not invest a sufficient portion of our assets in qualifying assets, we could lose our status as a BDC. If we do not maintain our status as a BDC, we would be subject to regulation as a registered closed-end investment company under the 1940 Act. As a registered closed-end investment company, we would be subject to substantially more regulatory restrictions under the 1940 Act, which would significantly decrease our operating flexibility.

***New or modified laws or regulations governing our operations may adversely affect our business.***

We and our portfolio companies are subject to regulation by laws at the U.S. federal, state and local levels. These laws and regulations, as well as their interpretation, may change from time to time, and new laws, regulations and interpretations may also come into effect. Any such new or changed laws or regulations could have a material adverse effect on our business. In particular, on July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act, or Dodd-Frank, became law. The scope of Dodd-Frank impacts many aspects of the financial services industry, and it requires the development and adoption of many implementing regulations over the next several months and years. The effects of Dodd-Frank on the financial services industry will depend, in large part, upon the extent to which regulators exercise the authority granted to them and the approaches taken in implementing regulations. The likely impact of Dodd-Frank cannot be ascertained with any degree of certainty.

Additionally, changes to the laws and regulations governing our operations, including those associated with RICs, may cause us to alter our investment strategy in order to avail ourselves of new or different opportunities or result in the imposition of corporate-level taxes on us. Such changes could result in material differences to our strategies and plans and may shift our investment focus from the areas of expertise of the Advisor to other types of investments in which the Advisor may have little or no expertise or experience. Any such changes, if they occur, could have a material adverse effect on our results of operations and the value of your investment.

***Our Advisor has significant potential conflicts of interest with us and our stockholders.***

As a result of our arrangements with our Advisor, there may be times when our Advisor has interests that differ from those of our stockholders, giving rise to a potential conflict of interest. Our executive officers and directors, as well as the current and future executives and employees of our Advisor, serve or may serve as officers, directors or principals of entities that operate in the same or a related line of business as we do. Accordingly, they may have obligations to investors in those entities, the fulfillment of which might not be in the best interests of our stockholders. In addition, our Advisor may manage other funds in the future that may have investment objectives that are similar, in whole or in part, to ours. Our Advisor may determine that an investment is appropriate for us and for one or more of those other funds. In such an event, depending on the availability of the investment and other appropriate factors, our Advisor will endeavor to allocate investment opportunities in a fair and equitable manner and act in accordance with its written conflicts of interest policy to address and, if necessary, resolve any conflict of interests. It is also possible that we may not be given the opportunity to participate in these other investment opportunities.

We pay management and incentive fees to our Advisor and reimburse our Advisor for certain expenses it incurs. As a result, investors in our common stock invest on a “gross” basis and receive distributions on a “net” basis after expenses, resulting in a lower rate of return than an investor might achieve through direct investments. Also, the incentive fee payable by us to our Advisor may create an incentive for our Advisor to pursue investments on our behalf that are riskier or more speculative than would be the case in the absence of such compensation arrangements.

We have entered into a license agreement with Horizon Technology Finance, LLC, pursuant to which it has agreed to grant us a non-exclusive, royalty-free right and license to use the service mark “Horizon Technology Finance.” Under this agreement, we have a right to use the “Horizon Technology Finance” service mark for so long as the Investment Management Agreement is in effect between us and our Advisor. In addition, we pay our Advisor, our allocable portion of overhead and other expenses incurred by our Advisor in performing its obligations under the Administration Agreement, including rent, the fees and expenses associated with performing compliance functions, and our allocable portion of the compensation of our Chief Financial Officer and Chief Compliance Officer and their respective staffs. Any potential conflict of interest arising as a result of our arrangements with our Advisor could have a material adverse effect on our business, results of operations and financial condition.

***Our incentive fee may impact our Advisor's structuring of our investments, including by causing our Advisor to pursue speculative investments.***

The incentive fee payable by us to our Advisor may create an incentive for our Advisor to pursue investments on our behalf that are riskier or more speculative than would be the case in the absence of such compensation arrangement. The incentive fee payable to our Advisor is calculated based on a percentage of our return on invested capital. This may encourage our Advisor to use leverage to increase the return on our investments. Under certain circumstances, the use of leverage may increase the likelihood of default, which would impair the value of our common stock. In addition, our Advisor receives the incentive fee based, in part, upon net capital gains realized on our investments. Unlike that portion of the incentive fee based on income, there is no hurdle rate applicable to the portion of the incentive fee based on net capital gains. As a result, our Advisor may have an incentive to invest more capital in investments that are likely to result in capital gains as compared to income-producing securities. Such a practice could result in our investing in more speculative investments than would otherwise be the case, which could result in higher investment losses, particularly during economic downturns. In addition, the incentive fee may encourage our Advisor to pursue different types of investments or structure investments in ways that are more likely to result in warrant gains or gains on equity investments, including upon exercise of equity participation rights, which are inconsistent with our investment strategy and disciplined underwriting process.

The incentive fee payable by us to our Advisor may also induce our Advisor to pursue investments on our behalf that have a deferred interest feature, even if such deferred payments would not provide cash necessary to enable us to pay current distributions to our stockholders. Under these investments, we would accrue interest over the life of the investment but would not receive the cash income from the investment until the end of the term. Our net investment income used to calculate the income portion of our investment fee, however, includes accrued interest. Thus, a portion of this incentive fee would be based on income that we have not yet received in cash. In addition, the "catch-up" portion of the incentive fee may encourage our Advisor to accelerate or defer interest payable by portfolio companies from one calendar quarter to another, potentially resulting in fluctuations in the timing and amounts of distributions. Our governing documents do not limit the number of debt investments we may make with deferred interest features or the proportion of our income we derive from such debt investments.

***Our ability to enter into transactions with our affiliates is restricted.***

As a BDC, we are prohibited under the 1940 Act from participating in certain transactions with our affiliates without the prior approval of our independent directors and, in some cases, the SEC. Any person that, among other things, owns, directly or indirectly, 5% or more of our outstanding voting securities is considered our affiliate for purposes of the 1940 Act. We are generally prohibited from buying or selling any security from or to an affiliate, absent the prior approval of our independent directors. The 1940 Act also prohibits certain "joint" transactions with an affiliate, which could include investments in the same portfolio company (whether at the same or different times), without prior approval of our independent directors. If a person acquires more than 25% of our voting securities, we are prohibited from buying or selling any security from or to that person or certain of that person's affiliates, or entering into prohibited joint transactions with those persons, absent the prior approval of the SEC. Similar restrictions limit our

ability to transact business with our officers or directors or their affiliates. These restrictions could limit or prohibit us from making certain attractive investments that we might otherwise make absent such restrictions.

While we have no current intention to enter into any principal transactions or joint arrangements with any affiliates, we have considered and evaluated, and will continue to consider and evaluate, the potential advantages and disadvantages of doing so. If we decide to enter into any such transactions in the future we will not do so until we have requested and received the requisite exemptive relief under Section 57 of the 1940 Act, the filing of which our Board has previously authorized.

*The valuation process for certain of our portfolio holdings creates a conflict of interest.*

The majority of our portfolio investments are expected to be made in the form of securities that are not publicly traded. As a result, the Board will determine the fair value of these securities in good faith as described above in “— Because many of our investments typically are not and will not be in publicly traded securities, the value of our investments may not be readily determinable, which could adversely affect the determination of our NAV.” In connection with that determination, investment professionals from the Advisor may provide the Board with portfolio company valuations based upon the most recent portfolio company financial statements available and projected financial results of each portfolio company. The participation of the Advisor’s investment professionals in our valuation process could result in a conflict of interest as the Advisor’s management fee is based, in part, on our average gross assets and our incentive fees will be based, in part, on unrealized appreciation and depreciation on our investments.

***Our Advisor's liability is limited, and we have agreed to indemnify our Advisor against certain liabilities, which may lead our Advisor to act in a riskier manner on our behalf than it would when acting for its own account.***

Under the Investment Management Agreement, our Advisor does not assume any responsibility to us other than to render the services called for under that agreement, and it is not responsible for any action of our Board in following or declining to follow our Advisor's advice or recommendations. Under the terms of the Investment Management Agreement, our Advisor, its officers, members, personnel and any person controlling or controlled by our Advisor is not liable to us, any subsidiary of ours, our directors, our stockholders or any subsidiary's stockholders or partners for acts or omissions performed in accordance with and pursuant to the Investment Management Agreement, except those resulting from acts constituting gross negligence, willful misconduct, bad faith or reckless disregard of our Advisor's duties under the Investment Management Agreement. In addition, we have agreed to indemnify our Advisor and each of its officers, directors, members, managers and employees from and against any claims or liabilities, including reasonable legal fees and other expenses reasonably incurred, arising out of or in connection with our business and operations or any action taken or omitted on our behalf pursuant to authority granted by the Investment Management Agreement, except where attributable to gross negligence, willful misconduct, bad faith or reckless disregard of such person's duties under the Investment Management Agreement. These protections may lead our Advisor to act in a riskier manner when acting on our behalf than it would when acting for its own account.

***If we are unable to manage our future growth effectively, we may be unable to achieve our investment objective, which could adversely affect our business, results of operations and financial condition and cause the value of your investment in us to decline.***

Our ability to achieve our investment objective depends on our ability to achieve and sustain growth, which depends, in turn, on our Advisor's direct origination capabilities and disciplined underwriting process in identifying, evaluating, financing, investing in and monitoring suitable companies that meet our investment criteria. Accomplishing this result on a cost-effective basis is largely a function of our Advisor's marketing capabilities, management of the investment process, ability to provide efficient services and access to financing sources on acceptable terms. In addition to monitoring the performance of our existing investments, our Advisor may also be called upon to provide managerial assistance to our portfolio companies. These demands on their time may distract them or slow the rate of investment. If we fail to manage our future growth effectively, our business, results of operations and financial condition could be materially adversely affected and the value of your investment in us could decrease.

***Our Board may change our operating policies and strategies, including our investment objective, without prior notice or stockholder approval, the effects of which may adversely affect our business.***

Our Board may modify or waive our current operating policies and strategies, including our investment objectives, without prior notice and without stockholder approval (provided that no such modification or waiver may change the nature of our business so as to cease to be, or withdraw our election as a BDC as provided by the 1940 Act without



stockholder approval at a special meeting called upon written notice of not less than ten or more than sixty days before the date of such meeting). We cannot predict the effect any changes to our current operating policies and strategies would have on our business, results of operations or financial condition or on the value of our stock. However, the effects of any changes might adversely affect our business, any or all of which could negatively impact our ability to pay distributions or cause you to lose all or part of your investment in us.

