

SPARTON CORP
Form PRER14A
September 16, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
SCHEDULE 14A
(RULE 14a-101)
INFORMATION REQUIRED IN PROXY STATEMENT

SCHEDULE 14A INFORMATION

PROXY STATEMENT PURSUANT TO SECTION 14(a) OF THE SECURITIES EXCHANGE ACT OF
1934 (AMENDMENT NO. __)

Filed by the registrant

Filed by a party other than the registrant

Check the appropriate box:

Preliminary proxy statement Confidential, for use of the Commission

only (as permitted by Rule 14a-6 (e) (2)).

Definitive proxy statement

Definitive additional materials

Soliciting material pursuant to Rule 14a-12

SPARTON CORPORATION

(Name of Registrant as Specified in Its Charter)

(Name of Person(s) Filing Proxy Statement if Other Than the Registrant)

Payment of filing fee (check the appropriate box):

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- N/A
7. (c) Filing Party:
- N/A
8. (d) Date Filed:
- N/A

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NOTICE OF ANNUAL MEETING OF SHAREHOLDERS

To Our Shareholders:

Notice is hereby given that the Annual Meeting of Shareholders of Sparton Corporation will be held at 425 North Martingale Road, Schaumburg, Illinois 60173-2213, at the 425 Executive Conference Center on October 22, 2014, at 10:00 a.m., local time, for the following purposes:

- (1) To elect six directors each for a term of one year as set forth in the Proxy Statement.
- (2) To ratify the appointment of independent registered public accountants by an advisory vote.
- (3) To approve the Named Executive Officer compensation by an advisory vote.
- (4) To approve an amendment to the Company's Amended and Restated Code of Regulations to provide that the state and federal courts located within the State of Ohio will be the exclusive forum for certain legal actions.
- (5) To re-approve the material terms of the performance goals specified in the Sparton Corporation 2010 Long-Term Stock Incentive Plan.
- (6) To transact such other business as may properly come before the meeting or at any adjournments thereof.

Only holders of common stock of record at the close of business on September 12, 2014 are entitled to notice of and to vote at the meeting.

By Order of the Board of Directors

/s/ Cary B. Wood

CARY B. WOOD
President and Chief Executive Officer
Schaumburg, Illinois

October 3, 2014

Scan this QR code to
view digital versions
of our Proxy Statement
and 2014 Annual Report

IMPORTANT

ALL SHAREHOLDERS ARE CORDIALLY INVITED TO ATTEND THE MEETING. WHETHER OR NOT YOU PLAN TO ATTEND IN PERSON, YOU ARE URGED TO SIGN AND DATE THE ENCLOSED PROXY AND RETURN IT PROMPTLY IN THE ENVELOPE PROVIDED, OR USE OUR INTERNET VOTING SYSTEM AS PROMPTLY AS POSSIBLE. THIS WILL ASSURE YOUR

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REPRESENTATION AND A QUORUM FOR THE TRANSACTION OF BUSINESS AT THE MEETING. IF YOU ATTEND THE MEETING IN PERSON, THE PROXY WILL NOT BE USED IF YOU SO REQUEST BY REVOKING IT AS DESCRIBED IN THE PROXY STATEMENT.

You may obtain directions to the Annual Meeting by sending a written request to Sparton Corporation, Attention: Corporate Secretary, 425 N. Martingale Road, Suite 2050, Schaumburg, Illinois 60173-2213.

Important Notice Regarding the Availability of Proxy Materials for Annual Meeting of Shareholders to Be Held on October 22, 2014. This Notice of Annual Meeting of Shareholders, Proxy Statement and our 2014 Annual Report are available at www.sparton.com.

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Sparton Corporation

2014 Proxy Statement Summary

The following is summary of certain information provided in the body of this Proxy Statement. This Summary does not contain all of the information contained in this Proxy Statement, and shareholders should review the entire Proxy Statement before voting on any matter proposed hereunder.

2014 Annual Meeting of Shareholders

Time and Date 10:00 a.m. Central Standard Time, October 22, 2014
425 North Martingale Road,

Place Schaumburg, Illinois 60173-2213,

at the 425 Executive Conference Center

Shareholders as of the record date, September 12, 2014, are entitled to vote. Each share of common stock is entitled to one vote for each director nominee and one vote for each of the other proposals to be voted on.

Voting

Meeting Agenda and Voting Matters	Board Vote Recommendation	Page Reference (for more detail)
Election of Six Directors	FOR each director nominee	11
Ratification of BDO USA, LLP as independent registered public accountant for fiscal year 2015 by advisory vote	FOR	15
Advisory vote on Named Executive Officer Compensation	FOR	17
Approve Amendment to Amended and Restated Code of Regulations	FOR	18
Re-Approve Material Terms of Performance Goals Under Sparton Corporation 2010 Long-Term Stock Incentive Plan	FOR	19
Transact other business that properly comes before the meeting		

Director Nominees

James D. Fast
Joseph J. Hartnett
Charles R. Kummeth
David P. Molfenter
James R. Swartwout (Chairman)

Independence

Other than Mr. Wood, who is the President and Chief Executive Officer of Sparton Corporation, all director nominees are independent.

Attendance

In fiscal year 2014, each of our director nominees attended at least 75% of all

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Cary B. Wood
Independent Registered Public Accountant

meetings of the Board and committees on which they serve (during the period served).

Sparton Corporation is asking the shareholders to ratify the appointment of BDO USA, LLP for fiscal year 2015. The following table summarizes the fees that BDO USA, LLP billed Sparton Corporation for the fiscal years ended June 30, 2014 and 2013:

(In thousands)	<u>Year Ended June 30,</u>	
	2014	2013
Audit Fees	\$ 412	\$ 400
Audit-Related Fees	24	304
Tax Fees	243	225
All Other Fees		
Total	\$ 679	\$ 929

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Executive Compensation

Sparton Corporation believes that its compensation policies and practices are effective in achieving its goals of attracting, motivating, retaining and rewarding its senior management team in order to achieve Sparton Corporation's corporate objectives and increase value for its shareholders. Please see "Executive Officer and Director Compensation" below at page 27 for details regarding compensation for fiscal year 2014.

2015 Annual Shareholders Meeting

Deadline for shareholder proposals to be included in the 2015 Proxy Statement: May 13, 2015.

Deadline for shareholder proposals: June 24, 2015.

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SPARTON CORPORATION

425 N. Martingale Road

Suite 2050

Schaumburg, Illinois 60173-2213

PROXY STATEMENT

For the Annual Meeting of Shareholders to be held on October 22, 2014

SOLICITATION

This Proxy Statement is furnished in connection with the solicitation by the Board of Directors of SPARTON CORPORATION, an Ohio corporation (the Company), of proxies for use at the 2014 Annual Meeting of Shareholders of the Company (the Annual Meeting) to be held at 425 North Martingale Road, Schaumburg, Illinois 60173-2213, at the 425 Executive Conference Center on Wednesday, October 22, 2014, at 10:00 a.m., Local Time, and at any and all adjournments thereof. The cost of solicitation will be paid by the Company. The Company has not retained a proxy solicitor to assist with the solicitation of proxies but retains the right to do so. Officers and employees of the Company and its subsidiaries may solicit proxies personally, by telephone, facsimile or other means, without additional compensation. This Proxy Statement and the form of proxy card are expected to be mailed to shareholders on or about October 3, 2014.

At the meeting, the Company's shareholders will act upon five proposals. The first proposal is the election of six directors, each to serve for a one-year term until the annual meeting held in the year 2015 and the election and qualification of their successors. The second proposal is the ratification of the appointment of independent registered public accountants by an advisory vote. The third proposal is the approval of the compensation of the Named Executive Officers (defined below) by an advisory vote. The fourth proposal is the approval of an amendment to the Company's Amended and Restated Code of Regulations, as amended to date (Code of Regulations) to provide that the state and federal courts located within the State of Ohio will be the exclusive jurisdiction for certain legal actions. The fifth proposal is the re-approval of the material terms of the performance goals specified in the Sparton Corporation 2010 Long-Term Stock Incentive Plan. The proposals are described in more detail in this Proxy Statement.

OUTSTANDING STOCK AND VOTING RIGHTS

In accordance with the Code of Regulations of the Company, the Board of Directors has fixed the close of business on September 12, 2014 as the record date for determination of shareholders entitled to notice of, and to vote at, the Annual Meeting. Only shareholders of record on that date will be entitled to vote. As of the record date for the Annual Meeting, the Company had outstanding 10,129,031 shares of common stock, each entitled to vote at the Annual Meeting. Votes cast at the meeting and votes submitted by proxy are counted by the inspectors of the election, who are appointed by the Company.

Voting by Proxy

If a shareholder is a corporation or partnership, the accompanying proxy card should be signed in the full corporate or partnership name by a duly authorized person. If the proxy card is signed pursuant to a power of attorney or by an executor, administrator, trustee or guardian, the signer's full title should be given and a certificate or other evidence of appointment should be furnished.

You can vote in one of three ways. You can vote by mail, you can authorize the voting of your shares over the Internet or you can vote in person at the Annual Meeting. Your proxy may be solicited up to the date and time of the meeting.

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Voting by Mail

If you choose to vote by mail, you may vote by completing and signing the proxy card that accompanies this Proxy Statement and promptly mailing it in the enclosed postage-prepaid envelope. You do not need to put a stamp on the enclosed envelope if you mail it in the United States. The shares you own will be voted according to the instructions on the proxy card you mail. If you return the proxy card, but do not give any instructions on a particular matter described in this Proxy Statement, the shares you own will be voted in accordance with the recommendations of the Company's Board of Directors. If you choose to vote by mail, your duly signed proxy card must be received by 11:59 p.m., Central Standard Time, on October 21, 2014.

Voting by Internet

If you choose to vote over the Internet, instructions for a shareholder of record to vote by the Internet are set forth on the enclosed proxy card. The Internet voting procedures are designed to authenticate votes cast by use of a personal identification number that appears on the proxy card. These procedures allow shareholders to appoint a proxy to vote their shares and to confirm that their instructions have been properly recorded. If you vote over the Internet, you do not have to mail in your proxy card, but your vote must be received by 11:59 p.m. Central Standard Time on October 21, 2014.

Voting 401(k) Plan Shares

If you participate in the Company's 401(k) retirement savings plan (the "401(k) Plan") and hold shares in your plan account, you may give voting instructions as to the number of shares credited to your account as of the record date. You may provide voting instructions (or a change or revocation in voting instructions) to the plan trustee, SunTrust Banks, Inc. ("SunTrust"), through any of the voting methods described above, except that you may not vote your plan shares in person at the Annual Meeting. Only the trustee of the 401(k) Plan, SunTrust, may vote your plan shares. Your voting instructions (or change or revocation in voting instructions) must be received before 11:59 p.m. Central Standard Time on October 21, 2014.

Shares Held in Street Name

If you are not the record holder of the shares you own because they are held in "street name" by a bank or brokerage firm, your bank or brokerage firm is required to vote your shares according to your instructions. In order to vote your shares, you will need to follow the directions your bank or brokerage firm provides you. Many banks and brokerage firms also offer the option of voting over the Internet or by telephone, instructions for which would be provided by your bank or brokerage firm on your vote instruction form. Under the rules of The New York Stock Exchange ("NYSE"), if you do not give instructions to your brokerage firm, it may still be able to vote your shares with respect to certain "discretionary" items that are deemed by the NYSE to be routine (e.g., the ratification of the appointment of independent registered public accountants), but it will not be allowed to vote your shares with respect to certain "non-discretionary" items. If you do not provide voting instructions to your broker with respect to non-discretionary items such as election of directors, amendment to the Company's Code of Regulations, re-approval of the material terms of the performance goals under the 2010 LTIP (defined below), and the advisory vote on the compensation of Named Executive Officers, your shares will not be voted for any such proposal. In such case, the shares will be treated as "broker non-votes."

Revocation and How Shares are Voted if No Instructions are Provided

Any proxy given pursuant to this solicitation may be revoked by the person giving it at any time before it is voted. Proxies may be revoked by (i) filing a written notice of revocation with the Chairman or Secretary of the Company, at or before the Annual Meeting, (ii) duly executing a subsequent proxy relating to the same shares and delivering it to the Chairman or Secretary of the Company either signed and returned by mail or transmitted using the Internet procedures at or before the Annual Meeting subject to deadlines set forth above or

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(iii) attending the Annual Meeting and voting in person with adequate notification (although attendance at the Annual Meeting will not in and of itself constitute a revocation of a proxy). Unless revoked, the shares represented by the enclosed proxy will be voted at the meeting in accordance with any specification made thereon, if the proxy is returned properly executed and delivered in time for voting in accordance with the deadlines set forth above.

Unless otherwise specified, the proxy will be voted FOR the election of the six director nominees, FOR the ratification of the appointment of independent registered public accountants, FOR approval of the compensation of the Named Executive Officers and FOR approval of the amendment to the Company's Code of Regulations.

Quorum and Vote Required

At all meetings of shareholders, including the Annual Meeting, the holders of record of a majority of the outstanding voting shares of the Company, present in person or by proxy, constitutes a quorum for the transaction of business.

In accordance with the Company's Second Amended Articles of Incorporation, and with respect to Proposal 1, a director nominee must receive, in an uncontested election of directors, a greater number of votes cast FOR his or her election than AGAINST his or her election. Under our governing documents and Ohio law, an incumbent director who is not re-elected will continue in office as a holdover director until his or her successor is elected by a subsequent shareholder vote, or his or her earlier resignation, removal from office or death. In order to address holdover terms for any incumbent directors who fail to be re-elected under our majority vote standard, our Corporate Governance Guidelines provide that if a director nominee does not receive a majority affirmative vote, he or she will promptly offer his or her resignation as a director to the Board of Directors. Within ninety (90) days, the Board of Directors will decide, after taking into account the recommendation of the Nominating and Corporate Governance Committee (in each case excluding the nominee(s) in question), whether to accept the resignation. The Nominating and Corporate Governance Committee and the Board of Directors may consider any relevant factors in deciding whether to accept a director's resignation. The Board of Directors explanation of its decision shall be promptly disclosed in a filing with the Securities and Exchange Commission (SEC).

With respect to Proposal 2, the ratification of the appointment of the independent registered public accountant requires the affirmative vote of a majority of the shares entitled to vote thereon and present in person or represented by proxy at the Annual Meeting.

With respect to Proposal 3, the approval of the compensation of the Named Executive Officers requires the affirmative vote of a majority of the shares entitled to vote thereon and present in person or represented by proxy at the Annual Meeting.

With respect to Proposal 4, the approval of the amendment to the Company's Code of Regulations requires the affirmative vote of a majority of the shares entitled to vote thereon and present in person or represented by proxy at the Annual Meeting.

With respect to Proposal 5, the re-approval of the material terms of the performance goals specified in the 2010 LTIP requires the affirmative vote of a majority of the shares entitled to vote thereon and present in person or represented by proxy at the Annual Meeting.

Broker non-votes and abstentions are not counted for purposes of any of the proposals, other than Proposals 4 and 5, for which abstentions are counted and have the effect of a negative vote against the Proposal. Proposals 2 and 3 are advisory in nature and not binding, although the Board will carefully consider the shareholder votes.

Other Matters

Management does not intend to present, and does not know of anyone who intends to present, any matters at the meeting to be acted upon by the shareholders not referred to in the Notice and this Proxy Statement. If any other matters should properly come before the meeting, it is the intention of the persons named in the proxy to vote in accordance with their judgment on such matters.

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CORPORATE GOVERNANCE AND BOARD MATTERS

Director Independence

Independence criteria and determination

The listing requirements under Section 303A.01 of the NYSE Listed Company Manual (the Manual) provide that a majority of the members of a listed company's board of directors must be independent. The question of independence is determined with respect to every director pursuant to standards set forth in the Manual. The Manual also requires that certain committees be composed entirely of independent directors. The committees covered by this requirement are the Audit, Compensation, and Nominating and Corporate Governance Committees. Based upon the standards set forth in the Manual, as of the date of this Proxy Statement, six of the Board's seven members, being more than a majority of the Board, are independent. All current members of the Audit, Compensation, and Nominating and Corporate Governance Committees are independent in that those directors do not have a material relationship with the Company directly or as a partner, shareholder or affiliate of an entity that has a relationship with the Company.

In making such determinations, the Board considered (i) whether a director had, within the last three years, any of the relationships under Section 303A.02(b) of the Manual with the Company that would disqualify a director from being considered independent, (ii) whether the director had any disclosable transaction or relationship with the Company under Item 404 of Regulation S-K of the Securities Exchange Act of 1934, as amended (Exchange Act), which relates to transactions and relationships between directors and their affiliates, on the one hand, and the Company and its affiliates (including management), on the other, and (iii) the factors suggested in the NYSE's Commentary to Section 303A.02, such as commercial, industrial, banking, consulting, legal, accounting, charitable or familial relationships, among other relationships, or other interactions with management that do not meet the absolute thresholds under Section 303A.02 or Item 404(a) but which, nonetheless, could reflect upon a director's independence from management. In considering the materiality of any transactions or relationships that do not require disqualification under Section 303A.02(b), the Board considered the materiality of the transaction or relationship to the director, the director's business organization and the Company and whether the relationship between (i) the director's business organization and the Company, (ii) the director and the Company and (iii) the director and his or her business organization interfered with the relevant director's business judgment.

Based on the foregoing, the Company has determined that the following directors are independent: James D. Fast, Joseph J. Hartnett, Charles R. Kummeth, David P. Molfenter, Douglas R. Schrank, and James R. Swartwout. Mr. Schrank will not stand for re-election at the Annual Meeting.

Meetings of Independent Directors

The independent directors schedule meetings in executive sessions without the presence of the Company's management. The Chairman presides over the sessions during the year.

The independent directors met 4 times during the last fiscal year.

Shareholder Communication with Independent Directors

Shareholders wishing to communicate directly with the independent directors may send correspondence addressed as follows:

Independent Directors

c/o Corporate Secretary

Sparton Corporation

425 N. Martingale Road, Suite 2050

Schaumburg, Illinois 60173-2213

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Mr. James R. Swartwout has been elected by the directors as the Chairman. The Chairman provides leadership to enhance the Board's effectiveness, presides over meetings of the directors, and serves as a liaison between the Board and management. The Chairman is responsible for determining when to hold, and who shall preside over, executive sessions held by the independent directors. If a shareholder, employee, or third party prefers not to communicate directly with the entire Board of Directors or management, communications may be sent to the Chairman, in care of the Corporate Secretary, using the above address.

Board and Committee Structure

As of the date of this Proxy Statement, the Company's Board of Directors consists of six independent directors, including the Chairman of the Board, Mr. Swartwout, and one non-independent director, Mr. Cary B. Wood, the President and Chief Executive Officer of the Company. The Board has established three committees, being the Audit, Compensation, and Nominating and Corporate Governance Committees, as further described below. Each of the committees is comprised solely of independent directors, and each committee has a different chair. The Company believes that its predominantly independent Board, mixed with the experience of its non-independent director, constitutes a leadership structure that is most appropriate for the Company and its shareholders.

The Board of Directors had 7 meetings during fiscal year 2014.

Board Committee Membership

Director	Independent	Audit	Compensation	Nominating and Corporate Governance
James D. Fast	Yes		x	x - Chairman
Joseph J. Hartnett	Yes	x		
Charles R. Kummeth	Yes		x	x
David P. Molfenter	Yes		x - Chairman	x
Douglas R. Schrank	Yes	x - Chairman		
James R. Swartwout	Yes	x		
Cary B. Wood	No			

x denotes committee membership

Audit Committee

The Audit Committee met 5 times during fiscal year 2014 and is comprised of Messrs. Douglas R. Schrank (Chairman), Joseph J. Hartnett and James R. Swartwout. The Audit Committee operates under a written charter and oversees auditing, financial reporting and internal control matters regarding accounting and financial controls. It also selects the firm that the Company retains as its independent registered public accountants and recommends the ratification of their selection by the shareholders. The Audit Committee consults with the independent registered public accountants and oversees their audit and other work. The Audit Committee also consults with the Chairman of the Board, President and Chief Executive Officer, and Chief Financial Officer and oversees those individuals who review the Company's internal controls and compliance with policies. Each member of the Audit Committee is independent, as defined under the NYSE listing standards.

Each of Mr. Hartnett and Mr. Schrank, in addition to being independent, qualifies as an audit committee financial expert as defined in the SEC Regulation S-K, Item 407(d)(5)(ii). Mr. Hartnett's relevant financial experience includes that he is a licensed Certified Public Accountant in the State of Illinois since 1982, and has advised multiple boards and audit committees with respect to accounting matters. Mr. Hartnett has a B.S. in Accounting from the University of Illinois - Chicago, served with Grant Thornton LLP from 1980 to 2000, and was an audit partner with Grant Thornton LLP from 1992 to 2000. Mr. Hartnett served as the Chief Financial

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Officer of U.S. Robotics Corporation, an Internet communications products company. Mr. Schrank's relevant financial experience includes that he was licensed as a Certified Public Accountant in the State of Minnesota in 1973 and prior to retirement served as the Chief Financial Officer of multiple companies, including a multinational publicly traded pharmaceutical company. Further, Mr. Schrank received a Master of Business Administration from the University of Michigan in 1972. For additional detail, see *Director Biographies* below at page 11 describing the members of the Board of Directors and their respective experience, qualifications, attributes and skills.

The independent registered public accountants have access to the Audit Committee without any other members of management being present. The Audit Committee met with management and the independent registered public accountants before the announcement of earnings each quarter. The Audit Committee also met with the independent registered public accountants without management present on 5 occasions during fiscal year 2014. The Audit Committee also reviewed the annual consolidated financial statements and annual report on Form 10-K and the Audit Committee report in this Proxy Statement before each was filed with the SEC.

Compensation Committee

The Compensation Committee held 16 meetings during fiscal year 2014. The Compensation Committee is comprised of Messrs. David P. Molfenter (Chairman), James D. Fast and Charles R. Kummeth, and it monitors the remuneration, including restricted stock and stock options, for the Company's management, including the Named Executive Officers.

The Compensation Committee may delegate its authority to subcommittees consisting of independent directors and may be assisted on compensation matters by members of the Company's staff. The Compensation Committee (the Committee) may, as needed, employ compensation consultants to assist the Committee with the Committee's determination of the amount and/or form of executive compensation. See page 33 below under the heading *Role of the Compensation Consultant* for discussion regarding the Compensation Committee's use of consultants. The compensation philosophy, the compensation components, and their application as described in the Compensation Discussion and Analysis, which appears below, are generally employed by the Compensation Committee in connection with the compensation for all of the executive officers of the Company.

Nominating and Corporate Governance Committee

The Nominating and Corporate Governance Committee, which is comprised of Messrs. James D. Fast (Chairman), Charles R. Kummeth and David P. Molfenter, held 6 meetings during fiscal year 2014. The Nominating and Corporate Governance Committee reviews corporate governance documents, and reviews the makeup of the existing Board of Directors and the tenure of its members, consistent with appropriate principles of corporate governance and applicable regulations, and reviews and recommends director remuneration to the full Board of Directors. The Nominating and Corporate Governance Committee also receives candidate resumes, and considers and recommends candidates for election to the Board consistent with the needs of the Company, regulatory requirements, and the qualifications of the candidates. The Nominating and Corporate Governance Committee has implemented a formal process for consideration of candidates, which is described under *Director Qualifications* below.

Board Role in Risk Oversight

The Board is ultimately responsible for oversight of risk management. As part of the risk management process, the Company's management team, through its Risk Management Committee, is responsible for identifying and monitoring potential risks facing the Company. The Risk Management Committee's Chairman will rotate annually and various business departments report potential risks to the Chairman on a periodic basis. The Chairman of the Risk Management Committee reviews such potential risks with the Committee and counsel and reports its determinations to the Board. The Company believes that reviewing risk at the business department level by the Risk Management Committee, as reported to the Board of Directors, provides the Board of Directors with a comprehensive and detailed overview of enterprise risk.

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The Audit Committee is charged with reviewing the adequacy and effectiveness of the accounting and financial controls, including the Company's systems to monitor, assess and manage financial, business, legal and compliance risk.

Further, the Board believes that the roles of Chief Executive Officer and Chairman of the Board of Directors should be separated and therefore two different individuals serve as the Company's Chief Executive Officer and Chairman. Mr. Cary B. Wood serves as the Company's Chief Executive Officer and Mr. James R. Swartwout serves as the Chairman of the Company's Board of Directors.

The Company's risk structure allows the Company's independent directors to exercise effective oversight of the actions of management, led by Mr. Cary B. Wood as Chief Executive Officer and President, in identifying risks and implementing effective risk management policies and controls.

Corporate Governance Guidelines and Charters

The Board of Directors has adopted Corporate Governance Guidelines applicable to the Company. The Nominating and Corporate Governance Committee reviews the Guidelines annually to determine whether to recommend changes to the Board of Directors to reflect new laws, rules and regulations and developing governance practices. The Guidelines address several key areas of corporate governance, including the Company's governance philosophy, director responsibilities, Board composition, Board meetings and committees, director independence, and director compensation. The Guidelines are available on the Company's website, www.sparton.com.

In addition to the Guidelines, the Board adopted charters for the Compensation, Audit and Nominating and Corporate Governance Committees addressing corporate governance issues. These charters address issues such as independence of the committee members, committee organization and powers, member qualifications, duties and responsibilities, and corporate governance.

As of June 30, 2014, all members of the Audit, Compensation, and Nominating and Corporate Governance Committees were independent directors. Copies of the charters for each of these committees are located on the Company's website, www.sparton.com. The Company continues to develop and refine its corporate governance policies and practices and their place within the committee structure of the Board of Directors.

The Board has determined that maintaining an Executive Committee as a standing committee is not necessary, in part due to the smaller size of the Board. The Board will continue to review whether or not it is appropriate to re-establish an Executive Committee in the future.

Code of Business Conduct and Ethics

The Company's Code of Business Conduct and Ethics sets forth the Company's corporate values. The Code of Business Conduct and Ethics governs the actions and working relationships of the Company's employees, officers and directors, and sets forth the standard of conduct of the Company's business at the highest ethical level and in compliance with all applicable laws and regulations.

To the extent any waiver is granted with respect to the Code of Business Conduct and Ethics that requires disclosure under applicable SEC rules, such waiver will also be posted on the Company's website, as will any amendment that may be adopted from time to time.

Additionally, the Company has established the following statement of its Corporate Values :

We demand performance excellence in all that we do.

We demand integrity of ourselves, our products, and our services.

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We foster growth and success in an environment of teamwork, collaboration, empowerment, and accountability.

We develop long term, trusting relationships to ensure mutually profitable growth.

We will maintain a safe and environmentally sound workplace.

We will be good corporate citizens in the communities in which we reside.

Whistleblower Provisions

It is the Company's policy to encourage its employees and other persons to disclose improper activities, and to address complaints alleging acts of reprisal or intimidation resulting from disclosure of improper activities. Individuals wishing to report improper activities may call the Company's Whistleblower service at 1-800-488-1933 (from within the United States) or 1-800-4818 (from Vietnam). Activities may be reported anonymously if desired.

Director Attendance at Meetings

All directors attended at least 75% of the aggregate total number of meetings of the Board and committees on which they serve during fiscal year 2014. In addition, the directors are expected to attend the Annual Meeting. At the Company's 2013 Annual Meeting of the Shareholders, all of the directors serving at that time were in attendance. Pursuant to our Corporate Governance Guidelines our directors are encouraged to attend director education programs on an annual basis.

Director Qualifications

The Nominating and Corporate Governance Committee is responsible for reviewing with the Board of Directors, from time to time, the appropriate qualities, skills and characteristics desired for members of the Board of Directors in the context of the current make-up of the Board. This assessment includes consideration of the following summary of qualifications that the Nominating and Corporate Governance Committee believes must be met by all directors, as well as the following considerations for the composition of the Board of Directors as a whole:

Essential Qualities

Relevant and substantial business experience, with an understanding of what is involved in leading a company

Sound business instincts and judgment, with the ability to make informed and strategic decisions

Professional and personal reputation and integrity consistent with the Company's Code of Business Conduct and Ethics

Strong interpersonal skills evidencing the ability to work as part of a group and express views that are both challenging to and supportive of management

Commitment and availability to the Company to perform necessary and desired duties, with the ability to accept accountability for their role in decisions of the Board of Directors

Genuine interest in the Company, its business, and its people, with a willingness to remain committed over a period of several years

Board Composition Considerations

Strategic mix of directors allowing for diverse expertise and experience fitting the specific needs of the Company, now and anticipated in the future

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Multiple directors possessing understanding and expertise in the area of accounting and finance

Multiple directors with specific experience and knowledge of the risks and challenges unique to the industries in which the Company operates

Visionaries with the ability to lead, manage change, and assist in the continued growth of the Company

Familiarity with and understanding of the media and various financial markets

The Board considers diversity, including cognitive and experiential diversity, of director nominees to be desirable to achieve balanced deliberation; however the Company does not have a formal written diversity policy. These and other factors are considered by the Board of Directors in selection of director nominees.

Process for Identifying and Evaluating Director Nominees

The Board of Directors is responsible for selecting director candidates. The Board of Directors delegates the identification, recruitment and recommendation of director nominees to the Nominating and Corporate Governance Committee, with the expectation that other members of the Board of Directors and management will be requested to take part in the process as appropriate.

When it is determined by the Board of Directors that a new director or nominee is to be recruited, the Nominating and Corporate Governance Committee undertakes a candidate selection process. The Committee maintains a selection criteria document, which has been approved by the Board of Directors and which the Committee reviews regularly to ensure that it is applicable. The criteria include both general criteria that all candidates must meet and specific criteria regarding skill or background that are desirable to the Board of Directors. The Nominating and Corporate Governance Committee, with the counsel of the full Board of Directors, determines which specific background should be represented in the candidate. The criteria are then given to a professional recruiter who specializes in board placements and a search is commenced. Potential candidates known to existing directors or suggested by shareholders who are believed to meet the criteria may be suggested to the recruiting agency for inclusion in the initial pool of candidates. Once candidates have been identified, the Nominating and Corporate Governance Committee confirms that the candidates meet all of the qualifications for director nominees established by the Nominating and Corporate Governance Committee. Based on the results of an evaluation process, the Nominating and Corporate Governance Committee recommends candidates for the Board's approval as director nominees for election to the Board of Directors. The Nominating and Corporate Governance Committee also recommends candidates for the Board's appointments to the committees of the Board.

