HARRIS & HARRIS GROUP INC /NY/
Form 10-Q
August 08, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

Form 10-Q

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

For the quarterly period ended June 30, 2014

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

For the transition period from ____________ to _____________

Commission file number: 0-11576

HARRIS & HARRIS GROUP, INC.

(Exact Name of Registrant as Specified in Its Charter)

New York	13-3119827
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

1450 Broadway, New York, New York 10018
(Address of Principal Executive Offices) (Zip Code)

(212) 582-0900

(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes ¨ No ¨

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ¨ No x

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at August 8, 2014

Common Stock, $0.01 par value per share	31,245,664 shares

Harris & Harris Group, Inc.

Form 10-Q, June 30, 2014

	Page Number
PART I. FINANCIAL INFORMATION	
Item 1. Consolidated Financial Statements	1
Consolidated Statements of Assets and Liabilities	2
Consolidated Statements of Operations	3
Consolidated Statements of Comprehensive Income (Loss)	4
Consolidated Statements of Cash Flows	5
Consolidated Statements of Changes in Net Assets	6
Consolidated Schedule of Investments	7
Notes to Consolidated Financial Statements	37
Financial Highlights	61
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	62
Cautionary Statement Regarding Forward-Looking Statements	62
Background	63
Overview	63
Realize	64
Invest	69
Partner	72
Return	72
Current Business Environment	73
Valuation of Investments	74
Results of Operations	76
Financial Condition	86
Cash Flow	88
Liquidity and Capital Resources	88
Borrowings	89
Contractual Obligations	90
Critical Accounting Policies	90
Recent Developments – Portfolio Companies	93
Item 3. Quantitative and Qualitative Disclosures About Market Risk	94
Item 4. Controls and Procedures	96
PART II. OTHER INFORMATION	
Item 1A. Risk Factors	97

Item 6. Exhibits	97
Signatures	98
Exhibit Index	99

PART I. FINANCIAL INFORMATION

Item 1. Consolidated Financial Statements

In the opinion of management, these financial statements reflect all adjustments, consisting of valuation adjustments and normal recurring accruals, necessary for a fair statement of our financial position, results of operations and cash flows for such periods.

Harris & Harris Group, Inc.® (the "Company," "us," "our" and "we"), is an internally managed, non-diversified management investment company that has elected to operate as a business development company ("BDC") under the Investment Company Act of 1940 (the "1940 Act"). Certain information and disclosures normally included in the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America ("GAAP") have been condensed or omitted as permitted by Regulation S-X and Regulation S-K. Accordingly, they do not include all information and disclosures necessary for a fair presentation of our financial position, results of operations and cash flows in conformity with GAAP. The results of operations for any interim period are not necessarily indicative of the results for the full year. The accompanying consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto contained in our Annual Report on Form 10-K for the year ended December 31, 2013.

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED STATEMENTS OF ASSETS AND LIABILITIES

(Unaudited)

	June 30, 2014	December 31, 2013
ASSETS		
Investments, in portfolio securities at value:		
Unaffiliated privately held companies (cost: $23,151,547 and $29,277,213, respectively)	$16,316,588	$ 29,199,564
Unaffiliated rights to milestone payments (adjusted cost basis: $3,921,420 and $3,291,750, respectively)	4,127,104	3,489,433
Unaffiliated publicly traded securities (cost: $1,741,128 and $2,451,410, respectively)	3,136,045	5,570,796
Non-controlled affiliated privately held companies (cost: $76,518,770 and $71,843,448, respectively)	70,276,348	54,287,040
Controlled affiliated privately held companies (cost: $9,636,633 and $9,065,972, respectively)	2,266,746	1,352,626
Total, investments in private portfolio companies, rights to milestone payments and public securities at value (cost: $114,969,498 and $115,929,793, respectively)	$96,122,831	$ 93,899,459
Investments, in U.S. Treasury securities at value (cost: $0 and $18,999,765, respectively)	0	18,999,810
Cash	24,676,324	8,538,548
Receivable from sales of investments (Note 3)	0	448,886
Funds held in escrow from sales of investments at value (Note 3)	1,447,933	1,786,390
Receivable from portfolio company	54,485	54,160
Interest receivable	21,602	22,804
Prepaid expenses (Note 3)	751,375	991,409
Other assets	299,305	322,480
Total assets	$123,373,855	$ 125,063,946
LIABILITIES & NET ASSETS		
Post retirement plan liabilities (Note 8)	$1,152,671	$ 1,120,262
Accounts payable and accrued liabilities	964,753	785,608
Deferred rent	330,708	353,001
Written call options payable (premiums received: $145,426 and $112,382, respectively) (Note 7)	47,500	103,500
Total liabilities	2,495,632	2,362,371
Net assets	$120,878,223	$ 122,701,575
Net assets are comprised of:		
Preferred stock, $0.10 par value, 2,000,000 shares authorized; none issued	$0	$ 0

Common stock, $0.01 par value, 45,000,000 shares authorized at 6/30/14 and 12/31/13; 33,074,404 and 33,026,178 issued at 6/30/14 and 12/31/13, respectively	330,744	330,262
Additional paid in capital (Note 9)	214,748,521	214,320,241
Accumulated net operating and realized loss	(72,869,464)	(67,449,176)
Accumulated unrealized depreciation of investments	(18,748,741)	(22,021,407)
Accumulated other comprehensive income (Note 8)	822,694	927,186
Treasury stock, at cost (1,828,740 shares at 6/30/14 and 12/31/13)	(3,405,531)	(3,405,531)
Net assets	$ 120,878,223	$ 122,701,575
Shares outstanding	31,245,664	31,197,438
Net asset value per outstanding share	$ 3.87	$ 3.93