***Our quarterly and annual operating results may fluctuate due to the nature of our business.***

We could experience fluctuations in our quarterly and annual operating results due to a number of factors, some of which are beyond our control, including: our ability to make investments in companies that meet our investment criteria, the interest rate payable on our debt investments, the default rate on these investments, the level of our expenses, variations in, and the timing of, the recognition of realized and unrealized gains or losses, the degree to which we encounter competition in our markets and general economic conditions. For example, we have historically experienced greater investment activity during the second and fourth quarters relative to other periods. As a result of these factors, you should not rely on the results for any prior period as being indicative of our performance in future periods.

***Our business plan and growth strategy depends to a significant extent upon our Advisor's referral relationships. If our Advisor is unable to develop new or maintain existing relationships, or if these relationships fail to generate investment opportunities, our business could be materially adversely affected.***

We have historically depended on our Advisor's referral relationships to generate investment opportunities. For us to achieve our future business objectives, members of our Advisor need to maintain these relationships with venture capital and private equity firms and management teams and legal firms, accounting firms, investment banks and other lenders, and we rely to a significant extent upon these relationships to provide us with investment opportunities. If they fail to maintain their existing relationships or develop new relationships with other firms or sources of investment opportunities, we may not be able to grow our investment portfolio. In addition, persons with whom our Advisor has relationships are not obligated to provide us with investment opportunities, and, therefore, there is no assurance that such relationships will lead to the origination of debt or other investments.

***Our Advisor can resign on 60 days' notice and we may not be able to find a suitable replacement within that time, resulting in a disruption in our operations that could adversely affect our business, results of operations or financial condition.***

Under our Investment Management Agreement and our Administration Agreement, our Advisor has the right to resign at any time, including during the first two years following the Investment Management Agreement's effective date, upon not more than 60 days' written notice, whether we have found a replacement or not. If our Advisor resigns, we may not be able to find a new investment adviser or administrator or hire internal management with similar expertise and ability to provide the same or equivalent services on acceptable terms within 60 days, or at all. If we are unable to do so, our operations are likely to be disrupted, our business, results of operations and financial condition and our ability to pay distributions may be adversely affected and the market price of our shares may decline. In addition, the coordination of our internal management and investment activities is likely to suffer if we are unable to identify and reach an agreement with a single institution or group of executives having the expertise possessed by our Advisor and its affiliates. Even if we are able to retain comparable management, whether internal or external, the integration of new management and their lack of familiarity with our investment objective may result in additional costs and time delays that may adversely affect our business, results of operations or financial condition.

***We incur significant costs as a result of being a publicly traded company.***

As a publicly traded company, we incur legal, accounting and other expenses, including costs associated with the periodic reporting requirements applicable to a company whose securities are registered under the Exchange Act as well as additional corporate governance requirements, including requirements under the Sarbanes-Oxley Act, and other rules implemented by the SEC.

***Compliance with Section 404 of the Sarbanes-Oxley Act involves significant expenditures, and non-compliance with Section 404 of the Sarbanes-Oxley Act would adversely affect us and the market price of our common stock.***

Under current SEC rules, we are required to report on our internal control over financial reporting pursuant to Section 404 of the Sarbanes-Oxley Act and related rules and regulations of the SEC. As a result, we incur additional expenses that negatively impact our financial performance and our ability to make distributions. This process also results in a diversion of management's time and attention. We cannot be certain as to the timing of completion of our annual re-evaluation, testing and remediation actions or the impact of the same on our operations, and we cannot assure you that our internal control over financial reporting is or will be effective. In the event that we are unable to maintain compliance with Section 404 of the Sarbanes-Oxley Act and related rules, we and the market price of our securities may be adversely affected.

***We are highly dependent on information systems and systems failures could significantly disrupt our business, which may, in turn, negatively affect the market price of our common stock and our ability to pay distributions.***

Our business is highly dependent on the Advisor and its affiliates' communications and information systems. Any failure or interruption of those systems, including as a result of the termination of an agreement with any third-party service providers, could cause delays or other problems in our activities. Our financial, accounting, data processing, backup or other operating systems and facilities may fail to operate properly or become disabled or damaged as a result of a number of factors including events that are wholly or partially beyond our control and adversely affect our business. There could be:

- sudden electrical or telecommunications outages;
- natural disasters such as earthquakes, tornadoes and hurricanes;
  - disease pandemics; and
- events arising from local or larger scale political or social matters, including terrorist acts.

Any of these events, could have a material adverse effect on our operating results and negatively affect the market price of our common stock and our ability to pay distributions to our stockholders.

In addition, these communications and information systems are subject to potential attacks, including through adverse events that threaten the confidentiality, integrity or availability of our information resources. These attacks, which may include cyber incidents, may involve a third party gaining unauthorized access to our communications or information systems for purposes of misappropriating assets, stealing confidential information, corrupting data or causing operational disruption. Any such attack could result in disruption to our business, misstated or unreliable financial data, liability for stolen assets or information, increased cybersecurity protection and insurance costs, litigation and damage to our business relationships, any of which could have a material adverse effect on our business, financial condition and results of operations.

### **Risks related to our investments**

#### ***Our stockholders are not able to evaluate our future investments.***

Our future investments will be selected by our Advisor, subject to the approval of its investment committee. Our stockholders do not have input into our Advisor's investment decisions. As a result, our stockholders are unable to evaluate any of our future portfolio company investments. These factors increase the uncertainty, and thus the risk, of investing in our securities.

***We are a non-diversified investment company within the meaning of the 1940 Act, and therefore we generally are not limited with respect to the proportion of our assets that may be invested in securities of a single issuer.***

We are classified as a non-diversified investment company within the meaning of the 1940 Act, which means that we are not limited by the 1940 Act with respect to the proportion of our assets that we may invest in securities of a single issuer, excluding limitations on stake holdings in investment companies. To the extent that we assume large positions in the securities of a small number of issuers, our NAV may fluctuate to a greater extent than that of a diversified investment company as a result of changes in the financial condition or the market's assessment of the issuer. We may also be more susceptible to any single economic or regulatory occurrence than a diversified investment company. Beyond our income tax diversification requirements, we do not have fixed guidelines for diversification, and our investments could be concentrated in relatively few portfolio companies.

***Our portfolio may be concentrated in a limited number of portfolio companies and industries, which will subject us to a risk of significant loss if any of these companies defaults on its obligations under any of its debt instruments or if there is a downturn in a particular industry.***

Our portfolio may be concentrated in a limited number of portfolio companies and industries. As a result, the aggregate returns we realize may be significantly and adversely affected if a small number of investments perform poorly or if we need to write down the value of any one investment. Additionally, our investments will be concentrated in relatively few industries. As a result, a downturn in any particular industry in which we are invested could also significantly impact the aggregate returns we realize. Our Target Industries are susceptible to changes in government policy and economic assistance, which could adversely affect the returns we receive.

***If our investments do not meet our performance expectations, you may not receive distributions.***

We intend to make distributions of income on a monthly basis to our stockholders. We may not be able to achieve operating results that will allow us to make distributions at a specific level or increase the amount of these distributions from time to time. In addition, due to the asset coverage test applicable to us as a BDC, we may be limited in our ability to make distributions. Also, restrictions and provisions in any existing or future credit facilities may limit our ability to make distributions. If we do not distribute a certain percentage of our income each tax year as dividends to stockholders, we will suffer adverse tax consequences, including the possible loss of the federal income tax benefits allowable to RICs.

***Most of our portfolio companies will need additional capital, which may not be readily available.***

Our portfolio companies typically require substantial additional financing to satisfy their continuing working capital and other capital requirements and service the interest and principal payments on our investments. We cannot predict the circumstances or market conditions under which our portfolio companies will seek additional capital. Each round of institutional equity financing is typically intended to provide a company with only enough capital to reach the next stage of development. It is possible that one or more of our portfolio companies will not be able to raise additional financing or may be able to do so only at a price or on terms that are unfavorable to the portfolio company, either of which would negatively impact our investment returns. Some of these companies may be unable to obtain sufficient financing from private investors, public capital markets or lenders, thereby requiring these companies to cease or curtail business operations. Accordingly, investing in these types of companies generally entails a higher risk of loss than investing in companies that do not have significant incremental capital raising requirements.

***Economic recessions or downturns could adversely affect our business and that of our portfolio companies which may have an adverse effect on our business, results of operations and financial condition.***

General economic conditions may affect our activities and the operation and value of our portfolio companies. Economic slowdowns or recessions may result in a decrease of institutional equity investment, which would limit our lending opportunities. Furthermore, many of our portfolio companies may be susceptible to economic slowdowns or recessions and may be unable to repay our debt investments during these periods. Therefore, our non-performing assets are likely to increase and the value of our portfolio is likely to decrease during these periods. Adverse economic conditions may also decrease the value of collateral securing some of our debt investments and the value of our equity investments. Economic slowdowns or recessions could lead to financial losses in our portfolio and a decrease in revenues, net income and assets. Unfavorable economic conditions could also increase our funding costs, limit our access to the capital markets or result in a decision by lenders not to extend credit to us.

A portfolio company's failure to satisfy financial or operating covenants imposed by us or other lenders could lead to defaults and, potentially, termination of its loans and foreclosure on its secured assets, which could trigger cross-defaults under other agreements and jeopardize the portfolio company's ability to meet its obligations under the loans that we hold. We may incur expenses to the extent necessary to recover our investment upon default or to negotiate new terms with a defaulting portfolio company. These events could harm our financial condition and operating results.

***Our investment strategy focuses on investments in development-stage companies in our Target Industries, which are subject to many risks, including volatility, intense competition, shortened product life cycles and periodic downturns, and would be rated below "investment grade."***

We intend to invest, under normal circumstances, most of the value of our total assets (including the amount of any borrowings for investment purposes) in development-stage companies, which may have relatively limited operating histories, in our Target Industries. Many of these companies may have narrow product lines and small market shares, compared to larger established publicly owned firms, which tend to render them more vulnerable to competitors' actions and market conditions, as well as general economic downturns. The revenues, income (or losses) and valuations of development-stage companies in our Target Industries can and often do fluctuate suddenly and dramatically. For these reasons, investments in our portfolio companies, if rated by one or more ratings agency, would typically be rated below "investment grade," which refers to securities rated by ratings agencies below the four highest rating categories. These companies may also have more limited access to capital and higher funding costs. In addition, development-stage technology markets are generally characterized by abrupt business cycles and intense competition, and the competitive environment can change abruptly due to rapidly evolving technology. Therefore, our portfolio companies may face considerably more risk than companies in other industry sectors. Accordingly, these factors could impair their cash flow or result in other events, such as bankruptcy, which could limit their ability to repay their obligations to us and may materially adversely affect the return on, or the recovery of, our investments in these businesses.