Procedure for Recommendation of Director Nominees by Shareholders

The Nominating and Corporate Governance Committee will consider director candidates who are recommended by shareholders of the Company. As required by Article I, Section 10 of the Company's Code of Regulations, to recommend a nominee, a shareholder should write to the Company's Corporate Secretary at 425 N. Martingale Road, Suite 2050, Schaumburg, Illinois 60173-2213. Under the current Code of Regulations, to be considered by the Nominating and Corporate Governance Committee for nomination and inclusion in the Company's Proxy Statement for its Annual Meeting of Shareholders, a shareholder recommendation for a director must be received by the Company's Secretary no later than 120 days nor more than 240 days prior to the one year anniversary of the preceding Annual Meeting.

Any recommendation must include (i) all information relating to such nominee that is required to be disclosed in a proxy statement or other filings required to be made in connection with solicitations of proxies for election of directors under Rule 14a-11 of the Exchange Act or in a contested election pursuant to Section 14 of the Exchange Act and the rules and regulations promulgated thereunder (including such person's written consent to

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being named in the proxy statement as a nominee and to serving as a director if elected); (ii) a description of all direct and indirect compensation and other material monetary agreements, arrangements and understandings during the past three years, and any other material relationships, between or among such shareholder and beneficial owner, if any, and their respective affiliates and associates, or others acting in concert therewith, on the one hand, and each proposed nominee, and his or her respective affiliates and associates, or others acting in concert therewith, on the other hand, including without limitation all information that would be required to be disclosed pursuant to Rule 404 promulgated under Regulation S-K; (iii) a representation of the shareholder that he or she intends to appear at the annual meeting to bring such nomination or other business before the annual meeting; and (iv) such other information as may reasonably be required by the Board of Directors as described in the Company's proxy statement for the preceding year's annual meeting. The Company may require any proposed nominee to furnish such other information as may reasonably be required by the Company to determine the eligibility of such proposed nominee to serve as an independent director of the Company or that could be material to a reasonable shareholder's understanding of the independence, or lack thereof, of such nominee.

Further information regarding shareholder recommendation of director candidates is contained in the Nominating and Corporate Governance Committee Charter, which is available at the Company's website at www.sparton.com.

Assuming the appropriate information is provided for candidates submitted by shareholders, the Nominating and Corporate Governance Committee will evaluate those candidates by following the same process, and applying the same criteria, as for candidates submitted by members of the Board of Directors. All director nominees recommended for election at the Annual Meeting are current members of the Board of Directors.

Shareholder Communications Policy

Shareholders should communicate with the Board of Directors by sending a letter to the Sparton Corporation Board of Directors, c/o the Corporate Secretary, 425 N. Martingale Road, Suite 2050, Schaumburg, Illinois 60173-2213. The Corporate Secretary will receive the correspondence and forward it to the director or directors to whom the communication is directed, unless the communication is unduly hostile, threatening, harassing, illegal, not reasonably related to the Company or its business, or similarly inappropriate. The Corporate Secretary has the authority to discard or disregard any inappropriate communications (other than a proposal submitted pursuant to Rule 14a-8 under the Exchange Act, or any communication made in connection with such a proposal) or to take other appropriate actions with respect to any such inappropriate communications. In addition, the Corporate Secretary is authorized to forward communications that are clearly more appropriately addressed by other departments, such as customer service or accounting, to the appropriate department. The foregoing instructions by the directors to the Corporate Secretary are subject to change by the directors. Additionally, all communications are available to any director who wishes to review them.

Availability of Information at Company Website

The Company's website address is www.sparton.com. Information provided at the website includes, among other items, the Company's Corporate Governance Guidelines, current charters for the Audit, Compensation, and Nominating and Corporate Governance Committees of the Board of Directors, Board committees and their membership, the Company's Code of Business Conduct and Ethics, any Shareholder Letters, the Company's Annual Report, Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, and news releases. The information is also available, without charge, by contacting the Shareholders' Relations Department at 1-847-762-5800.

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PROPOSAL 1
ELECTION OF DIRECTORS

Director Nominees

Messrs. James D. Fast, Joseph J. Hartnett, Charles R. Kummeth, David P. Molfenter, James R. Swartwout and Cary B. Wood, current directors whose terms of office expire at the Annual Meeting, are nominees for election to a one year term expiring in 2015 and the election and qualification of their successors. The nominations were made by the Nominating and Corporate Governance Committee and approved by the Board of Directors.

Our Code of Regulations provides that our Board of Directors will consist of not less than six members, but our Board is authorized to fix and change the actual number of our directors from time to time.

We currently have seven members on our Board of Directors. However, given the announcement by Douglas R. Schrank that he does not plan to stand for re-election at the Company's Annual Meeting, there will only be six members serving on our Board. The Board has commenced a search for a suitable replacement director; however, the process is not expected to be completed prior to the Annual Meeting. Accordingly, the Board has fixed the minimum number of members of directors of the Board at six and intends to increase the minimum number to seven once a candidate is selected.

It is believed that all six nominees are, and will be at the time of the Annual Meeting, available for election; and, if elected, will serve. Each of the nominees has consented to being named a nominee in this Proxy Statement and has agreed to serve as a director, if elected at the Annual Meeting. However, in the event one or more of them is or should become unavailable, or should decline to serve, it is intended that the proxies will be voted for the balance of the nominees and for such substitute nominee or nominees as the Board of Directors may in its discretion select.

Vote Required for Approval

Each share of common stock is entitled to one vote for each of the six director positions being filled at the Annual Meeting. In order to elect a nominee as a director of the Company, he or she must receive a greater number of votes cast FOR his or her election than AGAINST his or her election. Shares not voted at the Annual Meeting, whether by abstention, broker non-vote, or otherwise, will have no effect on the election of directors. See Outstanding Stock and Voting Rights Quorum and Vote Required at page 3 for additional information.

Board Recommendations

The Board of Directors recommends a vote FOR the election of each of the six nominees, James D. Fast, Joseph J. Hartnett, Charles R. Kummeth, David P. Molfenter, James R. Swartwout and Cary B. Wood.

Unless otherwise directed by marking the accompanying proxy, the proxy holders named therein will vote FOR the election of the six nominees.

Director Biographies

The following table summarizes the specific experience, qualifications, attributes and skills that led the Nominating and Corporate Governance Committee and the Board of Directors to conclude that the following individuals should serve as directors are set forth opposite each individual's name. The Company's Board of Directors consists primarily of individuals with broad leadership and business skills, as detailed below, who have relevant experience with companies ranging in size from smaller to much larger than the Company, including

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individuals who have served as chief executive officers and chief financial officers of such companies. The Nominating and Corporate Governance Committee and the Board of Directors consider the skill sets both individually and as a whole in considering who to recommend as nominees. The Board of Directors believes that all of the members of the Board have the highest professional and personal ethics and values.

Director since: 2001

Independent

James D. Fast, age 66

Retired since August 2008, formerly Chief Executive Officer, President and Director of Firstbank-West Michigan, Ionia, Michigan. Prior to joining Firstbank, Mr. Fast served as Group Vice President, Michigan National Bank-Michiana. Mr. Fast has forty years of experience in commercial banking and administration. Mr. Fast previously served as a Director of Volcor Finishing, a privately held company in Ionia, Michigan.

Mr. Fast has experience with respect to mergers and acquisitions, negotiation, compliance management and human resource oversight and supervision of financial statement preparation. His extensive skill set with respect to executive management and commercial finance provides the Board with beneficial insights with respect to business and finance matters.

Director since: 2008

Independent

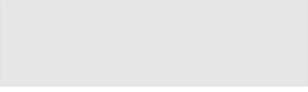
Joseph J. Hartnett, age 59

Mr. Hartnett served as President and Chief Executive Officer of Ingenient Technologies, Inc., a multimedia software development company located in Rolling Meadows, Illinois, from April 2008 through November 2010. He joined Ingenient as Chief Operating Officer in September 2007 and left Ingenient following the sale of the company and completion of post-sale transition activities. Prior to Ingenient, Mr. Hartnett served as President and Chief Executive Officer of U.S. Robotics Corporation, a global Internet communications product company headquartered in Schaumburg, Illinois, from May 2001 through October 2006. He was Chief Financial Officer of U.S. Robotics from June 2000 to May 2001. Prior to U.S. Robotics, Mr. Hartnett was a partner with Grant Thornton LLP where he served for over 20 years in various leadership positions at the regional, national, and international level.

Mr. Hartnett is a licensed Certified Public Accountant in the State of Illinois (licensed 1982 to present), and holds a Bachelor of Science degree in Accounting from the University of Illinois at Chicago.

Mr. Hartnett serves as a director and member of the audit committee, compensation committee and nominating and corporate governance committee of Garmin Ltd. since June 7, 2013, and is a former director of Crossroads Systems, Inc., U.S. Robotics Corporation and Ingenient Technologies, Inc.

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Mr. Hartnett brings significant industry experience in the areas of international business, operations management, executive leadership, strategic planning and finance, as well as extensive corporate governance, executive compensation and financial experience.

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Director since: 2011

Independent

Charles R. Kummeth, age 54

Mr. Kummeth serves as the Chief Executive Officer of Techne Corporation, a Minnesota corporation, since April 2013. Techne Corporation and its subsidiaries are engaged in the development, manufacture and sale of biotechnology products and hematology calibrators and controls. Mr. Kummeth served as President of the Mass Spectrometry and Chromatography division of Thermo Fisher Scientific, a Delaware corporation that provides services and products within the science industry, from April 2008 through March 2013. He previously served as President of the Medical Product Division of 3M, a Delaware corporation, beginning in 2006. From 2004 to 2006, Mr. Kummeth served as the Managing Director of 3M for the UK and Ireland.

Mr. Kummeth has served on the board of BSN Medical Inc., a private global medical device company, since March 2013.

Mr. Kummeth received a Bachelor of Science in Electrical Engineering from University of North Dakota in 1983, a Master of Science in Computer Science from University of St. Thomas in 1989, and a Master of Business Administration from the Carlson School of Business at the University of Minnesota in 1993.

Mr. Kummeth has significant industry experience in the areas of serving science, innovative technologies, software and laboratory operations. His extensive skill set with respect to executive management of a global company with high reputation in the scientific community provides the Board with industry expertise and added business insights.

Director since: 2000

Independent

David P. Molfenter, age 69

Mr. Molfenter retired in August 2000. He formerly was Vice President Command, Control, Communication and Information Systems Segment, Raytheon Systems Company, a high technology company specializing in defense electronics, Fort Wayne, Indiana. Mr. Molfenter has a Master of Business Administration from Indiana University and a M.S. Electrical Engineering from Purdue University. Prior to employment with Raytheon Systems Company, Mr. Molfenter served as Chief Executive Officer of Magnavox Electronics Systems, Co. from 1993 to 1995, and as President of Hughes Defense Communications from 1995 to 1997. Since March, 2010, Mr. Molfenter has served as a member of the board of directors of Bowmar, LLC, a privately held company in Fort Wayne, Indiana.

Mr. Molfenter's extensive executive management and board experience, including service as the principal executive officer of multiple companies and his fourteen years with the Company's Board, provides him with the necessary skills to serve on the Board of Directors.

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Director since: 2008

Independent

James R. Swartwout, age 68

Mr. Swartwout has been an advisor to private equity groups since 2008. From October 2006 to September 2008, he was Chief Executive Officer and member of the Board of Directors of Habasit Holding USA, the acquirer of Summa Industries, a California-based, publicly traded manufacturer of diversified plastic products for industrial and commercial markets. From October 1988 to October 2006, Mr. Swartwout held the following positions with Summa Industries (formerly NasdaqGM: SUMX): Chairman of the Board of Directors, Chief Executive Officer and Chief Financial Officer. Mr. Swartwout has served on the boards of directors of numerous public and private companies. He received a Bachelor of Science in Industrial Engineering from Lafayette College and a Master of Business Administration from the University of Southern California.

Mr. Swartwout has extensive experience in a broad array of matters relevant to the affairs of the Company, including mergers, acquisitions and divestitures; management of complex, multi-business corporations; corporate governance and other matters concerning public companies.

Director since: 2008

Management

Cary B. Wood, age 47

Mr. Wood has been President of the Company since April 2009 and Chief Executive Officer of the Company since November 2008.

During the period August 2004 to November 2008, Mr. Wood served in a variety of roles for Citation Corporation (now known as Grede Holdings, LLC). He served as interim CEO for a period of time, after which he served as the company's Chief Operating Officer for an extended period of time. Grede Holdings, LLC is located in Southfield, Michigan and is a private company manufacturing cast, machined and assembled components for the transportation and industrial markets. Mr. Wood began his career with General Motors Corporation followed by a period with United Technologies Corporation in a variety of roles, including general management, operations and engineering capacities. He has progressed through both private and public company settings and has a developed track record in performance turn-around and growth strategies. Mr. Wood received a Bachelor of Science in Technology from Purdue University in 1989 and a Master of Science in Industrial Operations in the School of Management from Lawrence Tech University in 1995.

Mr. Wood's experience in the areas of executive management, corporate turn-around, and growth strategies, as well as his in depth knowledge of the Company and its operating segments, are highly valuable attributes to the Company and its Board.

Table of Contents**PROPOSAL 2****RATIFICATION OF APPOINTMENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTANTS****Relationship with Independent Registered Public Accountants**

The Audit Committee appoints the independent registered public accounting firm to serve as the Company's independent registered public accountant. BDO USA, LLP (BDO USA) is currently the independent registered public accountant for the Company. In addition to performing the audit of the Company's consolidated financial statements, BDO USA provided various other services during fiscal year 2014. The Audit Committee has considered the provision of all non-audit services performed by BDO USA during fiscal year 2014 with respect to maintaining auditor independence. The Audit Committee reviewed and pre-approved all professional services requested of, and performed by, BDO USA. The aggregate fees billed for fiscal year 2014 and 2013 for each of the following categories of services are set forth below.

Pursuant to the Pre-Approval Policy, the Audit Committee annually reviews and pre-approves the services that may be provided by the independent registered public accountant, and such services are considered approved through the next annual review. The Audit Committee revises the list of pre-approved services from time to time based on subsequent determinations. The Audit Committee may delegate pre-approval authority to its Chairman. The Chairman shall report any pre-approval decisions to the Audit Committee at its next scheduled meeting. The Pre-Approval Policy for audit and non-audit services is available on the Company's website at www.sparton.com.

Fees

The following table presents fees for services provided by BDO USA for the years ended June 30, 2014 and 2013:

(In thousands)	Year Ended June 30,	
	2014	2013
Audit Fees	\$ 412	\$ 400
Audit-Related Fees	24	304
Tax Fees	243	225
All Other Fees		
Total	\$ 679	\$ 929

Audit Fees

These fees relate to the audit and reviews of the consolidated financial statements, including opening balance sheet work for three acquisitions during fiscal 2014 and for two acquisitions during fiscal 2013, and for other attest services.

Audit-Related Fees

These fees primarily relate to audits of employee benefit plans and for fiscal 2013, accounting consultation for contemplated transactions and the audit of historical financial statements for one acquisition.

Tax Fees

These fees relate to tax compliance, tax advice and tax planning and tax consultation for contemplated transactions.

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All Other Fees

There were no other fees for the years ended June 30, 2014 and 2013.

Auditor Independence

The Audit Committee is required to consider the independence of BDO USA when engaging the firm to perform audit-related and other services. In 2014, it was determined by the Audit Committee that audit-related and other services provided and the fees paid for those services were consistent with maintaining the independence of BDO USA.

Vote Required for Approval

At a meeting on August 19, 2014, the Audit Committee of the Board of Directors took action to recommend the appointment of the accounting firm of BDO USA as the independent registered public accountants for the Company for the fiscal year ending June 30, 2015 and, on August 20, 2014, the Board of Directors approved such appointment. The Board of Directors is asking the shareholders to ratify the appointment of BDO USA.

Each share of common stock is entitled to one vote for this Proposal. In order to be adopted, this Proposal must be ratified by the holders of a majority of the shares entitled to vote thereon present in person or represented by proxy at the Annual Meeting. Broker non-votes and abstentions are not counted for purposes of this Proposal. Because this vote is advisory, it will not be binding upon the Board of Directors. However, the Board values the opinion of its shareholders and, in the event that the shareholders do not ratify the appointment by approving this Proposal 2, the Board of Directors and the Audit Committee will consider the selection of other independent registered public accountants.

Board Recommendation

The Board of Directors recommends that shareholders vote FOR the ratification of the selection of BDO USA, LLP by an advisory vote.

Representatives of BDO USA, the Company's independent registered public accounting firm, are expected to be present at the Annual Meeting. They will have an opportunity to make a statement if they desire to do so and are expected to be available to respond to appropriate questions.

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PROPOSAL 3

ADVISORY VOTE ON NAMED EXECUTIVE OFFICER COMPENSATION

The Company has designed its executive compensation program to attract, motivate, retain and reward its senior management in order to achieve the Company's corporate objectives and increase value for our shareholders. The Company believes that its compensation policies and procedures are centered on a pay-for-performance philosophy and are aligned with the long-term interests of our shareholders.

The Company is presenting the following proposal, which gives each shareholder the opportunity to have a voice and endorse or not endorse the Company's executive compensation paid to our Named Executive Officers by voting for or against the following resolution:

RESOLVED, that the compensation paid to the Company's Named Executive Officers, as disclosed pursuant to Item 402 of Regulation S-K, including the Compensation Discussion and Analysis and related compensation tables and the narrative discussion, is hereby approved.

As discussed in the Compensation Discussion and Analysis contained in this Proxy Statement, the Compensation Committee of the Board of Directors believes that the executive compensation for fiscal year 2014 is justified by the performance of the Company in a very competitive environment, is reasonable and is the result of a carefully considered approach.

In deciding how to vote on this Proposal, the Company urges you to consider the various factors regarding compensation matters as discussed in the Compensation Discussion and Analysis. Your vote is not intended to address any specific item of compensation, but rather the overall compensation of our Named Executive Officers and the compensation policies and practices described in this Proxy Statement.

Because your vote is advisory, it will not be binding upon the Board of Directors. However, our Board values your opinion and the Board of Directors and the Compensation Committee will take into account the outcome of the vote when considering future executive compensation arrangements.

Vote Required for Approval

Approval of the proposal requires the affirmative vote of a majority of the shares of our common stock present in person or represented by proxy and entitled to be voted on the proposal at the Annual Meeting. Broker non-votes and abstentions are not counted for purposes of this Proposal.

Board Recommendation

The Board recommends a vote FOR approval of the compensation of the Company's Named Executive Officers as set forth in Proposal 3.

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PROPOSAL 4

**VOTE TO APPROVE AMENDMENT TO COMPANY S AMENDED AND
RESTATED CODE OF REGULATIONS**

The Board of Directors has approved and recommends your approval of an amendment to the Company s Code of Regulations to add a new provision which would provide that, unless the Company consents in writing to the selection of an alternative forum, the state and federal courts of the State of Ohio will be the sole and exclusive forum for (1) any derivative action or proceeding brought on behalf of the Company, (2) any direct action brought by a shareholder asserting a claim of breach of a fiduciary duty owed by any director, officer or other employee of the Company to the Company or the Company s shareholders, (3) any direct action brought by a shareholder asserting a claim against the Company or any of its directors, officers or other employees alleging a violation of Corporate Matters, or (4) any direct action brought by a shareholder asserting a claim against the Company governed by the internal affairs doctrine in all cases subject to the court having personal jurisdiction over the indispensable parties named as defendants. Corporate Matters means the Corporation Law of the Ohio Revised Code, the Company s Second Amended Articles of Incorporation, as amended, the Code of Regulations, and the bylaws. Through its diverse business, the Company has operations at locations in many different states. Plaintiffs seeking to bring claims against the Company for the matters to which the proposed amendment relates could use the Company s diverse operations to bring duplicative suits in multiple jurisdictions, or to choose a forum state that may not apply Ohio law to the Company s internal affairs in the same manner as the state and federal courts the State of Ohio would be expected to do so. The Board believes that Ohio courts are best suited to address disputes involving the Company given that the Company is incorporated in Ohio, operates a facility in Ohio, and the Ohio courts have expertise in matters involving Ohio law. Although some plaintiffs might prefer to litigate matters in a forum outside of Ohio because another court may be viewed as being more convenient and/or favorable to them, the Board believes that the benefits to the Company and its shareholders, including more efficient litigation, outweigh these concerns. The Ohio courts have expertise in dealing with Ohio corporate law issues and are the most familiar with the application of Ohio law to the matters that could be brought before them. In addition, adoption of this amendment helps to reduce the risk that the Company could be involved in duplicative litigation in more than one forum, as well as the risk that the outcome of cases in multiple forums could be inconsistent even though each forum purports to follow Ohio law. This amendment still gives the Board the flexibility to consent to an alternative forum in instances when the Board deems it appropriate.

The Board of Directors is aware of certain other potential burdens and disadvantages to shareholders in connection with the adoption of an exclusive forum clause, including that plaintiffs who wish to file actions in multiple jurisdictions against the Company and/or its directors, officers and/or employees to increase the settlement value of their actions by increasing the Company s costs to defend against multiple actions would prefer to be able to file actions in multiple jurisdictions. It is also possible that the exclusive forum clause could reduce the likelihood of litigation against the Company and its directors, officers and employees, which litigation may be in pursuit of matters beneficial to the Company and its shareholders if successful. Lastly, the Board of Directors is aware that certain proxy advisors and institutional holders may not support the adoption of an exclusive forum clause unless it can be shown that the Company has already suffered material harm as a result of multiple actions in different jurisdictions regarding the same matter.

However, the Company and the Board of Directors has reviewed these potential burdens and disadvantages and believes that the adoption of the exclusive forum clause is in the best interests of the Company and its shareholders. The Company and the Board of Directors have maintained strong governance standards based on best practices, many of which are described in this Proxy Statement. Accordingly, from a governance perspective the Board of Directors believes that it is more beneficial to the Company and its shareholders to take preventative action before the Company and shareholders are harmed by the practice of actions being filed in plaintiff s favorite jurisdiction or multiple jurisdictions.

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If approved, this provision would require that state courts in which applicable claims are asserted in contravention of the proposed amendment be willing to enforce its terms. It cannot be assured that all state courts will determine such a provision to be enforceable or will be willing to force the transfer of such proceedings to the Ohio courts.

The proposed amendment would amend the Code of Regulations of the Company to add a new Article VII, the full text of which is attached hereto as Appendix A. You should read Appendix A in its entirety before making a decision as to how to vote your shares in connection with Proposal 4.

Vote Required for Approval

Approval of the proposal requires the affirmative vote of a majority of the shares of our common stock present in person or represented by proxy and entitled to be voted on the proposal at the Annual Meeting. Broker non-votes are not counted for purposes of this Proposal. Abstentions will be counted and will have the effect of a negative vote against the Proposal.

Board Recommendation

The Board recommends a vote FOR approval of the amendment to the Company's Amended and Restated Code of Regulations as set forth in Proposal 4.

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PROPOSAL 5

**PROPOSAL TO RE-APPROVE THE MATERIAL TERMS OF THE
PERFORMANCE GOALS SPECIFIED IN THE SPARTON CORPORATION 2010
LONG-TERM STOCK INCENTIVE PLAN**

Background

The Sparton Corporation 2010 Long-Term Stock Incentive Plan was approved by the Board and by the Company's shareholders at the 2009 Annual Meeting of Shareholders, and was amended effective as of June 24, 2010 to modify the definition of Change of Control and effective as of September 1, 2014 to allow for the deferral of the payment of certain awards or grants (as so amended, the 2010 LTIP). The provisions of the 2010 LTIP are intended to ensure that the tax deductibility of payments under the 2010 LTIP is not limited by Section 162(m) of the Internal Revenue Code of 1986, as amended (the Code).

Shareholders are being asked to re-approve the material terms of the performance goals that are a part of the 2010 LTIP so that the Company may deduct from its U.S. Federal corporate income taxes the full amount of any incentive awards paid under the 2010 LTIP that otherwise qualify as qualified performance-based compensation under Section 162(m) of the Code (the Section 162(m) Re-approval). There has been no change to the material terms of the performance goals from those previously approved by shareholders. The Board and the Compensation Committee have re-approved the material terms of the performance goals, subject to approval by shareholders. The material terms will become effective upon Section 162(m) Re-approval. If Section 162(m) Re-approval is not received from shareholders at the Annual Meeting, while performance-based awards could still be granted, the Company would not be able to deduct compensation in excess of \$1 million to Covered Employees for federal income tax purposes.

If Section 162(m) Re-approval occurs, the Compensation Committee intends that any performance-based grants under the 2010 LTIP will be designed to satisfy the requirements of Section 162(m) of the Code to permit the deduction for tax purposes of the full amount of such awards.

Shareholders are not being asked to approve any amendments to the 2010 LTIP or to approve the 2010 LTIP itself under this proposal, but are only asked to re-approve the performance measures included in the plan for compliance with Section 162(m) of the Code.

Reasons for Proposal

Under Section 162(m) of the Code, compensation in excess of \$1 million paid in any one year to a public corporation's covered employees who are employed by the corporation at year-end will generally not be deductible for federal income tax purposes unless the compensation is considered qualified performance-based compensation under Section 162(m) of the Code (or another exemption is met, including, but not limited to, instances when options are granted with an exercise or base price at least equal to 100 percent of the fair market value of the stock as of the grant date). Covered employees include the Chief Executive Officer and the four other most highly compensated executive officers as of the last day of the taxable year other than the Chief Executive Officer whose compensation for the taxable year is required to be reported to shareholders (collectively, the Covered Employees).

In order to qualify as qualified performance-based compensation, among other requirements, Section 162(m) of the Code requires that shareholders approve the material terms of the performance goals every five years if the Compensation Committee has the authority to change the targets under a performance goal. The Company has not obtained Section 162(m) Re-approval since the approval of the 2010 LTIP at the 2009 Annual Meeting of Shareholders. Thus, shareholders are being asked to re-approve the materials terms of the performance goals in order for performance-based awards (as described below) made subsequent to October 28, 2014 (five years following shareholder approval of the 2010 LTIP) to be exempt from the \$1 million deduction limitation under

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Section 162(m) of the Code. If the shareholders re-approve the material terms of the performance goals at the Annual Meeting pursuant to Section 162(m) of the Code, then performance-based awards granted to Covered Employees following such shareholder re-approval can be designed to be Section 162(m) compliant awards.

The rules and regulations promulgated under Section 162(m) of the Code are subject to change from time to time, sometimes with retroactive effect. There can be no guarantee, therefore, that amounts potentially subject to the Section 162(m) limitations will be treated by the Internal Revenue Service as qualified performance-based compensation under Section 162(m) of the Code and/or deductible by the Company. A number of requirements must be met under Section 162(m) of the Code in order for particular compensation to so qualify for the exception such that there can be no assurance that qualified performance-based compensation under the 2010 LTIP will be fully deductible under all circumstances.

Section 162(m) Re-approval contemplates no changes to the material terms of the performance goals from those previously approved by shareholders. In accordance with Section 162(m) of the Code, the material terms include the employees eligible to receive compensation; a description of the business criteria on which the performance goal is based; and either the maximum amount of compensation that could be paid to any employee or the formula used to calculate the amount of compensation to be paid to the employee if the performance goal is attained (except that, in the case of a formula based, in whole or in part, on a percentage of salary or base pay, the maximum dollar amount of compensation that could be paid to the employee must be disclosed). The material terms of the performance goals of the 2010 LTIP are summarized below in this Proposal 5.

Eligible Participants

Any directors, officers and employees of the Company and its subsidiaries and affiliates, as well as prospective officers and employees who have accepted offers of employment, may be selected by the Compensation Committee to become participants in the 2010 LTIP. Presently, the Company estimates that approximately fourteen employees, including the Named Executive Officers, are eligible to receive awards each year under the 2010 LTIP.

Types of Awards Under the Plan

The Compensation Committee may grant stock options, stock appreciation rights, restricted stock, restricted stock units, performance awards and other stock-based awards under the 2010 LTIP.

Stock Options

The Compensation Committee may grant stock options qualifying as incentive stock options under the Code (ISOs) and non-qualified stock options. The term of each stock option will be fixed by the Compensation Committee, but may not exceed ten (10) years. The exercise price for each stock option will also be fixed by the Compensation Committee, but may not be less than the fair market value of the Company's common stock on the date of grant. ISOs may only be granted to officers and employees of the Company and corporations connected to it by chains of ownership of voting power representing fifty percent (50%) or more of the total outstanding voting power of all classes of stock of the lower-tier entity. Stock options will vest and become exercisable as determined by the Compensation Committee.

An option holder may pay the exercise price of an option in cash, through tender of shares already owned by the option holder, by pledging the proceeds from the sale of shares in connection with the exercise of the option, or by any combination of these methods.

Restricted Stock

The Compensation Committee may also award restricted stock, that is, shares of the Company's common stock, the vesting and transferability of which is subject to such requirements as the Compensation Committee may

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determine. These requirements may include continued services for a specified period and/or achievement of performance goals. At the discretion of the Compensation Committee, the recipient of restricted stock will be entitled to vote the shares and receive dividends and other distributions, although the Compensation Committee may make any and all dividends and other distributions with respect to restricted stock subject to the same or different vesting conditions as the restricted stock.

Restricted Stock Units

The Compensation Committee may also award restricted stock units, that is, grants representing a specified number of hypothetical shares of the Company's common stock, the vesting of which is subject to such requirements as the Compensation Committee may determine. These requirements may include continued services for a specified period and/or achievement of performance goals. Upon or after vesting, restricted stock units will be settled in cash or shares of the Company's common stock or a combination, as determined by the Compensation Committee. A participant to whom restricted stock units are granted will not have any rights as a shareholder with respect to the units, unless and until they are settled in shares of the Company's common stock, although at the discretion of the Compensation Committee, the recipient of a restricted stock unit award may be entitled to a dividend equivalent right.

Stock Appreciation Rights

The Compensation Committee may grant stock appreciation rights (SARs), with such terms and conditions as are determined by the Compensation Committee. Exercise of a SAR entitles a participant to receive an amount equal to the difference between the fair market value of one share of common stock on the date the SAR is exercised and the grant price, as the case may be, times the number of shares with respect to which the SAR is exercised. The Compensation Committee has discretion to determine whether any SAR will be settled in cash, shares or a combination thereof. SARs expire no more than ten years after the date they are granted.

Performance Awards

Performance awards may be denominated or payable in cash, shares of common stock (including, without limitation, shares of restricted stock), other securities, other awards, or other property. Performance awards confer on the award recipient the right to receive a dollar amount or number of shares upon the attainment of performance measures during a performance period, as established by the Compensation Committee.