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

2

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Investment income:				
Interest from:				
Unaffiliated companies	$ 36,447	$ 56,851	$ 86,682	$ 131,846
Non-controlled affiliated companies	41,095	22,207	83,371	37,512
Controlled affiliated companies	36,607	62,390	71,333	109,194
Cash and U.S. Treasury securities and other	2,929	3,374	6,478	9,033
Miscellaneous income	16,757	45,141	32,262	87,468
Total investment income	133,835	189,963	280,126	375,053
Expenses:				
Salaries, benefits and stock-based compensation (Note 9)	1,247,426	1,442,714	2,659,786	2,760,399
Administration and operations	206,960	169,950	337,440	304,042
Professional fees	385,352	277,138	597,223	662,868
Interest and other debt expenses	94,276	5,874	187,996	11,705
Directors' fees and expenses	93,131	58,406	186,408	130,876
Rent	80,065	101,486	148,091	202,701
Insurance expense	84,007	96,180	167,940	172,303
Custody fees	14,228	13,981	29,019	27,774
Depreciation	13,245	14,172	26,450	27,896
Total expenses	2,218,690	2,179,901	4,340,353	4,300,564
Net operating loss	(2,084,855)	(1,989,938)	(4,060,227)	(3,925,511)
Net realized gain (loss):				
Realized gain (loss) from investments:				
Unaffiliated companies	3,946,838	105,313	3,946,838	105,313
Non-Controlled affiliated companies	588,221	0	(6,711,063)	(4,236,033)
Publicly traded companies	960,882	7,651,057	1,333,497	8,544,061
Written call options	197,309	(150,710)	86,653	(126,762)
Purchased put options	0	(15,127)	0	(72,209)
Realized gain (loss) from investments	5,693,250	7,590,533	(1,344,075)	4,214,370
Income tax expense (Note 10)	0	161	15,986	22,171
Net realized gain (loss) from investments	5,693,250	7,590,372	(1,360,061)	4,192,199
Net decrease (increase) in unrealized depreciation on investments:				

Investments	796,969	(1,095,489)	3,183,622	2,052,705
Written call options	(77,309)	(400,184)	89,044	(274,824)
Net decrease (increase) in unrealized depreciation on investments	719,660	(1,495,673)	3,272,666	1,777,881
Net realized and unrealized gains on investments	6,412,910	6,094,699	1,912,605	5,970,080
Net increase (decrease) in net assets resulting from operations:				
Total	$ 4,328,055	$ 4,104,761	$ (2,147,622)	$ 2,044,569
Per average basic and diluted outstanding share	$ 0.14	$ 0.13	$ (0.07)	$ 0.07
Average outstanding shares	31,201,574	31,118,358	31,199,518	31,117,624

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

3

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(Unaudited)

	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
Net increase (decrease) resulting from operations	$ 4,328,055	$ 4,104,761	$ (2,147,622)	$ 2,044,569
Other comprehensive income (loss):				
Prior service cost (Note 8)	0	0	0	1,101,338
Amortization of prior service cost	(52,246)	(43,538)	(104,492)	(87,076)
Other comprehensive (loss) income	(52,246)	(43,538)	(104,492)	1,014,262
Comprehensive income (loss)	$ 4,275,809	$ 4,061,223	$ (2,252,114)	$ 3,058,831

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

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
Cash flows (used in) provided by operating activities:		
Net (decrease) increase in net assets resulting from operations	$ (2,147,622)	$ 2,044,569
Adjustments to reconcile net (decrease) increase in net assets resulting from operations to net cash provided by (used in) operating activities:		
Net realized gain and unrealized appreciation on investments	(1,928,591)	(5,992,251)
Depreciation of fixed assets, amortization of premium or discount on U.S. government securities and prepaid assets and accretion of bridge note interest	(140,878)	(138,475)
Stock-based compensation expense	497,634	630,201
Amortization of prior service cost	(104,492)	1,014,262
Purchase of U.S. government securities	(19,999,044)	(55,998,943)
Sale of U.S. government securities	38,998,052	56,000,000
Purchase of affiliated portfolio companies	(9,714,299)	(6,429,843)
Purchase of unaffiliated portfolio companies	(240,500)	(678,307)
Payments received on debt investments	224,711	627,773
Proceeds from sale of investments and conversion of bridge notes	9,766,197	13,161,839
Proceeds from call option premiums	338,229	844,498
Payments for put and call option purchases	(218,532)	(309,578)
Changes in assets and liabilities:		
Receivable from sales of investments	448,886	(3,783,586)
Restricted funds	0	(10)
Receivable from portfolio company	(325)	19,670
Interest receivable	1,202	32,942
Prepaid expenses	240,034	(143,923)
Other assets	(2,209)	0
Post retirement plan liabilities	32,409	(1,050,365)
Accounts payable and accrued liabilities	179,145	50,120
Deferred rent	(22,293)	(18,959)
Net cash provided by (used in) operating activities	16,207,714	(118,366)
Cash flows from investing activities:		
Purchase of fixed assets	(1,066)	(3,909)
Net cash used in investing activities	(1,066)	(3,909)
Cash flows from financing activities:		