Because of rapid technological change, the average selling prices of products and some services provided by development-stage companies in our Target Industries have historically decreased over their productive lives. These decreases could adversely affect their operating results and cash flow, their ability to meet obligations under their debt securities and the value of their equity securities. This could, in turn, materially adversely affect our business, financial condition and results of operations.

***Any unrealized depreciation we experience on our debt investments may be an indication of future realized losses, which could reduce our income available for distribution.***

As a BDC, we are required to carry our investments at fair value, which is the market value of our investments or, if no market value is ascertainable, at the fair value as determined in good faith pursuant to procedures approved by our Board in accordance with our valuation policy. We are not permitted to maintain a reserve for debt investment losses. Decreases in the fair values of our investments are recorded as unrealized depreciation. Any unrealized depreciation in our debt investments could be an indication of a portfolio company's inability to meet its repayment obligations to us with respect to the affected debt investments. This could result in realized losses in the future and ultimately reduces our income available for distribution in future periods.

***If the assets securing the debt investments we make decrease in value, we may not have sufficient collateral to cover losses and may experience losses upon foreclosure.***

We believe our portfolio companies generally are and will be able to repay our debt investments from their available capital, from future capital-raising transactions or from cash flow from operations. However, to mitigate our credit risks, we typically take a security interest in all or a portion of the assets of our portfolio companies, including the equity interests of their subsidiaries. There is a risk that the collateral securing our debt investments may decrease in value over time, may be difficult to appraise or sell in a timely manner and may fluctuate in value based upon the business and market conditions, including as a result of an inability of the portfolio company to raise additional capital, and, in some circumstances, our lien could be subordinated to claims of other creditors. In addition, deterioration of a portfolio company's financial condition and prospects, including its inability to raise additional capital, may be accompanied by deterioration of the value of the collateral for the debt investment. Consequently, although such debt investment is secured, we may not receive principal and interest payments according to the debt investment's terms and the value of the collateral may not be sufficient to recover our investment should we be forced to enforce our remedies.

In addition, because we invest in development-stage companies in our Target Industries, a substantial portion of the assets securing our investment may be in the form of intellectual property, if any, inventory, equipment, cash and accounts receivables. Intellectual property, if any, which secures a debt investment could lose value if the company's rights to the intellectual property are challenged or if the company's license to the intellectual property is revoked or expires. In addition, in lieu of a security interest in a portfolio company's intellectual property we may sometimes obtain a security interest in all assets of the portfolio company other than intellectual property and also obtain a commitment by the portfolio company not to grant liens to any other creditor on the company's intellectual property. In these cases, we may have additional difficulty recovering our principal in the event of a foreclosure. Similarly, any equipment securing our debt investments may not provide us with the anticipated security if there are changes in technology or advances in new equipment that render the particular equipment obsolete or of limited value or if the company fails to adequately maintain or repair the equipment. Any one or more of the preceding factors could materially impair our ability to recover principal in a foreclosure, which may adversely affect our ability to pay distributions in the future.



***We may choose to waive or defer enforcement of covenants in the debt securities held in our portfolio, which may cause us to lose all or part of our investment in these companies.***

We structure the debt investments in our portfolio companies to include business and financial covenants placing affirmative and negative obligations on the operation of the company's business and its financial condition. However, from time to time we may elect to waive breaches of these covenants, including our right to payment, or waive or defer enforcement of remedies, such as acceleration of obligations or foreclosure on collateral, depending upon the financial condition and prospects of the particular portfolio company. These actions may reduce the likelihood of our receiving the full amount of future payments of interest or principal and be accompanied by a deterioration in the value of the underlying collateral as many of these companies may have limited financial resources, may be unable to meet future obligations and may go bankrupt. These events could harm our financial condition and operating results.

***The lack of liquidity in our investments may adversely affect our business, and if we need to sell any of our investments, we may not be able to do so at a favorable price. As a result, we may suffer losses.***

We plan to generally invest in debt investments with terms of up to four years and hold such investments until maturity, unless earlier prepaid, and we do not expect that our related holdings of equity securities will provide us with liquidity opportunities in the near-term. We expect to primarily invest in companies whose securities are not publicly-traded, and whose securities are subject to legal and other restrictions on resale or are otherwise less liquid than publicly traded securities. The illiquidity of these investments may make it difficult for us to sell these investments when desired. We may also face other restrictions on our ability to liquidate an investment in a public portfolio company to the extent that we possess material non-public information regarding the portfolio company. In addition, if we are required to liquidate all or a portion of our portfolio quickly, we may realize significantly less than the value at which we had previously recorded these investments. As a result, we do not expect to dispose of our investments in the near term. However, we may be required to do so in order to maintain our qualification as a BDC and as a RIC if we do not satisfy one or more of the applicable criteria under the respective regulatory frameworks. Because most of our investments are illiquid, we may be unable to dispose of them, in which case we could fail to qualify as a RIC and/or BDC, or we may not be able to dispose of them at favorable prices, and as a result, we may suffer losses.

***Our portfolio companies may incur debt that ranks equally with, or senior to, our investments in such companies.***

We plan to invest primarily in debt investments issued by our portfolio companies. Some of our portfolio companies are permitted to have other debt that ranks equally with, or senior to, our debt investments in the portfolio company. By their terms, these debt instruments may provide that the holders thereof are entitled to receive payment of interest or principal on or before the dates on which we are entitled to receive payments in respect of our debt investments. These debt instruments may prohibit the portfolio companies from paying interest on or repaying our investments in the event of, and during, the continuance of a default under the debt instruments. In addition, in the event of insolvency, liquidation, dissolution, reorganization or bankruptcy of a portfolio company, holders of debt instruments ranking senior to our investment in that portfolio company would typically be entitled to receive payment in full before we receive any payment in respect of our investment. After repaying senior creditors, a portfolio company may not have any remaining assets to use for repaying its obligation to us. In the case of debt ranking equally with our debt investments, we would have to share on an equal basis any distributions with other creditors holding such debt in the event of an insolvency, liquidation, dissolution, reorganization or bankruptcy.

***There may be circumstances where our debt investments could be subordinated to claims of other creditors, or we could be subject to lender liability claims.***

Even though certain of our investments are structured as senior debt investments, if one of our portfolio companies were to go bankrupt, depending on the facts and circumstances, including the extent to which we actually provided managerial assistance to that portfolio company, a bankruptcy court might recharacterize our debt investment and subordinate all or a portion of our claim to that of other creditors. We may also be subject to lender liability claims for actions taken by us with respect to a portfolio company's business, including in rendering significant managerial assistance, or instances where we exercise control over the portfolio company.

***An investment strategy focused primarily on privately held companies presents certain challenges, including the lack of available information about these companies, a dependence on the talents and efforts of only a few key portfolio company personnel and a greater vulnerability to economic downturns.***

We currently invest, and plan to invest, primarily in privately held companies. Generally, very little public information exists about these companies, and we are required to rely on the ability of our Advisor to obtain adequate information to evaluate the potential returns from investing in these companies. If we are unable to uncover all material information about these companies, we may not make a fully informed investment decision, and we may lose money on our investments. Also, privately held companies frequently have less diverse product lines and a smaller market presence than larger competitors. Thus, they are generally more vulnerable to economic downturns and may experience substantial variations in operating results. These factors could affect our investment returns.

In addition, our success depends, in large part, upon the abilities of the key management personnel of our portfolio companies, who are responsible for the day-to-day operations of our portfolio companies. Competition for qualified personnel is intense at any stage of a company's development. The loss of one or more key managers can hinder or delay a company's implementation of its business plan and harm its financial condition. Our portfolio companies may not be able to attract and retain qualified managers and personnel. Any inability to do so may negatively affect our investment returns.

***We may hold the debt securities of leveraged companies that may, due to the significant volatility of such companies, experience bankruptcy or similar financial distress.***

Leveraged companies may experience bankruptcy or similar financial distress. The debt investments of distressed companies may not produce income, may require us to bear certain expenses to protect our investment and may subject us to uncertainty as to when, in what manner (e.g., through liquidation, reorganization or bankruptcy) and for what value such distressed debt will eventually be satisfied. Proceeds received from such proceedings may not be income that satisfies the Qualifying Income Test for RICs. In the event that a plan of reorganization is adopted, we may receive equity securities in exchange of the debt investment that we currently hold, which may require significantly more of our management's time and attention.

If a portfolio company enters a bankruptcy process, we will be subject to a number of significant inherent risks. Many events in a bankruptcy proceeding are the product of contested matters and adversary proceedings and are beyond the control of the creditors. A bankruptcy filing by an issuer may adversely and permanently affect the issuer. If the proceeding is converted to a liquidation, the value of the issuer may not equal the liquidation value that was believed to exist at the time of the investment. The duration of a bankruptcy proceeding is also difficult to predict, and a creditor's return on investment can be adversely affected by delays until the plan of reorganization or liquidation ultimately becomes effective. The administrative costs of a bankruptcy proceeding are frequently high and would be paid out of the debtor's estate prior to any return to creditors. Because the standards for classification of claims under bankruptcy law are vague, our influence with respect to the class of securities or other obligations we own may be lost by increases in the number and amount of claims in the same class or by different classification and treatment. In the early stages of the bankruptcy process, it is often difficult to estimate the extent of, or even to identify, any contingent claims that might be made. In addition, certain claims that have priority by law (for example, claims for taxes) may be substantial.