Other Stock-Based Awards

Other stock-based awards may be denominated or payable in, valued in whole or in part by reference to, or otherwise based on or related to, shares of common stock of the Company (including, without limitation, securities convertible into shares of common stock), as the Compensation Committee deems consistent with the purpose of the 2010 LTIP. They also may be subject to such additional terms and conditions, including performance measures, not inconsistent with the provisions of the 2010 LTIP, as determined by the Compensation Committee.

Shares Available Under the 2010 LTIP

The maximum number of shares of the Company's common stock that will be available under the 2010 LTIP is 1,000,000. To the extent that any award is forfeited, terminates, expires or lapses without exercise or settlement, the shares subject to such awards forfeited or not delivered as a result thereof shall again be available for awards under the 2010 LTIP. As of June 30, 2014, a total of 499,099 shares were available under the 2010 LTIP.

In the event of (i) a stock dividend, stock split, reverse stock split, share combination, or recapitalization or similar event affecting the capital structure of the Company or (ii) a merger, consolidation, acquisition of

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property or shares, separation, spinoff, reorganization, stock rights offering, liquidation, disaffiliation, or similar event affecting the Company or any of its subsidiaries, the Compensation Committee or the Board of Directors shall make such substitutions or adjustments as it deems appropriate and equitable to (A) the aggregate number and kind of shares or other securities reserved for issuance and delivery under the 2010 LTIP, (B) the various maximum limitations set forth above upon certain types of awards and upon the grants to individuals of certain types of awards, (C) the number and kind of shares or other securities subject to outstanding awards, and (D) the exercise price of outstanding options and stock appreciation rights. Any such adjustment is required to be made in a manner that would be consistent with Section 409A of the Code.

Performance Goals

Section 162(m) of the Code generally places a \$1,000,000 annual limit on a company's tax deduction for compensation paid to a public company's chief executive officer and the other four highest paid officers named in its proxy statement. This limit does not apply to compensation that satisfies the applicable requirements for the performance-based compensation exception (referred to in this proposal as the performance exception), including approval by shareholders of the material terms of the compensation. The approval in 2009 of the 2010 LTIP by the Company's shareholders satisfied and the Section 162(m) Re-approval will continue to satisfy this shareholder approval requirement, and grants under the 2010 LTIP are intended to satisfy the requirements for the performance exception.

The 2010 LTIP incorporates the provisions required so that stock options and SARs will be qualified performance-based awards. These provisions include allowing such stock options and SARs to be granted only by the Compensation Committee, and requiring that their exercise price be not less than the fair market value of the Company's common stock on the date of grant. Therefore, it is expected that all stock options and SARs granted under the 2010 LTIP that are subject to performance goals will qualify for the performance exception. In addition, the 2010 LTIP gives the Compensation Committee the ability to grant restricted stock, restricted stock units and performance-based awards designed to be qualified performance-based awards.

These qualified performance-based awards must be subject to the achievement of performance goals based upon the attainment of specified levels of one or more of the following measures: (a) earnings per share, (b) return measures (including, but not limited to, return on assets, equity or sales), (c) net income (before or after taxes), (d) cash flow (including, but not limited to, operating cash flow and free cash flow), (e) cash flow return on investments, which equals net cash flows divided by owner's equity, (f) earnings before or after taxes, interest, depreciation and/or amortization, (g) internal rate of return or increase in net present value, (h) gross revenues, (i) gross margins or (j) stock price (including, but not limited to, growth measures and total shareholder return). Performance measures may be absolute in their terms or measured against or in relationship to other companies comparably, similarly or otherwise situated and may be based on or adjusted for any other objective goals, events, or occurrences established by the Compensation Committee for a performance period. Such performance measures may be particular to a line of business, subsidiary or other unit or may be based on the performance of the Company generally.

Performance measures may be adjusted by the Compensation Committee in its sole discretion to eliminate the unbudgeted effects of charges for restructurings, charges for discontinued operations, charges for extraordinary items and other unusual or non-recurring items of loss or expense, merger related charges, cumulative effect of accounting changes, the unbudgeted financial impact of any acquisition or divestiture made during the applicable performance period, and any direct or indirect change in the federal corporate tax rate affecting the performance period, each as defined by generally accepted accounting principles and identified in the audited financial statements, notes to the audited financial statements, management's discussion and analysis or other Company filings with the SEC.

In granting qualified performance-based awards other than stock options and SARs, the Compensation Committee must establish the applicable performance measures within the time allowed by the performance

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exception and at a time when achievement of the goals is substantially uncertain, and it must certify the achievement of those goals before the vesting or payment of the qualified performance-based awards. In addition, in order to assure that qualified performance-based awards in fact qualify for the performance exception, the 2010 LTIP provides that (1) except in the event of death, disability, or other events permitted by the performance exception, the achievement of the applicable performance goals may not be waived, and (2) awards may not be amended, and the Compensation Committee may not exercise discretionary authority, in a way that would cause the awards to cease to qualify for the performance exemption.

As one of the factors in its decisions regarding grants under and administration of the 2010 LTIP, the Compensation Committee will consider the anticipated effects of Section 162(m) of the Code. These effects will depend upon a number of factors, including not only whether the grants qualify for the performance exception, but also the timing of executives' vesting in or exercise of previously granted equity awards and receipt of other compensation. Furthermore, interpretations of and changes in the tax laws and other factors beyond the Compensation Committee's control may also affect the deductibility of compensation. For these and other reasons, the Compensation Committee may make grants that do not qualify for the performance exception, and the Company's tax deductions for those grants may be limited or eliminated as a result of the application of Section 162(m) of the Code. Further, if grants vest or are paid on an accelerated basis upon a change in control or a subsequent termination of employment, some or all of the value of that acceleration may be considered an excess parachute payment under Section 280G of the Code, which would result in the imposition of a twenty percent (20%) federal excise tax on the recipients of the excess parachute payments and a loss of the Company's deduction for the excess parachute payments.

Summary of Other Principal Terms of the 2010 LTIP

Attached to this Proxy Statement as [Appendix B](#) is a summary of the principal terms of the 2010 LTIP, other than the terms addressed above, and other related information. The summary is qualified in its entirety by reference to the full text of the 2010 LTIP, which attached to this Proxy Statement as [Appendix C](#).

Vote Required for Approval

Approval of the proposal requires the affirmative vote of a majority of the shares of our common stock present in person or represented by proxy and entitled to be voted on the proposal at the Annual Meeting. Broker non-votes are not counted for purposes of this Proposal. Abstentions will be counted and will have the effect of a negative vote against the Proposal.

Board Recommendation

The Board recommends a vote FOR approval of the amendment to the Company's Amended and Restated Code of Regulations as set forth in Proposal 5.

Table of Contents**STOCK OWNERSHIP AND SECTION 16 COMPLIANCE****Director and Executive Officer Beneficial Ownership**

The following table shows the shares of the Company's common stock beneficially owned (except as noted) by the Named Executive Officers, the members of our Board, and all executive officers and directors of the Company as a group as of June 30, 2014. Named Executive Officers, consistent with Item 402(a) of Regulation S-K promulgated under the Exchange Act, include: (i) the Company's Chief Executive Officer and individuals acting in a similar capacity during fiscal year 2014, regardless of compensation level; (ii) all individuals serving as the Company's Chief Financial Officer or acting in a similar capacity during fiscal year 2014, regardless of compensation level; (iii) the Company's three most highly compensated executive officers other than the Chief Executive Officer and the Chief Financial Officer who were serving as executive officers at the end of fiscal year 2014; and (iv) up to two additional individuals who would have been included under (iii) above but for the fact that the applicable individual was not serving as an executive officer of the Company at the end of fiscal year 2014.

Name of Beneficial Owner	Number of Shares		Shares Underlying Options (2)	Total Number of Shares Beneficially Owned	Percent of Class (3)
	Unrestricted	Restricted (1)			
James D. Fast (4)	30,432			30,432	*
Joseph J. Hartnett	15,604			15,604	*
Charles R. Kummeth	8,022			8,022	*
David P. Molfenter	33,881			33,881	*
Douglas R. Schrank	22,000			22,000	*
James R. Swartwout (5)	32,343			32,343	*
Cary B. Wood	152,987	116,401		269,388	2.66%
Mark Schlei	5,300	25,418		30,718	*
Gordon B. Madlock	13,132	29,347		42,479	*
Michael W. Osborne (6)	25,102	10,750	10,750		
	Yield Enhancement ^(J)			584	
	Preferred Stock (1,599 shares) ^{(C)(F)}		1,599	1,827	
	Common Stock (1,598,616 shares) ^{(C)(F)}			995	
			17,835	19,642	
Noble Logistics, Inc.	Service aftermarket auto parts delivery	Line of Credit, \$0 available (10.5%, Due 1/2015) ^(D)	800	800	340
		Senior Term Debt (11.0%, Due 1/2015) ^(D)	7,227	7,227	3,071
		Senior Term Debt (10.5%, Due	3,650	3,650	1,551

		1/2015) ^(D) Senior Term Debt (10.5%, Due 1/2015) ^{(D)(E)}	3,650	3,650	1,551
		Preferred Stock (1,075,000 shares) ^{(C)(F)}		1,750	
		Common Stock (1,682,444 shares) ^{(C)(F)}		1,682	
				18,759	6,513
Packerland Whey Products, Inc.	Manufacturing dairy, meat, and protein supplements	Preferred Stock (248 shares) ^{(C)(F)}		2,479	
		Common Stock (247 shares) ^{(C)(F)}		21	
				2,500	
Quench Holdings Corp.	Service sales, installation and service of water coolers	Preferred Stock (388 shares) ^{(C)(F)}		2,950	1,639
		Common Stock (35,242 shares) ^{(C)(F)}		447	
				3,397	1,639
Total Affiliate Investments (represents 13.0% of total investments at fair value)				\$ 50,706	\$ 37,248

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GLADSTONE INVESTMENT CORPORATION
CONDENSED CONSOLIDATED SCHEDULE OF INVESTMENTS (Continued)

SEPTEMBER 30, 2013

(DOLLAR AMOUNTS IN THOUSANDS)

(UNAUDITED)

Company ^(A)	Industry	Investment ^(B)	Principal	Cost	Fair Value
NON-CONTROL/NON-AFFILIATE INVESTMENTS:					
B-Dry, LLC	Service basement waterproofer	Line of Credit, \$0 available (6.5%, Due 5/2014) ^(D)	\$ 750	\$ 750	\$ 188
		Senior Term Debt (14.0%, Due 5/2014) ^(D)	6,433	6,443	1,610
		Senior Term Debt (14.0%, Due 5/2014) ^(D)	2,840	2,840	710
		Common Stock Warrants (85 shares) ^{(C)(F)}		300	
				10,333	2,508
Funko, LLC	Retail designer and distributor of pop-culture collectibles	Senior Subordinated Term Debt (12.0% and 1.5% PIK, Due 5/2019) ^(D)	7,530	7,530	7,530
		Preferred Stock (1,250 shares) ^{(C)(F)}		1,250	1,646
				8,780	9,176
Schylling Investments, LLC	Retail and Service designer and distributor of children's toys	Senior Term Debt (13.0%, Due 8/2017) ^(H)	16,000	16,000	16,000
		Preferred Stock (4,000,000 shares) ^{(C)(F)(H)}		4,000	4,000
				20,000	20,000
Total Non-Control/Non-Affiliate Investments (represents 11.0% of total investments at fair value)				\$ 39,113	\$ 31,684
TOTAL INVESTMENTS				\$ 354,241	\$ 287,212

(A) Certain of the securities listed above are issued by affiliate(s) of the indicated portfolio company.

- (B) Percentages represent the weighted average cash interest rates in effect at September 30, 2013, and due date represents the contractual maturity date. If applicable, paid in kind (PIK) interest rates are noted separately from the cash interest rates.
- (C) Security is non-income producing.
- (D) Fair value based primarily on opinions of value submitted by Standard & Poor s Securities Evaluations, Inc. as of September 30, 2013.
- (E) Last Out Tranche (LOT) of senior debt, meaning if the portfolio company is liquidated, the holder of the LOT is paid after the other senior debt but before the senior subordinated debt.
- (F) Where applicable, aggregates all shares of such class of stock owned without regard to specific series owned within such class (some series of which may or may not be voting shares) or aggregates all warrants to purchase shares of such class of stock owned without regard to specific series of such class of stock such warrants allow us to purchase.
- (G) Debt security is on non-accrual status.
- (H) New proprietary portfolio investment valued at cost, as it was determined that the price paid during the three months ended September 30, 2013 best represents fair value as of September 30, 2013.
- (I) \$5.0 million of the debt security participated to a third party but accounted for as collateral for a secured borrowing for GAAP purposes.
- (J) Security was exited, subsequent to September 30, 2013, and was valued based on the payoff.

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.

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GLADSTONE INVESTMENT CORPORATION
CONDENSED CONSOLIDATED SCHEDULE OF INVESTMENTS

MARCH 31, 2013

(DOLLAR AMOUNTS IN THOUSANDS)

Company ^(A)	Industry	Investment ^(B)	Principal	Cost	Fair Value	
CONTROL INVESTMENTS:						
Acme Cryogenics, Inc.	Manufacturing manifolds and pipes for industrial gasses	Senior Subordinated Term Debt (11.5%, Due 3/2015)	\$ 14,500	\$ 14,500	\$ 14,500	
		Preferred Stock (898,814 shares) ^(F)		6,984	11,292	
		Common Stock (418,072 shares) ^{(C)(F)}			1,045	1,179
		Common Stock Warrants (465,639 shares) ^{(C)(F)}			25	369
				22,554	27,340	
ASH Holdings Corp.	Retail and Service school buses and parts	Line of Credit, \$288 available (3.0%, Due 3/2015) ^(G)	7,912	7,856		
		Senior Subordinated Term Debt (2.0%, Due 3/2015) ^(G)	6,250	6,050		
		Preferred Stock (4,644 shares) ^{(C)(F)}			2,500	
		Common Stock (1 share) ^{(C)(F)}				
		Common Stock Warrants (73,599 shares) ^{(C)(F)}				4
		Guaranty (\$500)				
				16,410		
Country Club Enterprises, LLC	Service golf cart distribution	Senior Subordinated Term Debt (18.6%, Due 11/2014)	4,000	4,000	4,000	
		Preferred Stock (7,304,792 shares) ^{(C)(F)}			7,725	3,467
		Guaranty (\$2,000)				
		Guaranty (\$1,370)				
				11,725	7,467	
Danco Acquisition Corp.	Manufacturing machining and sheet metal work	Line of Credit, \$282 available (4.0%, Due 8/2015) ^(D)	2,868	2,868	717	
		Senior Term Debt (4.0%, Due 8/2015) ^(D)	2,575	2,575	644	
		Senior Term Debt (4.0%, Due 8/2015) ^(D)	8,795	8,795	2,199	

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		Senior Term Debt (5.0%, Due 8/2015) ^{(D)(E)}	1,150	1,150	287
		Preferred Stock (25 shares) ^{(C)(F)}		2,500	
		Common Stock Warrants (420 shares) ^{(C)(F)}		3	
				17,891	3,847
Drew Foam Company, Inc.	Manufacturing molds and fabricates expanded polystyrene	Senior Term Debt (13.5%, Due 8/2017)	10,913	10,913	10,913
		Preferred Stock (34,045 shares) ^(F)		3,375	3,511
		Common Stock (5,372 shares) ^{(C)(F)}		63	676
				14,351	15,100
Frontier Packaging, Inc.	Manufacturing packaging products	Senior Term Debt (12.0%, Due 12/2017)	12,500	12,500	12,500
		Preferred Stock (1,373 shares) ^{(C)(F)}		1,373	653
		Common Stock (152 shares) ^{(C)(F)}		153	
				14,026	13,153
Galaxy Tool Holding Corp.	Manufacturing aerospace and plastics	Senior Subordinated Term Debt (13.5%, Due 8/2017)	15,520	15,520	15,520
		Preferred Stock (5,373,186 shares) ^(F)		11,464	5,356
		Common Stock (48,093 shares) ^{(C)(F)}		48	
				27,032	20,876
Ginsey Home Solutions, Inc.	Retail and Service children and home products	Senior Subordinate Term Debt (13.5%, Due 1/2018)	13,050	13,050	13,050
		Preferred Stock (18,898 shares) ^{(C)(F)}		9,393	8,783
		Common Stock (63,747 shares) ^{(C)(F)}		8	
				22,451	21,833
Mathey Investments, Inc.	Manufacturing pipe-cutting and pipe-fitting equipment	Senior Term Debt (10.0%, Due 3/2014)	1,375	1,375	1,375
		Senior Term Debt (12.0%, Due 3/2014)	3,727	3,727	3,727
		Senior Term Debt (12.5%, Due 3/2014) ^(E)	3,500	3,500	3,500
		Common Stock (29,102 shares) ^{(C)(F)}		777	5,817
				9,379	14,419
Mitchell Rubber Products, Inc.	Manufacturing rubber compounds	Subordinated Term Debt (13.0%, Due 10/2016) ^(D)	13,560	13,560	13,679
		Preferred Stock (27,900 shares) ^{(C)(F)}		2,790	3,051
		Common Stock (27,900 shares) ^{(C)(F)}		28	
				16,378	16,730

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Precision Southeast, Inc.	Manufacturing injection molding and plastics	Senior Term Debt (14.0%, Due 12/2015)	7,775	7,775	7,775
		Preferred Stock (19,091 shares) ^{(C)(F)}		1,909	2,273
		Common Stock (90,909 shares) ^{(C)(F)}		91	955
				9,775	11,003

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GLADSTONE INVESTMENT CORPORATION
CONDENSED CONSOLIDATED SCHEDULE OF INVESTMENTS (Continued)

MARCH 31, 2013

(DOLLAR AMOUNTS IN THOUSANDS)

Company ^(A)	Industry	Investment ^(B)	Principal	Cost	Fair Value	
SBS, Industries, LLC	Manufacturing specialty fasteners and threaded screw products	Senior Term Debt (14.0%, Due 8/2016)	\$ 11,355	\$ 11,355	\$ 11,355	
		Preferred Stock (19,935 shares) ^{(C)(F)}		1,994	2,253	
		Common Stock (221,500 shares) ^{(C)(F)}		221	4,635	
				13,570	18,243	
SOG Specialty K&T, LLC	Manufacturing specialty knives and tools	Senior Term Debt (13.3%, Due 8/2016)	6,200	6,200	6,200	
		Senior Term Debt (14.8%, Due 8/2016)	12,199	12,199	12,199	
		Preferred Stock (9,749 shares) ^{(C)(F)}		9,749	11,423	
				28,148	29,822	
Tread Corp.	Manufacturing storage and transport equipment	Line of Credit, \$1,014 available (12.5%, Due 6/2013) ^(G)	1,736	1,736		
		Senior Subordinated Term Debt (12.5%, Due 5/2013) ^(G)	5,000	5,000		
		Senior Subordinated Term Debt (12.5%, Due 5/2013) ^(G)	2,750	2,750		
		Senior Subordinated Term Debt (12.5%, Due 5/2015) ^(G)	1,000	1,000		
		Senior Subordinated Term Debt (12.5%, Due on Demand) ^{(D)(G)}	510	510		
		Preferred Stock (3,332,765 shares) ^{(C)(F)}			3,333	
		Common Stock (7,716,320 shares) ^{(C)(F)}			501	
		Common Stock Warrants (2,372,727 shares) ^{(C)(F)}				3
			14,833			
Venyu Solutions, Inc.	Service online servicing suite	Senior Subordinated Term Debt (11.3%, Due 10/2015)	7,000	7,000	7,000	
			12,000	12,000	12,000	

Senior Subordinated Term Debt (14.0%, Due 10/2015)		
Preferred Stock (5,400 shares) ^{(C)(F)}	6,000	24,970
	25,000	43,970

Total Control Investments (represents 85.1% of total investments at fair value)	\$ 263,522	\$ 243,803
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GLADSTONE INVESTMENT CORPORATION
CONDENSED CONSOLIDATED SCHEDULE OF INVESTMENTS (Continued)

MARCH 31, 2013

(DOLLAR AMOUNTS IN THOUSANDS)

Company ^(A)	Industry	Investment ^(B)	Principal	Cost	Fair Value
AFFILIATE INVESTMENTS:					
Cavert II Holding Corp.	Manufacturing bailing wire	Senior Subordinated Term Debt (11.8%, Due 4/2016) ^(D)	\$ 2,200	\$ 2,200	\$ 2,258
		Subordinated Term Debt (13.0%, Due 4/2016) ^(D)	4,671	4,671	4,805
		Preferred Stock (18,446 shares) ^{(C)(F)}		1,844	2,803
				8,715	9,866
Channel Technologies Group, LLC	Manufacturing acoustic products	Line of Credit, \$0 available (7.0%, Due 5/2013) ^(D)	1,250	1,250	1,248
		Senior Term Debt (8.3%, Due 12/2014) ^(D)	5,596	5,596	5,589
		Senior Term Debt (12.3%, Due 12/2016) ^(D)	10,750	10,750	10,737
		Preferred Stock (1,599 shares) ^{(C)(F)}		1,599	275
		Common Stock (1,598,616 shares) ^{(C)(F)}			
				19,195	17,849
Noble Logistics, Inc.	Service aftermarket auto parts delivery	Line of Credit, \$0 available (10.5%, Due 1/2015) ^(D)	800	800	360
		Senior Term Debt (11.0%, Due 1/2015) ^(D)	7,227	7,227	3,252
		Senior Term Debt (10.5%, Due 1/2015) ^(D)	3,650	3,650	1,643
		Senior Term Debt (10.5%, Due 1/2015) ^{(D)(E)}	3,650	3,650	1,643
		Preferred Stock (1,075,000 shares) ^{(C)(F)}			1,750
		Common Stock (1,682,444 shares) ^{(C)(F)}			1,682

			18,759	6,898
Packerland Whey Products, Inc.	Manufacturing dairy, meat, and protein supplements	Preferred Stock (248 shares) ^{(C)(F)} Common Stock (247 shares) ^{(C)(F)}	2,479 21	367
			2,500	367
Quench Holdings Corp.	Service sales, installation and service of water coolers	Preferred Stock (388 shares) ^{(C)(F)} Common Stock (35,242 shares) ^{(C)(F)}	2,950 447	1,679
			3,397	1,679

Total Affiliate Investments (represents 12.8% of total investments at fair value)

\$ 52,566 \$ 36,659

NON-CONTROL/NON-AFFILIATE INVESTMENTS:

B-Dry, LLC	Service basement waterproofer	Line of Credit, \$0 available (6.5%, Due 5/2014) ^(D) Senior Term Debt (14.0%, Due 5/2014) ^(D) Senior Term Debt (14.0%, Due 5/2014) ^(D) Common Stock Warrants (85 shares) ^{(C)(F)}	\$ 750 6,433 2,840	\$ 750 6,443 2,840	\$ 450 3,866 1,704
				300	
				10,333	6,020

Total Non-Control/Non-Affiliate Investments (represents 2.1% of total investments at fair value)

\$ 10,333 \$ 6,020

TOTAL INVESTMENTS^(H)

\$ 326,421 \$ 286,482

- (A) Certain of the listed securities are issued by affiliate(s) of the indicated portfolio company.
- (B) Percentages represent the weighted average interest rates in effect as of March 31, 2013, and due date represents the contractual maturity date.
- (C) Security is non-income producing.
- (D) Fair value based primarily on opinions of value submitted by Standard & Poor's Securities Evaluations, Inc. as of March 31, 2013.
- (E) LOT of senior debt, meaning if the portfolio company is liquidated, the holder of the LOT is paid after the other senior debt and before the senior subordinated debt.
- (F) Where applicable, aggregates all shares of such class of stock owned without regard to specific series owned within such class, some series of which may or may not be voting shares or aggregates all warrants to purchase shares of such class of stock owned without regard to specific series of such class of stock such warrants allow us to purchase.
- (G) Debt security is on non-accrual status.
- (H)

Aggregate gross unrealized depreciation for federal income tax purposes is \$78,959; aggregate gross unrealized appreciation for federal income tax purposes is \$38,650. Net unrealized depreciation is \$40,309 based on a tax cost of \$326,792.

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.

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GLADSTONE INVESTMENT CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2013

**(DOLLAR AMOUNTS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA AND AS
OTHERWISE INDICATED)**

NOTE 1. ORGANIZATION

Gladstone Investment Corporation (Gladstone Investment) was incorporated under the General Corporation Law of the State of Delaware on February 18, 2005, and completed an initial public offering on June 22, 2005. The terms the Company, we, our and us all refer to Gladstone Investment and its consolidated subsidiaries. We are an externally advised, closed-end, non-diversified management investment company that has elected to be treated as a business development company (BDC) under the Investment Company Act of 1940, as amended (the 1940 Act). In addition, we have elected to be treated for tax purposes as a regulated investment company (RIC) under the Internal Revenue Code of 1986, as amended (the Code). We were established for the purpose of investing in debt and equity securities of established private businesses in the United States (U.S.). Debt investments primarily come in the form of three types of loans: senior term loans, senior subordinated loans and junior subordinated debt. Equity investments primarily take the form of preferred or common equity (or warrants or options to acquire the foregoing), often in connection with buyouts and other recapitalizations. To a much lesser extent, we may also invest in syndicated loans. Our investment objectives are: (a) to achieve and grow current income by investing in debt securities of established businesses that we believe will provide stable earnings and cash flow to pay expenses, make principal and interest payments on our outstanding indebtedness and make distributions to stockholders that grow over time, and (b) to provide our stockholders with long-term capital appreciation in the value of our assets by investing in equity securities of established businesses that we believe can grow over time to permit us to sell our equity investments for capital gains. We aim to maintain a portfolio allocation of approximately 80% debt investments and 20% equity investments, at cost.

Gladstone Business Investment, LLC (Business Investment), a wholly-owned subsidiary of ours, was established on August 11, 2006 for the sole purpose of owning our portfolio of investments in connection with our line of credit. The financial statements of Business Investment are consolidated with those of Gladstone Investment. We also have significant subsidiaries whose financial statements are not consolidated with ours. Refer to Note 13 *Unconsolidated Significant Subsidiaries* for additional information regarding our unconsolidated significant subsidiaries.

We are externally managed by Gladstone Management Corporation (the Adviser), an affiliate of ours and a Securities and Exchange Commission (SEC) registered investment adviser, pursuant to an investment advisory agreement and management agreement.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Unaudited Interim Financial Statements and Basis of Presentation

We prepare our interim financial statements in accordance with accounting principles generally accepted in the U.S. (GAAP) for interim financial information and pursuant to the requirements for reporting on Form 10-Q and Articles 6

and 10 of Regulation S-X. Accordingly, we have omitted certain disclosures accompanying annual financial statements prepared in accordance with GAAP. The accompanying condensed consolidated financial statements include our accounts and those of our wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated. Under Article 6 of Regulation S-X, and the authoritative accounting guidance provided by the American Institute of Certified Public Accountants Audit and Accounting Guide for Investment Companies, we are not permitted to consolidate any portfolio company investments, including those in which we have a controlling interest. In our opinion, all adjustments, consisting solely of normal recurring accruals, necessary for the fair statement of financial statements for the interim periods have been included. The results of operations for the three months and six months ended September 30, 2013, are not necessarily indicative of results that ultimately may be achieved for the year. The interim financial statements and notes thereto should be read in conjunction with the financial statements and notes thereto included in our annual report on Form 10-K for the fiscal year ended March 31, 2013, as filed with the SEC on May 14, 2013.

Our fiscal year-end *Condensed Consolidated Statement of Assets and Liabilities* presented in this Form 10-Q was derived from audited financial statements, but does not include all disclosures required by GAAP.

Investment Valuation Policy

We carry our investments at fair value to the extent that market quotations are readily available and reliable and otherwise at fair value as determined in good faith by our board of directors (our Board of Directors or the Board). In determining the fair value of our investments, the Adviser has established an investment valuation policy (the Policy). The Policy has been approved by our Board,

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and our Board reviews the Policy quarterly to determine if changes thereto are advisable. Additionally, our Board reviews whether the Adviser has applied the Policy consistently and votes whether to accept the recommended valuation of our investment portfolio. Such determination of fair values may involve subjective judgments and estimates.

The Adviser uses generally accepted valuation techniques to value our portfolio unless it has specific information about the value of an investment to determine otherwise. From time to time, the Adviser may accept an appraisal of a business in which we hold securities. These appraisals are expensive and occur infrequently, but provide a third-party valuation opinion that may differ in results, techniques and scope used by the Adviser to value our investments. When the Adviser obtains these specific third-party appraisals, the Adviser uses estimates of value provided by such appraisals and its own assumptions, including estimated remaining life, current market yield and interest rate spreads of similar securities as of the measurement date, to value our investments.

The Policy, summarized below, applies to publicly traded securities, securities for which a limited market exists and securities for which no market exists.

Publicly-traded securities: The Adviser determines the value of publicly-traded securities based on the closing price for the security on the exchange or securities market on which it is listed and primarily traded on the valuation date. To the extent that we own restricted securities that are not freely tradable, but for which a public market otherwise exists, the Adviser will use the market value of the securities, adjusted for any decrease in value resulting from the restrictive feature. As of September 30 and March 31, 2013, we did not have any investments in publicly-traded securities.

Securities for which a limited market exists: The Adviser values securities that are not traded on an established secondary securities market but for which a limited market for the security exists, such as certain participations in, or assignments of, syndicated loans, at the quoted bid price, which are non-binding. In valuing these assets, the Adviser assesses trading activity in an asset class and evaluates variances in prices and other market insights to determine if any available quoted prices are reliable. In general, if the Adviser concludes that quotes based on active markets or trading activity may be relied upon, firm bid prices are requested; however, if firm bid prices are unavailable, the Adviser bases the value of the security upon the indicative bid price (IBP) offered by the respective originating syndication agent's trading desk, or secondary desk, on or near the valuation date. To the extent that the Adviser uses the IBP as a basis for valuing the security, the Adviser may take further steps to consider additional information to validate that price in accordance with the Policy, including but not limited to reviewing a range of indicative bids to the extent it has ready access to such qualified information.