Payment of withholdings related to net settlement of restricted stock	(68,872)	(61,917)
Net cash used in financing activities	(68,872)	(61,917)
Net increase (decrease) in cash	$ 16,137,776	$ (184,192)
Cash at beginning of the period	8,538,548	8,379,111
Cash at end of the period	$ 24,676,324	$ 8,194,919
Supplemental disclosures of cash flow information:		
Income taxes paid	$ 15,986	$ 22,171
Supplemental schedule of non-cash activities:		
Impact of plan amendment on post-retirement plan liabilities	$ (104,492)	$ 1,014,262

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

5

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS

(Unaudited)

	Six Months Ended June 30, 2014	Year Ended December 31, 2013
Changes in net assets from operations:		
Net operating loss	$ (4,060,227)	$ (8,022,206)
Net realized (loss) gain on investments	(1,360,061)	18,516,268
Net decrease (increase) in unrealized depreciation on investments	3,183,622	(18,284,402)
Net increase in unrealized appreciation on written call options	89,044	1,382
Net decrease in net assets resulting from operations	(2,147,622)	(7,788,958)
Changes in net assets from capital stock transactions:		
Acquisition of vested restricted stock awards to pay required employee withholding tax	(68,872)	(123,183)
Stock-based compensation expense	497,634	1,249,756
Net increase in net assets resulting from capital stock transactions	428,762	1,126,573
Changes in net assets from accumulated other comprehensive income:		
Other comprehensive (loss) income	(104,492)	927,186
Net (decrease) increase in net assets resulting from accumulated other comprehensive income	(104,492)	927,186
Net decrease in net assets	(1,823,352)	(5,735,199)
Net Assets:		
Beginning of the period	122,701,575	128,436,774
End of the period	$ 120,878,223	$ 122,701,575

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

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF JUNE 30, 2014

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	Shares/ Principal	Value
Investments in Unaffiliated Companies (3) – 19.5% of net assets at value					
Private Placement Portfolio (Illiquid) (4) – 13.5% of net assets at value					
Bridgelux, Inc. (5)(8)(10)		Energy			
Manufacturing high-power light emitting diodes (LEDs) and arrays					
Series B Convertible Preferred Stock	(M)		$1,000,000	1,861,504	$330,208
Series C Convertible Preferred Stock	(M)		1,352,196	2,130,699	377,961
Series D Convertible Preferred Stock	(M)		1,371,622	999,999	1,152,335
Series E Convertible Preferred Stock	(M)		672,599	440,334	707,435
Series E-1 Convertible Preferred Stock	(M)		386,073	399,579	471,034
Warrants for Series C Convertible Preferred Stock expiring 12/31/14	(I)		168,270	163,900	540
Warrants for Series D Convertible Preferred Stock expiring 8/26/14	(I)		88,531	124,999	11,416
Warrants for Series D Convertible Preferred Stock expiring 3/10/15	(I)		40,012	41,666	12,502
Warrants for Series E Convertible Preferred Stock expiring 12/31/17	(I)		93,969	170,823	181,791
Warrants for Common Stock expiring 6/1/16	(I)		72,668	132,100	928
Warrants for Common Stock expiring 8/9/18	(I)		148,409	171,183	12,726
Warrants for Common Stock expiring 10/21/18	(I)		18,816	84,846	3,140
			5,413,165		3,262,016
Cambrios Technologies Corporation (5)(8)(10)		Electronics			
Developing nanowire-enabled electronic materials for the display industry					
Series B Convertible Preferred Stock	(M)		1,294,025	1,294,025	790,475
Series C Convertible Preferred Stock	(M)		1,300,000	1,300,000	794,126
Series D Convertible Preferred Stock	(M)		515,756	515,756	709,165
Series D-2 Convertible Preferred Stock	(M)		92,400	92,400	80,850
Series D-4 Convertible Preferred Stock	(M)		216,168	216,168	189,147
			3,418,349		2,563,763

Cobalt Technologies, Inc. (5)(8)(9)(10)(11)		Energy			
Developing processes for making bio-butanol through biomass fermentation					
Series C-1 Convertible Preferred Stock	(M)		749,998	352,112	469,577
Series D-1 Convertible Preferred Stock	(M)		122,070	48,828	70,771
Series E-1 Convertible Preferred Stock	(M)		114,938	46,089	56,424
Warrants for Series E-1 Pref. Stock expiring on 10/9/22	(I)		2,781	1,407	1,440
Warrants for Series E-1 Pref. Stock expiring on 3/11/23	(I)		5,355	2,707	2,813
			995,142		601,025

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

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF JUNE 30, 2014

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	Shares/ Principal	Value
Investments in Unaffiliated Companies (3) – 19.5% of net assets at value (Cont.)					
Private Placement Portfolio (Illiquid) (4) – 13.5% of net assets at value (Cont.)					
GEO Semiconductor Inc. (5)		Electronics			
Developing programmable, high-performance video and geometry processing solutions					
Participation Agreement with Montage Capital relating to the following assets:					
Warrants for Series A Pref. Stock expiring on 9/17/17	(I)		$66,684	100,000	$97,724
Warrants for Series A-1 Pref. Stock expiring on 6/30/18	(I)		23,566	34,500	37,601
Loan and Security Agreement with GEO Semiconductor relating to the following assets:					
Warrants for Series A Pref. Stock expiring on 3/1/18	(I)		7,512	10,000	9,227
Warrants for Series A-1 Pref. Stock expiring on 6/29/18	(I)		7,546	10,000	9,461
			105,308		154,013
Mersana Therapeutics, Inc. (5)(8)(9)(10)(12)		Life Sciences			
Developing antibody drug conjugates for cancer therapy					
Series A-1 Convertible Preferred Stock	(M)		683,538	635,081	683,538
Common Stock	(M)		3,875,395	350,539	108,667
			4,558,933		792,205
Molecular Imprints, Inc. (5)(8)(10)(13)		Electronics			
Manufacturing nanoimprint lithography capital equipment for non-semiconductor manufacturing markets					
Series A Convertible Preferred Stock	(M)		928,884	928,884	928,884