***Prepayments of our debt investments by our portfolio companies could adversely impact our results of operations and reduce our return on equity.***

We are subject to the risk that the investments we make in our portfolio companies may be repaid prior to maturity. For example, most of our debt investments have historically been repaid prior to maturity by our portfolio companies. At the time of a liquidity event, such as a sale of the business, refinancing or public offering, many of our portfolio companies have availed themselves of the opportunity to repay our debt investments prior to maturity. Our investments generally allow for repayment at any time subject to certain penalties. When this occurs, we generally reinvest these proceeds in temporary investments, pending their future investment in new portfolio companies. These temporary investments have substantially lower yields than the debt being repaid, and we could experience significant delays in reinvesting these amounts. Any future investment in a new portfolio company may also be at lower yields than the debt that was repaid. As a result, our results of operations could be materially adversely affected if one or more of our portfolio companies elects to prepay amounts owed to us. Additionally, prepayments could negatively impact our return on equity, which could result in a decline in the market price of our common stock.

***Our business and growth strategy could be adversely affected if government regulations, priorities and resources impacting the industries in which our portfolio companies operate change.***

Some of our portfolio companies operate in industries that are highly regulated by federal, state and/or local agencies. Changes in existing laws, rules or regulations, or judicial or administrative interpretations thereof, or new laws, rules or regulations could have an adverse impact on the business and industries of our portfolio companies. In addition, changes in government priorities or limitations on government resources could also adversely impact our portfolio companies. We are unable to predict whether any such changes in laws, rules or regulations will occur and, if they do occur, the impact of these changes on our portfolio companies and our investment returns.

***Our portfolio companies operating in the life science industry are subject to extensive government regulation and certain other risks particular to that industry.***

As part of our investment strategy, we have invested, and plan to invest in the future, in companies in the life science industry that are subject to extensive regulation by the Food and Drug Administration and to a lesser extent, other federal and state agencies. If any of these portfolio companies fail to comply with applicable regulations, they could be subject to significant penalties and claims that could materially and adversely affect their operations. Portfolio companies that produce medical devices or drugs are subject to the expense, delay and uncertainty of the regulatory approval process for their products and, even if approved, these products may not be accepted in the marketplace. In addition, new laws, regulations or judicial interpretations of existing laws and regulations might adversely affect a portfolio company in this industry. Portfolio companies in the life science industry may also have a limited number of suppliers of necessary components or a limited number of manufacturers for their products, and therefore face a risk of disruption to their manufacturing process if they are unable to find alternative suppliers when needed. Any of these factors could materially and adversely affect the operations of a portfolio company in this industry and, in turn, impair our ability to timely collect principal and interest payments owed to us.

***Our portfolio companies operating in the drug discovery industry are subject to numerous risks, including competition, extensive government regulation, product liability and commercial difficulties.***

Our portfolio companies in the drug discovery industry are subject to numerous risks. The successful and timely implementation of the business model of drug discovery companies depends on their ability to adapt to changing technologies and introduce new products. As competitors continue to introduce competitive products, the development and acquisition of innovative products and technologies that improve efficacy, safety, patient's and clinician's ease of use and cost-effectiveness are important to the success of such companies. The success of new product offerings will depend on many factors, including the ability to properly anticipate and satisfy customer needs, obtain regulatory approvals on a timely basis, develop and manufacture products in an economic and timely manner, obtain or maintain advantageous positions with respect to intellectual property, and differentiate products from those of competitors. Failure by companies to introduce planned products or other new products or to introduce products on schedule could materially and adversely affect the operations of the companies and, in turn, impair our ability to timely collect principal and interest payments owed to us.

Further, the development of products by drug discovery companies requires significant research and development, clinical trials and regulatory approvals. The results of product development efforts may be affected by a number of factors, including the ability to innovate, develop and manufacture new products, complete clinical trials, obtain regulatory approvals and reimbursement by insurers in the United States (including Medicare and Medicaid) and abroad, or gain and maintain market approval of products. In addition, patents attained by others can preclude or delay the commercialization of a product. There can be no assurance that any products now in development will achieve technological feasibility, obtain regulatory approval, or gain market acceptance. Failure can occur at any point in the development process, including after significant funds have been invested. Products may fail to reach the market or may have only limited commercial success because of efficacy or safety concerns, failure to achieve positive clinical outcomes, inability to obtain necessary regulatory approvals, failure to achieve market adoption, limited scope of approved uses, excessive costs to manufacture, failure to establish or maintain intellectual property rights, infringement by others of a company's intellectual property rights, or infringement by a company of intellectual property rights of others. Any of these factors could materially and adversely affect the operations of the companies and, in turn, impair our ability to timely collect principal and interest payments owed to us.

***Our investments in the clean technology industry are subject to many risks, including volatility, intense competition, unproven technologies, periodic downturns and potential litigation.***

Our investments in clean technology, or cleantech, companies are subject to substantial operational risks, such as underestimated cost projections, unanticipated operation and maintenance expenses, loss of government subsidies, and inability to deliver cost-effective alternative energy solutions compared to traditional energy products. In addition, energy companies employ a variety of means of increasing cash flow, including increasing utilization of existing facilities, expanding operations through new construction or acquisitions, or securing additional long-term contracts. Thus, some energy companies may be subject to construction risk, acquisition risk or other risks arising from their specific business strategies. Furthermore, production levels for solar, wind and other renewable energies may be

dependent upon adequate sunlight, wind, or biogas production, which can vary from market to market and period to period, resulting in volatility in production levels and profitability. In addition, our cleantech companies may have narrow product lines and small market shares, which tend to render them more vulnerable to competitors' actions and market conditions, as well as to general economic downturns. The revenues, income (or losses) and valuations of clean technology companies can and often do fluctuate suddenly and dramatically and the markets in which clean technology companies operate are generally characterized by abrupt business cycles and intense competition. Demand for cleantech and renewable energy is also influenced by the available supply and prices for other energy products, such as coal, oil and natural gas. A decrease in prices in these energy products could reduce demand for alternative energy. Cleantech companies face potential litigation, including significant warranty and product liability claims, as well as class action and government claims. Such litigation could adversely affect the business and results of operations of our cleantech portfolio companies.

***Cleantech companies are subject to extensive government regulation and certain other risks particular to the sectors in which they operate and our business and growth strategy could be adversely affected if government regulations, priorities and resources impacting such sectors change or if our portfolio companies fail to comply with such regulations.***

As part of our investment strategy we invest in portfolio companies in cleantech sectors that may be subject to extensive regulation by foreign, U.S. federal, state and/or local agencies. Changes in existing laws, rules or regulations, or judicial or administrative interpretations thereof, or new laws, rules or regulations could have an adverse impact on the business and industries of our portfolio companies. In addition, changes in government priorities or limitations on government resources could also adversely impact our portfolio companies. We are unable to predict whether any such changes in laws, rules or regulations will occur and, if they do occur, the impact of these changes on our portfolio companies and our investment returns. Furthermore, if any of our portfolio companies fail to comply with applicable regulations, they could be subject to significant penalties and claims that could materially and adversely affect their operations. Our portfolio companies may be subject to the expense, delay and uncertainty of the regulatory approval process for their products and, even if approved, these products may not be accepted in the marketplace.

In addition, there is considerable uncertainty about whether foreign, U.S., state and/or local governmental entities will enact or maintain legislation or regulatory programs that mandate reductions in greenhouse gas emissions or provide incentives for cleantech companies. Without such regulatory policies, investments in cleantech companies may not be economical and financing for cleantech companies may become unavailable, which could materially adversely affect the ability of our portfolio companies to repay the debt they owe to us. Any of these factors could materially and adversely affect the operations and financial condition of a portfolio company and, in turn, the ability of the portfolio company to repay the debt they owe to us.

***If our portfolio companies are unable to commercialize their technologies, products, business concepts or services, the returns on our investments could be adversely affected.***

The value of our investments in our portfolio companies may decline if our portfolio companies are not able to commercialize their technology, products, business concepts or services. Additionally, although some of our portfolio companies may already have a commercially successful product or product line at the time of our investment, technology-related products and services often have a more limited market or life span than products in other industries. Thus, the ultimate success of these companies often depends on their ability to innovate continually in increasingly competitive markets. If they are unable to do so, our investment returns could be adversely affected and their ability to service their debt obligations to us over the life of a loan could be impaired. Our portfolio companies may be unable to acquire or develop successful new technologies and the intellectual property they currently hold may not remain viable. Even if our portfolio companies are able to develop commercially viable products, the market for new products and services is highly competitive and rapidly changing. Neither our portfolio companies nor we have any control over the pace of technology development. Commercial success is difficult to predict, and the marketing efforts of our portfolio companies may not be successful.



***Our portfolio companies may rely upon licenses for all or part of their intellectual property.***

A portfolio company may license all or part of its intellectual property from another unrelated party. While the portfolio company may continue development on that licensed intellectual property, it can be difficult to ascertain who has title to the intellectual property. We may also rely upon the portfolio company's management team's representations as to the nature of the licensing agreement. There are implications in workouts and in bankruptcy where intellectual property is not wholly owned by a portfolio company. Further, the licensor may have an actual or contingent claim on the intellectual property (for instance, a payment due upon change in control) that would supersede other claims in that asset in certain situations.

***If our portfolio companies are unable to protect their intellectual property rights, our business and prospects could be harmed, and if portfolio companies are required to devote significant resources to protecting their intellectual property rights, the value of our investment could be reduced.***

Our future success and competitive position depends in part upon the ability of our portfolio companies to obtain, maintain and protect proprietary technology used in their products and services. The intellectual property held by our portfolio companies often represents a substantial portion of the collateral securing our investments and/or constitutes a significant portion of the portfolio companies' value that may be available in a downside scenario to repay our debt investments. Our portfolio companies rely, in part, on patent, trade secret and trademark law to protect that technology, but competitors may misappropriate their intellectual property, and disputes as to ownership of intellectual property may arise. Portfolio companies may, from time to time, be required to institute litigation to enforce their patents, copyrights or other intellectual property rights, protect their trade secrets, determine the validity and scope of the proprietary rights of others or defend against claims of infringement.

Such litigation could result in substantial costs and diversion of resources. Similarly, if a portfolio company is found to infringe or misappropriate a third party's patent or other proprietary rights, it could be required to pay damages to the third party, alter its products or processes, obtain a license from the third party and/or cease activities utilizing the proprietary rights, including making or selling products utilizing the proprietary rights. Any of the foregoing events could negatively affect both the portfolio company's ability to service our debt investment and the value of any related debt and equity securities that we own, as well as the value of any collateral securing our investment.