In the event these limited markets become illiquid such that market prices are no longer readily available, the Adviser will value our syndicated loans using alternative methods, such as estimated net present values of the future cash flows, or discounted cash flows (DCF). The use of a DCF methodology follows that prescribed by the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 820, Fair Value Measurements and Disclosures, which provides guidance on the use of a reporting entity's own assumptions about future cash flows and risk-adjusted discount rates when relevant, observable inputs, such as quotes in active markets, are not available. When relevant, observable market data does not exist, an alternative outlined in ASC 820 is the valuation of investments based on DCF. For the purposes of using DCF to provide fair value estimates, the Adviser considers multiple inputs, such as a risk-adjusted discount rate that incorporates adjustments that market participants would make, both for nonperformance and liquidity risks. As such, the Adviser develops a modified discount rate approach that incorporates risk premiums including, among other things, increased probability of default, higher loss given default or increased liquidity risk. The DCF valuations applied to the syndicated loans provide an estimate of what the Adviser believes a market participant would pay to purchase a syndicated loan in an active market, thereby

establishing a fair value. The Adviser applies the DCF methodology in illiquid markets until quoted prices are available or are deemed reliable based on trading activity. As of September 30 and March 31, 2013, we had no securities for which a limited market exists.

Securities for which no market exists: The Adviser's valuation methodology for securities for which no market exists falls into four categories: (A) portfolio investments comprised solely of debt securities; (B) portfolio investments in controlled companies comprised of a bundle of securities, which can include debt and equity securities; (C) portfolio investments in non-controlled companies comprised of a bundle of investments, which can include debt and equity securities; and (D) portfolio investments comprised of non-publicly traded, non-control equity securities of other funds.

- (A) **Portfolio investments comprised solely of debt securities:** Debt securities for which no market exists (Non-Public Debt Securities), and that are issued by portfolio companies in which we have no equity or equity-like securities, are fair valued utilizing opinions of value submitted to us by Standard & Poor's Securities Evaluations, Inc. (SPSE). The Adviser may also submit paid-in-kind (PIK) interest to SPSE for its evaluation when it is determined that PIK interest is likely to be received.
- (B) **Portfolio investments in controlled companies comprised of a bundle of investments, which can include debt and equity securities:** The fair value of these investments is determined based on the total enterprise value (TEV) of the portfolio company, or issuer, utilizing a liquidity waterfall approach under ASC 820 for our Non-Public Debt Securities and equity or equity-like securities (e.g., preferred equity, common equity or other equity-like securities) that are purchased together as part of a

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package where we have control or could gain control through an option or warrant security; both the debt and equity securities of the portfolio investment would exit in the mergers and acquisitions market as the principal market, generally through a sale or recapitalization of the portfolio company. We generally exit the debt and equity securities of an issuer at the same time. Applying the liquidity waterfall approach to all of our investments in an issuer, the Adviser first calculates the TEV of the issuer by incorporating some or all of the following factors:

the issuer's ability to make payments;

the earnings of the issuer;

recent sales to third parties of similar securities;

the comparison to publicly-traded securities; and

DCF or other pertinent factors.

In gathering the sales to third parties of similar securities, the Adviser generally references industry statistics and may use outside experts. TEV is only an estimate of value and may not be the value received in an actual sale. Once the Adviser has estimated the TEV of the issuer, it will subtract the value of all the debt securities of the issuer, which are valued at the contractual principal balance. Fair values of these debt securities are discounted for any shortfall of TEV over the total debt outstanding for the issuer. Once the values for all outstanding senior securities, which include all the debt securities, have been subtracted from the TEV of the issuer, the remaining amount, if any, is used to determine the value of the issuer's equity or equity-like securities. If, in the Adviser's judgment, the liquidity waterfall approach does not accurately reflect the value of the debt component, the Adviser may recommend that we use a valuation by SPSE, or, if that is unavailable, a DCF valuation technique.

(C) Portfolio investments in non-controlled companies comprised of a bundle of investments, which can include debt and equity securities: The Adviser values Non-Public Debt Securities that are purchased together with equity or equity-like securities from the same portfolio company, or issuer, for which we do not control or cannot gain control as of the measurement date, using a hypothetical, secondary market as our principal market. In accordance with ASC 820 (as amended by the FASB's Accounting Standards Update No. 2011-04, Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and International Financial Reporting Standards (IFRS)), (ASU 2011-04)), the Adviser has defined our unit of account at the investment level (either debt or equity) and, as such, determines our fair value of these non-control investments assuming the sale of an individual security using the standalone premise of value. As such, the Adviser estimates the fair value of the debt component using estimates of value provided by SPSE and its own assumptions in the absence of observable market data, including synthetic credit ratings, estimated remaining life, current market yield and interest rate spreads of similar securities as of the measurement date. For equity or equity-like securities of investments for which we do not control or cannot gain control as of the measurement date, the Adviser estimates the fair value of the equity based on factors such as the overall value of the issuer, the relative fair value of other units of account, including debt, or other relative value

approaches. Consideration is also given to capital structure and other contractual obligations that may impact the fair value of the equity. Furthermore, the Adviser may utilize comparable values of similar companies, recent investments and indices with similar structures and risk characteristics or DCF valuation techniques and, in the absence of other observable market data, its own assumptions.

(D) Portfolio investments comprised of non-publicly traded, non-control equity securities of other funds: The Adviser generally values any uninvested capital of the non-control fund at par value and values any invested capital at the value provided by the non-control fund. As of September 30 and March 31, 2013, we had no non-control equity securities of other funds.

Due to the uncertainty inherent in the valuation process, such estimates of fair value may differ significantly and materially from the values that would have been obtained had a ready market for the securities existed. Additionally, changes in the market environment and other events that may occur over the life of the investments may cause the gains or losses ultimately realized on these investments to be different than the valuations currently assigned. There is no single standard for determining fair value in good faith, as fair value depends upon circumstances of each individual case. In general, fair value is the amount that the Adviser might reasonably expect us to receive upon the current sale of the security in an orderly transaction between market participants at the measurement date.

Refer to Note 3 *Investments* for additional information regarding fair value measurements and our application of ASC 820.

Interest Income Recognition

Interest income, adjusted for amortization of premiums, amendment fees and acquisition costs and the accretion of discounts, is recorded on the accrual basis to the extent that such amounts are expected to be collected. Generally, when a loan becomes 90 days or more past due, or if our qualitative assessment indicates that the debtor is unable to service its debt or other obligations, we will place the loan on non-accrual status and cease recognizing interest income on that loan until the borrower has demonstrated the ability and intent to pay contractual amounts due. However, we remain contractually entitled to this interest. Interest payments received on non-accrual loans may be recognized as income or applied to the cost basis, depending upon management's judgment. Generally, non-accrual loans are restored to accrual status when past-due principal and interest are paid, and, in management's judgment, are likely to

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remain current, or due to a restructuring, the interest income is deemed to be collectible. As of September 30, 2013, loans to two portfolio companies, ASH Holdings Corp. (ASH) and Tread Corp. (Tread), were on non-accrual, with an aggregate debt cost basis of \$25.9 million, or 9.9% of the cost basis of all debt investments in our portfolio, and an aggregate fair value of \$0. As of March 31, 2013, ASH and Tread were on non-accrual, with an aggregate debt cost basis of \$24.9 million, or 10.4% of the cost basis of all debt investments in our portfolio, and an aggregate fair value of \$0.

PIK interest, computed at the contractual rate specified in the loan agreement, is added to the principal balance of the loan and recorded as interest income. To maintain our status as a RIC, this non-cash source of income must be included in our calculation of distributable income for purposes of complying with our distribution requirements, even though we have not yet collected the cash. During the three and six months ended September 30, 2013, we recorded PIK income of \$29 and \$39, respectively. We did not hold any loans in our portfolio that contained a PIK provision as of September 30, 2012 and no PIK income was recorded during the three and six months ended September 30, 2012.

Other Income Recognition

We generally record success fees upon receipt of cash. Success fees are contractually due upon a change of control in a portfolio company. We recorded \$2.1 million and \$2.3 million of success fees during the three and six months ended September 30, 2013, respectively. During the three months ended September 30, 2013, we received \$0.3 million from Cavert II Holding Corp. (Cavert) in success fee prepayments and we received \$1.8 million related to the exit of Venyu Solutions, Inc. (Venyu). During the three and six months ended September, 30, 2012, we recorded \$0.4 million and \$0.8 million of success fees, respectively, representing prepayments received from Mathey Investments, Inc. (Mathey) and Cavert.

We accrue dividend income on preferred and common equity securities to the extent that such amounts are expected to be collected and if we have the option to collect such amounts in cash or other consideration. For the three and six months ended September 30, 2013, we recorded \$1.4 million in dividend income related to the exit of Venyu. We recorded \$0.1 million in dividend income during the three and six months ended September 30, 2012 on accrued preferred shares of Drew Foam Company, Inc. (Drew Foam).

Both dividends and success fees are recorded in Other income in our accompanying *Condensed Consolidated Statements of Operations*.

Recent Accounting Pronouncements

In June 2013, the FASB issued ASU 2013-08, Financial Services Investment Companies (Topic 946): Amendments to the Scope, Measurement, and Disclosure Requirements, which amends the criteria that define an investment company and clarifies the measurement guidance and requires new disclosures for investment companies. Under ASU 2013-08, an entity already regulated under the 1940 Act is automatically an investment company under the new GAAP definition, so we anticipate no impact from adopting this standard on our financial position or results of operations. We are currently assessing whether additional disclosure requirements will be necessary. ASU 2013-08 is effective for interim and annual reporting periods in fiscal years that begin after December 15, 2013.

Table of Contents**NOTE 3. INVESTMENTS**

ASC 820 defines fair value, establishes a framework for measuring fair value and expands disclosures about assets and liabilities measured at fair value. ASC 820 provides a consistent definition of fair value that focuses on exit price in the principal, or most advantageous, market and prioritizes, within a measurement of fair value, the use of market-based inputs over entity-specific inputs. ASC also establishes the following three-level hierarchy for fair value measurements based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date.

Level 1 inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets;

Level 2 inputs to the valuation methodology include quoted prices for similar assets and liabilities in active or inactive markets and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument. Level 2 inputs are in those markets for which there are few transactions, the prices are not current, little public information exists or instances where prices vary substantially over time or among brokered market makers; and

Level 3 inputs to the valuation methodology are unobservable and significant to the fair value measurement. Unobservable inputs are those inputs that reflect assumptions that market participants would use when pricing the asset or liability and can include the Adviser's assumptions based upon the best available information.

As of September 30 and March 31, 2013, all of our investments were valued using Level 3 inputs. We transfer investments in and out of Level 1, 2 and 3 securities as of the beginning balance sheet date, based on changes in the use of observable and unobservable inputs utilized to perform the valuation for the period. During the three and six months ended September 30, 2013 and 2012, there were no transfers in or out of Level 1, 2 and 3.

The following table presents the financial assets carried at fair value as of September 30 and March 31, 2013, by caption on our accompanying *Condensed Consolidated Statements of Assets and Liabilities* and by security type for each of the three applicable levels of hierarchy established by ASC 820 that we used to value our financial assets:

	September 30, 2013			March 31, 2013		
	Total Recurring Fair Value Measurement Reported in <i>Condensed Consolidated Statements of Assets and Liabilities</i>			Total Recurring Fair Value Measurement Reported in <i>Condensed Consolidated Statements of Assets and Liabilities</i>		
	Level 1	Level 3		Level 1	Level 3	
Control Investments						
Senior debt	\$	\$ 93,026	\$ 93,026	\$	\$ 73,391	\$ 73,391
Senior subordinated debt		60,664	60,664		79,748	79,748
Preferred equity		50,490	50,490		77,032	77,032
Common equity/equivalents		14,100	14,100		13,632	13,632

Total Control Investments		218,280	218,280	243,803	243,803				
Affiliate Investments									
Senior debt		23,334	23,334	24,471	24,471				
Senior subordinated debt		6,546	6,546	7,063	7,063				
Preferred equity		6,373	6,373	5,125	5,125				
Common equity/equivalents		995	995						
Total Affiliate Investments		37,248	37,248	36,659	36,659				
Non-Control/Non-Affiliate Investments									
Senior debt		18,508	18,508	6,020	6,020				
Senior subordinated debt		7,530	7,530						
Preferred equity		5,646	5,646						
Total Non-Control/Non-Affiliate Investments		31,684	31,684	6,020	6,020				
Total Investments at fair value	\$	\$ 287,212	\$	287,212	\$	\$ 286,482	\$	286,482	
Cash Equivalents		25,000		25,000		65,000		65,000	
Total Investments and Cash Equivalents		\$ 25,000	\$ 287,212	\$	312,212	\$ 65,000	\$ 286,482	\$	351,482

In accordance with ASU 2011-04, the following table provides quantitative information about our Level 3 fair value measurements of our investments as of September 30 and March 31, 2013. In addition to the techniques and inputs noted in the table below, according to our valuation policy, the Adviser may also use other valuation techniques and methodologies when determining our fair value measurements. The below table is not intended to be all-inclusive, but rather provides information on the significant Level 3 inputs as they relate to our fair value measurements. The weighted average calculations in the table below are based on the principal balances for all debt-related calculations and on the cost basis for all equity-related calculations for the particular input.

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Quantitative Information about Level 3 Fair Value Measurements

	Fair Value as of September 30, 2013	Fair Value as of March 31, 2013	Valuation Technique/ Methodology	Unobservable Input	Range / Weighted Average as of September 30, 2013	Range / Weighted Average as of March 31, 2013
Senior debt	\$ 105,294	\$ 69,544	TEV	EBITDA multiples ^(B)	3.7x - 7.1x / 5.4x	4.6x - 7.3x / 5.6x
				EBITDA ^(B)	\$95 - \$5,271 / \$3,685	(\$997) - \$6,640 / \$3,752
	29,574	34,338	SPSE ^(A)	EBITDA ^(B)	\$557 - \$2,830 / \$1,437	\$29 - \$3,225 / \$1,248
				Risk Ratings ^(C)	3.3 - 7.9 / 5.0	3.7 - 6.9 / 5.1
Senior subordinated debt	47,070	66,070	TEV	EBITDA multiples ^(B)	4.4x - 7.1x / 5.4x	4.5x - 9.7x / 6.5x
				EBITDA ^(B)	(\$590) - \$6,755 / \$3,754	(\$2,866) - \$8,695 / \$4,400
	27,670	20,741	SPSE ^(A)	EBITDA ^(B)	\$5,441 - \$7,734 / \$6,083	\$5,169 - \$6,026 / \$5,738
				Risk Ratings ^(C)	5.3 - 6.2 / 5.6	4.1 - 6.2 / 4.8
Preferred equity	62,509	82,157	TEV	EBITDA multiples ^(B)	3.7x - 8.0x / 5.4x	4.2x - 9.7x / 5.9x
				EBITDA ^(B)	(\$590) - \$7,734 / \$4,114	(\$2,866) - \$8,695 / \$4,344
Common equity/equivalents	15,095	13,632	TEV	EBITDA multiples ^(B)	3.7x - 8.0x / 5.8x	3.7x - 7.8x / 6.2x
				EBITDA ^(B)	(\$590) - \$6,755 / \$2,435	(\$2,866) - \$6,026 / \$1,959
Total	\$ 287,212	\$ 286,482				

(A) SPSE makes an independent assessment of the data the Adviser submits to them (which includes the financial and operational performance, as well as the Adviser's internally assessed risk ratings of the portfolio companies – see footnote (C) below) and its own independent data to form an opinion as to what they consider to be the market values for our securities. With regard to its work, SPSE has stated that the data submitted to us is proprietary in nature.

(B) Adjusted earnings before interest expense, taxes, depreciation and amortization (EBITDA) is an unobservable input, which is generally based on the most recently available trailing twelve month financial statements submitted to the Adviser from the portfolio companies. EBITDA multiples, generally indexed, represent the Adviser's estimate of where market participants might price these investments. For our bundled debt and equity investments, the EBITDA and EBITDA multiple inputs are used in the TEV fair value determination, and the issuer's debt, equity, and/or equity-like securities are valued in accordance with the Adviser's liquidity waterfall approach. In limited cases, the revenue from the most recently available trailing twelve month financial statements submitted to the Adviser from the portfolio companies and the related revenue multiples, generally indexed, are used to provide a TEV fair value determination of our bundled debt and equity investments.

- (C) As part of the Adviser's valuation procedures, it risk rates all of our investments in debt securities. The Adviser uses a proprietary risk rating system for all debt securities. The Adviser's risk rating system uses a scale of 0 to >10, with >10 being the lowest probability of default. The risk rating system covers both qualitative and quantitative aspects of the portfolio company business and the securities we hold.

A portfolio company's EBITDA and EBITDA multiples are the significant unobservable inputs generally included in the Adviser's internally-assessed TEV models used to value our proprietary debt and equity investments. Holding all other factors constant, increases (decreases) in the EBITDA and/or the EBITDA multiples inputs would result in a higher (lower) fair value measurement. Per our valuation policy, the Adviser generally uses an indexed EBITDA multiple. EBITDA and EBITDA multiple inputs do not necessarily directionally correlate since EBITDA is a company performance metric and EBITDA multiples can be influenced by market, industry, size and other factors.

Changes in Level 3 Fair Value Measurements of Investments

The following tables provide the changes in fair value, broken out by security type, during the three and six months ended September 30, 2013 and 2012 for all investments for which we determine fair value using unobservable (Level 3) factors. When a determination is made to classify a financial instrument within Level 3 of the valuation hierarchy, such determination is based upon the significance of the unobservable factors to the overall fair value measurement. However, Level 3 financial instruments typically include, in addition to the unobservable, or Level 3, inputs, observable inputs (that is, components that are actively quoted and can be validated to external sources). In these cases, we categorize the fair value measurement in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement. Accordingly, the gains and losses in the tables below include changes in fair value, due in part to observable factors that are part of the valuation methodology.

Table of Contents**Fair Value Measurements of Investments Using Significant Unobservable Inputs (Level 3)**

	Senior Debt	Senior Subordinated Debt	Preferred Equity	Common Equity/ Equivalents	Total
Three months ended September 30, 2013:					
Fair value as of June 30, 2013	\$ 118,790	\$ 93,969	\$ 84,541	\$ 11,027	\$ 308,327
Total gains (losses):					
Net realized gains ^{(A)(D)}			24,804		24,804
Net unrealized appreciation (depreciation) ^(B)	438	(158)	(2,658)	4,068	1,690
Reversal of previously-recorded appreciation upon realization ^(B)			(17,374)		(17,374)
New investments, repayments and settlements ^(C) :					
Issuances / Originations	16,000	429	4,000		20,429
Settlements / Repayments	(360)	(19,500)			(19,860)
Sales ^(D)			(30,804)		(30,804)
Fair value as of September 30, 2013	\$ 134,868	\$ 74,740	\$ 62,509	\$ 15,095	\$ 287,212

Six months ended September 30, 2013:					
Fair value as of March 31, 2013	\$ 103,882	\$ 86,811	\$ 82,157	\$ 13,632	\$ 286,482
Total gains (losses):					
Net realized gains ^{(A)(D)}			24,804		24,804
Net unrealized (depreciation) appreciation ^(B)	(3,406)	(1,102)	(6,580)	1,370	(9,718)
Reversal of previously-recorded appreciation upon realization ^(B)	2		(17,374)		(17,372)
New investments, repayments and settlements ^(C) :					
Issuances / Originations	36,690	8,931	10,306	93	56,020
Settlements / Repayments	(2,300)	(19,900)			(22,200)
Sales ^(D)			(30,804)		(30,804)
Fair value as of September 30, 2013	\$ 134,868	\$ 74,740	\$ 62,509	\$ 15,095	\$ 287,212

	Senior Debt	Senior Subordinated Debt	Preferred Equity	Common Equity/ Equivalents	Total
Three months ended September 30, 2012:					
Fair value as of June 30, 2012	\$ 90,081	\$ 80,398	\$ 44,192	\$ 15,099	\$ 229,770
Total (losses) gains:					
Net realized gains ^{(A)(D)}				798	798
Net unrealized (depreciation) appreciation ^(B)	(3,084)	442	3,073	(4,315)	(3,884)
New investments, repayments and settlements ^(C) :					
Issuances / Originations	17,820	17,500	15,074	105	50,499
Settlements / Repayments	(7,560)	(1,600)			(9,160)

Sales ^(D)			(539)	(798)	(1,337)
Transfers ^(E)		(3,000)	2,500	500	
Fair value as of September 30, 2012	\$ 97,257	\$ 93,740	\$ 64,300	\$ 11,389	\$ 266,686

Six months ended September 30, 2012:

Fair value as of March 31, 2012	\$ 94,886	\$ 70,661	\$ 46,669	\$ 13,436	\$ 225,652
Total (losses) gains:					
Net realized gains ^{(A)(D)}				753	753
Net unrealized (depreciation) appreciation ^(B)	(8,075)	3,030	(1,884)	(2,672)	(9,601)
New investments, repayments and settlements ^(C) :					
Issuances / Originations	18,770	26,815	17,553	125	63,263
Settlements / Repayments	(8,324)	(3,766)			(12,090)
Sales ^(D)			(538)	(753)	(1,291)
Transfers ^(E)		(3,000)	2,500	500	
Fair value as of September 30, 2012	\$ 97,257	\$ 93,740	\$ 64,300	\$ 11,389	\$ 266,686

(A) Included in Net realized gain (loss) on our accompanying *Condensed Consolidated Statements of Operations* for the periods ended September 30, 2013 and 2012.

(B) Included in Net unrealized appreciation (depreciation) on our accompanying *Condensed Consolidated Statements of Operations* for the periods ended September 30, 2013 and 2012.

(C) Includes increases in the cost basis of investments resulting from new portfolio investments, the amortization of discounts, PIK and other non-cash disbursements to portfolio companies, as well as decreases in the cost basis of investments resulting from principal repayments or sales, the amortization of premiums and acquisition costs, and other cost-basis adjustments.

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- (D) Included in Net realized gains (losses) and Sales are post-closing adjustments recorded in the current period related to exits from prior periods.
- (E) Transfers represent \$3.0 million of senior subordinated term debt of Tread, at cost, as of June 30, 2012, which was converted into preferred and common equity during the quarter ended September 30, 2012.

Investment Activity

During the six months ended September 30, 2013, the following significant transactions occurred:

In April 2013, we invested \$17.7 million in Jackrabbit, Inc. (Jackrabbit) through a combination of debt and equity. Jackrabbit, headquartered in Ripon, California, is a manufacturer of nut harvesting equipment.

In May 2013, we invested \$8.8 million in Funko, LLC (Funko) through a combination of debt and equity. Funko, headquartered in Lynnwood, Washington, is a designer, importer and marketer of pop-culture collectibles. This was our first co-investment with our affiliated fund Gladstone Capital Corporation pursuant to an exemptive order granted by the SEC in July 2012.

In June 2013, we invested \$9.0 million in Star Seed, Inc. (Star Seed) through a combination of debt and equity. Based in Osborne, Kansas, Star Seed provides its customers with a variety of specialty seeds and related products.

In August 2013, we invested \$20.0 million in Schylling, Inc. (Schylling) through a combination of debt and equity. Schylling, headquartered in Rowley, Massachusetts, is a premier provider of high quality specialty toys.

In August 2013, our portfolio company Venyu was sold. As a result of the sale, we received net cash proceeds of \$32.2 million, resulting in a realized gain of approximately \$24.8 million and dividend income of \$1.4 million. In addition, we received full repayment of our debt investment of \$19 million in principal repayment and \$1.9 million in fee income.

Refer to Note 14, Subsequent Events, for significant portfolio activity that occurred after September 30, 2013.

Investment Concentrations

As of September 30, 2013, our investment portfolio consisted of investments in 24 portfolio companies located in 14 states across 14 different industries with an aggregate fair value of \$287.2 million, of which Acme Cryogenics, Inc. (Acme), Galaxy Tool Holding Corp. (Galaxy), and SOG Specialty K&T, LLC (SOG), collectively, comprised approximately \$76.1 million, or 26.5%, of our total investment portfolio at fair value. The following table outlines our investments by security type as of September 30 and March 31, 2013:

September 30, 2013		March 31, 2013	
Cost	Fair Value	Cost	Fair Value

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Senior debt	\$ 170,135	48.0%	\$ 134,868	47.0%	\$ 135,745	41.6%	\$ 103,882	36.3%
Senior subordinated debt	92,576	26.1	74,740	26.0	103,547	31.7	86,811	30.3
Total debt	262,711	74.1	209,608	73.0	239,292	73.3	190,693	66.6
Preferred equity	86,016	24.3	62,509	21.7	81,710	25.0	82,157	28.7
Common equity/equivalents	5,514	1.6	15,095	5.3	5,419	1.7	13,632	4.7
Total equity/equivalents	91,530	25.9	77,604	27.0	87,129	26.7	95,789	33.4
Total Investments	\$ 354,241	100.0%	\$ 287,212	100.0%	\$ 326,421	100.0%	\$ 286,482	100.0%

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Investments at fair value consisted of the following industry classifications as of September 30 and March 31, 2013:

	September 30, 2013		March 31, 2013	
	Fair Value	Percentage of Total Investments	Fair Value	Percentage of Total Investments
Chemicals, Plastics, and Rubber	\$ 55,880	19.5%	\$ 59,170	20.7%
Leisure, Amusement, Motion Pictures, Entertainment	44,132	15.4	29,822	10.4
Diversified/Conglomerate Manufacturing	33,316	11.6	32,698	11.4
Machinery	29,962	10.4	32,662	11.4
Farming and Agriculture	29,087	10.1		
Containers, Packaging, and Glass	24,459	8.5	23,019	8.0
Aerospace and Defense	24,156	8.4	20,876	7.3
Home and Office Furnishings, Housewares, and Durable Consumer Products	18,970	6.6	23,512	8.2
Personal and Non-Durable Consumer Products	9,176	3.2		
Automobile	9,052	3.1	7,467	2.6
Cargo Transport	6,514	2.3	6,897	2.4
Buildings and Real Estate	2,508	0.9	6,020	2.2
Beverage, Food, and Tobacco			369	0.1
Electronics			43,970	15.3
Total Investments	\$ 287,212	100.0%	\$ 286,482	100.0%

The investments, at fair value, were included in the following geographic regions of the U.S. as of September 30 and March 31, 2013:

	September 30, 2013		March 31, 2013	
	Fair Value	Percentage of Total Investments	Fair Value	Percentage of Total Investments
West	\$ 106,022	36.9%	\$ 81,400	28.4%
Northeast	75,791	26.4	58,319	20.4
South	71,316	24.8	125,518	43.8
Midwest	34,083	11.9	21,245	7.4
Total Investments	\$ 287,212	100.0%	\$ 286,482	100.0%

The geographic region indicates the location of the headquarters for our portfolio companies. A portfolio company may have additional business locations in other geographic regions.

Investment Principal Repayments

The following table summarizes the contractual principal repayments and maturity of our investment portfolio by fiscal year, assuming no voluntary prepayments, as of September 30, 2013:

		Amount
For the remaining six months ending March 31:	2014	\$ 9,022
For the fiscal year ending March 31:	2015	76,334
	2016	23,164
	2017	59,035
	2018	51,982
	Thereafter	43,430
	Total contractual repayments	\$ 262,967
	Investments in equity securities	91,530
	Adjustments to cost basis on debt securities	(256)
	Total cost basis of investments held as of September 30, 2013:	\$ 354,241

Receivables from Portfolio Companies

Receivables from portfolio companies represent non-recurring costs that we incurred on behalf of portfolio companies and are included in other assets on our accompanying *Condensed Consolidated Statements of Assets and Liabilities*. We maintain an allowance for uncollectible receivables from portfolio companies, which is determined based on historical experience and management's expectations of future losses. We charge the accounts receivable to the established provision when collection efforts have been exhausted and the receivables are deemed uncollectible. As of September 30 and March 31, 2013, we had gross receivables from portfolio companies of \$1.2 million. The allowance for uncollectible receivables was \$159 and \$44 as of September 30 and March 31, 2013, respectively.

Table of Contents**NOTE 4. RELATED PARTY TRANSACTIONS***Investment Advisory and Management Agreement*

We entered into an investment advisory and management agreement with the Adviser (the *Advisory Agreement*). The Adviser is controlled by our chairman and chief executive officer. In accordance with the *Advisory Agreement*, we pay the Adviser certain fees as compensation for its services, such fees consisting of a base management fee and an incentive fee, each as described below. On July 9, 2013, our Board of Directors approved the renewal of the *Advisory Agreement* through August 31, 2014.

The following table summarizes the management fees, incentive fees and associated credits reflected in our accompanying *Condensed Consolidated Statements of Operations*:

	Three Months Ended		Six Months Ended	
	September 30,		September 30,	
	2013	2012	2013	2012
Average gross assets subject to base management fee	\$ 312,200	\$ 261,600	\$ 311,000	\$ 249,900
Multiplied by prorated annual base management fee of 2%	0.5%	0.5%	1.0%	1.0%
Base management fee ^(A)	1,561	1,308	3,110	2,499
Credit for fees received by Adviser from the portfolio companies ^(A)	(334)	(515)	(845)	(700)
Net base management fee	\$ 1,227	\$ 793	\$ 2,265	\$ 1,799
Incentive fee ^(A)	\$ 1,557	\$ 541	\$ 1,722	\$ 541

^(A) Reflected as a line item on our accompanying *Condensed Consolidated Statements of Operations*.

Base Management Fee

The base management fee is computed and payable quarterly and is assessed at an annual rate of 2.0%. It is computed on the basis of the value of our average gross assets at the end of the two most recently completed quarters, which are total assets, including investments made with proceeds of borrowings, less any uninvested cash or cash equivalents resulting from borrowings. As a BDC, we make available significant managerial assistance to our portfolio companies and provide other services to such portfolio companies. Although neither we nor our Adviser receive fees in connection with managerial assistance, the Adviser provides other services to our portfolio companies and receives fees for these other services. 50% of certain of these fees and 100% of others are credited against the base management fee that we would otherwise be required to pay to our Adviser. Effective beginning the third quarter ending December 31, 2013, 100% of all these fees are credited against the base management fee that we would otherwise be required to pay to our Adviser.

Incentive Fee

The incentive fee consists of two parts: an income-based incentive fee and a capital gains-based incentive fee. The income-based incentive fee rewards the Adviser if our quarterly net investment income (before giving effect to any incentive fee) exceeds 1.75% of our net assets (the hurdle rate). We will pay the Adviser an income-based incentive fee with respect to our pre-incentive fee net investment income in each calendar quarter as follows:

no incentive fee in any calendar quarter in which our pre-incentive fee net investment income does not exceed the hurdle rate (7.0% annualized);

100% of our 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% in any calendar quarter (8.75% annualized); and

20% of the amount of our pre-incentive fee net investment income, if any, that exceeds 2.1875% in any calendar quarter (8.75% annualized).