Nanosys, Inc. (5)(8)		Energy			
Developing inorganic nanowires and quantum dots for use in LED-backlit devices					
Series C Convertible Preferred Stock	(M)		1,500,000	803,428	977,659
Series D Convertible Preferred Stock	(M)		3,000,003	1,016,950	2,014,088
Series E Convertible Preferred Stock	(M)		496,573	433,688	661,331
Unsecured Convertible Bridge Note, 4%, acquired 7/16/12	(M)		47,255	$43,821	123,080
			5,043,831		3,776,158

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

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF JUNE 30, 2014

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	Shares/ Principal	Value
Investments in Unaffiliated Companies (3) – 19.5% of net assets at value (Cont.)					
Private Placement Portfolio (Illiquid) (4) – 13.5% of net assets at value (Cont.)					
Nano Terra, Inc. (5)(9)		Energy			
Developing surface chemistry and nano-manufacturing solutions					
Senior secured debt, 12.0%, maturing on 12/1/15	(I)		$525,012	$560,415	$554,400
Warrants for Series A-2 Pref. Stock expiring on 2/22/21	(I)		69,168	446,248	21,125
Warrants for Series C Pref. Stock expiring on 11/15/22	(I)		35,403	241,662	88,979
			629,583		664,504
Nantero, Inc. (5)(8)(9)(10)		Electronics			
Developing a high-density, nonvolatile, random access memory chip, enabled by carbon nanotubes					
Series A Convertible Preferred Stock	(M)		489,999	345,070	1,349,224
Series B Convertible Preferred Stock	(M)		323,000	207,051	809,569
Series C Convertible Preferred Stock	(M)		571,329	188,315	736,312
Series D Convertible Preferred Stock	(M)		139,075	35,569	139,075
			1,523,403		3,034,180
OHSO Clean, Inc. (5)(14)		Life Sciences			
Developing natural, hypoallergenic household cleaning products enabled by nanotechnology-enabled formulations of thyme oil					
Participation Agreement with Montage Capital relating to the following assets:					
Senior secured debt, 13.00%, maturing on 3/31/15	(I)		443,207	$552,640	523,840
Warrants for Series C Pref. Stock expiring on 3/30/22	(I)		91,742	1,109,333	16,000
			534,949		539,840

Total Unaffiliated Private Placement Portfolio (cost: $23,151,547)	$16,316,588

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

9

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF JUNE 30, 2014

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	Shares/ Principal	Va
Rights to Milestone Payments (Illiquid) (6) – 3.4% of net assets at value					
Amgen, Inc. (8)(10)		Life Sciences			
Rights to Milestone Payments from Acquisition of BioVex Group, Inc.	(I)		$3,291,750	$3,291,750	$3
Laird Technologies, Inc. (8)(10)		Energy			
Rights to Milestone Payments from Merger & Acquisition of Nextreme Thermal Solutions, Inc.	(I)		0	0	(
Canon, Inc. (8)(10)		Electronics			
Rights to Milestone Payments from Acquisition of Molecular Imprints, Inc.	(I)		629,670	$629,670	6
Total Unaffiliated Rights to Milestone Payments (cost: $3,921,420)					$4
Publicly Traded Portfolio (7) – 2.6% of net assets at value					
Solazyme, Inc. (5)(10)(15) Developing algal biodiesel, industrial chemicals and specialty ingredients using synthetic biology		Energy			
Common Stock	(M)		$118,099	50,000	$5
Champions Oncology, Inc. (5)(10) Developing its TumorGraft™ platform for personalized medicine and drug development		Life Sciences			
Common Stock	(M)		1,622,629	2,523,895	2
Warrants for Common Stock expiring 1/29/18	(I)		400	40,000	2
			1,623,029		2
Total Unaffiliated Publicly Traded Portfolio (cost: $1,741,128)					$3
Total Investments in Unaffiliated Companies (cost: $28,814,095)					$2

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

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF JUNE 30, 2014

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	Shares/ Principal	Value
Investments in Non-Controlled Affiliated Companies (3) – 58.1% of net assets at value					
Private Placement Portfolio (Illiquid) (16) – 58.1% of net assets at value					
ABSMaterials, Inc. (5)(8)(9)		Energy			
Developing nano-structured absorbent materials for environmental remediation					
Series A Convertible Preferred Stock	(M)		$435,000	390,000	$471,900
Series B Convertible Preferred Stock	(M)		1,217,644	1,037,751	1,255,679
			1,652,644		1,727,579
Adesto Technologies Corporation (5)(8)(17)		Electronics			
Developing low-power, high-performance memory devices					
Series A Convertible Preferred Stock	(M)		2,200,000	6,547,619	1,388,276
Series B Convertible Preferred Stock	(M)		2,200,000	5,952,381	1,262,070
Series C Convertible Preferred Stock	(M)		1,485,531	2,122,187	479,218
Series D Convertible Preferred Stock	(M)		1,393,147	1,466,470	1,040,812
Series D-1 Convertible Preferred Stock	(M)		703,740	987,706	561,291
Series E Convertible Preferred Stock	(M)		2,499,999	3,508,771	9,969,781
			10,482,417		14,701,448
AgBiome, LLC (formerly AgInnovation, LLC) (5)(8)(9)(10)		Life Sciences			
Providing early stage research and discovery for agriculture and utilizing the crop microbiome to identify products that reduce risk and improve yield					
Series A-1 Convertible Preferred Stock	(M)		2,000,000	2,000,000	2,456,834
Series A-2 Convertible Preferred Stock	(M)		521,740	417,392	564,906
			2,521,740		3,021,740
Contour Energy Systems, Inc. (5)(8)(9)(10)		Energy			
Developing batteries using nano-structured materials					