***We do not expect to control any of our portfolio companies.***

We do not control, or expect to control in the future, any of our portfolio companies, even though our debt agreements may contain certain restrictive covenants that limit the business and operations of our portfolio companies. We also do not maintain, or intend to maintain in the future, a control position to the extent we own equity interests in any portfolio company. As a result, we are subject to the risk that a portfolio company in which we invest may make business decisions with which we disagree and the management of such company, as representatives of the holders of their common equity, may take risks or otherwise act in ways that do not serve our interests as debt investors. Due to the lack of liquidity of the investments that we typically hold in our portfolio companies, we may not be able to dispose of our investments in the event we disagree with the actions of a portfolio company and we may therefore, suffer a decrease in the value of our investments.

***Our portfolio companies may have foreign subsidiaries.***

Although our debt investments consist of secured loans to portfolio companies with headquarters and primary operations located within the United States, certain debt investments may be secured by the assets of a portfolio company's foreign subsidiary which may involve greater risks. These risks include: (i) less publicly available information; (ii) varying levels of governmental regulation and supervision; and (iii) the difficulty of enforcing legal rights in a foreign jurisdiction and uncertainties as to the status, interpretation and application of laws. Moreover, foreign companies are generally not subject to uniform accounting, auditing and financial reporting standards, practices and requirements comparable to those applicable to United States companies. Debt investments secured by the assets of a portfolio company's foreign subsidiary may be subject to various laws enacted in their home countries for the protection of debtors or creditors, which could adversely affect our ability to recover amounts owed. These insolvency considerations will differ depending on the country in which each foreign subsidiary is located and may differ depending on whether the foreign subsidiary is a non-sovereign or a sovereign entity. The economies of individual non-U.S. countries may also differ from the U.S. economy in such respects as growth of gross domestic product, rate of inflation, volatility of currency exchange rates, depreciation, capital reinvestment, resources self-sufficiency and balance of payments position. Accordingly, debt investments secured by the assets of a portfolio company's foreign subsidiary could face risks which would not pertain to debt investments solely in U.S. portfolio companies.

*We may not realize expected returns on warrants received in connection with our debt investments.*

As discussed above, we generally receive warrants in connection with our debt investments. If we do not receive the returns that are anticipated on the warrants, our investment returns on our portfolio companies, and the value of your investment in us, may be lower than expected.

#### **Risks related to our common stock**

*There is a risk that investors in our equity securities may not receive distributions, that our distributions may not grow over time or that a portion of distributions paid to you may be a return of capital.*

We intend to make distributions on a monthly basis to our stockholders out of assets legally available for distribution. We cannot assure you that we will achieve investment results that will allow us to make a specified level of cash distributions or year-to-year increases in cash distributions. Our ability to pay distributions might be adversely affected by the impact of one or more risk factors described in this report. In addition, due to the asset coverage test applicable to us as a BDC, we may be limited in our ability to make distributions. All distributions will be paid at the discretion of our Board and will depend on our earnings, our financial condition, maintenance of our RIC status, compliance with BDC regulation and such other factors as our Board may deem relevant from time to time. We cannot assure you that we will pay distributions to our stockholders in the future. Further, if we invest a greater amount of assets in equity securities that do not pay current dividends, the amount available for distribution could be reduced.

On an annual basis, we must determine the extent to which any distributions we made were paid out of current or accumulated earnings, recognized capital gains or capital. Distributions that represent a return of capital (which is the return of your original investment in us, after subtracting sales load, fees and expenses directly or indirectly paid by you) rather than a distribution from earnings or profits, reduce your basis in our stock for U.S. federal income tax purposes, which may result in higher tax liability when the shares are sold, even if they have not increased in value or have lost value.

***Our common stock price may be volatile and may decrease substantially.***

The trading price of our common stock may fluctuate substantially and the liquidity of our common stock may be limited, in each case depending on many factors, some of which are beyond our control and may not be directly related to our operating performance. These factors include the following:

- price and volume fluctuations in the overall stock market or in the market for BDCs from time to time;
  - investor demand for our shares of common stock;
- significant volatility in the market price and trading volume of securities of registered closed-end management investment companies, BDCs or other financial services companies;
  - our inability to raise capital, borrow money or deploy or invest our capital;
    - fluctuations in interest rates;

any shortfall in revenue or net income or any increase in losses from levels expected by investors or securities analysts;

- operating performance of companies comparable to us;
- changes in regulatory policies or tax guidelines with respect to RICs or BDCs;
  - losing RIC status;

- actual or anticipated changes in our earnings or fluctuations in our operating results;
- changes in the value of our portfolio of investments;
- general economic conditions, trends and other external factors;
- departures of key personnel; or
- loss of a major source of funding.

***We and our Advisor could be the target of litigation.***

We or our Advisor could become the target of securities class action litigation or other similar claims if our stock price fluctuates significantly or for other reasons. The outcome of any such proceedings could materially adversely affect our business, financial condition, and/or operating results and could continue without resolution for long periods of time. Any litigation or other similar claims could consume substantial amounts of our management's time and attention, and that time and attention and the devotion of associated resources could, at times, be disproportionate to the amounts at stake. Litigation and other claims are subject to inherent uncertainties, and a material adverse impact on our financial statements could occur for the period in which the effect of an unfavorable final outcome in litigation or other similar claims becomes probable and reasonably estimable. In addition, we could incur expenses associated with defending ourselves against litigation and other similar claims, and these expenses could be material to our earnings in future periods.

***Shares of closed-end investment companies, including BDCs, frequently trade at a discount to their NAV, and we cannot assure you that the market price of our common stock will not decline following an offering.***

We cannot predict the price at which our common stock will trade. Shares of closed-end investment companies, including BDCs, frequently trade at a discount to their NAV and our stock may also be discounted in the market. This characteristic of closed-end investment companies is separate and distinct from the risk that our NAV per share may decline. We cannot predict whether shares of our common stock will trade above, at or below our NAV. In addition, if our common stock trades below its NAV, we will generally not be able to issue additional shares of our common stock at its market price without first obtaining the approval of our stockholders and our independent directors.

***We currently invest a portion of our capital in high-quality short-term investments, which generate lower rates of return than those expected from investments made in accordance with our investment objective.***

We currently invest a portion of our capital in cash, cash equivalents, U.S. government securities, money market funds and other high-quality short-term investments. These securities may earn yields substantially lower than the income that we anticipate receiving once these proceeds are fully invested in accordance with our investment objective.

***Investing in shares of our common stock may involve an above average degree of risk.***

The investments we make in accordance with our investment objective may result in a higher amount of risk, volatility or loss of principal than alternative investment options. Our investments in portfolio companies may be highly speculative and aggressive, and therefore, an investment in our common stock may not be suitable for investors with lower risk tolerance.

***Anti-takeover provisions in our charter documents and other agreements and certain provisions of the Delaware General Corporation Law, or DGCL, could deter takeover attempts and have an adverse impact on the price of our common stock.***

The DGCL, our certificate of incorporation and our bylaws contain provisions that may have the effect of discouraging a third party from making an acquisition proposal for us. Among other things, our certificate of incorporation and bylaws:

provide for a classified board of directors, which may delay the ability of our stockholders to change the membership of a majority of our Board;

authorize the issuance of “blank check” preferred stock that could be issued by our Board to thwart a takeover attempt;

- do not provide for cumulative voting;

provide that vacancies on the Board, including newly created directorships, may be filled only by a majority vote of directors then in office;

- limit the calling of special meetings of stockholders;
- provide that our directors may be removed only for cause;

• require supermajority voting to effect certain amendments to our certificate of incorporation and our bylaws; and

require stockholders to provide advance notice of new business proposals and director nominations under specific procedures.

These anti-takeover provisions may inhibit a change in control in circumstances that could give the holders of our common stock the opportunity to realize a premium over the market price of our common stock. It is a default under our Key Facility if (i) a person or group of persons (within the meaning of the Exchange Act) acquires beneficial ownership of 20% or more of our issued and outstanding common stock or (ii) during any twelve-month period, individuals who at the beginning of such period constituted our Board cease for any reason, other than death or disability, to constitute a majority of the directors in office. If either event were to occur, Key could accelerate our repayment obligations under, and/or terminate, our Key Facility.

***If we elect to issue preferred stock, holders of any such preferred stock will have the right to elect members of our Board and have class voting rights on certain matters.***

The 1940 Act requires that holders of shares of preferred stock must be entitled as a class to elect two directors at all times and to elect a majority of the directors if distributions on such preferred stock are in arrears by two years or more, until such arrearage is eliminated. In addition, certain matters under the 1940 Act require the separate vote of the holders of any issued and outstanding preferred stock, including changes in fundamental investment restrictions and conversion to open-end status and, accordingly, preferred stockholders could veto any such changes. Restrictions imposed on the declarations and payment of distributions to the holders of our common stock and preferred stock, both by the 1940 Act and by requirements imposed by rating agencies, might impair our ability to maintain our qualification as a RIC for U.S. federal income tax purposes.

***Your interest in us may be diluted if you do not fully exercise your subscription rights in any rights offering. In addition, if the subscription price is less than our NAV per share, then you will experience an immediate dilution of the aggregate NAV of your shares.***

In the event we issue subscription rights, stockholders who do not fully exercise their rights should expect that they will, at the completion of a rights offering, own a smaller proportional interest in us than would otherwise be the case if they fully exercised their rights. Such dilution is not currently determinable because it is not known what proportion of the shares will be purchased as a result of such rights offering. Any such dilution will disproportionately affect nonexercising stockholders. If the subscription price per share is substantially less than the current NAV per share, this dilution could be substantial.

In addition, if the subscription price is less than our NAV per share, our stockholders would experience an immediate dilution of the aggregate NAV of their shares as a result of such rights offering. The amount of any decrease in NAV is not predictable because it is not known at this time what the subscription price and NAV per share will be on the expiration date of the rights offering or what proportion of the shares will be purchased as a result of such rights offering. Such dilution could be substantial.

***Investors in offerings of our common stock may incur immediate dilution upon the closing of an offering.***

If the public offering price for any offering of shares of our common stock is higher than the book value per share of our outstanding common stock, investors purchasing shares of common stock in any offering will pay a price per share that exceeds the tangible book value per share after such offering.



***If we sell common stock at a discount to our NAV per share, stockholders who do not participate in such sale will experience immediate dilution in an amount that may be material.***

The issuance or sale by us of shares of our common stock at a discount to NAV poses a risk of dilution to our current stockholders. In particular, stockholders who do not purchase additional shares at or below the discounted price in proportion to their current ownership will experience an immediate decrease in NAV per share (as well as in the aggregate NAV of their shares if they do not participate at all). These stockholders will also experience a disproportionately greater decrease in their participation in our earnings and assets and their voting power than the increase we experience in our assets, potential earning power and voting interests from such issuance or sale. In addition, such sales may adversely affect the price at which our common stock trades.