The second part of the incentive fee is a capital gains-based incentive fee that will be determined and payable in arrears as of the end of each fiscal year (or upon termination of the Advisory Agreement, as of the termination date) and equals 20% of our realized capital gains as of the end of the fiscal year. In determining the capital gains-based incentive fee payable to the Adviser, we will calculate the cumulative aggregate realized capital gains and cumulative aggregate realized capital losses since our inception, and the aggregate net unrealized capital depreciation as of the date of the calculation, as applicable, with respect to each of the investments in our portfolio. For this purpose, cumulative aggregate realized capital gains, if any, equals the sum of the differences between the net sales price of each investment, when sold, and the original cost of such investment since our inception. Cumulative aggregate realized capital losses equals the sum of the amounts by which the net sales price of each investment, when sold, is less than the original cost of such investment since our inception. Aggregate net unrealized capital depreciation equals the sum of the difference, if negative, between the valuation of each investment as of the applicable

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calculation date and the original cost of such investment. At the end of the applicable year, the amount of capital gains that serves as the basis for our calculation of the capital gains-based incentive fee equals the cumulative aggregate realized capital gains less cumulative aggregate realized capital losses, less aggregate net unrealized capital depreciation, with respect to our portfolio of investments. If this number is positive at the end of such year, then the capital gains-based incentive fee for such year equals 20% of such amount, less the aggregate amount of any capital gains-based incentive fees paid in respect of our portfolio in all prior years. No capital gains-based incentive fee has been recorded since our inception through September 30, 2013, as cumulative net unrealized capital depreciation has exceeded cumulative realized capital gains net of cumulative realized capital losses.

Additionally, in accordance with GAAP, a capital gains-based incentive fee accrual is calculated using the aggregate cumulative realized capital gains and losses and aggregate cumulative unrealized capital depreciation included in the calculation of the capital gains-based incentive fee plus the aggregate cumulative unrealized capital appreciation. If such amount is positive at the end of a period, then GAAP requires us to record a capital gains-based incentive fee equal to 20% of such amount, less the aggregate amount of actual capital gains-based incentive fees paid in all prior years. If such amount is negative, then there is no accrual for such year. GAAP requires that the capital gains-based incentive fee accrual consider the cumulative aggregate unrealized capital appreciation in the calculation, as a capital gains-based incentive fee would be payable if such unrealized capital appreciation were realized. There can be no assurance that such unrealized capital appreciation will be realized in the future. No GAAP accrual for a capital gains-based incentive fee has been recorded since our inception through September 30, 2013.

Administration Agreement

We have entered into an administration agreement (the *Administration Agreement*) with Gladstone Administration, LLC (the *Administrator*), an affiliate of ours and the Adviser, whereby we pay separately for administrative services. The *Administration Agreement* provides for payments equal to our allocable portion of the *Administrator's* overhead expenses in performing its obligations under the *Administration Agreement*, including, but not limited to, rent and the salaries and benefits expenses of our chief financial officer and treasurer, chief compliance officer, internal counsel and secretary and their respective staffs. Our allocable portion of administrative expenses is generally derived by multiplying the *Administrator's* total allocable expenses by the percentage of our total assets at the beginning of the quarter in comparison to the total assets at the beginning of the quarter of all companies managed by the Adviser under similar agreements. On July 9, 2013, our Board of Directors approved the annual renewal of the *Administration Agreement* through August 31, 2014.

Related Party Fees Due

Amounts due to related parties on our accompanying *Condensed Consolidated Statements of Assets and Liabilities* were as follows:

	September 30, 2013	March 31, 2013
Base management fee due to Adviser	\$ 376	\$ 625
Incentive fee due to Adviser	1,557	1,454
Other due to (from) Adviser	14	(12)
Fees due to Adviser ^(A)	\$ 1,947	\$ 2,067

Fee due to Administrator ^(A)	\$	156	\$	221
Total related party fees due	\$	2,103	\$	2,288

^(A) Reflected as a line item on our accompanying *Condensed Consolidated Statements of Assets and Liabilities*. In addition, as of September 30, 2013, we had a receivable from our affiliated fund Gladstone Capital Corporation (GLAD) of \$0.2 million for its proportional share of reimbursable expenses associated with acquiring securities in a Co-Investment Transaction, which were paid in full at the funding of the co-investment transaction subsequent to quarter-end. This affiliate receivable is recorded in Other assets on our accompanying Condensed Consolidated Statements of Assets and Liabilities.

NOTE 5. BORROWINGS

Line of Credit

On April 30, 2013, we, through our wholly-owned subsidiary, Business Investment, entered into a fifth amended and restated credit agreement with Key Equipment Finance Inc., as administrative agent, lead arranger and a lender (the Administrative Agent), Branch Banking and Trust Company as a lender and managing agent, and the Adviser, as servicer, to increase the commitment amount of the revolving line of credit (the Credit Facility) from \$60.0 million to \$70.0 million and to extend the maturity date as described below. The maturity date was extended to April 30, 2016 (the Maturity Date) and, if not renewed or extended by the Maturity Date, all principal and interest will be due and payable on or before April 30, 2017 (one year after the Maturity Date). In addition, there are two one-year extension options to be agreed upon by all parties, which may be exercised on or before April 30, 2014 and 2015,

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respectively. Subject to certain terms and conditions, the Credit Facility may be expanded up to a total of \$200.0 million through the addition of other lenders to the facility. Advances under the Credit Facility generally bear interest at 30-day LIBOR, plus 3.75% per annum, with an unused fee of 0.50% on undrawn amounts. We incurred fees of approximately \$0.3 million in connection with this amendment.

On June 12, 2013, we further increased the borrowing capacity under the Credit Agreement from \$70.0 million to \$105.0 million by entering into Joinder Agreements pursuant to the Credit Agreement, by and among Business Investment, the Administrative Agent, the Adviser and each of Alostair Bank of Commerce and Everbank Commercial Finance, Inc.

The following tables summarize noteworthy information related to our Credit Facility:

	As of September 30, 2013	As of March 31, 2013
Commitment amount	\$ 105,000	\$ 60,000
Borrowings outstanding at cost	34,000	31,000
Availability	71,000	29,000

	For the Three Months Ended September 30,		For the Six Months Ended September 30,	
	2013	2012	2013	2012
Weighted average borrowings outstanding	\$ 41,424	\$ 39,022	\$ 37,063	\$ 20,011
Effective interest rate ^(A)	4.8%	4.4%	4.7%	5.1%
Commitment (unused) fees incurred	\$ 81	\$ 27	\$ 133	\$ 102

(A) Excludes the impact of deferred financing fees.

Interest is payable monthly during the term of the Credit Facility. Available borrowings are subject to various constraints imposed under the Credit Facility, based on the aggregate loan balance pledged by Business Investment, which varies as loans are added and repaid, regardless of whether such repayments are prepayments or made as contractually required.

The Administrative Agent also requires that any interest or principal payments on pledged loans be remitted directly by the borrower into a lockbox account with The Bank of New York Mellon Trust Company, N.A as custodian. The Administrative Agent is also the trustee of the account and remits the collected funds to us once a month.

Generally, our Credit Facility contains covenants that require Business Investment to, among other things, maintain its status as a separate legal entity, prohibit certain significant corporate transactions (such as mergers, consolidations, liquidations or dissolutions) and restrict certain material changes to our credit and collection policies without the lenders' consent. Our Credit Facility also limits payments on distributions to the aggregate net investment income for each of the twelve month periods ending March 31, 2014, 2015, 2016 and 2017. Business Investment is also subject to certain limitations on the type of loan investments it can apply toward availability credit in the borrowing base, including restrictions on geographic concentrations, sector concentrations, loan size, payment frequency and status, average life and lien property. Our Credit Facility further requires Business Investment to comply with other financial

and operational covenants, which obligate Business Investment to, among other things, maintain certain financial ratios, including asset and interest coverage and a minimum number of obligors required in the borrowing base of the credit agreement. Additionally, we are subject to a performance guaranty that requires us to maintain (i) a minimum net worth (defined in our Credit Facility to include our mandatory redeemable term preferred stock) of \$170.0 million plus 50% of all equity and subordinated debt raised after April 30, 2013, which equates to \$170.0 million as of September 30, 2013, (ii) asset coverage with respect to senior securities representing indebtedness of at least 200%, in accordance with Section 18 of the 1940 Act and (iii) its status as a BDC under the 1940 Act and as a RIC under the Code. As of September 30, 2013, and as defined in the performance guaranty of our Credit Facility, we had a minimum net worth of \$281.3 million, an asset coverage of 328% and an active status as a BDC and RIC. Our Credit Facility requires a minimum of 12 obligors in the borrowing base and, as of September 30, 2013, Business Investment had 19 obligors. As of September 30, 2013, we were in compliance with all covenants.

Short-Term Loan

Similar to previous quarter ends, to maintain our status as a RIC, we purchased \$25.0 million of short-term U.S. Treasury Bills (T-Bills) through Jefferies & Company, Inc. (Jefferies) on September 27, 2013. As these T-Bills have a maturity of less than three months, we consider them to be cash equivalents and include them in cash and cash equivalents on our accompanying *Condensed Consolidated Statement of Assets and Liabilities* as of September 30, 2013. The T-Bills were purchased on margin using \$3.0 million in cash and the proceeds from a \$22.0 million short-term loan from Jefferies with an effective annual interest rate of approximately 1.35%. On October 3, 2013, when the T-Bills matured, we repaid the \$22.0 million loan from Jefferies and we received back the \$3.0 million margin payment sent to Jefferies to complete the transaction.

Table of Contents*Secured Borrowing*

In August 2012, we entered into a participation agreement with a third-party related to \$5.0 million of our senior subordinated term debt investment in Ginsey Home Solutions, Inc. (Ginsey). We evaluated whether the transaction should be accounted for as a sale or a financing-type transaction under the applicable guidance of ASC 860. Based on the terms of the participation agreement, we are required to treat the participation as a financing-type transaction. Specifically, the third-party has a senior claim to our remaining investment in the event of default by Ginsey which, in part, resulted in the loan participation bearing a rate of interest lower than the contractual rate established at origination. Therefore, our accompanying *Condensed Consolidated Statements of Assets and Liabilities* reflects the entire senior subordinated term debt investment in Ginsey and a corresponding \$5.0 million secured borrowing liability. The secured borrowing has a stated interest rate of 7.0% and a maturity date of January 3, 2018.

Fair Value

We elected to apply ASC 825, Financial Instruments, specifically for our Credit Facility and short-term loan, which was consistent with the application of ASC 820 to our investments. Generally, the Adviser estimates the fair value of our Credit Facility using estimates of value provided by an independent third party and its own assumptions in the absence of observable market data, including estimated remaining life, counterparty credit risk, current market yield and interest rate spreads of similar securities as of the measurement date. Additionally, due to the seven-day duration of the short-term loan, cost was deemed to approximate fair value. At each of September 30 and March 31, 2013, all of our borrowings were valued using Level 3 inputs. The following tables present the short-term loan and Credit Facility carried at fair value as of September 30 and March 31, 2013, by caption on our accompanying *Condensed Consolidated Statements of Assets and Liabilities* for Level 3 of the hierarchy established by ASC 820 and a roll-forward of the changes in fair value during the three and six months ended September 30, 2013 and 2012:

	Level 3 Borrowings	
	Total Recurring Fair Value Measurement	
	Reported in <i>Condensed</i>	
	<i>Consolidated</i>	
	<i>Statements of Assets and</i>	
	<i>Liabilities</i>	
	September 30, 2013	March 31, 2013
Short-Term Loan	\$ 22,005	\$ 58,016
Credit Facility	34,341	31,854
Total	\$ 56,346	\$ 89,870

Fair Value Measurements of Borrowings Using Significant Unobservable Inputs (Level 3)

	Short-Term Loan	Credit Facility	Total
Three months ended September 30, 2013:			
Fair value at June 30, 2013	\$ 26,009	\$ 49,000	\$ 75,009
Borrowings	22,005	43,000	65,005

Table of Contents**Fair Value Measurements of Borrowings Using Significant Unobservable Inputs (Level 3)**

	Short-Term Loan	Credit Facility	Total
Three months ended September 30, 2012:			
Fair value at June 30, 2012	\$ 76,010	\$ 31,492	\$ 107,502
Borrowings	71,525	60,000	131,525
Repayments	(76,010)	(35,000)	(111,010)
Net unrealized appreciation ^(A)		717	717
Fair value at September 30, 2012	\$ 71,525	\$ 57,209	\$ 128,734
Six months ended September 30, 2012:			
Fair value at March 31, 2012	\$ 76,005	\$	\$ 76,005
Borrowings	147,535	91,000	238,535
Repayments	(152,015)	(35,000)	(187,015)
Net unrealized appreciation ^(A)		1,209	1,209
Fair value at September 30, 2012	\$ 71,525	\$ 57,209	\$ 128,734

(A) Included in net unrealized (depreciation) appreciation on our accompanying *Condensed Consolidated Statement of Operations* for periods ended September 30, 2013 and 2012.

The fair value of the collateral under our Credit Facility was approximately \$283.6 million and \$263.7 million as of September 30 and March 31, 2013, respectively. The fair value of the collateral under the short-term loan was approximately \$25.0 million and \$65.0 million as of September 30 and March 31, 2013, respectively.

NOTE 6. INTEREST RATE CAP AGREEMENTS

We have entered into multiple interest rate cap agreements with BB&T and Keybank National Association that effectively limit the interest rate on a portion of our borrowings under the line of credit pursuant to the terms of our Credit Facility. The agreements provide that the interest rate on a portion of our borrowings is capped at a certain interest rate when 30-day LIBOR is in excess of that certain interest rate. The fair value of the interest rate cap agreements is recorded in other assets on our accompanying *Condensed Consolidated Statements of Assets and Liabilities*. We record changes in the fair value of the interest rate cap agreements quarterly based on the current market valuations at quarter end as net unrealized appreciation (depreciation) of other on our accompanying *Condensed Consolidated Statements of Operations*. Generally, the Adviser estimates the fair value of our interest rate cap agreements using estimates of value provided by the counterparty and its own assumptions in the absence of observable market data, including estimated remaining life, counterparty credit risk, current market yield and interest rate spreads of similar securities as of the measurement date. As of September 30 and March 31, 2013, our interest rate cap agreements were valued using Level 3 inputs. The following table summarizes the key terms of each interest rate cap agreement:

Interest Rate Cap^(A)	Notional Amount	LIBOR Cap	Effective Date	Maturity Date	As of September 30, 2013		As of March 31, 2013	
					Cost	Fair Value	Cost	Fair Value
December 2011	\$ 50,000	6.0%	May 2012	October 2013 ^(B)	\$ 29	\$	\$ 29	\$ 2
July 2013	45,000	6.0	October 2013	April 2016	75	7		

(A) Indicates date we entered into the interest rate cap agreement.

(B) The interest rate cap agreement matured in October 2013 and was not extended.

The use of a cap agreement involves risks that are different from those associated with ordinary portfolio securities transactions. Cap agreements may be considered to be illiquid. Although we will not enter into any such agreements unless we believe that the other party to the transaction is creditworthy, we do bear the risk of loss of the amount expected to be received under such agreements in the event of default or bankruptcy of the agreement counterparty.

NOTE 7. MANDATORILY REDEEMABLE PREFERRED STOCK

In March 2012, we completed a public offering of 1,600,000 shares of 7.125% Series A Cumulative Term Preferred Stock (our Term Preferred Stock) at a public offering price of \$25.00 per share. Gross proceeds totaled \$40.0 million and net proceeds, after deducting underwriting discounts and offering expenses borne by us, were \$38.0 million. We incurred \$2.0 million in total offering costs related to these transactions, which have been recorded as deferred financing costs on our accompanying *Condensed Consolidated Statements of Assets and Liabilities* and will be amortized over the redemption period ending February 28, 2017.

The shares have a redemption date of February 28, 2017, and are traded under the ticker symbol GAINP on the NASDAQ Global Select Market. The Term Preferred Stock is not convertible into our common stock or any other security. The Term Preferred Stock provides for a fixed dividend equal to 7.125% per year, payable monthly. We are required to redeem all of the outstanding Term Preferred Stock on February 28, 2017, for cash at a redemption price equal to \$25.00 per share, plus an amount equal to accumulated but unpaid dividends, if any, to, but excluding, the date of redemption. In addition, three other potential redemption triggers are as

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follows: 1) upon the occurrence of certain events that would constitute a change in control of us, we would be required to redeem all of the outstanding Term Preferred Stock, 2) if we fail to maintain an asset coverage ratio of at least 200%, we are required to redeem a portion of the outstanding Term Preferred Stock or otherwise cure the ratio redemption trigger and 3) at our sole option, at any time on or after February 28, 2016, we may redeem some or all of the Term Preferred Stock.

Our Board of Directors declared and paid the following monthly distributions to preferred stockholders for the six months ended September 30, 2013 and 2012:

Fiscal Year	Time Period	Declaration		Record Date	Payment Date	Distribution per Term
		Date				Preferred Share
2014	April 1 - 30	April 9, 2013	April 22, 2013	April 30, 2013	\$ 0.1484375	
	May 1 - 31	April 9, 2013	May 20, 2013	May 31, 2013	0.1484375	
	June 1 - 30	April 9, 2013	June 19, 2013	June 28, 2013	0.1484375	
	July 1 - 31	July 9, 2013	July 19, 2013	July 31, 2013	0.1484375	
	August 1 - 31	July 9, 2013	August 21, 2013	August 30, 2013	0.1484375	
	September 1 - 30	July 9, 2013	September 18, 2013	September 30, 2013	0.1484375	
Six months ended September 30, 2013: \$ 0.8906250						

Fiscal Year	Time Period	Declaration		Record Date	Payment Date	Distribution per Term
		Date				Preferred Share
2013	April 1 - 30	April 11, 2012	April 20, 2012	April 30, 2012	\$ 0.1484375	
	May 1 - 31	April 11, 2012	May 18, 2012	May 31, 2012	0.1484375	
	June 1 - 30	April 11, 2012	June 20, 2012	June 29, 2012	0.1484375	
	July 1 - 31	July 10, 2012	July 19, 2012	July 31, 2012	0.1484375	
	August 1 - 31	July 10, 2012	August 21, 2012	August 31, 2012	0.1484375	
	September 1 - 30	July 10, 2012	September 18, 2012	September 28, 2012	0.1484375	
Six months ended September 30, 2012: \$ 0.8906250						

In accordance with ASC 480, Distinguishing Liabilities from Equity, mandatorily redeemable financial instruments should be classified as liabilities on the balance sheet and, therefore, the related dividend payments are treated as dividend expense on our accompanying *Condensed Consolidated Statements of Operations* at the ex-dividend date. The fair value of the Term Preferred Stock based on the last reported closing price as of September 30 and March 31, 2013, was approximately \$41.9 million and \$42.7 million, respectively.

Aggregate Term Preferred Stock distributions declared and paid for the three and six months ended September 30, 2013, were approximately \$0.7 million and \$1.4 million, respectively. The tax character of distributions paid by us to preferred stockholders is from ordinary income.

NOTE 8. COMMON STOCK

We filed a registration statement on Form N-2 (File No. 333-181879) with the SEC on June 4, 2012, and subsequently filed a Pre-effective Amendment No. 1 to the registration statement on July 17, 2012, which the SEC declared effective on July 26, 2012. On June 7, 2013, we filed Post-Effective Amendment No. 2 to the registration statement, which the SEC declared effective on July 26, 2013. The registration statement permits us to issue, through one or more transactions, up to an aggregate of \$300.0 million in securities, consisting of common stock, preferred stock, subscription rights, debt securities and warrants to purchase common stock, including through a combined offering of two or more of such securities.

On October 5, 2012, we completed a public offering of 4.0 million shares of our common stock at a public offering price of \$7.50 per share, which was below our then current net asset value (NAV) per share. Gross proceeds totaled \$30.0 million and net proceeds, after deducting underwriting discounts and offering expenses borne by us, were \$28.3 million, which was used to repay borrowings under our Credit Facility. In connection with the offering, the underwriters exercised their option to purchase an additional 395,825 shares at the public offering price to cover over-allotments, which resulted in gross proceeds of \$3.0 million and net proceeds, after deducting underwriting discounts, of \$2.8 million.

NOTE 9. NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS PER COMMON SHARE

The following table sets forth the computation of basic and diluted net increase (decrease) in net assets resulting from operations per weighted average common share for the three and six months ended September 30, 2013 and 2012:

	Three Months Ended September 30,		Six Months Ended	
	2013	2012	September 30,	2012
	2013	2012	2013	2012
Numerator for basic and diluted net increase (decrease) in net assets resulting from operations per common share	\$ 14,939	\$ (353)	\$ 8,420	\$ (3,369)
Denominator for basic and diluted weighted average common shares	26,475,958	22,080,133	26,475,958	22,080,133
Basic and diluted net increase (decrease) in net assets resulting from operations per average common share	\$ 0.57	\$ (0.02)	\$ 0.32	\$ (0.15)

Table of Contents**NOTE 10. DISTRIBUTIONS TO COMMON STOCKHOLDERS**

To qualify to be taxed as a RIC under Subtitle A, Chapter 1 of Subchapter M of the Code, we are required to distribute to our stockholders 90% of our investment company taxable income, which is generally our net ordinary income plus the excess of our net short-term capital gains over net long-term capital losses. The amount to be paid out as a distribution is determined by our Board of Directors each quarter and is based on our estimated taxable income by management. Based on that estimate, three monthly distributions are declared each quarter.

Our Board of Directors declared the following monthly distributions to common stockholders for the six months ended September 30, 2013 and 2012:

Fiscal Year	Declaration Date	Record Date	Payment Date	Distribution per Common Share
2014	April 9, 2013	April 22, 2013	April 30, 2013	\$ 0.050
	April 9, 2013	May 20, 2013	May 31, 2013	0.050
	April 9, 2013	June 19, 2013	June 28, 2013	0.050
	July 9, 2013	July 17, 2013	July 31, 2013	0.050
	July 9, 2013	August 19, 2013	August 30, 2013	0.050
	July 9, 2013	September 16, 2013	September 30, 2013	0.050
Six months ended September 30, 2013:				\$ 0.300
2013	April 11, 2012	April 20, 2012	April 30, 2012	\$ 0.050
	April 11, 2012	May 18, 2012	May 31, 2012	0.050
	April 11, 2012	June 20, 2012	June 29, 2012	0.050
	July 10, 2012	July 20, 2012	July 31, 2012	0.050
	July 10, 2012	August 22, 2012	August 31, 2012	0.050
	July 10, 2012	September 19, 2012	September 28, 2012	0.050
Six months ended September 30, 2012:				\$ 0.300

Aggregate common distributions declared quarterly and paid for the six months ended September 30, 2013 and 2012 were approximately \$7.9 million and \$6.6 million, respectively, which were declared based on estimates of net investment income for the respective fiscal years. The tax characterization of the common distributions declared and paid for the fiscal year ended March 31, 2014, will be determined at fiscal year end and cannot be determined at this time. For the fiscal year ended March 31, 2013, taxable income available for common distributions exceeded distributions declared and paid, and, in accordance with Section 855(a) of the Code, we elected to treat \$3.1 million of the common distributions paid in fiscal year 2014 as having been paid in the prior year.

NOTE 11. COMMITMENTS AND CONTINGENCIES

As of September 30, 2013, we have lines of credit commitments to certain of our portfolio companies that have not been fully drawn. Since these lines of credit have expiration dates and we expect many will never be fully drawn, the total line of credit commitment amounts do not necessarily represent future cash requirements.

In addition to the lines of credit to certain portfolio companies, we have also extended certain guarantees on behalf of some of our portfolio companies. As of September 30, 2013, we have not been required to make any payments on the guarantees discussed below, and we consider the credit risk to be remote and the fair values of the guarantees to be minimal.

In October 2008, we executed a guarantee of a vehicle finance facility agreement (the Finance Facility) between Ford Motor Credit Company (Ford) and ASH. The Finance Facility provides ASH with a line of credit of up to \$0.5 million for component Ford parts used by ASH to build truck bodies under a separate contract. Ford retains title and ownership of the parts. The guarantee of the Finance Facility will expire upon termination of the separate parts supply contract with Ford or upon replacement of us as guarantor.

In February 2010, we executed a guarantee of a wholesale financing facility agreement (the Floor Plan Facility) between Agricredit Acceptance, LLC (Agricredit) and Country Club Enterprises, LLC (CCE). The Floor Plan Facility provides CCE with financing of up to \$2.0 million to bridge the time and cash flow gap between the order and delivery of golf carts to customers. The guarantee was renewed in February 2011, 2012 and 2013 and expires in February 2014, unless it is renewed again by us, CCE and Agricredit. In connection with this guarantee and its subsequent renewals, we recorded aggregate premiums of \$0.4 million from CCE.

In April 2010, we executed a guarantee of vendor recourse for up to \$2.0 million in individual customer transactions (the Recourse Facility) between Wells Fargo Financial Leasing, Inc. and CCE. The Recourse Facility provides CCE with the ability to provide vendor recourse up to a limit of \$2.0 million on transactions with long-time customers who lack the financial history to qualify for third-party financing. The terms to maturity of these individual transactions range from October 2014 to October 2016. In connection with this guarantee, we received aggregate premiums of \$0.1 million from CCE.

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The following table summarizes the dollar balance of unused line of credit commitments and guarantees as of September 30 and March 31, 2013:

	September 30, 2013	March 31, 2013
Unused line of credit commitments	\$ 2,834	\$ 1,584
Guarantees	3,580	3,870
Total	\$ 6,414	\$ 5,454

Escrow Holdbacks

From time to time, we will enter into arrangements relating to exits of certain investments whereby specific amounts of the proceeds are held in escrow to be used to satisfy potential obligations, as stipulated in the sales agreements. We record escrow amounts in restricted cash on our accompanying *Condensed Consolidated Statements of Assets and Liabilities*. In August 2013, the sale of Venyu resulted in \$4.9 million in escrow amounts, of which \$0.7 million is held on behalf of the other sellers. The \$0.7 million amount held on behalf of the other sellers is recorded in other liabilities on our accompanying *Condensed Consolidated Statements of Assets and Liabilities*. We establish a contingent liability against the escrow amounts if we determine that it is probable and estimable that a portion of the escrow amounts will not be ultimately received at the end of the escrow period. The aggregate contingent liability recorded against the escrow amounts was \$74 and \$41 as of September 30 and March 31, 2013, respectively.

NOTE 12. FINANCIAL HIGHLIGHTS

	Three Months Ended September 30,		Six Months Ended September 30,	
	2013	2012	2013	2012
Per Common Share Data				
NAV at beginning of period ^(A)	\$ 8.70	\$ 9.10	\$ 9.10	\$ 9.38
Net investment income ^(B)	0.24	0.16	0.39	0.31
Realized gain on sale of investments and other ^(B)	0.94	0.03	0.94	0.03
Net unrealized depreciation of investments and other ^(B)	(0.61)	(0.21)	(1.01)	(0.49)
Total from investment operations ^(B)	0.57	(0.02)	0.32	(0.15)
Cash distributions from net investment income ^{(B)(C)}	(0.15)	(0.15)	(0.30)	(0.30)
NAV at end of period ^(A)	\$ 9.12	\$ 8.93	\$ 9.12	\$ 8.93
	\$ 7.35	\$ 7.40	\$ 7.31	\$ 7.57

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Per common share market value at beginning of period				
Per common share market value at end of period	7.05	7.82	7.05	7.82
Total return ^(D)	(2.02)%	7.79%	0.54%	7.53%
Common stock outstanding at end of period	26,475,958	22,080,133	26,475,958	22,080,133
Statement of Assets and Liabilities				
Data:				
Net assets at end of period	\$ 241,440	\$ 197,223	\$ 241,440	\$ 197,223
Average net assets ^(E)	237,871	200,182	237,509	202,520
Senior Securities Data^(F):				
Total borrowings, at cost	\$ 61,005	\$ 132,525	\$ 61,005	\$ 132,525
Mandatorily redeemable preferred stock	40,000	40,000	40,000	40,000
Asset coverage ratio ^(G)	328%	210%	328%	210%
Average coverage per unit ^(H)	\$ 3,276	\$ 2,101	\$ 3,276	\$ 2,101
Ratios/Supplemental Data:				
Ratio of expenses to average net assets ^{(I)(J)}	9.19%	8.07%	7.87%	6.80%
Ratio of net expenses to average net assets ^{(I)(K)}	8.63	7.04	7.15	6.11
Ratio of net investment income to average net assets ^(L)	10.47	6.90	8.64	6.61

- (A) Based on actual common shares outstanding at the end of the corresponding period.
- (B) Based on weighted average per basic common share data.
- (C) Distributions are determined based on taxable income calculated in accordance with income tax regulations, which may differ from amounts determined under GAAP.
- (D) Total return equals the change in the market value of our common stock from the beginning of the period, taking into account dividends reinvested in accordance with the terms of our dividend reinvestment plan. Total return does not take into account distributions that may be characterized as a return of capital. For further information on the estimated character of our distributions to common stockholders, please refer to Note 10 *Distributions to Common Stockholders*.
- (E) Calculated using the average balance of net assets at the end of each month of the reporting period.

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- (F) The 1940 Act currently permits BDCs to issue senior securities representing indebtedness and senior securities that are stock, to which we refer as senior securities.
- (G) As a BDC, we are generally required to maintain an asset coverage ratio (as defined in Section 18(h) of the 1940 Act) of at least 200% on our senior securities representing indebtedness and our senior securities that are stock. Our mandatorily redeemable preferred stock is a senior security that is stock.
- (H) Asset coverage per unit is the asset coverage ratio expressed in terms of dollar amounts per one thousand dollars of indebtedness.
- (I) Amounts are annualized.
- (J) Ratio of expenses to average net assets is computed using expenses before credits from the Adviser.
- (K) Ratio of net expenses to average net assets is computed using total expenses net of any credits received from the Adviser.

NOTE 13. UNCONSOLIDATED SIGNIFICANT SUBSIDIARIES

In accordance with the SEC's Regulation S-X, we have subsidiaries that are not required to be consolidated. We have certain unconsolidated subsidiaries, specifically Galaxy Tool Holdings, Inc. (Galaxy), SOG Specialty K&T, LLC (SOG), Danco Acquisition Corp. (Danco) and Venyu, as of March 31 and September 30, 2013 and for the six months ended September 30, 2013 and 2012, that meet the significance conditions of the SEC's Regulation S-X. Accordingly, summarized, comparative financial information, in aggregate, is presented below for our significant unconsolidated subsidiaries.