Series A Convertible Preferred Stock	(M)	2,009,995	2,565,798	0
Series B Convertible Preferred Stock	(M)	1,300,000	812,500	0
Series C Convertible Preferred Stock	(M)	1,200,000	1,148,325	0
		4,509,995		0

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

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF JUNE 30, 2014

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	Shares/ Principal	Value
Investments in Non-Controlled Affiliated Companies (3) – 58.1% of net assets at value (Cont.)					
Private Placement Portfolio (Illiquid) (16) – 58.1% of net assets at value (Cont.)					
D-Wave Systems, Inc. (8)(9)(18)		Electronics			
Developing high-performance quantum computing systems					
Series 1 Class B Convertible Preferred Stock	(M)		$1,002,074	1,144,869	$2,327,977
Series 1 Class C Convertible Preferred Stock	(M)		487,804	450,450	915,945
Series 1 Class D Convertible Preferred Stock	(M)		748,473	855,131	1,738,823
Series 1 Class E Convertible Preferred Stock	(M)		248,049	269,280	547,554
Series 1 Class F Convertible Preferred Stock	(M)		238,323	258,721	526,083
Series 1 Class H Convertible Preferred Stock	(M)		909,088	460,866	937,125
Series 2 Class D Convertible Preferred Stock	(M)		736,019	678,264	1,379,182
Series 2 Class E Convertible Preferred Stock	(M)		659,493	513,900	1,044,964
Series 2 Class F Convertible Preferred Stock	(M)		633,631	493,747	1,003,985
Warrants for Common Stock expiring 6/30/15	(I)		98,644	153,890	71,258
Warrants for Common Stock expiring 5/12/19	(I)		26,357	20,415	10,721
			5,787,955		10,503,617
EchoPixel, Inc. (5)(8)(9)(10)		Life Sciences			
Developing algorithms and software to improve visualization of data for life science and healthcare applications					
Series Seed Convertible Preferred Stock	(M)		1,250,000	4,194,630	1,250,000
Ensemble Therapeutics Corporation (5)(8)(9)		Life Sciences			
Developing DNA-Programmed Chemistry™ for the discovery of new classes of therapeutics					
Series B Convertible Preferred Stock	(H)		2,000,000	1,449,275	1,030,781
Series B-1 Convertible Preferred Stock	(H)		679,754	492,575	2,719,014
			2,679,754		3,749,795
Enumeral Biomedical Corp. (5)(8)(9)(19)		Life Sciences			
Developing therapeutics and diagnostics					

through functional assaying of single cells				
Series A Convertible Preferred Stock	(M)	1,026,832	957,038	908,635
Series A-1 Convertible Preferred Stock	(M)	750,000	576,923	613,852
Series A-2 Convertible Preferred Stock	(M)	1,050,001	724,138	859,395
Series B Convertible Preferred Stock	(M)	1,000,000	470,588	818,471
Secured Convertible Bridge Note, 12%, acquired 2/3/14	(I)	204,766	$250,000	629,821
Warrants for Common Stock expiring 2/2/24	(I)	57,567	231,481	138,876
		4,089,166		3,969,050

The accompanying unaudited notes are an integral part of these consolidated financial statements

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF JUNE 30, 2014

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	Shares/ Principal	Value
Investments in Non-Controlled Affiliated Companies (3) – 58.1% of net assets at value (Cont.)					
Private Placement Portfolio (Illiquid) (16) – 58.1% of net assets at value (Cont.)					
HZO, Inc. (5)(8)(9)		Electronics			
Developing novel industrial coatings that protect electronics against damage from liquids					
Common Stock	(M)		$666,667	405,729	$436,605
Series I Convertible Preferred Stock	(M)		5,709,835	2,266,894	8,144,723
Series II Convertible Preferred Stock	(M)		2,000,003	539,710	2,255,610
			8,376,505		10,836,938
Laser Light Engines, Inc. (5)(8)(9)		Energy			
Manufacturing solid-state light sources for digital cinema and large-venue projection displays					
Series A Convertible Preferred Stock	(I)		2,000,000	7,499,062	0
Series B Convertible Preferred Stock	(I)		3,095,802	13,571,848	0
Secured Convertible Bridge Note, 12%, acquired 10/7/11	(I)		200,000	$200,000	0
Secured Convertible Bridge Note, 12%, acquired 11/17/11	(I)		95,652	$95,652	0
Secured Convertible Bridge Note, 12%, acquired 12/21/11	(I)		82,609	$82,609	0
Secured Convertible Bridge Note, 12%, acquired 3/5/12	(I)		434,784	$434,784	0
Secured Convertible Bridge Note, 12%, acquired 7/26/12	(I)		186,955	$186,955	0
Secured Convertible Bridge Note, 20%, acquired 4/29/13	(I)		166,667	$166,667	0
Secured Convertible Bridge Note, 20%, acquired 7/22/13	(I)		166,667	$166,667	0
Secured Convertible Bridge Note, 10%, acquired 10/30/13	(I)		80,669	$80,669	0