***Stockholders will experience dilution in their ownership percentage if they do not participate in our dividend reinvestment plan.***

All distributions payable to stockholders that are participants in our dividend reinvestment plan, or DRIP, are automatically reinvested in shares of our common stock. As a result, stockholders that do not participate in the DRIP will experience dilution in their ownership interest over time.

***The trading market or market value of our publicly issued debt securities that we may issue may fluctuate.***

Upon issuance, any publicly issued debt securities that we may issue will not have an established trading market. We cannot assure you that a trading market for our publicly issued debt securities will ever develop or, if developed, will be maintained. In addition to our creditworthiness, many factors may materially adversely affect the trading market for, and market value of, our publicly issued debt securities. These factors include:

- the time remaining to the maturity of these debt securities;

- the outstanding principal amount of debt securities with terms identical to these debt securities;
  - the supply of debt securities trading in the secondary market, if any;
  - the redemption or repayment features, if any, of these debt securities;
  - the level, direction and volatility of market interest rates generally; and
- market rate of interest higher or lower than the rate borne by the debt securities.

You should also be aware that there may be a limited number of buyers when you decide to sell your debt securities. This too may materially adversely affect the market value of the debt securities or the trading market for the debt securities.

***Terms relating to redemption may materially adversely affect your return on the debt securities that we may issue.***

If we issue debt securities that are redeemable at our option, we may choose to redeem the debt securities at times when prevailing interest rates are lower than the interest rate paid on the debt securities. In addition, if such debt securities are subject to mandatory redemption, we may be required to redeem the debt securities at times when prevailing interest rates are lower than the interest rate paid on the debt securities. In this circumstance, you may not be able to reinvest the redemption proceeds in a comparable security at an effective interest rate as high as your debt securities being redeemed.

***Credit ratings provided by third party credit rating agencies may not reflect all risks of an investment in debt securities that we may issue.***

Credit ratings provided by third party credit rating agencies are an assessment by third parties of our ability to pay our obligations. Consequently, real or anticipated changes in our credit ratings will generally affect the market value of debt securities that we may issue. Credit ratings provided by third party credit rating agencies, however, may not reflect the potential impact of risks related to market conditions generally or other factors discussed above on the market value of or trading market for any publicly issued debt securities that we may issue.

*Sales in the public market of substantial amounts of our common stock may have an adverse effect on the market price of our common stock, and the registration of a substantial amount of insider shares, whether or not actually sold, may have a negative impact on the market price of our common stock.*

Sales of substantial amounts of our common stock, or the availability of such common stock for sale, whether or not actually sold, could adversely affect the prevailing market price of our common stock. If this occurs and continues, it could impair our ability to raise additional capital through the sale of equity securities should we desire to do so.

**Item 1B. *Unresolved Staff Comments***

None

**Item 2. *Properties***

We do not own any real estate or other physical properties materially important to our operation. Our headquarters and our Advisor's headquarters are currently located at 312 Farmington Avenue, Farmington, Connecticut 06032. We believe that our office facilities are suitable and adequate to our business.

**Item 3. *Legal Proceedings***

Neither we nor our Advisor is currently subject to any material legal proceedings.

**Item 4. *Mine Safety Disclosures***

Not applicable

**PART II****Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities****Price range of common stock**

Our common stock is traded on NASDAQ, under the symbol "HRZN." The following table sets forth, for each fiscal quarter since January 1, 2014, the range of high and low closing sales price of our common stock, the closing sales price as a percentage of our NAV and the distributions declared per share by us for each quarter.

Period	NAV <sup>(1)</sup>	Closing Sales Price		Premium/ Discount of	High Sales Price to NAV <sup>(2)</sup>	Premium/ Discount of	Distributions Declared  Per Share <sup>(3)</sup>
		High	Low	Low Sales Price to NAV <sup>(2)</sup>			
<b><i>Year ended December 31, 2015</i></b>							
Fourth Quarter	\$ 13.85	\$ 12.41	\$ 9.32	(10	)%	(33	)% \$ 0.345 <sup>(4)</sup>
Third Quarter	\$ 13.94	\$ 12.67	\$ 9.05	(9	)%	(35	)% \$ 0.345
Second Quarter	\$ 13.99	\$ 14.36	\$ 12.56	3	%	(10	)% \$ 0.345
First Quarter	\$ 14.19	\$ 14.39	\$ 13.61	1	%	(4	)% \$ 0.345
<b><i>Year ended December 31, 2014</i></b>							
Fourth Quarter	\$ 14.36	\$ 14.27	\$ 13.45	(1	)%	(6	)% \$ 0.345
Third Quarter	\$ 14.38	\$ 14.72	\$ 12.90	2	%	(10	)% \$ 0.345
Second Quarter	\$ 14.23	\$ 14.89	\$ 12.59	5	%	(12	)% \$ 0.345
First Quarter	\$ 14.32	\$ 14.61	\$ 12.43	2	%	(13	)% \$ 0.345

NAV per share determined as of the last day in the relevant quarter and therefore may not reflect the NAV per (1) share on the date of the high and low sales prices. The NAVs shown are based on outstanding shares at the end of each period.

(2) Calculated as of the respective high or low closing sales price divided by the quarter end NAV.

(3) We have adopted an "opt out" DRIP for our common stockholders. As a result, if we declare a distribution, then stockholders' cash distributions are automatically reinvested in additional shares of our common stock, unless they

specifically opt out of the DRIP so as to receive cash distributions.

(4) \$0.115 of which is payable on March 15, 2016.

The last reported price for our common stock on March 1, 2016 was \$11.16 per share. As of March 1, 2016 we had 13 stockholders of record, which did not include stockholders for whom shares are held in nominee or "street" name.

Shares of BDCs may trade at a market price that is less than the NAV that is attributable to those shares. The possibility that our shares of common stock will trade at a discount from NAV or at a premium that is unsustainable over the long term is separate and distinct from the risk that our NAV will decrease. It is not possible to predict whether our shares will trade at, above or below NAV in the future.

#### **Sales of unregistered securities**

We did not engage in any sales of unregistered equity securities during the years ended December 31, 2015, 2014 and 2013.

## Issuer Purchases of Equity Securities

The following table provides information regarding our purchases of our common stock for each month in the three month period ended December 31, 2015:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs <sup>(1)</sup>	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs
(In thousands, except share and per share data)				
October 1, 2015 through October 31, 2015	—	\$ —	—	\$ 5,000
November 1, 2015 through November 30, 2015	22,982	11.23	22,982	\$ 4,742
December 1, 2015 through December 31, 2015	90,400	11.60	90,400	\$ 3,693
Total	113,382	\$ 11.53	113,382	

On September 28, 2015, we announced a share repurchase plan which allows us to repurchase up to \$5.0 million of (1) our outstanding common stock. Unless extended by our board of directors, the repurchase program will expire on the earlier of September 30, 2016 and the repurchase of \$5.0 million of common stock.

## Distributions

We intend to continue making monthly distributions to our stockholders. The timing and amount of our monthly distributions, if any, is determined by our Board. Any distributions to our stockholders are declared out of assets legally available for distribution. We monitor available net investment income to determine if a tax return of capital may occur for the fiscal year. To the extent our taxable earnings fall below the total amount of our distributions for any given fiscal year, a portion of those distributions may be deemed to be a return of capital to our common stockholders for U.S. federal income tax purpose. Thus, the source of distribution to our stockholders may be the original capital invested by the stockholder rather than our income or gains. Stockholders should read any written disclosure accompanying a distribution payment carefully and should not assume that the source of any distribution is our ordinary income or gains.

In order to qualify as a RIC, we must meet certain source-of-income, asset diversification and annual distribution requirements. Generally, in order to qualify as a RIC, we must derive at least 90% of our gross income during each tax year from dividends, interest, payments with respect to certain securities, loans, gains from the sale or other disposition of stock, securities or foreign currencies, or other income derived with respect to its business of investing

in stock or other securities. We must also meet certain asset diversification requirements at the end of each quarter of each tax year. Failure to meet these diversification requirements on the last day of a quarter may result in us having to dispose of certain investments quickly in order to prevent the loss of RIC status. Any such dispositions could be made at disadvantageous prices or times, and may cause us to incur substantial losses.

In addition, in order to be eligible for the special tax treatment accorded to RICs and to avoid corporate level tax on the income and gains we distribute to our stockholders, each tax year we are required under the Code to distribute as dividends of an amount generally at least 90% of our investment company taxable income to our stockholders. We refer to such amount as the Annual Distribution Requirement in this annual report on Form 10-K. Additionally, we must distribute, in respect of each calendar year, dividends of an amount generally at least equal to the sum of 98% of our calendar year net ordinary income (taking into account certain deferrals and elections); 98.2% of our capital gain net income (adjusted for certain ordinary losses) for the one year period ending on October 31 of such calendar year; and any net ordinary income and capital gain net income for preceding years that were not distributed during such years and on which we previously paid no U.S. federal income tax to avoid a U.S. federal excise tax. If we fail to qualify as a RIC for any reason and become subject to corporate tax, the resulting corporate taxes could substantially reduce our net assets, the amount of income available for distribution and the amount of our distributions. Such a failure would have a material adverse effect on us and our stockholders. In addition, we could be required to recognize unrealized gains, pay substantial taxes and interest and make substantial distributions in order to re-qualify as a RIC. We cannot assure stockholders that they will receive any distributions.

Depending on the level of taxable income earned in a tax year, we may choose to carry forward taxable income in excess of current year distributions into the next tax year and pay a 4% excise tax on such undistributed income. Distributions of any such carryover taxable income must be made through a distribution declared as of the earlier of the filing date of the corporate income tax return related to the tax year in which such taxable income was generated or the 15<sup>th</sup> day of the ninth month following the end of such tax year, in order to count towards the satisfaction of the Annual Distribution Requirement for the tax year in which such taxable income was generated. We can offer no assurance that we will achieve results that will permit the payment of any cash distributions and, if we issue senior securities, we may be prohibited from making distributions if doing so causes us to fail to maintain the asset coverage stipulated by the 1940 Act or if distributions are limited by the terms of any of our borrowings. See “Item 1. Business — Regulation — Taxation as a RIC.”