Income Statement^(A)	For the Six Months Ended September 30,	
	2013	2012
Net Sales	\$ 52,898	\$ 44,965
Gross Profit	17,972	17,267
Net loss	(755)	(412)

- (A) Reflects only five months of summarized income statement information of Venyu in 2013, as it was exited in August 2013 and is no longer in our portfolio as of September 30, 2013.

NOTE 14. SUBSEQUENT EVENTS*Portfolio Activity*

Subsequent to September 30, 2013, the following significant transactions occurred:

In October 2013, we invested \$16.3 million in Alloy Die Casting Co. (ADC) through a combination of debt and equity. ADC, headquartered in Buena Park, California, is a manufacturer of high quality, finished aluminum and zinc castings for aerospace, defense, aftermarket automotive and industrial applications. Our affiliated fund Gladstone Capital Corporation participated as a co-investor by providing \$7.0 million of debt and equity financing at the same price and with the same terms as our investment.

In October 2013, we received full repayment of our debt investments in Channel Technologies Group, LLC (Channel) in the aggregate amount of \$16.2 million. We also received prepayment and success fee income in the amount of \$0.8 million. Simultaneously, we invested \$1.3 million in additional preferred and common equity securities in Channel.

In October 2013, our portfolio company ASH was sold to certain members of the existing management team at ASH. As a result of the sale, we received \$12 in net cash proceeds, recognized a realized loss of \$11.4 million and have retained a \$5.0 million accruing revolving credit facility in ASH. As of September 30, 2013, our debt investments in ASH were on non-accrual status and the entire investment in ASH had a fair value of zero.

Short-Term Loan

On September 27, 2013, we purchased \$25.0 million of T-Bills through Jefferies. The T-Bills were purchased on margin using \$3.0 million in cash and the proceeds from a \$22.0 million short-term loan from Jefferies with an effective annual interest rate of approximately 1.35%. On October 3, 2013, when the T-Bills matured, we repaid the \$22.0 million loan from Jefferies and received the \$3.0 million margin payment sent to Jefferies to complete the transaction.

Distributions

On October 8, 2013, our Board of Directors declared the following monthly cash distributions to common and preferred stockholders:

Declaration Date	Record Date	Payment Date	Distribution per Term	
			Common Share	Share
October 8, 2013	October 22, 2013	October 31, 2013	\$ 0.06	\$ 0.1484375
October 8, 2013	November 14, 2013	November 29, 2013	0.06	0.1484375
October 8, 2013	December 16, 2013	December 31, 2013	0.06	0.1484375
Total for the Quarter:			\$ 0.18	\$ 0.4453125

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The monthly common distributions for the quarter ending December 31, 2013 represent a 20% increase from the common distributions declared by our Board of Directors for the quarter ended September 30, 2013. The October 2013 common distribution will represent the 100th consecutive monthly common distribution we have made since our initial public offering in June 2005.

On October 28, 2013, our Board of Directors declared the following one-time special cash distribution to common stockholders:

Declaration Date	Record Date	Payment Date	Distribution per Common Share
October 28, 2013	November 18, 2013	November 29, 2013	\$ 0.05

Table of Contents**ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

All statements contained herein, other than historical facts, may constitute forward-looking statements. These statements may relate to, among other things, our future operating results, our business prospects and the prospects of our portfolio companies, actual and potential conflicts of interest with Gladstone Management Corporation and its affiliates, the use of borrowed money to finance our investments, the adequacy of our financing sources and working capital, and our ability to co-invest, among other factors. In some cases, you can identify forward-looking statements by terminology such as estimate, may, might, believe, will, provided, anticipate, future, could, growth, plan, intend, expect, should, would, if, seek, possible, negative of such terms or comparable terminology. These forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by such forward-looking statements. We caution readers not to place undue reliance on any such forward-looking statements. We have based forward-looking statements on information available to us on the date of this report, and we undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, after the date of this Quarterly Report on Form 10-Q.

The following analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and the notes thereto contained elsewhere in this Quarterly Report on Form 10-Q and in our Annual Report on Form 10-K for the fiscal year ended March 31, 2013, filed with the Securities and Exchange Commission (SEC) on May 14, 2013.

OVERVIEW**General**

We are an externally-managed, closed-end, non-diversified management investment company that has elected to be regulated as a business development company (BDC) under the Investment Company Act of 1940, as amended (the 1940 Act). In addition, for United States (U.S.) federal income tax purposes, we have elected to be treated as a regulated investment company (RIC) under Subchapter M of the Internal Revenue Code of 1986, as amended (the Code). As a BDC and a RIC, we are also subject to certain constraints, including limitations imposed by the 1940 Act and the Code.

We were incorporated under the General Corporation Law of the State of Delaware on February 18, 2005. We were established for the purpose of investing in debt and equity securities of established private businesses in the U.S. Debt investments primarily come in the form of three types of loans: senior term loans, senior subordinated loans and junior subordinated debt. Equity investments primarily take the form of preferred or common equity (or warrants or options to acquire the foregoing), often in connection with buyouts and other recapitalizations. To a much lesser extent, we also invest in senior and subordinated syndicated loans. Our investment objectives are (a) to achieve and grow current income by investing in debt securities of established businesses that we believe will provide stable earnings and cash flow to pay expenses, make principal and interest payments on our outstanding indebtedness and make distributions to stockholders that grow over time and (b) to provide our stockholders with long-term capital appreciation in the value of our assets by investing in equity securities of established businesses that we believe can grow over time to permit us to sell our equity investments for capital gains. We aim to maintain a portfolio allocation of approximately 80% debt investments and 20% equity investments, at cost.

We focus on investing in small and medium-sized private U.S. businesses that meet certain criteria, including some but not all of the following: the potential for growth in cash flow, adequate assets for loan collateral, experienced management teams with a significant ownership interest in the borrower, profitable operations based on the borrower's cash flow, reasonable capitalization of the borrower (usually by leveraged buyout funds or venture capital funds) and the potential to realize appreciation and gain liquidity in our equity position, if any. We anticipate that liquidity in our equity position will be achieved through a merger or acquisition of the borrower, a public offering of the borrower's stock or by exercising our right to require the borrower to repurchase our warrants, though there can be no assurance that we will always have these rights. We lend to borrowers that need funds to finance growth, restructure their balance sheets or effect a change of control. We invest by ourselves or jointly with other funds and/or management of the portfolio company, depending on the opportunity. If we are participating in an investment with one or more co-investors, our investment is likely to be smaller than if we were investing alone.

Our common stock and 7.125% Series A Cumulative Term Preferred Stock (our Term Preferred Stock) are traded on the NASDAQ Global Select Market (NASDAQ) under the symbols GAIN and GAINP, respectively.

We are externally managed by our investment advisor, Gladstone Management Corporation (our Adviser), an SEC registered investment adviser and an affiliate of ours, pursuant to an investment advisory and management agreement (the Advisory

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Agreement). The Adviser manages our investment activities. Our Board of Directors, which is composed of a majority of independent directors, supervises such investment activities. We have also entered into an administration agreement (the Administration Agreement) with Gladstone Administration, LLC (our Administrator), an affiliate of ours and the Adviser, whereby we pay separately for administrative services.

Business Environment

The strength of the global economy, and the U.S. economy in particular, continues to be uncertain and volatile, and we remain cautious about a long-term economic recovery. The effects of the previous recession and the disruptions in the capital markets in particular, have impacted our liquidity options and increased our cost of debt and equity capital. In addition, the recent federal government shutdown and debt ceiling impasse combined with the uncertainty surrounding the ability of the federal government to address its fiscal condition in both the near and long term have increased domestic and global economic instability. Many of our portfolio companies, as well as those that we evaluate for possible investments, are adversely impacted by these political and economic conditions. If these conditions persist, it may adversely affect their ability to repay our loans or engage in a liquidity event, such as a sale, recapitalization or initial public offering.

New Investment and Realized Gains from Exits

While conditions remain challenging, we are seeing an increase in the number of new investment opportunities consistent with our investing strategy of providing a combination of debt and equity in support of management and sponsor-led buyouts of small and medium-sized companies in the U.S. These opportunities along with the capital raising efforts discussed below have allowed us to invest approximately \$239.1 million in 14 new proprietary debt and equity deals since October 2010. During the three months ended September 30, 2013, we invested a total of \$20.0 million in one new deal, and subsequent to September 30, 2013, we invested \$16.3 million in another new deal.

These new investments, as well as the majority of our debt securities in our portfolio, have a success fee component, which enhances the yield on our debt investments. Unlike paid in kind (PIK) income, we do not recognize the fee into income until it is received in cash. As a result, as of September 30, 2013, we had an off-balance sheet success fee receivable of \$15.1 million, or approximately \$0.57 per common share. Due to their contingent nature, there are no guarantees that we will be able to collect all of these success fees or know the timing of such collections.

The improved investing environment in the second quarter presented us with an opportunity to realize gains and other income from our investment in Venyu Solutions, Inc. (Venyu) as a result of its sale in August 2013. As a result of the sale, we received net cash proceeds of \$32.2 million, resulting in a realized gain of \$24.8 million and dividend income of \$1.4 million. In addition, we received full repayment of our debt investments of \$19.0 million and \$1.8 million in success fee income. This represents our fourth management-supported buyout liquidity event since June 2010, and in the aggregate, these four liquidity events have generated \$54.5 million in realized gains and \$13.1 million in other income, for a total increase to our net assets of \$67.6 million. We believe each of these transactions was an equity investment success and support our investment strategy of striving to achieve returns through current income on the debt portion of our investments and capital gains from the equity portion. These successes, in part, enabled us to increase the monthly distribution 50% since March 2011, allowed us to declare a one-time special distribution in fiscal year 2012, and most recently, to declare a \$0.05 per common share one-time special distribution in November 2013.

Capital Raising Efforts

Despite the challenges that have existed in the economy for the past several years, we have been able to meet our capital needs through enhancements to our revolving line of credit (our Credit Facility) and by accessing the capital

markets in the form of public offerings of preferred and common stock. For example, in March 2012, we issued 1.6 million shares of our Term Preferred Stock for gross proceeds of \$40.0 million, and, in October 2012, we issued 4.4 million shares of common stock for gross proceeds of \$33.0 million. In October 2012, we extended the maturity date on our Credit Facility an additional year to 2015, and subsequently, in April and May 2013, we further extended the maturity date another six months into 2016 and increased the commitment amount from \$60 million to \$105 million.

Although we have been able to access the capital markets over the past two years, we believe market conditions continue to affect the trading price of our common stock and thus our ability to finance new investments through the issuance of equity. On November 5, 2013, the closing market price of our common stock was \$7.07, which represented a 22.5% discount to our September 30, 2013, net asset value (NAV) per share of \$9.12. When our stock trades below NAV, our ability to issue equity is constrained by provisions of the Investment Company Act of 1940 (the 1940 Act), which generally prohibits the issuance and sale of our common stock at an issuance price below the then current NAV per share without stockholder approval, other than through sales to our then-existing stockholders pursuant to a rights offering.

At our Annual Meeting of Stockholders held on August 8, 2013, our stockholders ratified a proposal authorizing us to issue and sell shares of our common stock at a price below our then current NAV per share, subject to certain limitations, including that the number

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of shares issued and sold pursuant to such authority does not exceed 25% of our then outstanding common stock immediately prior to each such sale, provided that our Board of Directors makes certain determinations prior to any such sale. This August 2013 shareholder authorization is in effect for one year from the date of stockholder approval. Prior to the August 2013 shareholder authorization, we sought and obtained shareholder approval concerning a similar proposal at the Annual Meeting of Stockholders held in August 2012, and with our Board of Directors' approval, we issued shares of our common stock in October and November 2012 at a price per share below the then current NAV per share. The resulting proceeds, in part, have allowed us to grow the portfolio by making new investments, generate additional income through these new investments, provide us additional equity capital to help ensure continued compliance with regulatory tests and increase our debt capital while still complying with our applicable debt-to-equity ratios.

Regulatory Compliance

Due to the limited number of investments in our portfolio, our current asset composition has affected our ability to satisfy certain elements of the rules of the Code, for maintenance of our status as a RIC under the Code. To maintain our status as a RIC, in addition to other requirements, as of the close of each quarter of our taxable year, we must meet the asset diversification test, which requires that at least 50% of the value of our assets consist of cash, cash items, U.S. government securities or certain other qualified securities (the 50% threshold). During the six months ended September 30, 2013, we again fell below the 50% threshold.

Failure to meet the 50% threshold alone will not result in our loss of RIC status. In circumstances where the failure to meet the 50% threshold is the result of fluctuations in the value of our assets, including as a result of the sale of assets, we will still be deemed to have satisfied the 50% threshold and, therefore, maintain our RIC status, provided that we have not made any new investments, including additional investments in our existing portfolio companies (such as advances under outstanding lines of credit), since the time that we fell below the 50% threshold. As of September 30, 2013, we satisfied the 50% threshold primarily through the purchase of short-term qualified securities, which was funded through a short-term loan agreement. Subsequent to the September 30, 2013, measurement date, the short-term qualified securities matured and we repaid the short-term loan. See *Recent Developments Short-Term Loan* for more information regarding this transaction. As of the date of this filing, we are once again below the 50% threshold.

Thus, while we currently qualify as a RIC despite our recent inability to continuously meet the 50% threshold and potential inability to do so in the future, if we make any new or additional investments before regaining continuous compliance with the asset diversification test, our RIC status could be threatened. If we make a new or additional investment and fail to regain compliance with the 50% threshold on the next quarterly measurement date following such investment, we will not be in compliance with the RIC rules and will have thirty days to cure our failure to meet the 50% threshold to avoid the loss of our RIC status. Potential cures for failure of the asset diversification test include raising additional equity or debt capital, or changing the composition of our assets, which could include full or partial divestitures of investments, such that we would once again exceed the 50% threshold on a consistent basis.

Until the composition of our assets satisfies the required 50% threshold on a consistent basis, we will continue to seek to employ similar purchases of qualified securities using short-term loans that would allow us to satisfy the 50% threshold, thereby allowing us to make additional investments. There can be no assurance, however, that we will be able to enter into such a transaction on reasonable terms, if at all. We also continue to explore a number of other strategies, including changing the composition of our assets, which could include full or partial divestitures of investments, and raising additional equity or debt capital, such that we would once again exceed the 50% threshold on a consistent basis. Our ability to implement any of these strategies will be subject to market conditions and a number of risks and uncertainties that are, in part, beyond our control.

Our ability to seek external debt financing, to the extent that it is available under current market conditions, is further subject to the asset coverage limitations of the 1940 Act, which require us to have an asset coverage ratio (as defined in Section 18(h) of the 1940 Act), of at least 200% on our senior securities representing indebtedness and our senior securities that are stock, which we refer to collectively as senior securities. As of September 30, 2013, our asset coverage ratio was 328%. The ratio is impacted, in part, by our need to obtain a short-term loan at quarter end to satisfy the 50% threshold for our RIC status. Between the quarter end measurement dates, when we do not have a short-term loan outstanding, our leverage and asset coverage ratio improve. However, until the composition of our assets is above the required 50% threshold on a consistent basis, we will have to continue to obtain short-term loans on a quarterly basis. This strategy, while allowing us to satisfy the 50% threshold for our RIC status, limits our ability to use increased debt capital to make new investments, due to our asset coverage ratio limitations under the 1940 Act. Our common stock offering in October 2012, was undertaken, in part, to provide us additional equity capital to help ensure continued compliance with the 200% asset coverage ratio.

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Investment Highlights

During the three months ended September 30, 2013, we disbursed \$20.0 million in new debt and equity investments and extended \$0.4 million of investments to existing portfolio companies through revolver draws or additions to term notes. From our initial public offering in June 2005 through September 30, 2013, we have made 203 investments in 102 companies for a total of approximately \$854.6 million, before giving effect to principal repayments on investments and divestitures.

Investment Activity

During the six months ended September 30, 2013, the following significant transactions occurred:

In April 2013, we invested \$17.7 million in Jackrabbit, Inc. (Jackrabbit) through a combination of debt and equity. Jackrabbit, headquartered in Ripon, California, is a manufacturer of nut harvesting equipment.

In May 2013, we invested \$8.8 million in Funko, LLC (Funko) through a combination of debt and equity. Funko, headquartered in Lynnwood, Washington, is a designer, importer and marketer of pop-culture collectibles. This was our first co-investment with our affiliated fund Gladstone Capital Corporation pursuant to an exemptive order granted by the SEC in July 2012.

In June 2013, we invested \$9.0 million in Star Seed, Inc. (Star Seed) through a combination of debt and equity. Based in Osborne, Kansas, Star Seed provides its customers with a variety of specialty seeds and related products.

In August 2013, we invested \$20.0 million in Schylling, Inc. (Schylling) through a combination of debt and equity. Schylling, headquartered in Rowley, Massachusetts, is a premier provider of high quality specialty toys.

In August 2013, our portfolio company Venyu was sold. As a result of the sale, we received net cash proceeds of \$32.2 million, resulting in a realized gain of approximately \$24.8 million and dividend income of \$1.4 million. In addition, we received full repayment of our debt investment of \$19 million in principal repayment and \$1.9 million in fee income.

Subsequent to September 30, 2013, the following significant transactions occurred:

In October 2013, we invested \$16.3 million in Alloy Die Casting Co. (ADC) through a combination of debt and equity. ADC, headquartered in Buena Park, California, is a manufacturer of high quality, finished aluminum and zinc castings for aerospace, defense, aftermarket automotive and industrial applications. Our affiliated fund Gladstone Capital Corporation participated as a co-investor by providing \$7.0 million of debt and equity financing at the same price and with the same terms as our investment.

In October 2013, we received full repayment of our debt investments in Channel Technologies Group, LLC (Channel) in the aggregate amount of \$16.2 million. We also received prepayment and success fee income in the amount of \$0.8 million. Simultaneously, we invested \$1.3 million in additional preferred and common equity securities in Channel

In October 2013, our portfolio company ASH Holding Corp. (ASH) was sold to certain members of the existing management team at ASH. As a result of the sale, we received \$12 in net cash proceeds, recognized a realized loss of \$11.4 million and have retained a \$5.0 million accruing revolving credit facility in ASH. As of September 30, 2013, our debt investments in ASH were on non-accrual status and the entire investment in ASH had a fair value of zero.

Recent Developments

Credit Facility Extension and Expansion

On April 30, 2013, we, through our wholly-owned subsidiary, Business Investment, entered into a fifth amended and restated credit agreement with Key Equipment Finance Inc., as administrative agent, lead arranger and a lender (the Administrative Agent), Branch Banking and Trust Company as a lender and managing agent, and the Adviser, as servicer, to increase the commitment amount of the Credit Facility from \$60.0 million to \$70.0 million and to extend the maturity date as described below. The maturity date was extended to April 30, 2016 (the Maturity Date) and, if not renewed or extended by the Maturity Date, all principal and interest will be due and payable on or before April 30, 2017 (one year after the Maturity Date). In addition, there are two one-year extension options to be agreed upon by all parties, which may be exercised on or before April 30, 2014 and 2015, respectively. Subject to certain terms and conditions, the Credit Facility may be expanded up to a total of \$200.0 million through the addition of other lenders to the facility. Advances under the Credit Facility generally bear interest at 30-day LIBOR, plus 3.75% per annum, and the Credit Facility includes an unused fee of 0.50% on undrawn amounts. We incurred fees of approximately \$0.3 million in connection with this amendment.

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On June 12, 2013, we further increased the borrowing capacity under the Credit Agreement from \$70.0 million to \$105.0 million by entering into Joinder Agreements pursuant to the Credit Agreement by and among Business Investment, the Administrative Agent, the Adviser and each of Alostar Bank of Commerce and Everbank Commercial Finance, Inc.

Short-Term Loan

For each quarter end since December 31, 2009 (the measurement dates), we satisfied the 50% threshold to maintain our status as a RIC, in part, through the purchase of short-term qualified securities, which were funded primarily through a short-term loan agreement. Subsequent to each of the measurement dates, the short-term qualified securities matured, and we repaid the short-term loan, at which time we again fell below the 50% threshold.

For the September 30, 2013 measurement date, we purchased \$25.0 million of short-term United States Treasury Bills (T-Bills) through Jefferies & Company, Inc. (Jefferies) on September 27, 2013. The T-Bills were purchased on margin using \$3.0 million in cash and the proceeds from a \$22.0 million short-term loan from Jefferies with an effective annual interest rate of approximately 1.35%. On September 3, 2013, when the T-Bills matured, we repaid the \$22.0 million loan from Jefferies and received the \$3.0 million margin payment sent to Jefferies to complete the transaction.

RESULTS OF OPERATIONS*Comparison of the Three months ended September 30, 2013, to the Three months ended September 30, 2012*

	For the Three Months Ended September 30,			
	2013	2012	\$ Change	% Change
INVESTMENT INCOME				
Interest income	\$ 7,706	\$ 6,461	\$ 1,245	19.3%
Other income	3,653	513	3,140	612.1
Total investment income	11,359	6,974	4,385	62.9
EXPENSES				
Base management fee	1,561	1,308	253	19.3
Incentive fee	1,557	541	1,016	187.8
Administration fee	156	189	(33)	(17.5)
Interest and dividend expense	1,309	1,197	112	9.4
Amortization of deferred financing costs	256	203	53	26.1
Other	626	600	26	4.3
Expenses before credits from Adviser	5,465	4,038	1,427	35.3
Credits to fees	(334)	(515)	181	(35.1)
Total expenses net of credits to fees	5,131	3,523	1,608	45.6
NET INVESTMENT INCOME	6,228	3,451	2,777	80.5

REALIZED AND UNREALIZED GAIN (LOSS):

Net realized gain on investments	24,804	798	24,006	3,008.3
Net unrealized depreciation of investments	(15,684)	(3,884)	(11,800)	(303.8)
Net unrealized (appreciation) of other	(409)	(718)	309	43.0

Net realized and unrealized gain (loss) on investments and other	8,711	(3,804)	12,515	NM
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NET INCREASE (DECREASE) IN NET

ASSETS RESULTING FROM OPERATIONS	\$ 14,939	\$ (353)	\$ 15,292	NM
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BASIC AND DILUTED PER COMMON SHARE:

Net investment income	\$ 0.24	\$ 0.16	\$ 0.08	50.0%
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Net increase (decrease) in net assets resulting from operations	\$ 0.57	\$ (0.02)	\$ 0.59	NM
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NM = Not Meaningful

Investment Income

Total investment income increased by 62.9% for the three months ended September 30, 2013, as compared to the prior year period. This increase was primarily due an overall increase in interest income in the three months ended September 30, 2013, as a result of an increase in the size of our loan portfolio and holding higher-yielding debt investments during the three months ended September 30, 2013, as well as an increase in other income, which primarily consisted of success fee and dividend income resulting from our exit of Venyu during the three months ended September 30, 2013.

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Interest income from our investments in debt securities increased 19.3% for the three months ended September 30, 2013, as compared to the prior year period. The level of interest income from investments is directly related to the principal balance of our interest-bearing investment portfolio outstanding during the period multiplied by the weighted average yield. The weighted average principal balance of our interest-bearing investment portfolio during the three months ended September 30, 2013, was approximately \$242.8 million, compared to approximately \$204.7 million for the prior year period. This increase was primarily due to approximately \$71.9 million in new investments originated after September 30, 2012, including Frontier Packaging, Inc. (Frontier), Jackrabbit, Funko, Star Seed, and Schylling, as well as the recapitalization of Galaxy Tool Holding Corp (Galaxy), partially offset with the exit of Venyu. As of September 30, 2013 and 2012, loans to two portfolio companies, ASH and Tread Corp. (Tread), were on non-accrual, with an aggregate weighted average principal balance of \$26.1 million and \$17.2 million during the three months ended September 30, 2013 and 2012, respectively. The weighted average yield on our interest-bearing investments for the three months ended September 30, 2013 and 2012, excluding cash and cash equivalents and receipts recorded as other income, was 12.6% and 12.5%, respectively. The weighted average yield varies from period to period, based on the current stated interest rate on interest-bearing investments.

The following table lists the investment income for our five largest portfolio company investments based on fair value during the respective periods:

Portfolio Company	As of September 30, 2013		Three months ended September 30, 2013	
	Fair Value	% of Portfolio	Investment Income	% of Total Investment Income
Acme Cryogenics, Inc.	\$ 27,771	9.7%	\$ 426	3.8%
Galaxy Tool Holding Corp.	24,156	8.4	535	4.7
SOG Specialty Knives and Tools, LLC	24,131	8.4	670	5.9
Schylling Investments, LLC ^(A)	20,000	7.0	312	2.7
Channel Technologies Group, LLC	19,642	6.8	468	4.1
Subtotal five largest investments^(B)	115,700	40.3	2,411	21.2
Other portfolio companies	171,512	59.7	8,948	78.8
Total investment portfolio	\$ 287,212	100.0%	\$ 11,359	100.0%

Portfolio Company	As of September 30, 2012		Three months ended September 30, 2012	
	Fair Value	% of Portfolio	Investment Income	% of Total Investment Income
SOG Specialty Knives and Tools, LLC	\$ 29,731	11.2%	\$ 670	9.6%
Acme Cryogenics, Inc.	26,215	9.8	426	6.1
Venyu Solutions, Inc.	22,663	8.5	631	9.1
Ginsey Holdings, Inc. ^(A)	22,452	8.4	440	6.3
SBS, Industries, LLC	18,227	6.8	406	5.8
Subtotal five largest investments	119,288	44.7	2,573	36.9
Other portfolio companies	147,398	55.3	4,401	63.1

Total investment portfolio	\$ 266,686	100.0%	\$ 6,974	100.0%
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(A) New investment during the applicable period.

(B) Venyu was exited in August 2013. Investment income for Venyu for the three months ended September 30, 2013 was \$3.7 million, or 32.6% of total investment income.

Other income increased 612.1% from the prior year period, primarily due to \$3.3 million in success fee and dividend income received in connection with the exit of Venyu and \$0.3 million in success fee income resulting from prepayments received from Cavert II Holding Corp. (Cavert) during the three months ended September 30, 2013. During the three months ended September 30, 2012, other income primarily consisted of \$0.4 million in success fee income resulting from prepayments received from Cavert.

Expenses

Total expenses, excluding any voluntary and irrevocable credits to the base management and incentive fees, increased 35.3% for the three months ended September 30, 2013, as compared to the prior year period, primarily due to an increase in the base management fee, incentive fee and interest expense, as compared to the prior year period.

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The base management fee increased for the three months ended September 30, 2013, as compared to the prior year period, as a result of the increased size of our portfolio over the respective periods. Additionally, an incentive fee of \$1.6 million was earned by the Adviser during the three months ended September 30, 2013, compared to \$0.5 million for the prior year period. The base management and incentive fees are computed quarterly, as described under Investment Advisory and Management Agreement in Note 4 of the notes to our accompanying *Condensed Consolidated Financial Statements*, and are summarized in the following table:

	Three Months Ended September 30,	
	2013	2012
Average gross assets subject to base management fee ^(A)	\$ 312,200	\$ 261,600
Multiplied by prorated annual base management fee of 2%	0.5%	0.5%
Base management fee ^(B)	1,561	1,308
Credit for fees received by Adviser from the portfolio companies ^(B)	(334)	(515)
Net base management fee	\$ 1,227	\$ 793
Incentive fee ^(B)	\$ 1,557	\$ 541

(A) Average gross assets subject to the base management fee is defined as total assets, including investments made with proceeds of borrowings, less any uninvested cash or cash equivalents resulting from borrowings, valued at the end of the applicable quarters within the respective periods and adjusted appropriately for any share issuances or repurchases during the periods.

(B) Reflected as a line item on our accompanying *Condensed Consolidated Statement of Operations*. Interest and dividend expense increased 9.4% for the three months ended September 30, 2013, as compared to the prior year period, primarily due to increased commitment (unused) fees related to the expansion of our Credit Facility from \$60.0 million to \$105.0 and increased average borrowings under the Credit Facility. The average balance outstanding on our Credit Facility during the three months ended September 30, 2013, was \$41.4 million, as compared to \$39.0 million in the prior year period.

Realized and Unrealized Gain (Loss) on Investments*Realized Gain*

During the three months ended September 30, 2013, we recorded a realized gain of \$24.8 million related to the Venyu exit. During the three months ended September 30, 2012, we recorded a realized gain of \$0.8 million relating to post-closing adjustments on the previous investment exit of A. Stucki Holding Corp. (A. Stucki).

Unrealized Depreciation

During the three months ended September 30, 2013, we recorded net unrealized depreciation on investments in the aggregate amount of \$15.7 million, which included the reversal of \$17.4 million in aggregate unrealized appreciation, related to the Venyu exit. Excluding reversals, we had \$1.7 million in net unrealized appreciation for the three months ended September 30, 2013.

The realized gains (losses) and unrealized appreciation (depreciation) across our investments for the three months ended September 30, 2013, were as follows:

Portfolio Company	Three months ended September 30, 2013			
	Realized Gain	Unrealized Appreciation (Depreciation)	Reversal of Unrealized (Appreciation)	Net Gain (Loss)
Venyu Solutions, Inc. ^(A)	\$ 24,804	\$	\$ (17,374)	\$ 7,430
Channel Technologies Group, LLC		3,372		3,372
Jackrabbit, Inc.		3,261		3,261
Country Club Enterprises, LLC		1,565		1,565
Star Seed, Inc.		926		926
Acme Cryogenics, Inc.		864		864
Frontier Packaging, Inc.		757		757
Funko, LLC		396		396
B-Dry, LLC		(502)		(502)
Mitchell Rubber Products, Inc.		(629)		(629)
Ginsey Home Solutions, Inc.		(800)		(800)
Drew Foam Company, Inc.		(998)		(998)
Quench Holdings Corp.		(1,648)		(1,648)
SBS, Industries, LLC		(2,291)		(2,291)
SOG Specialty K&T, LLC		(2,767)		(2,767)
Other, net (<\$250 Net)		184		184
Total	\$ 24,804	\$ 1,690	\$ (17,374)	\$ 9,120

(A) Venyu was sold in August 2013.

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Excluding reversals, the primary changes in our net unrealized appreciation of \$1.7 million for the three months ended September 30, 2013, were due to increased equity valuations in several of our portfolio companies, primarily due to increased portfolio company performance, and, to a lesser extent, an increase in certain comparable multiples used to estimate the fair value of our investments.