Secured Convertible Bridge Note, 10%, acquired 2/5/14	(I)		19,331	$19,331	0
Secured Convertible Bridge Note, 10%, acquired 6/24/14	(I)		13,771	$13,745	13,771
			6,542,907		13,771
Metabolon, Inc. (5)(8)(10)		Life Sciences			
Developing service and diagnostic products through the use of a metabolomics, or biochemical, profiling platform					
Series B Convertible Preferred Stock	(M)		2,500,000	371,739	2,997,991
Series B-1 Convertible Preferred Stock	(M)		706,214	148,696	1,199,196
Series C Convertible Preferred Stock	(M)		1,000,000	1,000,000	2,756,500
Series D Convertible Preferred Stock	(M)		1,499,999	835,882	2,304,109
Series E Convertible Preferred Stock	(M)		1,225,000	444,404	1,225,000
Warrants for Series B-1 Convertible Preferred Stock expiring 3/25/15	(I)		293,786	74,348	172,233
			7,224,999		10,655,029

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

13

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF JUNE 30, 2014

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	Shares/ Principal	Value
Investments in Non-Controlled Affiliated Companies (3) – 58.1% of net assets at value (Cont.)					
Private Placement Portfolio (Illiquid) (16) – 58.1% of net assets at value (Cont.)					
OpGen, Inc. (8)		Life Sciences			
Developing tools for genomic sequence assembly and analysis					
Series A Convertible Preferred Stock	(M)		$610,017	610,017	$610,017
Common Stock	(M)		3,260,000	29,883	1,494
			3,870,017		611,511
Produced Water Absorbents, Inc. (5)(8)(9)		Energy			
Developing nano-structured absorbent materials for environmental remediation of contaminated water in the oil and gas industries					
Series A Convertible Preferred Stock	(M)		1,000,000	1,000,000	187,500
Series B Convertible Preferred Stock	(M)		1,496,865	5,987,460	2,390,004
Series B-2 Convertible Preferred Stock	(M)		1,015,427	4,322,709	1,645,885
Series B-3 Convertible Preferred Stock	(M)		978,641	3,914,564	1,562,570
Series C Convertible Preferred Stock	(M)		1,000,268	2,667,380	923,584
Warrants for Series B-2 Preferred Stock expiring upon liquidation event	(I)		65,250	300,000	73,557
			5,556,451		6,783,100
Senova Systems, Inc. (5)(8)(9)		Life Sciences			
Developing next-generation sensors to measure pH					
Series B Convertible Preferred Stock	(M)		1,218,462	1,350,000	540,000
Series B-1 Convertible Preferred Stock	(M)		1,083,960	2,759,902	1,103,960
Secured Convertible Bridge Note, 10%, acquired 6/25/14	(M)		250,411	$250,000	250,411
Warrants for Series B Preferred Stock expiring 10/15/17	(I)		131,538	164,423	65,753
Warrants for Series B Preferred Stock expiring 4/24/18	(I)		20,000	25,000	9,997
			2,704,371		1,970,121

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

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF JUNE 30, 2014

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	Shares/ Principal	Value
Investments in Non-Controlled Affiliated Companies (3) – 58.1% of net assets at value (Cont.)					
Private Placement Portfolio (Illiquid) (16) – 58.1% of net assets at value (Cont.)					
SiOnyx, Inc. (5)(8)(9)		Electronics			
Developing silicon-based optoelectronic products enabled by its proprietary Black Silicon					
Series A Convertible Preferred Stock	(M)		$750,000	233,499	$0
Series A-1 Convertible Preferred Stock	(M)		890,000	2,966,667	0
Series A-2 Convertible Preferred Stock	(M)		2,445,000	4,207,537	0
Series B-1 Convertible Preferred Stock	(M)		1,169,561	1,892,836	0
Series C Convertible Preferred Stock	(M)		1,171,316	1,674,030	0
Secured Convertible Bridge Note, 8%, acquired 1/31/14	(M)		1,324,114	$1,281,125	174,436
Secured Convertible Bridge Note, 8%, acquired 5/9/14	(M)		78,073	$93,976	234,220
Warrants for Series B-1 Convertible Preferred Stock expiring 2/23/17	(I)		130,439	247,350	0
Warrants for Common Stock expiring 3/28/17	(I)		84,207	418,507	0
Warrants for Common Stock expiring 5/9/19	(I)		17,010	3,208	0
			8,059,720		408,656
Ultora, Inc. (5)(8)(9)(10)		Energy			
Developing energy-storage devices enabled by carbon nanotubes					
Series A Convertible Preferred Stock	(M)		886,830	17,736	0
Series B Convertible Preferred Stock	(M)		236,603	2,347,254	0
Secured Convertible Bridge Note, 5%, acquired 5/7/14	(M)		86,696	$86,039	73,993
			1,210,129		73,993
Total Non-Controlled Private Placement Portfolio (cost: $76,518,770)					$70,276,348
Total Investments in Non-Controlled Affiliated Companies (cost: $76,518,770)					$70,276,348