We have adopted an “opt out” DRIP for our common stockholders. As a result, if we make a distribution, then stockholders’ cash distributions are automatically reinvested in additional shares of our common stock, unless they specifically opt out of the DRIP. If a stockholder opts out, that stockholder receives cash distributions. Although distributions paid in the form of additional shares of common stock are generally subject to U.S. federal, state and local taxes, stockholders participating in our DRIP do not receive any corresponding cash distributions with which to pay any such applicable taxes. We may use newly issued shares to implement the DRIP, or we may purchase shares in the open market in connection with our obligations under the DRIP.

The following table reflects the monthly cash distributions, including dividends and returns of capital per share that our Board has declared since January 1, 2014, including shares issued under our DRIP, on our common stock:

Record Dates	Payment Date	Distributions Declared
Year ended December 31, 2015		
February 22, 2016	March 15, 2016	\$ 0.115
January 21, 2016	February 17, 2016	0.115
December 18, 2015	January 15, 2016	0.115
November 19, 2015	December 15, 2015	0.115
October 20, 2015	November 16, 2015	0.115
September 18, 2015	October 15, 2015	0.115
August 19, 2015	September 15, 2015	0.115
July 20, 2014	August 14, 2015	0.115
June 18, 2015	July 15, 2015	0.115
May 20, 2015	June 15, 2015	0.115
April 20, 2015	May 15, 2015	0.115
March 20, 2015	April 15, 2015	0.115
Total		\$ 1.380



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Year ended December 31, 2014

February 19, 2015	March 16, 2015	\$ 0.115
January 20, 2015	February 13, 2015	0.115
December 17, 2014	January 15, 2015	0.115
November 19, 2014	December 15, 2014	0.115
October 20, 2014	November 17, 2014	0.115
September 18, 2014	October 15, 2014	0.115
August 19, 2014	September 15, 2014	0.115
July 21, 2014	August 15, 2014	0.115
June 18, 2014	July 17, 2014	0.115
May 20, 2014	June 16, 2014	0.115
April 17, 2014	May 15, 2014	0.115
March 19, 2014	April 15, 2014	0.115
Total		\$ 1.380

On March 3, 2016, our Board declared distributions as set forth in the following table:

<b>Ex-Dividend Date</b>	<b>Record Date</b>	<b>Payment Date</b>	<b>Distributions Declared</b>
May 17, 2016	May 19, 2016	June 15, 2016	\$0.115
April 18, 2016	April 20, 2016	May 16, 2016	\$0.115
March 16, 2016	March 18, 2016	April 15, 2016	\$0.115

*Stock performance graph*

The following graph compares the return on our common stock with that of the Standard & Poor's 500 Stock Index, the NASDAQ Financial-100 Index and the S&P BDC Index, for the period from October 29, 2010 (the date that our common stock was first listed on NASDAQ) through December 31, 2015. The graph assumes that, on October 29, 2010, a person invested \$100 in each of our common stock, the S&P 500 Index, the NASDAQ Financial-100 Index and the S&P BDC Index. The graph measures total stockholder return, which takes into account both changes in stock price and distributions. It assumes that distributions paid are invested in like securities. The graph and other information furnished under this Part II Item 5 of Form 10-K shall not be deemed to be "soliciting material" or to be "filed" with the SEC or subject to Regulation 14A or 14C, or to the liabilities of Section 18 of the Exchange Act. The stock price performance included in this graph is not necessarily indicative of future stock price performance.

**Item 6. Selected Financial Data**

The following selected consolidated financial data of the Company as of December 31, 2015, 2014, 2013, 2012, and 2011, and for the years ended December 31, 2015, 2014, 2013, 2012 and 2011 are derived from the consolidated financial statements that have been audited by RSM US LLP, an independent registered public accounting firm. These selected financial data should be read in conjunction with our financial statements and related notes thereto and “Management’s Discussion and Analysis of Financial Condition and Results of Operations.”

(In thousands, except per share data)	As of and for the years ended December 31,					
	2015	2014	2013	2012	2011	
<b>Statement of Operations Data:</b>						
Total investment income	\$31,110	\$31,254	\$33,643	\$26,664	\$24,054	
Base management fee	4,747	4,648	5,353	4,208	4,192	
Performance based incentive fee	3,501	2,112	3,318	2,847	3,013	
All other expenses	9,212	13,962	11,605	7,382	6,127	
Base management and performance based incentive fees waived	(346 )	(345 )	(144 )	—	—	
Net investment income before excise tax	13,996	10,877	13,511	12,227	10,722	
Provision for excise tax	—	160	240	231	211	
Net investment income	13,996	10,717	13,271	11,996	10,511	
Net realized (loss) gain on investments	(1,650 )	(3,576 )	(7,509 )	108	6,316	
Provision for excise tax	—	—	—	—	129	
Net unrealized (depreciation) appreciation on investments	(490 )	8,289	(2,254 )	(8,113 )	(5,702 )	
Net increase in net assets resulting from operations	\$11,856	\$15,430	\$3,508	\$3,991	\$10,996	
<b>Per Share Data:</b>						
Net asset value	\$13.85	\$14.36	\$14.14	\$15.15	\$17.01	
Net investment income	1.25	1.11	1.38	1.41	1.38	
Net realized (loss) gain on investments	(0.15 )	(0.37 )	(0.78 )	0.01	0.81	
Net change in unrealized (depreciation) appreciation on investments	(0.04 )	0.86	(0.23 )	(0.95 )	(0.75 )	
Net increase in net assets resulting from operations	1.06	1.60	0.37	0.47	1.44	
Per share distributions declared	1.38	1.38	1.38	2.15	1.18	
Dollar amount of distributions declared	\$15,793	\$13,282	\$13,236	\$18,777	\$8,983	
<b>Statement of Assets and Liabilities Data at Period End:</b>						
Investments, at fair value	\$250,267	\$205,101	\$221,284	\$228,613	\$178,013	
Other assets	31,221	20,095	42,453	11,045	19,798	
Total assets	281,488	225,196	263,737	239,658	197,811	
Borrowings	115,546	81,753	122,343	89,020	64,571	
Total liabilities	121,737	86,948	127,902	94,686	67,927	
Total net assets	\$159,751	\$138,248	\$135,835	\$144,972	\$129,884	
Other data:	14.2	% 15.3	% 14.4	% 14.2	% 14.6	%

Weighted annualized yield on income producing  
investments at fair value

Number of portfolio companies at period end:

Debt investments	52	50	49	45	38
Warrants investments	83	75	73	62	47
Equity investments	6	4	4	2	3

## Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Operations*

*The information contained in this section should be read in conjunction with our consolidated financial statements and related notes thereto appearing elsewhere in this annual report on Form 10-K.*

### **Forward-looking statements**

This annual report on Form 10-K, including the Management's Discussion and Analysis of Financial Condition and Results of Operations, contains statements that constitute forward-looking statements, which relate to future events or our future performance or financial condition. These forward-looking statements are not historical facts, but rather are based on current expectations, estimates and projections about our industry, our beliefs and our assumptions. The forward-looking statements contained in this annual report on Form 10-K involve risks and uncertainties, including statements as to:

- our future operating results, including the performance of our existing debt investments and warrants;
  - the introduction, withdrawal, success and timing of business initiatives and strategies;
- changes in political, economic or industry conditions, the interest rate environment or financial and capital markets, which could result in changes in the value of our assets;
  - the relative and absolute investment performance and operations of our Advisor;
    - the impact of increased competition;
  - the impact of investments we intend to make and future acquisitions and divestitures;
    - the unfavorable resolution of legal proceedings;
  - our business prospects and the prospects of our portfolio companies;
- the impact, extent and timing of technological changes and the adequacy of intellectual property protection;
  - our regulatory structure and tax status;
  - our ability to qualify and maintain qualification as a RIC and as a BDC;
  - the adequacy of our cash resources and working capital;
  - the timing of cash flows, if any, from the operations of our portfolio companies;
- the impact of interest rate volatility on our results, particularly if we use leverage as part of our investment strategy;
  - the ability of our portfolio companies to achieve their objective;
- the impact of legislative and regulatory actions and reforms and regulatory supervisory or enforcement actions of government agencies relating to us or our Advisor;
  - our contractual arrangements and relationships with third parties;
  - our ability to access capital and any future financings by us;
  - the ability of our Advisor to attract and retain highly talented professionals; and
  - the impact of changes to tax legislation and, generally, our tax position.

We use words such as “anticipates,” “believes,” “expects,” “intends,” “seeks” and similar expressions to identify forward-looking statements. Undue influence should not be placed on the forward looking statements as our actual results could differ

materially from those projected in the forward-looking statements for any reason, including the factors in “Item 1A – Risk Factors” and elsewhere in our annual report on Form 10-K.

We have based the forward-looking statements included in this report on information available to us on the date of this report, and we assume no obligation to update any such forward-looking statements. Although we undertake no obligation to revise or update any forward-looking statements in this annual report on Form 10-K, whether as a result of new information, future events or otherwise, you are advised to consult any additional disclosures that we may make directly to you or through reports that we in the future may file with the SEC, including periodic reports on Form 10-Q and current reports on Form 8-K.

You should understand that under Sections 27A(b)(2)(B) and (D) of the Securities Act and Sections 21E(b)(2)(B) and (D) of the Exchange Act, the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995 do not apply to statements made in connection with this annual report on Form 10-K or any periodic reports we file under the Exchange Act.

## **Overview**

We are a specialty finance company that lends to and invests in development-stage companies in our Target Industries. Our investment objective is to generate current income from the debt investments we make and capital appreciation from the warrants we receive when making such debt investments. We are focused on making Venture Loans to venture capital backed companies in our Target Industries, which we refer to as “Venture Lending.” We also selectively lend to publicly traded companies in our Target Industries. Venture Lending is typically characterized by (1) the making of a secured debt investment after a venture capital or equity investment in the portfolio company has been made, which investment provides a source of cash to fund the portfolio company’s debt service obligations under the Venture Loan, (2) the senior priority of the Venture Loan which requires repayment of the Venture Loan prior to the equity investors realizing a return on their capital, (3) the relatively rapid amortization of the Venture Loan and (4) the lender’s receipt of warrants or other success fees with the making of the Venture Loan.