During the three months ended September 30, 2012, we recorded net unrealized depreciation on investments in the aggregate amount of \$3.9 million. The realized gains (losses) and unrealized appreciation (depreciation) across our investments for the three months ended September 30, 2012 was as follows:

Portfolio Company	Three months ended September 30, 2012		
	Realized Gain (Loss)	Unrealized Appreciation (Depreciation)	Net Gain (Loss)
Galaxy Tool Holding Corp.	\$	\$ 5,762	\$ 5,762
Country Club Enterprises, LLC		2,292	2,292
A. Stucki Corp. ^(A)	799		799
Venyu Solutions, Inc.		711	711
SBS, Industries, LLC		424	424
B-Dry, LLC		(315)	(315)
ASH Holdings Corp.		(320)	(320)
Quench Holdings Corp.		(580)	(580)
Noble Logistics, Inc.		(586)	(586)
Channel Technologies Group, LLC		(671)	(671)
SOG Specialty K&T, LLC		(823)	(823)
Acme Cryogenics, Inc.		(1,166)	(1,166)
Packerland Whey Products, Inc.		(1,490)	(1,490)
Danco Acquisition Corp.		(1,996)	(1,996)
Mitchell Rubber Products, Inc.		(2,356)	(2,356)
Tread Corp.		(2,652)	(2,652)
Other, net (<\$250 Net)	(1)	(118)	(119)
Total	\$ 798	\$ (3,884)	\$ (3,086)

^(A) A. Stucki Corp. was sold in June 2010.

The primary changes in our net unrealized depreciation for the three months ended September 30, 2012, were notable depreciation of our debt investments in Danco Acquisition Corp. (Danco) and in our equity investments in Tread and Mitchell Rubber Products, Inc. (Mitchell), primarily due to decreased portfolio company performance and, to a lesser extent, a decrease in certain comparable multiples used to estimate the fair value of our investments. This depreciation was partially offset by increased appreciation in Galaxy and Country Club Enterprises, LLC (CCE), primarily due to increased portfolio company performance.

Over our entire investment portfolio, we recorded, in the aggregate, approximately \$0.3 million of net unrealized appreciation on our debt positions and \$16.1 million of net unrealized depreciation on our equity holdings for the three months ended September 30, 2013. As of September 30, 2013, the fair value of our investment portfolio was less than

our cost basis by approximately \$67.2 million, as compared to \$51.4 million at June 30, 2013, representing net unrealized depreciation of \$15.8 million for the three months ended September 30, 2013. We believe that our aggregate investment portfolio was valued at a depreciated value due to the lingering effects of the recent recession on the performance of certain of our portfolio companies. Our entire portfolio was fair valued at 81.0% of cost as of September 30, 2013. The unrealized depreciation of our investments does not have an impact on our current ability to pay distributions to stockholders; however, it may be an indication of future realized losses, which could ultimately reduce our income available for distribution.

Unrealized Appreciation on Other

The net unrealized appreciation on our Credit Facility for the three months ended September 30, 2013 and 2012, was \$0.4 million and \$0.7 million, respectively, primarily due to increased borrowings outstanding and comparable market rates decreasing during both periods. The Credit Facility was fair valued at \$34.3 million and \$31.9 million as of September 30 and March 31, 2013, respectively.

Table of Contents**Comparison of the Six Months Ended September 30, 2013, to the Six Months Ended September 30, 2012**

	Six Months Ended September 30,			
	2013	2012	\$ Change	% Change
INVESTMENT INCOME				
Interest income	\$ 14,888	\$ 11,971	\$ 2,917	24.4%
Other income	3,869	907	2,962	326.6
Total investment income	18,757	12,878	5,879	45.7
EXPENSES				
Base management fee	3,110	2,499	611	24.4
Incentive fee	1,722	541	1,181	218.3
Administration fee	399	372	27	7.3
Interest and dividend expense	2,499	2,001	498	24.9
Amortization of deferred financing fees	499	403	96	23.8
Other	1,112	1,073	39	3.6
Expenses before credits from Adviser	9,341	6,889	2,452	35.6
Credits to fees	(845)	(700)	(145)	20.7
Total expenses net of credits to fee	8,496	6,189	2,307	37.3
NET INVESTMENT INCOME	10,261	6,689	3,572	53.4
REALIZED AND UNREALIZED LOSS ON:				
Net realized gain on sale of investments	24,804	753	24,051	3,194.0
Net realized loss on other		(41)	41	NM
Net unrealized depreciation on investments	(27,090)	(9,601)	(17,489)	(182.2)
Net unrealized depreciation (appreciation) on other	445	(1,169)	1,614	NM
Net loss on investments and other	(1,841)	(10,058)	8,217	81.7
NET INCREASE (DECREASE) IN NET ASSETS RESULTING FROM OPERATIONS	\$ 8,420	\$ (3,369)	\$ 11,789	NM
BASIC AND DILUTED PER COMMON SHARE:				
Net investment income	\$ 0.39	\$ 0.31	\$ 0.08	25.8%
Net increase (decrease) in net assets resulting from operations	\$ 0.32	\$ (0.15)	\$ 0.47	NM

NM = Not Meaningful

Total investment income increased by 45.7% for the six months ended September 30, 2013, as compared to the prior year period. This increase was primarily due an overall increase in interest income in the six months ended September 30, 2013, as a result of an increase in the size of our loan portfolio and holding higher-yielding debt investments during the six months ended September 30, 2013, as well as an increase in other income, which primarily consisted of success fee and dividend income resulting from our exit from Venyu during the six months ended September 30, 2013.

Interest income from our investments in debt securities increased 24.4% for the six months ended September 30, 2013, as compared to the prior year period. The level of interest income from investments is directly related to the principal balance of our interest-bearing investment portfolio outstanding during the period multiplied by the weighted average yield. The weighted average principal balance of our interest-bearing investment portfolio during the six months ended September 30, 2013, was approximately \$236.4 million, compared to approximately \$191.0 million for the prior year period. This increase was primarily due to approximately \$71.9 million in new investments originated after September 30, 2012, including Frontier, Jackrabbit, Funko, Star Seed, and Schylling, as well as the recapitalization of Galaxy, partially offset by the exit of Venyu. As of September 30, 2013 and 2012, loans to two portfolio companies, ASH and Tread, were on non-accrual, with an aggregate weighted average principal balance of \$25.8 million and \$17.1 million during the six months ended September 30, 2013 and 2012, respectively. The weighted average yield on our interest-bearing investments for the six months ended September 30, 2013 and 2012, excluding cash and cash equivalents and receipts recorded as other income, was 12.6% and 12.5%, respectively. The weighted average yield varies from period to period, based on the current stated interest rate on interest-bearing investments.

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The following table lists the investment income from investments for our five largest portfolio company investments based on fair value during the respective periods:

Portfolio Company	Fair Value	% of Portfolio	As of September 30, 2013 Months Ended September 30, 2013	
			Investment Income	% of Total Investment Income
Acme Cryogenics, Inc.	\$ 27,771	9.7%	\$ 848	4.5%
Galaxy Tool Holding Corp.	24,156	8.4	1,065	5.7
SOG Specialty Knives and Tools, LLC	24,131	8.4	1,332	7.1
Schylling Investments, LLC ^(A)	20,000	7.0	312	1.7
Channel Technologies Group, LLC	19,642	6.8	926	4.9
Subtotal five largest investments^(B)	115,700	40.3	4,483	23.9
Other portfolio companies	171,512	59.7	14,274	76.1
Total investment portfolio	\$ 287,212	100.0%	\$ 18,757	100.0%

Portfolio Company	Fair Value	% of Portfolio	As of September 30, 2012 Months Ended September 30, 2012	
			Investment Income	% of Total Investment Income
SOG Specialty Knives and Tools, LLC	\$ 29,731	11.2%	\$ 1,332	10.4%
Acme Cryogenics, Inc.	26,215	9.8	848	6.6
VenYu Solutions, Inc.	22,663	8.5	1,254	9.7
Ginsey Holdings, Inc. ^(A)	22,452	8.4	440	3.4
SBS, Industries, LLC	18,227	6.8	809	6.3
Subtotal five largest investments	119,288	44.7	4,683	36.4
Other portfolio companies	147,398	55.3	8,195	63.6
Total investment portfolio	\$ 266,686	100.0%	\$ 12,878	100.0%

(A) New investment during the applicable period.

(B) VenYu was exited in August 2013. Investment income for VenYu for the six months ended September 30, 2013 was \$4.3 million, or 23.1% of total investment income.

Other income increased 326.6% from the prior year period, primarily due to \$3.3 million in success fee and dividend income received in connection with the exit of VenYu and \$0.3 million and \$0.2 million in success fee income resulting from prepayments received from Cavert and Mathey Investments, Inc. (Mathey), respectively, during the six months ended September 30, 2013. During the three months ended September 20, 2012, other income primarily consisted of \$0.8 million in success fee income resulting from prepayments received from Cavert and Mathey of \$0.4 million each.

Expenses

Total expenses, excluding any voluntary and irrevocable credits to the base management and incentive fees, increased 35.6% for the six months ended September 30, 2013, as compared to the prior year period, primarily due to an increase in the base management fee, incentive fee and interest expense, as compared to the prior year period.

The base management fee increased for the six months ended September 30, 2013, as compared to the prior year period, as a result of the increased size of our portfolio over the respective periods. Additionally, an incentive fee of \$1.7 million was earned by the Adviser during the six months ended September 30, 2013, compared to \$0.5 million for the prior year period. The base management and incentive fees are computed quarterly, as described under

Investment Advisory and Management Agreement in Note 4 of the notes to our accompanying *Condensed Consolidated Financial Statements* and are summarized in the following table:

	Six Months Ended September 30,	
	2013	2012
Average gross assets subject to base management fee ^(A)	\$ 311,000	\$ 249,900
Multiplied by prorated annual base management fee of 2%	1.0%	1.0%
Base management fee ^(B)	3,110	2,499
Credit for fees received by Adviser from the portfolio companies ^(B)	(845)	(700)
Net base management fee	\$ 2,265	\$ 1,799
Incentive fee ^(B)	\$ 1,722	\$ 541

(A) Average gross assets subject to the base management fee is defined as total assets, including investments made with proceeds of borrowings, less any uninvested cash or cash equivalents resulting from borrowings, valued at the end of the applicable quarters within the respective periods and adjusted appropriately for any share issuances or repurchases during the periods.

(B) Reflected as a line item on our accompanying *Condensed Consolidated Statement of Operations*.

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Interest and dividend expense increased 24.9% for the six months ended September 30, 2013, as compared to the prior year period, primarily due to increased commitment (unused) fees related to the expansion of our Credit Facility from \$60.0 million to \$105.0 and increased average borrowings under the Credit Facility. The average balance outstanding on our Credit Facility during the six months ended September 30, 2013, was \$37.1 million, as compared to \$20.0 million in the prior year period.

Realized and Unrealized Gain (Loss) on Investments*Realized Gain*

During the six months ended September 30, 2013, we recorded a realized gain of \$24.8 million related to the Venyu sale. During the six months ended September 30, 2012, we recorded a realized gain of \$0.8 million relating to post-closing adjustments on the previous investment exit of A. Stucki.

Unrealized Depreciation

During the six months ended September 30, 2013, we recorded net unrealized depreciation on investments in the aggregate amount of \$27.1 million, which included the reversal of \$17.4 million in aggregate unrealized appreciation, related to the Venyu sale. Excluding reversals, we had \$9.7 million in net unrealized depreciation for the six months ended September 30, 2013.

The realized gains (losses) and unrealized appreciation (depreciation) across our investments for the six months ended September 30, 2013, were as follows:

Portfolio Company	Six months ended September 30, 2013			
	Realized Gain	Unrealized Appreciation (Depreciation)	Reversal of Unrealized (Appreciation) Depreciation	Net Gain (Loss)
Venyu Solutions, Inc. ^(A)	\$ 24,804	\$ (1,596)	\$ (17,374)	\$ 5,834
Galaxy Tool Holding Corp.		3,280		3,280
Jackrabbit, Inc.		3,261		3,261
Channel Technologies Group, LLC		3,152	2	3,154
Frontier Packaging, Inc.		1,852		1,852
Country Club Enterprises, LLC		1,584		1,584
Star Seed, Inc.		926		926
Acme Cryogenics, Inc.		430		430
Funko, LLC		396		396
Noble Logistics, Inc.		(383)		(383)
Tread Corp.		(1,000)		(1,000)
Precision Southeast, Inc.		(1,059)		(1,059)
Mitchell Rubber Products, Inc.		(1,554)		(1,554)
Drew Foam Company, Inc.		(2,166)		(2,166)
SBS, Industries, LLC		(2,808)		(2,808)
B-Dry, LLC		(3,512)		(3,512)
Ginsey Home Solutions, Inc.		(4,502)		(4,502)

SOG Specialty K&T, LLC		(5,691)		(5,691)
Other, net (<\$250 Net)		(328)		(328)
Total	\$ 24,804	\$ (9,718)	\$ (17,372)	\$ (2,286)

(A) Venyu was sold in August 2013.

The primary changes in our net unrealized depreciation for the six months ended September 30, 2013, were due to decreased equity valuations in several of our portfolio companies, primarily due to decreased portfolio company performance and decreases in certain comparable multiples used to estimate the fair value of our investments.

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During the six months ended September 30, 2012, we recorded net unrealized depreciation on investments in the aggregate amount of \$9.6 million. The realized gains (losses) and unrealized appreciation (depreciation) across our investments for the six months ended September 30, 2012 were as follows:

Portfolio Company	Six Months Ended September 30, 2012		
	Realized Gain (Loss)	Unrealized Appreciation (Depreciation)	Net Gain (Loss)
Country Club Enterprises, LLC	\$	\$ 6,926	\$ 6,926
Galaxy Tool Holding Corp.		4,596	4,596
SBS, Industries, LLC		1,223	1,223
Mathey Investments, Inc.		1,006	1,006
Precision Southeast, Inc.		907	907
A. Stucki Corp. ^(A)	790		790
SOG Specialty K&T, LLC		(364)	(364)
Venyu Solutions, Inc.		(667)	(667)
B-Dry, LLC		(674)	(674)
ASH Holdings Corp.		(695)	(695)
Mitchell Rubber Products, Inc.		(1,101)	(1,101)
Channel Technologies Group, LLC		(1,108)	(1,108)
Packerland Whey Products, Inc.		(1,490)	(1,490)
Acme Cryogenics, Inc.		(2,087)	(2,087)
Noble Logistics, Inc.		(4,887)	(4,887)
Danco Acquisition Corp.		(5,538)	(5,538)
Tread Corp.		(5,741)	(5,741)
Other, net (<\$250 Net)	(37)	93	56
Total	\$ 753	\$ (9,601)	\$ (8,848)

(A) A. Stucki Corp. was sold in June 2010.

The primary changes in our net unrealized depreciation for the six months ended September 30, 2012, were notable depreciation of our debt investments in Danco and in our debt and equity investments in Tread and Noble Logistics, Inc. (Noble), primarily due to decreased portfolio company performance and, to a lesser extent, a decrease in certain comparable multiples used to estimate the fair value of our investments. This depreciation was partially offset by increased appreciation in Galaxy and CCE, primarily due to increased portfolio company performance.

Over our entire investment portfolio, we recorded, in the aggregate, approximately \$4.5 million of net unrealized depreciation on our debt positions and \$22.6 million of net unrealized depreciation on our equity holdings for the six months ended September 30, 2013. As of September 30, 2013, the fair value of our investment portfolio was less than our cost basis by approximately \$67.0 million, as compared to \$39.9 million at March 31, 2013, representing net unrealized depreciation of \$27.1 million for the six months ended September 30, 2013. We believe that our aggregate investment portfolio was valued at a depreciated value due to the lingering effects of the recent recession on the performance of certain of our portfolio companies. Our entire portfolio was fair valued at 81.1% of cost as of September 30, 2013. The unrealized depreciation of our investments does not have an impact on our current ability to

pay distributions to stockholders; however, it may be an indication of future realized losses, which could ultimately reduce our income available for distribution.

Realized and Unrealized (Loss) Gain on Other

Realized Loss on Interest Rate Cap

For the six months ended September 30, 2012, we recorded a net realized loss of \$41, due to the expiration of an interest rate cap agreement. No realized losses on interest rate caps were recorded during the six months ended September 30, 2013.

Net Unrealized Depreciation (Appreciation) on Borrowings

For the six months ended September 30, 2013 and 2012, we recorded \$0.4 million and (\$1.2) million, respectively, of net unrealized depreciation (appreciation).

Table of Contents**LIQUIDITY AND CAPITAL RESOURCES****Operating Activities**

Net cash provided by (used in) operating activities for the six months ended September 30, 2013, was approximately \$3.4 million, as compared to (\$48.4) million during the six months ended September 30, 2012. This decrease in cash used in operating activities as compared to the prior year period was primarily due to the cash proceeds of \$53.0 million from the repayment of debt during the period and sale of our equity investment in Venyu in August 2013. Our cash flows from operations generally come from cash collections of interest and dividend income from our portfolio companies, as well as cash proceeds received through repayments of loan investments and sales of equity investments. These cash collections are primarily used to pay distributions to our stockholders, interest payments on our Credit Facility, dividend payments on our Term Preferred Stock, management fees to our Adviser, and other entity-level expenses.

As of September 30, 2013, we had equity investments in or loans to 24 private companies with an aggregate cost basis of approximately \$354.2 million. As of September 30, 2012, we had investments in equity investments in or loans to 20 private companies with an aggregate cost basis of approximately \$317.0 million. The following table summarizes our total portfolio investment activity during the six months ended September 30, 2013 and 2012:

	Six Months Ended September 30,	
	2013	2012
Beginning investment portfolio, at fair value	\$ 286,482	\$ 225,652
New investments	54,590	52,978
Disbursements to existing portfolio companies	1,400	10,285
Increase in investment balance due to PIK	30	
Scheduled principal repayments	(110)	(215)
Unscheduled principal repayments	(22,090)	(11,850)
Proceeds from sales	(30,804)	(1,291)
Net realized gain	24,804	753
Net unrealized depreciation	(9,718)	(9,601)
Reversal of net unrealized appreciation	(17,372)	
Other cash activity, net		(25)
Ending investment portfolio, at fair value	\$ 287,212	\$ 266,686

The following table summarizes the contractual principal repayment and maturity of our investment portfolio by fiscal year, assuming no voluntary prepayments, as of September 30, 2013:

		Amount
For the remaining six months ending March 31:	2014	\$ 9,022
For the fiscal year ending March 31:	2015	76,334
	2016	23,164
	2017	59,035
	2018	51,982

Thereafter	43,430
Total contractual repayments	\$ 262,967
Investments in equity securities	91,530
Adjustments to cost basis on debt securities	(256)
Total cost basis of investments held as of September 30, 2013:	\$ 354,241

Financing Activities

Net cash used in financing activities for the six months ended September 30, 2013, was approximately \$42.1 million and consisted primarily of net repayments of our short-term borrowings of \$36.0 million and distributions to common stockholders of \$7.9 million, partially offset by \$3.0 million in net borrowings from our Credit Facility. Net cash provided by financing activities for the six months ended September 30, 2012, was approximately \$49.8 million and consisted primarily of net proceeds from our Credit Facility of \$56.0 million, partially offset by \$6.6 million in distributions to common stockholders.

Distributions

To qualify to be taxed as a RIC and thus avoid corporate level tax on the income we distribute to our stockholders, we are required under Subchapter M of the Code, to distribute at least 90% of our ordinary income and short-term capital gains to our stockholders on an annual basis. In accordance with these requirements, we declared and paid monthly cash distributions of \$0.05 per common share for each of the six months from April 2013 through September 2013. In October 2013, our Board of Directors declared a monthly

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distribution of \$0.06 per common share for each of October, November and December 2013. Distributions for the quarter ending December 31, 2013 represent a 20% increase from the distributions declared by our Board of Directors for the quarter ended September 30, 2013. Subsequent to September 30, 2013, our Board of Directors declared a one-time special distribution of \$0.05 per common share for November 2013. Our Board of Directors declared these distributions based on estimates of net taxable income for the fiscal year.

For the fiscal year ended March 31, 2013, which includes the three months ended September 30, 2012, our distributions to common stockholders totaled approximately \$14.5 million. Distributions to common stockholders declared for the fiscal year ended March 31, 2013, were comprised 100% from ordinary income and none from a return of capital. At year-end, we elected to treat \$3.1 million of the first distribution paid after year-end as having been paid in the prior year, in accordance with Section 855(a) of the Code. The characterization of the common distributions declared and paid for the fiscal year ending March 31, 2014 will be determined at year end and cannot be determined at this time. Additionally, the covenants in our Credit Facility generally restrict the amount of distributions that we can pay out to be no greater than our net investment income.

We also declared and paid monthly cash distributions of \$0.1484375 per share of Term Preferred Stock for each of the six months from April 2013 through September 2013. In October 2013, our Board of Directors also declared a monthly distribution of \$0.1484375 per preferred share for each of October, November and December 2013. In accordance with accounting principles generally accepted in the U.S. (GAAP), we treat these monthly distributions as an operating expense. For tax purposes, these preferred distributions are deemed to be paid entirely out of ordinary income to preferred stockholders.

Equity*Registration Statement*

We filed a registration statement on Form N-2 (File No. 333-181879) with the SEC on June 4, 2012, and subsequently filed a Pre-effective Amendment No. 1 to the registration statement on July 17, 2012, which the SEC declared effective on July 26, 2012. On June 7, 2013, we filed Post-Effective Amendment No. 2 to the registration statement, which the SEC declared effective on July 26, 2013. The registration statement permits us to issue, through one or more transactions, up to an aggregate of \$300.0 million in securities, consisting of common stock, preferred stock, subscription rights, debt securities and warrants to purchase common stock, including through a combined offering of two or more of such securities.

Common Stock

Pursuant to our registration statement on Form N-2 (Registration No. 333-181879), on October 5, 2012, we completed a public offering of 4.0 million shares of our common stock at a public offering price of \$7.50 per share, which was below then current NAV of \$8.65 per share. Gross proceeds totaled \$30.0 million and net proceeds, after deducting underwriting discounts and offering expenses borne by us, were \$28.3 million, which was used to repay borrowings under our Credit Facility. In connection with the offering, the underwriters exercised their option to purchase an additional 395,825 shares at the public offering price to cover over-allotments, which resulted in gross proceeds of \$3.0 million and net proceeds, after deducting underwriting discounts, of \$2.8 million.

We anticipate issuing equity securities to obtain additional capital in the future. However, we cannot determine the terms of any future equity issuances or whether we will be able to issue equity on terms favorable to us, or at all. When our common stock is trading below NAV per share, as it has consistently since September 30, 2008, the 1940 Act places regulatory constraints on our ability to obtain additional capital by issuing common stock. Generally, the

1940 Act provides that we may not issue and sell our common stock at a price below our NAV per common share, other than to our then existing common stockholders pursuant to a rights offering, without first obtaining approval from our stockholders and our independent directors. On November 5, 2013, the closing market price of our common stock was \$7.07 per share, representing a 22.5% discount to our NAV of \$9.12 as of September 30, 2013. To the extent that our common stock continues to trade at a market price below our NAV per common share, we will generally be precluded from raising equity capital through public offerings of our common stock, other than pursuant to stockholder approval or through a rights offering to existing common stockholders. At our Annual Meeting of Stockholders held on August 8, 2013, our stockholders ratified a proposal authorizing us to issue and sell shares of our common stock at a price below our then current NAV per common share for a period of one year from the date of such approval, provided that our Board of Directors makes certain determinations prior to any such sale.

Term Preferred Stock

Pursuant to our prior registration statement on Form N-2 (Registration No. 333-160720), in March 2012, we completed an offering of 1.6 million shares of Term Preferred Stock at a public offering price of \$25.00 per share. Gross proceeds totaled \$40.0 million, and net proceeds, after deducting underwriting discounts and offering expenses borne by us were approximately \$38.0 million, a portion of which was used to repay borrowings under our Credit Facility, with the remaining proceeds being held to make additional investments and for general corporate purposes. We incurred \$2.0 million in total offering costs related to the offering, which have been recorded as an asset in accordance with GAAP and are being amortized over the redemption period ending February 28, 2017.

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The Term Preferred Stock provides for a fixed dividend equal to 7.125% per year, payable monthly (which equates to approximately \$2.9 million per year). We are required to redeem all of the outstanding Term Preferred Stock on February 28, 2017, for cash at a redemption price equal to \$25.00 per share plus an amount equal to accumulated but unpaid dividends, if any, to the date of redemption. The Term Preferred Stock has a preference over our common stock with respect to dividends, whereby no distributions are payable on our common stock unless the stated dividends, including any accrued and unpaid dividends, on the Term Preferred Stock have been paid in full. The Term Preferred Stock is not convertible into our common stock or any other security. In addition, three other potential redemption triggers are as follows: 1) upon the occurrence of certain events that would constitute a change in control of us, we would be required to redeem all of the outstanding Term Preferred Stock; 2) if we fail to maintain an asset coverage ratio of at least 200%, we are required to redeem a portion of the outstanding Term Preferred Stock or otherwise cure the ratio redemption trigger and 3) at our sole option, at any time on or after February 28, 2016, we may redeem some or all of the Term Preferred Stock.

The Term Preferred Stock has been recorded as a liability in accordance with GAAP and, as such, affects our asset coverage, exposing us to additional leverage risks.

Revolving Credit Facility

On April 30, 2013, we, through our wholly-owned subsidiary, Business Investment, entered into a fifth amended and restated credit agreement with Key Equipment Finance Inc., as administrative agent, lead arranger and a lender (the Administrative Agent), Branch Banking and Trust Company as a lender and managing agent, and the Adviser, as servicer, to increase the commitment amount of the revolving line of credit (the Credit Facility) from \$60.0 million to \$70.0 million and to extend the maturity date as described below. The maturity date was extended to April 30, 2016 (the Maturity Date) and, if not renewed or extended by the Maturity Date, all principal and interest will be due and payable on or before April 30, 2017 (one year after the Maturity Date). In addition, there are two one-year extension options to be agreed upon by all parties, which may be exercised on or before April 30, 2014 and 2015, respectively. Subject to certain terms and conditions, the Credit Facility may be expanded up to a total of \$200.0 million through the addition of other lenders to the facility. Advances under the Credit Facility generally bear interest at 30-day LIBOR, plus 3.75% per annum, and the Credit Facility includes an unused fee of 0.50% on undrawn amounts. We incurred fees of approximately \$0.3 million in connection with this amendment.

On June 12, 2013, we further increased the borrowing capacity under the Credit Agreement from \$70.0 million to \$105.0 million by entering into Joinder Agreements pursuant to the Credit Agreement by and among Business Investment, the Administrative Agent, the Adviser and each of Alostar Bank of Commerce and Everbank Commercial Finance, Inc.

The Credit Facility contains covenants that require Business Investment to maintain its status as a separate legal entity; prohibit certain significant corporate transactions (such as mergers, consolidations, liquidations or dissolutions) and restrict material changes to our credit and collection policies without lenders' consent. The facility also limits payments as distributions to the aggregate net investment income for each of the twelve month periods ending March 31, 2014, 2015, 2016 and 2017. We are also subject to certain limitations on the type of loan investments we can make, including restrictions on geographic concentrations, sector concentrations, loan size, dividend payout, payment frequency and status, average life and lien property. The Credit Facility also requires us to comply with other financial and operational covenants, which obligate us to, among other things, maintain certain financial ratios, including asset and interest coverage, a minimum net worth and a minimum number of obligors required in the borrowing base of the credit agreement. Additionally, we are subject to a performance guaranty that requires us to maintain (i) a minimum net worth of \$170.0 million plus 50% of all equity and subordinated debt raised after April 30, 2013, which equates to \$170.0 million as of September 30, 2013, (ii) asset coverage with respect to senior

securities representing indebtedness of at least 200%, in accordance with Section 18 of the 1940 Act and (iii) our status as a BDC under the 1940 Act and as a RIC under the Code. As of October 25, 2013, we were in compliance with all covenants.

In December 2011, we entered into a forward interest rate cap agreement, effective May 2012, for a notional amount of \$50.0 million. We incurred a premium fee of \$29 in conjunction with this agreement, which expired in October 2013 and has resulted in a \$29 realized loss for the three months ending December 31, 2013. In July 2013, we entered into a forward interest rate cap agreement, effective October 2013 and expiring April 2016, for a notional amount of \$45.0 million. We incurred a premium fee of \$75 in conjunction with this agreement. Both of these interest rate cap agreements effectively limit the interest rate on a portion of the borrowings pursuant to the terms of the Credit Facility.

The Administrative Agent also requires that any interest or principal payments on pledged loans be remitted directly by the borrower into a lockbox account, with The Bank of New York Mellon Trust Company, N.A. as custodian. The Administrative Agent is also the trustee of the account and generally remits the collected funds to us once a month.

Table of Contents**Short-Term Loan**

Similar to previous quarter ends, to maintain our status as a RIC, we purchased \$25.0 million of short-term United States Treasury Bills (T-Bills) through Jefferies & Company, Inc. (Jefferies) on September 27, 2013. The T-Bills were purchased on margin using \$3.0 million in cash and the proceeds from a \$22.0 million short-term loan from Jefferies with an effective annual interest rate of approximately 1.35%. On September 3, 2013, when the T-Bills matured, we repaid the \$22.0 million loan from Jefferies and received the \$3.0 million margin payment sent to Jefferies to complete the transaction.

Contractual Obligations and Off-Balance Sheet Arrangements

We have lines of credit to certain of our portfolio companies that have not been fully drawn. Since these lines of credit have expiration dates and we expect many will never be fully drawn, the total line of credit commitment amounts do not necessarily represent future cash requirements. We estimate the fair value of the unused line of credit commitments as of September 30, 2013 and 2012 to be minimal.

In addition to the lines of credit to our portfolio companies, we have also extended certain guaranties on behalf of some of our portfolio companies, whereby we have guaranteed an aggregate of \$3.6 million of obligations of ASH and CCE. As of September 30, 2013, we have not been required to make any payments on any of the guaranties, and we consider the credit risks to be remote and the fair value of the guaranties to be minimal.