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

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF JUNE 30, 2014

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	**Shares/** Principal	Value
Investments in Controlled Affiliated Companies (3) – 1.9% of net assets at value					
Private Placement Portfolio (Illiquid) (20) – 1.9% of net assets at value					
ProMuc, Inc. (5)(8)(9)		Life Sciences			
Developing synthetic mucins for the nutritional, food and healthcare markets					
Common Stock	(M)		$1	1,000	$1
Secured Convertible Bridge Note, 8%, acquired 12/18/13	(M)		364,959	$350,000	364,959
			364,960		364,960
SynGlyco, Inc. (5)(8)(9)		Life Sciences			
Developed synthetic carbohydrates for pharmaceutical applications					
Common Stock	(I)		2,729,817	57,463	0
Series A' Convertible Preferred Stock	(I)		4,855,627	4,855,627	0
Senior Secured Debt, 12.00%, maturing on 12/11/14	(I)		466,298	$500,000	751,500
Secured Convertible Bridge Note, 8%, acquired 1/23/13	(I)		391,173	$350,000	350,154
Secured Convertible Bridge Note, 8%, acquired 4/25/13	(I)		328,758	$300,000	300,132
			8,771,673		1,401,786
UberSeq, Inc. (5)(8)(9)(10)(21)		Life Sciences			
Developing translational genomics solutions					
Series Seed Convertible Preferred Stock	(M)		500,000	500,000	500,000
Total Controlled Private Placement Portfolio (cost: $9,636,633)					$2,266,746
Total Investments in Controlled Affiliated Companies (cost: $9,636,633)					$2,266,746
Total Private Placement and Publicly Traded Portfolio (cost: $114,969,498)					$96,122,831

Total Investments (cost: $114,969,498)	$96,122,831

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

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF JUNE 30, 2014

(Unaudited)

	Method of Valuation (1)	Number of Contracts	Value
Written Call Options – (0.04)% of net assets at value			
Solazyme, Inc. — Strike Price $12.50, September 20, 2014	(M)	500	$(47,500)
Total Written Call Options (Premiums Received $145,426)			$(47,500)

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

17

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF JUNE 30, 2014

(Unaudited)

Notes to Consolidated Schedule of Investments

(1) See "Footnote to Consolidated Schedule of Investments" on page 32 for a description of the "Valuation Procedures."

(2) We classify "Energy" companies as those that seek to improve performance, productivity or efficiency, and to reduce environmental impact, waste, cost, energy consumption or raw materials. We classify "Electronics" companies as those that address problems in electronics-related industries, including semiconductors. We classify "Life Sciences" companies as those that address problems in life sciences-related industries, including biotechnology, agriculture, advanced materials and chemicals, healthcare, bioprocessing, water, industrial biotechnology, food, nutrition and energy.

(3) Investments in unaffiliated companies consist of investments in which we own less than five percent of the voting shares of the portfolio company. Investments in non-controlled affiliated companies consist of investments in which we own five percent or more, but less than 25 percent, of the voting shares of the portfolio company, or where we hold one or more seats on the portfolio company's Board of Directors but do not control the company. Investments in controlled affiliated companies consist of investments in which we own 25 percent or more of the voting shares of the portfolio company or otherwise control the company.

(4) The aggregate cost for federal income tax purposes of investments in unaffiliated privately held companies is $23,151,547. The gross unrealized appreciation based on the tax cost for these securities is $1,599,294. The gross unrealized depreciation based on the tax cost for these securities is $8,434,253.

(5) All or a portion of the investments or instruments are pledged as collateral under our loan facility.

(6) The aggregate cost for federal income tax purposes of investments in unaffiliated rights to milestone payments is $3,921,420. The gross unrealized appreciation based on the tax cost for these securities is $205,684. The gross unrealized depreciation based on the tax cost for these securities is $0.

(7) The aggregate cost for federal income tax purposes of investments in unaffiliated publicly traded companies is $1,741,128. The gross unrealized appreciation based on the tax cost for these securities is $1,394,917. The gross unrealized depreciation based on the tax cost for these securities is $0.

(8) We are subject to legal restrictions on the sale of our investment(s) in this company.

(9) These investments are development-stage companies. A development-stage company is defined as a company that is devoting substantially all of its efforts to establishing a new business, and either it has not yet commenced its planned principal operations, or it has commenced such operations but has not realized significant revenue from them.

(10) Represents a non-income producing security. Investments that have not paid dividends or interest within the last 12 months are considered to be non-income producing.

(11) Cobalt Technologies, Inc., also does business as Cobalt Biofuels.

(12) With our investment in the Mersana Therapeutics, Inc., Series A-1 financing, we received a warrant to purchase 277,760 shares of Series A-2 Convertible Preferred Stock. The ability to exercise the warrant is contingent upon Mersana's achievement of certain milestones. Mersana has not achieved those milestones as of June 30, 2014, and, therefore, this warrant is a contingent asset as of that date. The warrant will expire on July 27, 2022.

The accompanying unaudited notes are an integral part of this consolidated schedule.

18

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF JUNE 30, 2014

(Unaudited)

(13) Upon the closing of Canon's acquisition of Molecular Imprints, Inc.'s semiconductor lithography equipment business, a new spin-out company, which retained the name Molecular Imprints, Inc., was formed. These shares represent our investment in the new company.

(14) OHSO Clean, Inc. also does business as CleanWell Company.

(15) All of the shares of this security are held in connection with written call option contracts and are, therefore, pledged to brokers.