We are an externally managed, closed-end, non-diversified management investment company that has elected to be regulated as a BDC under the 1940 Act. In addition, for U.S. federal income tax purposes, we have elected to be treated as a RIC under Subchapter M of the Code. As a BDC, we are required to comply with regulatory requirements, including limitations on our use of debt. We are permitted to, and expect to, finance our investments through borrowings. However, as a BDC, we are only generally allowed to borrow amounts such that our asset coverage, as defined in the 1940 Act, equals at least 200% after such borrowing. The amount of leverage that we employ depends on our assessment of market conditions and other factors at the time of any proposed borrowing. As a RIC, we generally do not have to pay corporate-level federal income taxes on our investment company taxable income and net capital gain that we distribute to our stockholders as long as we meet certain source-of-income, distribution, asset diversification and other requirements.

Compass Horizon, our predecessor company, commenced operations in March 2008. We were formed in March 2010 for the purpose of acquiring Compass Horizon and continuing its business as a public entity.

Our investment activities, and our day-to-day operations, are managed by our Advisor and supervised by our Board, of which a majority of the members are independent of us. Under the Investment Management Agreement, we have agreed to pay our Advisor a base management fee and an incentive fee for its advisory services to us. We have also entered into the Administration Agreement with our Advisor under which we have agreed to reimburse our Advisor for our allocable portion of overhead and other expenses incurred by our Advisor in performing its obligations under the Administration Agreement.

### Portfolio composition and investment activity

The following table shows our portfolio by type of investment as of December 31, 2015 and 2014:

	December 31, 2015			December 31, 2014		
	<b>Number of Fair Value Investments</b>	<b>Percentage of Total Portfolio</b>	<b>(Dollars in thousands)</b>	<b>Number of Fair Value Investments</b>	<b>Percentage of Total Portfolio</b>	<b>(Dollars in thousands)</b>
Term loans	52	\$242,167	96.8 %	49	\$189,127	92.2 %
Revolving loans	—	—	—	1	10,053	4.9
Total loans	52	242,167	96.8	50	199,180	97.1
Warrants	83	6,645	2.6	75	4,603	2.2

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Other investments	1	300	0.1	1	300	0.2	
Equity	6	1,155	0.5	4	1,018	0.5	
Total		\$250,267	100.0%		\$205,101	100.0	%

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The following table shows total portfolio investment activity as of and for the years ended December 31, 2015 and 2014:

	December 31,	
	2015	2014
	(In thousands)	
Beginning portfolio	\$205,101	\$221,284
New debt investments	123,281	95,323
Principal payments received on investments	(27,016 )	(42,830 )
Early pay-offs	(47,624 )	(66,675 )
Accretion of debt investment fees	1,350	2,339
New debt investment fees	(1,147 )	(1,392 )
New equity	101	12
Sale of investments	(1,669 )	(7,673 )
Net realized loss on investments	(1,620 )	(3,576 )
Net (depreciation) appreciation on investments	(490 )	8,289
Ending portfolio	\$250,267	\$205,101

We receive payments on our debt investments based on scheduled amortization of the outstanding balances. In addition, we receive repayments of some of our debt investments prior to their scheduled maturity date. The frequency or volume of these repayments may fluctuate significantly from period to period.

The following table shows our debt investments by industry sector as of December 31, 2015 and 2014:

	December 31, 2015		December 31, 2014		
	Debt	Percentage	Debt	Percentage	
	Investmentsof	Total	Investmentsof Total	Total	
	at Fair	Portfolio	at Fair	Portfolio	
	Value	(Dollars in	Value	Portfolio	
		thousands)			
Life Science					
Biotechnology	\$ 36,005	14.9 %	\$ 21,253	10.7 %	
Medical Device	22,472	9.2	22,225	11.2	
Technology					
Communications	19,511	8.1	17,732	8.9	
Consumer-Related	18,268	7.5	6,337	3.2	
Materials	9,825	4.1	—	—	
Networking	693	0.3	981	0.5	

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Power Management	2,456	1.0	—	—	
Semiconductors	18,237	7.5	30,355	15.2	
Software	59,664	24.6	53,583	26.9	
Cleantech					
Alternative Energy	2,849	1.2	8,009	4.0	
Consumer-Related	—	—	396	0.2	
Energy Efficiency	3,227	1.3	4,414	2.2	
Waste Recycling	5,936	2.5	—	—	
Healthcare Information and Services					
Diagnostics	7,247	3.0	17,637	8.8	
Other	8,236	3.4	6,946	3.5	
Software	27,541	11.4	9,312	4.7	
Total	\$ 242,167	100.0 %	\$ 199,180	100.0	%

The largest debt investments in our portfolio may vary from year to year as new debt investments are originated and existing debt investments are repaid. Our five largest debt investments represented 21% and 24% of total debt investments outstanding as of December 31, 2015 and 2014, respectively. No single debt investment represented more than 10% of our total debt investments as of December 31, 2015 or 2014.

### Debt investment asset quality

We use an internal credit rating system which rates each debt investment on a scale of 4 to 1, with 4 being the highest credit quality rating and 3 being the rating for a standard level of risk. A rating of 2 represents an increased level of risk and, while no loss is currently anticipated for a 2-rated debt investment, there is potential for future loss of principal. A rating of 1 represents a deteriorating credit quality and a high degree of risk of loss of principal. Our internal credit rating system is not a national credit rating system. See “Item 1 – Business” for a more detailed description of the internal credit rating system. As of December 31, 2015 and 2014, our debt investments had a weighted average credit rating of 3.0 and 3.1, respectively. The following table shows the classification of our debt investment portfolio by credit rating as of December 31, 2015 and December 31, 2014:

Credit Rating	December 31, 2015			December 31, 2014		
	Number of Debt Investments	Debt Investments Value	Percentage of Debt Investments (Dollars in thousands)	Number of Debt Investments	Debt Investments Value	Percentage of Debt Investments
4	7	\$ 23,603	9.8 %	9	\$ 44,082	22.1 %
3	37	199,185	82.2	36	138,109	69.4
2	7	18,879	7.8	3	11,746	5.9
1	1	500	0.2	2	5,243	2.6
Total	52	\$ 242,167	100.0 %	50	\$ 199,180	100.0 %

As of December 31, 2015, there was one debt investment with an internal credit rating of 1, with a cost of \$2.7 million and a fair value of \$0.5 million. As of December 31, 2014, there were two debt investments with an internal credit rating of 1, with an aggregate cost of \$5.4 million and an aggregate fair value of \$5.2 million.

### Consolidated results of operations

As a BDC and a RIC, we are subject to certain constraints on our operations, including limitations imposed by the 1940 Act and the Code. The consolidated results of operations described below may not be indicative of the results we report in future periods.

The following table shows consolidated results of operations for the years ended December 31, 2015, 2014 and 2013:

	2015	2014	2013
	(In thousands)		
Total investment income	\$31,110	\$31,254	\$33,643
Total net expenses	17,114	20,377	20,132
Net investment income before excise tax	13,996	10,877	13,511
Provision for excise tax	—	160	240
Net investment income	13,996	10,717	13,271
Net realized loss on investments	(1,650 )	(3,576 )	(7,509 )
Net unrealized (depreciation) appreciation on investments	(490 )	8,289	(2,254 )
Net increase in net assets resulting from operations	\$11,856	\$15,430	\$3,508
Average debt investments, at fair value	\$219,848	\$204,862	\$233,045
Average borrowings outstanding	\$87,976	\$102,754	\$115,562

Net increase in net assets resulting from operations can vary substantially from period to period for various reasons, including the recognition of realized gains and losses and unrealized appreciation and depreciation on investments. As a result, annual comparisons of net increase in net assets resulting from operations may not be meaningful.

### ***Investment income***

Total investment income remained flat at \$31.1 million for the year ended December 31, 2015 as compared to the year ended December 31, 2014. For the year ended December 31, 2015, total investment income consisted primarily of \$28.7 million in interest income from investments, which included \$4.5 million in income from the accretion of origination fees and ETPs, and \$2.5 million in income from fees. Interest income on investments remained flat at \$28.7 million for the year ended December 31, 2015 as compared to the year ended December 31, 2014, as the increase in the average size of our investment portfolio of \$15.0 million, or 7.3%, was offset by lower acceleration of fees and ETPs from prepayments. Other income, which includes prepayment fee income and fee income on debt investments, decreased by \$0.2 million, or 6.0%, primarily due to a lower aggregate amount of principal prepayments for the year ended December 31, 2015.

Total investment income decreased by \$2.4 million, or 7.1%, to \$31.2 million for the year ended December 31, 2014 as compared to the year ended December 31, 2013. For the year ended December 31, 2014, total investment income consisted primarily of \$28.6 million in interest income from investments, which included \$6.0 million in income from the accretion of origination fees and ETPs, and \$2.6 million of fee income. Interest income on investments decreased by \$3.3 million, or 10.2%, for the year ended December 31, 2014 as compared to the year ended December 31, 2013. Interest income on investments decreased primarily due to a decrease of \$28.2 million, or 12.1%, in the average size of our investment portfolio. Other income, which includes prepayment fee income and fee income on debt investments, increased by \$0.9 million, or 50.5% primarily due to a larger aggregate amount of principal prepayments for the year ended December 31, 2014.

For the years ended December 31, 2015, 2014 and 2013, our dollar-weighted annualized yield on average debt investments was 14.2%, 15.3% and 14.4%, respectively. We calculate the yield on dollar-weighted average debt investments for any period measured as (1) total investment income during the period divided by (2) the average of the fair value of debt investments outstanding on (a) the last day of the calendar month immediately preceding the first day of the period and (b) the last day of each calendar month during the period. The dollar-weighted annualized yield represents the portfolio yield and will be higher than what investors will realize because it does not reflect our expenses or any sales load paid by investors.

Investment income, consisting of interest income and fees on debt investments, can fluctuate significantly upon repayment of large debt investments. Interest income from the five largest debt investments in the aggregate accounted for 14%, 20% and 23% of investment income for the years ended December 31, 2015, 2014 and 2013, respectively.

### ***Expenses***

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Total net expenses decreased by \$3.3 million, or 16.0%, to \$17.1 million for the year ended December 31, 2015 as compared to the year ended December 31, 2014. Total net expenses increased by \$0.2 million, or 1.2%, to \$20.4 million for the year ended December 31, 2014 as compared to the year ended December 31, 2013. Total expenses for each period consisted principally of interest expense, base management fee, incentive and administrative fees, professional fees and general and administrative expenses.

Interest expense decreased by \$3.0 million, or 33.9%, to \$5.8 million for the year ended December 31, 2015 as compar