The following table shows our contractual obligations as of September 30, 2013, at cost:

Contractual Obligations ^(A)	Total	Payments Due by Period			More than 5 Years
		Less than 1 Year	1-3 Years	3-5 Years	
Short-term loan	\$ 22,005	\$ 22,005	\$	\$	\$
Credit Facility	34,000		34,000		
Term Preferred Stock	40,000			40,000	
Other secured borrowings	5,000			5,000	
Interest payments on obligations ^(B)	15,680	4,921	9,134	1,625	
Total	\$ 116,685	\$ 26,926	\$ 43,134	\$ 46,625	\$

(A) Excludes our unused line of credit commitments and guaranties to our portfolio companies in the aggregate amount of \$6.4 million.

(B) Includes interest payments due on our Credit Facility and dividend obligations on the Term Preferred Stock. Dividend payments on the Term Preferred Stock assume quarterly declarations and monthly distributions through the date of mandatory redemption.

The majority of our debt securities in our portfolio have a success fee component, which can enhance the yield on our debt investments. Unlike PIK income, we do not recognize the fee into income until it is received in cash. As a result, as of September 30, 2013, we have an off-balance sheet success fee receivable of \$15.1 million, or approximately \$0.57 per common share. There is no guarantee that we will be able to collect any or all of our success fee receivables

due to their contingent nature. It is also impossible to predict the timing of such collections.

Critical Accounting Policies

The preparation of financial statements and related disclosures in conformity with GAAP requires management to make estimates and assumptions that affect the reported consolidated amounts of assets and liabilities, including disclosure of contingent assets and liabilities at the date of the financial statements, and revenues and expenses during the period reported. Actual results could differ materially from those estimates. We have identified our investment valuation process as our most critical accounting policy.

Investment Valuation

The most significant estimate inherent in the preparation of our consolidated financial statements is the valuation of investments and the related amounts of unrealized appreciation and depreciation of investments recorded.

General Valuation Policy: We value our investments in accordance with the requirements of the 1940 Act. As discussed more fully below, we value securities for which market quotations are readily available and reliable at their market value. We value all other securities and assets at fair value, as determined in good faith by our Board of Directors. Such determination of fair values may involve subjective judgments and estimates.

The Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 820, Fair Value Measurements and Disclosures, defines fair value, establishes a framework for measuring fair value and expands disclosures about assets and liabilities measured at fair value. ASC 820 provides a consistent definition of fair value that focuses on exit price in the principal, or most advantageous, market and prioritizes, within a measurement of fair value, the use of market-based inputs over entity-specific inputs. ASC 820 also establishes the following three-level hierarchy for fair value measurements based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date.

Level 1 inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets;

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Level 2 inputs to the valuation methodology include quoted prices for similar assets and liabilities in active or inactive markets and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument. Level 2 inputs are in those markets for which there are few transactions, the prices are not current, little public information exists or instances where prices vary substantially over time or among brokered market makers; and

Level 3 inputs to the valuation methodology are unobservable and significant to the fair value measurement. Unobservable inputs are those inputs that reflect assumptions that market participants would use when pricing the asset or liability and can include the Adviser's assumptions based upon the best available information.

As of September 30 and March 31, 2013, all of our investments were valued using Level 3 inputs. See Note 3 *Investments* in our accompanying notes to our *Condensed Consolidated Financial Statements* included elsewhere in this report for additional information regarding fair value measurements and our application of ASC 820.

The Adviser uses generally accepted valuation techniques to value our portfolio unless it has specific information about the value of an investment to determine otherwise. From time to time we may accept an appraisal of a business in which we hold securities. These appraisals are expensive and occur infrequently but provide a third-party valuation opinion that may differ in results, techniques and scope used to value our investments. When these specific, third-party appraisals are obtained, the Adviser would use estimates of value provided by such appraisals and its own assumptions, including estimated remaining life, current market yield and interest rate spreads of similar securities as of the measurement date, to value our investments.

In determining the value of our investments, the Adviser has established an investment valuation policy (the *Policy*). The *Policy* has been approved by our Board of Directors, and each quarter, our Board of Directors reviews the *Policy* to determine if changes thereto are advisable and also reviews whether the Adviser has applied the *Policy* consistently and votes whether to accept the recommended valuation of our investment portfolio. Such determination of fair values may involve subjective judgments and estimates.

The *Policy*, which is summarized below, applies to the following categories of securities:

Publicly-traded securities;

Securities for which a limited market exists; and

Securities for which no market exists.

Valuation Methods:

Publicly-traded securities: The Adviser determines the value of publicly-traded securities based on the closing price for the security on the exchange or securities market on which it is listed and primarily traded on the valuation date. To the extent that we own restricted securities that are not freely tradable, but for which a public market otherwise exists, we use the market value of the securities, adjusted for any decrease in value resulting from the restrictive feature. As of September 30 and March 31, 2013, we did not have any investments in publicly-traded securities.

Securities for which a limited market exists: The Adviser values securities that are not traded on an established secondary securities market but for which a limited market for the security exists, such as certain participations in, or assignments of, syndicated loans, at the quoted bid price, which are non-binding. In valuing these assets, the Adviser assesses trading activity in an asset class and evaluates variances in prices and other market insights to determine if any available quoted prices are reliable. In general, if the Adviser concludes that quotes based on active markets or trading activity may be relied upon, firm bid prices are requested; however, if firm bid prices are unavailable, the Adviser bases the value of the security upon the indicative bid price (IBP) offered by the respective originating syndication agent s trading desk, or secondary desk, on or near the valuation date. To the extent that the Adviser uses the IBP as a basis for valuing the security, the Adviser may take further steps to consider additional information to validate that price in accordance with the Policy, including but not limited to reviewing a range of indicative bids to the extent it has ready access to such qualified information.

In the event these limited markets become illiquid such that market prices are no longer readily available, the Adviser will value our syndicated loans using alternative methods, such as estimated net present values of the future cash flows, or discounted cash flows (DCF). The use of a DCF methodology follows that prescribed by the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 820, Fair Value Measurements and Disclosures, which provides guidance on the use of a reporting entity s own assumptions about future cash flows and risk-adjusted discount rates when relevant, observable inputs, such as quotes in active markets, are not available. When relevant, observable market data does not exist, an alternative outlined in ASC 820 is the valuation of investments based on DCF. For the purposes of using DCF to provide fair value estimates, the Adviser considers

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multiple inputs, such as a risk-adjusted discount rate that incorporates adjustments that market participants would make, both for nonperformance and liquidity risks. As such, the Adviser develops a modified discount rate approach that incorporates risk premiums including, among other things, increased probability of default, higher loss given default or increased liquidity risk. The DCF valuations applied to the syndicated loans provide an estimate of what the Adviser believes a market participant would pay to purchase a syndicated loan in an active market, thereby establishing a fair value. The Adviser applies the DCF methodology in illiquid markets until quoted prices are available or are deemed reliable based on trading activity. As of September 30 and March 31, 2013, we had no securities for which a limited market exists.

Securities for which no market exists: The Adviser's valuation methodology for securities for which no market exists falls into four categories: (A) portfolio investments comprised solely of debt securities; (B) portfolio investments in controlled companies comprised of a bundle of securities, which can include debt and equity securities; (C) portfolio investments in non-controlled companies comprised of a bundle of investments, which can include debt and equity securities; and (D) portfolio investments comprised of non-publicly traded, non-control equity securities of other funds.

(A) Portfolio investments comprised solely of debt securities: Debt securities that are not publicly traded on an established securities market, or for which a limited market does not exist (Non-Public Debt Securities), and that are issued by portfolio companies in which we have no equity or equity-like securities, are fair valued in accordance with the terms of the Policy, which utilizes opinions of value submitted to the Adviser by Standard & Poor's Securities Evaluations, Inc. (SPSE). The Adviser may also submit PIK interest to SPSE for their evaluation when it is determined that PIK interest is likely to be received.

In the case of Non-Public Debt Securities, the Adviser has engaged SPSE to submit opinions of value for our debt securities that are issued by portfolio companies in which we own no equity, or equity-like securities. SPSE will only evaluate the debt portion of our investments for which the Adviser specifically requests evaluation and may decline to make requested evaluations for any reason, at its sole discretion. Quarterly, the Adviser collects data with respect to the investments (which includes portfolio company financial and operational performance and the information described below under Credit Information, the risk ratings of the loans described below under Loan Grading and Risk Rating and the factors described hereunder). This portfolio company data is then forwarded to SPSE for review and analysis. SPSE makes its independent assessment of the data that the Adviser has assembled and assesses its independent data to form an opinion as to what they consider to be the market values for the securities. With regard to its work, SPSE has issued the following paragraph:

SPSE provides evaluated price opinions which are reflective of what SPSE believes the bid side of the market would be for each loan after careful review and analysis of descriptive, market and credit information. Each price reflects SPSE's best judgment based upon careful examination of a variety of market factors. Because of fluctuation in the market and in other factors beyond its control, SPSE cannot guarantee these evaluations. The evaluations reflect the market prices, or estimates thereof, on the date specified. The prices are based on comparable market prices for similar securities. Market information has been obtained from reputable secondary market sources. Although these sources are considered reliable, SPSE cannot guarantee their accuracy.

SPSE opinions of the value of our debt securities that are issued by portfolio companies in which we do not own equity, or equity-like securities, are submitted to our Board of Directors along with the Adviser's supplemental assessment and recommendation regarding valuation of each of these investments. The Adviser generally accepts the opinion of value given by SPSE; however, in certain limited circumstances, such as when the Adviser may learn new information regarding an investment between the time of submission to SPSE and the date of our Board of Directors

assessment, the Adviser's conclusions as to value may differ from the opinion of value delivered by SPSE. Our Board of Directors then reviews whether the Adviser has followed its established procedures for determinations of fair value and votes to accept or reject the recommended valuation of our investment portfolio. The Adviser and our management recommended, and our Board of Directors voted to accept, the opinions of value delivered by SPSE on the loans in our portfolio as denoted on our accompanying Condensed Consolidated Schedule of Investments.

Because there is a delay between when we close an investment and when the investment can be evaluated by SPSE, new loans are not valued immediately by SPSE; rather, the Adviser makes its own determination about the value of these investments in accordance with our Policy using the methods described herein.

(B) Portfolio investments in controlled companies comprised of a bundle of investments, which can include debt and equity securities: The fair value of these investments is determined based on the total enterprise value (TEV) of the portfolio company, or issuer, utilizing a liquidity waterfall approach under ASC 820 for our Non-Public Debt Securities and equity or

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equity-like securities (e.g., preferred equity, common equity or other equity-like securities) that are purchased together as part of a package, where we have control or could gain control through an option or warrant security; both the debt and equity securities of the portfolio investment would exit in the mergers and acquisitions market as the principal market, generally through a sale of the portfolio company. We generally exit the debt and equity securities of an issuer at the same time. Applying the liquidity waterfall approach to all of our investments in an issuer, the Adviser first calculates the TEV of the issuer by incorporating some or all of the following factors:

the issuer's ability to make payments;

the earnings of the issuer;

recent sales to third parties of similar securities;

the comparison to publicly traded securities; and

DCF or other pertinent factors.

In gathering the sales to third parties of similar securities, the Adviser generally references industry statistics and may use outside experts. TEV is only an estimate of value and may not be the value received in an actual sale. Once the Adviser has estimated the TEV of the issuer, the Adviser will subtract the value of all the debt securities of the issuer, which are valued at the contractual principal balance. Fair values of these debt securities are discounted for any shortfall of TEV over the total debt outstanding for the issuer. Once the values for all outstanding senior securities, which include all the debt securities, have been subtracted from the TEV of the issuer, the remaining amount, if any, is used to determine the value of the issuer's equity or equity-like securities. If, in the Adviser's judgment, the liquidity waterfall approach does not accurately reflect the value of the debt component, the Adviser may recommend that we use a valuation by SPSE, or, if that is unavailable, a DCF valuation technique.

(C) Portfolio investments in non-controlled companies comprised of a bundle of investments, which can include debt and equity securities: The Adviser values Non-Public Debt Securities that are purchased together with equity or equity-like securities from the same portfolio company, or issuer, for which we do not control or cannot gain control as of the measurement date, using a hypothetical secondary market as our principal market. In accordance with ASC 820 (as amended by the FASB's Accounting Standards Update No. 2011-04, Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and International Financial Reporting Standards (IFRS)), (ASU 2011-04)), the Adviser has defined our unit of account at the investment level (either debt or equity) and as such, determined our fair value of these non-control investments assuming the sale of an individual security using the standalone premise of value. As such, the Adviser estimates the fair value of the debt component using estimates of value provided by SPSE and the Adviser's own assumptions in the absence of observable market data, including synthetic credit ratings, estimated remaining life, current market yield and interest rate spreads of similar securities as of the measurement date. For equity or equity-like securities of investments for which we do not control or cannot gain control as of the measurement date, the Adviser estimates the fair value of the equity based on factors such as the overall value of the issuer, the relative fair value of other units of account including debt, or

other relative value approaches. Consideration also is given to capital structure and other contractual obligations that may impact the fair value of the equity. Furthermore, the Adviser may utilize comparable values of similar companies, recent investments and indices with similar structures and risk characteristics or DCF valuation techniques and, in the absence of other observable market data, the Adviser's own assumptions.

(D) Portfolio investments comprised of non-publicly traded non-control equity securities of other funds: The Adviser generally values any uninvested capital of the non-control fund at par value and values any invested capital at the NAV provided by the non-control fund. As September 30 and March 31, 2013, we had no non-control equity securities of other funds.

Due to the uncertainty inherent in the valuation process, such estimates of fair value may differ significantly and materially from the values that would have been obtained had a ready market for the securities existed. Additionally, changes in the market environment and other events that may occur over the life of the investments may cause the gains or losses ultimately realized on these investments to be different than the valuations currently assigned. There is no single standard for determining fair value in good faith, as fair value depends upon circumstances of each individual case. In general, fair value is the amount that we might reasonably expect to receive upon the current sale of the security in an orderly transaction between market participants at the measurement date.

Valuation Considerations: From time to time, depending on certain circumstances, the Adviser may use the following valuation considerations, including but not limited to:

the nature and realizable value of the collateral;

the portfolio company's earnings and cash flows and its ability to make payments on its obligations;

the markets in which the portfolio company does business;

the comparison to publicly traded companies; and

DCF and other relevant factors.

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Because such valuations, particularly valuations of private securities and private companies, are not susceptible to precise determination, may fluctuate over short periods of time, and may be based on estimates, the Adviser's determinations of fair value may differ from the values that might have actually resulted had a readily available market for these securities been available.

Credit Information: The Adviser monitors a wide variety of key credit statistics that provide information regarding our portfolio companies to help us assess credit quality and portfolio performance. We and the Adviser generally participate in the periodic board meetings of our portfolio companies in which we hold Control and Affiliate investments and also generally require them to provide annual audited and monthly unaudited financial statements. Using these statements or comparable information and board discussions, the Adviser calculates and evaluates the credit statistics.

Loan Grading and Risk Rating: As part of our valuation procedures above, we risk rate all of our investments in debt securities. We use a proprietary risk rating system. Our risk rating system uses a scale of 0 to >10, with >10 being the lowest probability of default. This system is used to estimate the probability of default on debt securities and the expected loss if there is a default. These types of systems are referred to as risk rating systems and are used by banks and rating agencies. The risk rating system covers both qualitative and quantitative aspects of the business and the securities we hold.

We seek to have our risk rating system mirror the risk rating systems of major risk rating organizations, such as those provided by a Nationally Recognized Statistical Rating Organization (NRSRO). While we seek to mirror the NRSRO systems, we cannot provide any assurance that our risk rating system will provide the same risk rating as an NRSRO for these securities. The following chart is an estimate of the relationship of our risk rating system to the designations used by two NRSROs as they risk rate debt securities of major companies. Because our system rates debt securities of companies that are unrated by any NRSRO, there can be no assurance that the correlation to the NRSRO set out below is accurate. We believe our risk rating would be significantly higher than a typical NRSRO risk rating because the risk rating of the typical NRSRO is designed for larger businesses. However, our risk rating has been designed to risk rate the securities of smaller businesses that are not rated by a typical NRSRO. Therefore, when we use our risk rating on larger business securities, the risk rating is higher than a typical NRSRO rating. We believe the primary difference between our risk rating and the rating of a typical NRSRO is that our risk rating uses more quantitative determinants and includes qualitative determinants that we believe are not used in the NRSRO rating. It is our understanding that most debt securities of medium-sized companies do not exceed the grade of BBB on an NRSRO scale, so there would be no debt securities in the middle market that would meet the definition of AAA, AA or A. Therefore, the scale begins with the designation >10 as the best risk rating which may be equivalent to a BBB or Baa2 from an NRSRO, however, no assurance can be given that a >10 on the scale is equal to a BBB or Baa2 on an NRSRO scale.

	First	Second	
Adviser's System	NRSRO	NRSRO	Description ^(A)
>10	Baa2	BBB	Probability of Default (PD) during the next ten years is 4% and the Expected Loss upon Default (EL) is 1% or less
10	Baa3	BBB-	PD is 5% and the EL is 1% to 2%
9	Ba1	BB+	PD is 10% and the EL is 2% to 3%
8	Ba2	BB	PD is 16% and the EL is 3% to 4%
7	Ba3	BB-	PD is 17.8% and the EL is 4% to 5%
6	B1	B+	PD is 22% and the EL is 5% to 6.5%

5	B2	B	PD is 25% and the EL is 6.5% to 8%
4	B3	B-	PD is 27% and the EL is 8% to 10%
3	Caa1	CCC+	PD is 30% and the EL is 10% to 13.3%
2	Caa2	CCC	PD is 35% and the EL is 13.3% to 16.7%
1	Caa3	CC	PD is 65% and the EL is 16.7% to 20%
0	N/A	D	PD is 85% or there is a payment default and the EL is greater than 20%

^(A) *The default rates set forth are for a ten year term debt security. If a debt security is less than ten years, then the probability of default is adjusted to a lower percentage for the shorter period, which may move the security higher on this risk rating scale.*

The above scale gives an indication of the probability of default and the magnitude of the expected loss if there is a default. Generally, our policy is to stop accruing interest on an investment if we determine that interest is no longer collectable. As of September 30 and March 31, 2013, two investments, ASH and Tread, were on non-accrual with an aggregate fair value of \$0. Additionally, we do not risk rate our equity securities.

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The following table lists the risk ratings for all proprietary loans in our portfolio as of September 30 and March 31, 2013, representing approximately 100.0%, of the principal balance of all loans in our portfolio at the end of each period:

Rating	As of September 30, 2013	As of March 31, 2013
Highest	9.1	7.4
Average	5.7	5.2
Weighted Average	5.4	5.3
Lowest	2.6	1.3

As of September 30 and March 31, 2013, we did not have any non-proprietary loans in our investment portfolio.

Tax Status*Federal Income Taxes*

We intend to continue to qualify for treatment as a RIC under Subtitle A, Chapter 1 of Subchapter M of the Code. As a RIC, we are not subject to federal income tax on the portion of our taxable income and gains distributed to stockholders. To qualify as a RIC, we must meet certain source-of-income, asset diversification and annual distribution requirements. For more information regarding the requirements we must meet as a RIC, see Business Environment. Under the annual distribution requirements, we are required to distribute to stockholders at least 90% of our investment company taxable income, as defined by the Code. Our practice has been to pay out as distributions up to 100% of that amount.

In an effort to limit certain excise taxes imposed on RICs, we generally distribute during each calendar year, an amount at least equal to the sum of (1) 98% of our ordinary income for the calendar year, (2) 98.2% of our capital gains in excess of capital losses for the one-year period ending on October 31 of the calendar year and (3) any ordinary income and capital gains in excess of capital losses for preceding years that were not distributed during such years. However, we did incur an excise tax of \$31 and \$30 for the calendar years ended December 31, 2012 and 2011, respectively, and expect to incur excise taxes again for the calendar year ending December 31, 2013. Under the RIC Modernization Act (the RIC Act), we are permitted to carry forward capital losses incurred in taxable years beginning after March 31, 2011, for an unlimited period. However, any losses incurred during those future taxable years must be used prior to the losses incurred in pre-enactment taxable years, which carry an expiration date. Additionally, post-enactment capital loss carryforwards will retain their character as either short-term or long-term capital losses rather than only being considered short-term as permitted under previous regulation. Our total capital loss carryforward balance was \$8.7 million as of March 31, 2013, and, as a result of the \$24.8 million capital gain related to the Venyu exit in August 2013, we expect that all losses incurred in pre-enactment taxable years will be fully utilized during the fiscal year ending March 31, 2014.

Revenue Recognition*Interest Income Recognition*

Interest income, adjusted for amortization of premiums, amendment fees and acquisition costs and the accretion of discounts, is recorded on the accrual basis to the extent that such amounts are expected to be collected. Generally, when a loan becomes 90 days or more past due, or if our qualitative assessment indicates that the debtor is unable to

service its debt or other obligations, we will place the loan on non-accrual status and cease recognizing interest income on that loan until the borrower has demonstrated the ability and intent to pay contractual amounts due. However, we remain contractually entitled to this interest. Interest payments received on non-accrual loans may be recognized as income or applied to the cost basis, depending upon management's judgment. Generally, non-accrual loans are restored to accrual status when past-due principal and interest are paid, and, in management's judgment, are likely to remain current, or due to a restructuring, the interest income is deemed to be collectible. As of September 30, 2013, loans to two portfolio companies, ASH and Tread, were on non-accrual, with an aggregate debt cost basis of \$25.9 million, or 9.9% of the cost basis of all debt investments in our portfolio, and an aggregate fair value of \$0. As of March 31, 2013, ASH and Tread were on non-accrual, with an aggregate debt cost basis of \$24.9 million, or 10.4% of the cost basis of all debt investments in our portfolio, and an aggregate fair value of \$0.

During the three and six months ended September 30, 2013, we recorded PIK income of \$29 and \$39, respectively. PIK interest, computed at the contractual rate specified in the loan agreement, is added to the principal balance of the loan and recorded as interest income. To maintain our status as a RIC, this non-cash source of income must be included in our calculation of distributable income for purposes of complying with our distribution requirements, even though we have not yet collected the cash. We did not hold any loans in our portfolio that contained a PIK provision as of September 30, 2012 and no PIK income was recorded during the three and six months ended September 30, 2012.

Other Income Recognition

We generally record success fees upon receipt of cash. Success fees are contractually due upon a change of control in a portfolio company. We recorded \$2.1 million and \$2.3 million of success fees during the three and six months ended September 30, 2013, respectively. During the three months ended September 30, 2013, we received \$0.3 million from Cavert in success fee prepayments and we received \$1.8 million related to the exit of Venyu. During the three and six months ended September, 30, 2012, we recorded \$0.4 million and \$0.8 million of success fees, respectively, representing prepayments received from Mathey and Cavert.

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We accrue dividend income on preferred and common equity securities to the extent that such amounts are expected to be collected

and if we have the option to collect such amounts in cash or other consideration. For the three and six months ended September 30, 2013, we recorded \$1.4 million in dividend income related to the exit of Venyu. We recorded \$0.1 million in dividend income during the three and six months ended September 30, 2012 on accrued preferred shares of Drew Foam Company, Inc. (Drew Foam).

Both dividends and success fees are recorded in Other income in our accompanying *Condensed Consolidated Statements of Operations*.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk includes risks that arise from changes in interest rates, foreign currency exchange rates, commodity prices, equity prices and other market changes that affect market sensitive instruments. The prices of securities held by us may decline in response to certain events, including those directly involving the companies whose securities are owned by us; conditions affecting the general economy; overall market changes; local, regional or global political, social or economic instability; and interest rate fluctuations.

The primary risk we believe we are exposed to is interest rate risk. Because we borrow money to make investments, our net investment is dependent upon the difference between the rate at which we borrow funds and the rate at which we invest those funds. As a result, there can be no assurance that a significant change in market interest rates will not have a material adverse effect on our net investment income. We use a combination of debt and equity capital to finance our investing activities. We do use interest rate risk management techniques to limit our exposure to interest rate fluctuations. Such techniques may include various interest rate hedging activities to the extent permitted by the 1940 Act.

Our target is to have approximately 20% of the loans in our portfolio at fixed rates and approximately 80% at variable rates or variables rates with a floor mechanism. Currently, all of our variable-rate loans have rates associated with either the current LIBOR or prime rate. As of September 30, 2013, our portfolio consisted of the following breakdown based on total principal balance of all outstanding debt investments:

81.5%	Variable rates with a floor
18.5	Fixed rates

100.0%	Total
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There have been no material changes in the quantitative and qualitative market risk disclosures for the three months ended September 30, 2013 from that disclosed in our Annual Report on Form 10-K for the fiscal year ended March 31, 2013, as filed with the SEC on May 14, 2013.

ITEM 4. CONTROLS AND PROCEDURES.

a) Evaluation of Disclosure Controls and Procedures

As of September 30, 2013 (the end of the period covered by this report), we, including our chief executive officer and chief financial officer, evaluated the effectiveness and design and operation of our disclosure controls and procedures. Based on that evaluation, our management, including the chief executive officer and chief financial officer, concluded that our disclosure controls and procedures were effective at a reasonable assurance level in timely alerting management, including the chief executive officer and chief financial officer, of material information about us required to be included in periodic SEC filings. However, in evaluation of the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

b) Changes in Internal Control over Financial Reporting

There were no changes in internal controls for the three months ended September 30, 2013 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

Neither we, nor any of our subsidiaries, are currently subject to any material legal proceeding, nor, to our knowledge, is any material legal proceeding threatened against us or any of our subsidiaries.

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ITEM 1A. RISK FACTORS.

Our business is subject to certain risks and events that, if they occur, could adversely affect our financial condition and results of operations and the trading price of our securities. For a discussion of these risks, please refer to the Risk Factors section in our Post-Effective Amendment No. 2 to our registration statement on Form N-2 (No. 333-181879) as filed with the SEC on June 7, 2013.

The failure of U.S. lawmakers to reach an agreement on the national debt ceiling or a budget could have a material adverse effect on our business, financial condition and results of operations.

On October 16, 2013, the U.S. Congress passed legislation to reopen the government through January 15, 2014 and effectively suspend the debt ceiling through February 7, 2014 to permit broader negotiations over budget issues. In the event U.S. lawmakers fail to reach a viable agreement on the national debt ceiling or a budget, the U.S. could default on its obligations, which could negatively impact the trading market for U.S. government securities. This may, in turn, negatively affect our ability to obtain financing for our investments. As a result, it may materially adversely affect our business, financial condition and results of operations.

On August 5, 2011, Standard & Poor's downgraded its long-term sovereign credit rating on the U.S. to AA+ for the first time due to the U.S. Congress' inability to reach an effective agreement on the national debt ceiling and a budget in a timely manner. The current U.S. debt ceiling and budget deficit concerns have increased the possibility of the credit-rating agencies further downgrading the U.S. credit rating. On October 15, 2013, Fitch Ratings Service placed the U.S. credit rating on negative watch, warning that a failure by the U.S. Government to honor interest or principal payments on U.S. treasury securities would impact its decision on whether to downgrade the U.S. credit rating. Fitch also stated that the manner and duration of an agreement to raise the debt ceiling and resolve the budget impasse, as well as the perceived risk of such events occurring in the future, would weigh on its ratings.

The impact of any further downgrades to the U.S. government's sovereign credit rating, or its perceived creditworthiness, and deteriorating sovereign debt conditions in Europe, is inherently unpredictable and could adversely affect the U.S. and global financial markets and economic conditions. There can be no assurance that governmental or other measures to aid economic recovery will be effective. These developments and the government's credit concerns in general could cause interest rates and borrowing costs to rise, which may negatively impact our ability to access the debt markets on favorable terms. In addition, the decreased credit rating could create broader financial turmoil and uncertainty, which may weigh heavily on our stock price. Continued adverse economic conditions could have a material adverse effect on our business, financial condition and results of operations.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

Not applicable.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

Not applicable.

ITEM 4. MINE SAFETY DISCLOSURES.

Not applicable.

ITEM 5. OTHER INFORMATION.

Not applicable.

ITEM 6. EXHIBITS

See the exhibit index.

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SIGNATURE

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

**GLADSTONE INVESTMENT
CORPORATION**

By: /s/ David Watson
David Watson
Chief Financial Officer and Treasurer

Dated: November 6, 2013

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EXHIBIT INDEX

Exhibit	Description
3.1	Amended and Restated Certificate of Incorporation, incorporated by reference to Exhibit A.2 to Pre-Effective Amendment No. 1 to the Registration Statement on Form N-2 (File No. 333-123699), filed May 13, 2005.
3.2	Certificate of Designation of 7.125% Series A Cumulative Term Preferred Stock, incorporated by reference to Exhibit 2.A.2 to Post-Effective Amendment No. 5 to the Registration Statement on Form N-2 (File No. 333-160720), filed February 29, 2012.
3.3	Amended and Restated Bylaws, incorporated by reference to Exhibit B.2 to the Pre-Effective Amendment No. 3 to the Registration Statement on Form N-2 (File No. 333-123699), filed June 21, 2005.
3.4	First Amendment to Amended and Restated Bylaws of the Registrant, incorporated by reference to Exhibit 99.1 to the Current Report on Form 8-K (File No. 814-00704), filed July 10, 2007.
4.1	Specimen Stock Certificate, incorporated by reference to Exhibit 99.D to Pre-Effective Amendment No. 3 to the Registration Statement on Form N-2 (File No. 333-123699), filed June 21, 2005.
4.2	Specimen 7.125% Series A Cumulative Term Preferred Stock Certificate, incorporated by reference to Exhibit 2.D.4 to Post-Effective Amendment No. 5 to the Registration Statement on Form N-2 (File No. 333-160720), filed February 29, 2012.
4.3	Dividend Reinvestment Plan, incorporated by reference to Exhibit 99.E to Pre-Effective Amendment No. 3 to the Registration Statement on Form N-2 (File No. 333-123699), filed June 21, 2005.
11	Computation of Per Share Earnings (included in the notes to the financial statements contained in this report).*
31.1	Certification of Chief Executive Officer pursuant to section 302 of The Sarbanes-Oxley Act of 2002.*
31.2	Certification of Chief Financial Officer pursuant to section 302 of The Sarbanes-Oxley Act of 2002.*
32.1	Certification of Chief Executive Officer pursuant to section 906 of The Sarbanes-Oxley Act of 2002.*
32.2	Certification of Chief Financial Officer pursuant to section 906 of The Sarbanes-Oxley Act of 2002.*

* Filed herewith

All other exhibits for which provision is made in the applicable regulations of the Securities and Exchange Commission are not required under the related instruction or are inapplicable and therefore have been omitted.