(16) The aggregate cost for federal income tax purposes of investments in non-controlled affiliated privately held companies is $76,518,770. The gross unrealized appreciation based on the tax cost for these securities is $17,696,781. The gross unrealized depreciation based on the tax cost for these securities is $23,939,203.

(17) Adesto Technologies Corporation's Series E shares have certain rights and preferences in a sale or IPO that are not ascribed to the other classes of stock.

(18) D-Wave Systems, Inc., is located and is doing business primarily in Canada. We invested in D-Wave Systems, Inc., through Parallel Universes, Inc., a Delaware company. Our investment is denominated in Canadian dollars and is subject to foreign currency translation. See "Note 3. Summary of Significant Accounting Policies."

(19) At June 30, 2014, Enumeral Biomedical Corp. was part of our private placement portfolio. On July 31, 2014, Enumeral completed a reverse merger into a publicly traded shell company and is traded publicly on the OTC market. See "Note 12. Subsequent Events."

(20) The aggregate cost for federal income tax purposes of investments in controlled affiliated companies is $9,636,633. The gross unrealized appreciation based on the tax cost for these securities is $0. The gross unrealized depreciation based on the tax cost for these securities is $7,369,887.

(21) Initial investment was made in 2014.

The accompanying unaudited notes are an integral part of this consolidated schedule.

19

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2013

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	Shares/ Principal	Value
Investments in Unaffiliated Companies (3) – 31.2% of net assets at value					
Private Placement Portfolio (Illiquid) (4) – 23.8% of net assets at value					
Bridgelux, Inc. (5)(8)(10)		Energy			
Manufacturing high-power light emitting diodes (LEDs) and arrays					
Series B Convertible Preferred Stock	(M)		$1,000,000	1,861,504	$318,898
Series C Convertible Preferred Stock	(M)		1,352,196	2,130,699	365,014
Series D Convertible Preferred Stock	(M)		1,371,622	999,999	1,070,897
Series E Convertible Preferred Stock	(M)		672,599	440,334	704,760
Series E-1 Convertible Preferred Stock	(M)		386,073	399,579	468,606
Warrants for Series C Convertible Preferred Stock expiring 12/31/14	(I)		168,270	163,900	2,762
Warrants for Series D Convertible Preferred Stock expiring 8/26/14	(I)		88,531	124,999	40,686
Warrants for Series D Convertible Preferred Stock expiring 3/10/15	(I)		40,012	41,666	19,466
Warrants for Series E Convertible Preferred Stock expiring 12/31/17	(I)		93,969	170,823	190,679
Warrants for Common Stock expiring 6/1/16	(I)		72,668	132,100	1,656
Warrants for Common Stock expiring 8/9/18	(I)		148,409	171,183	13,538
Warrants for Common Stock expiring 10/21/18	(I)		18,816	84,846	3,680
			5,413,165		3,200,642
Cambrios Technologies Corporation (5)(8)(10)		Electronics			
Developing nanowire-enabled electronic materials for the display industry					
Series B Convertible Preferred Stock	(M)		1,294,025	1,294,025	1,165,383
Series C Convertible Preferred Stock	(M)		1,300,000	1,300,000	1,170,764
Series D Convertible Preferred Stock	(M)		515,756	515,756	773,634
Series D-2 Convertible Preferred Stock	(M)		92,400	92,400	92,400
Series D-4 Convertible Preferred Stock	(M)		216,168	216,168	216,168
			3,418,349		3,418,349

Cobalt Technologies, Inc. (5)(8)(9)(11)		Energy			
Developing processes for making bio-butanol through biomass fermentation					
Series C-1 Convertible Preferred Stock	(M)		749,998	352,112	704,400
Series D-1 Convertible Preferred Stock	(M)		122,070	48,828	106,152
Series E-1 Convertible Preferred Stock	(M)		114,938	46,089	84,634
Warrants for Series E-1 Pref. Stock expiring on 10/9/22	(I)		2,781	1,407	2,163
Warrants for Series E-1 Pref. Stock expiring on 3/11/23	(I)		5,355	2,707	4,209
			995,142		901,558

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

20

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2013

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	Shares/ Principal	Value
Investments in Unaffiliated Companies (3) – 31.2% of net assets at value (Cont.)					
Private Placement Portfolio (Illiquid) (4) – 23.8% of net assets at value (Cont.)					
Ensemble Therapeutics Corporation (5)(8)(9)(12)		Life Sciences			
Developing DNA-Programmed Chemistry™ for the discovery of new classes of therapeutics					
Series B Convertible Preferred Stock	(H)		$2,000,000	1,449,275	$1,419,855
Secured Convertible Bridge Note, 8%, acquired 9/11/08	(H)		356,567	$250,211	1,321,657
Secured Convertible Bridge Note, 8%, acquired 12/10/09	(H)		64,767	$48,868	253,257
Secured Convertible Bridge Note, 8%, acquired 1/25/12	(H)		126,386	$109,400	548,354
Secured Convertible Bridge Note, 8%, acquired 3/28/13	(H)		78,121	$73,598	361,996
Secured Convertible Bridge Note, 8%, acquired 6/24/13	(H)		26,845	$25,759	126,201
Secured Convertible Bridge Note, 8%, acquired 7/8/13	(H)		14,530	$13,983	68,467
			2,667,216		4,099,787
GEO Semiconductor Inc. (5)		Electronics			
Developing programmable, high-performance video and geometry processing solutions					
Participation Agreement with Montage Capital relating to the following assets:					
Warrants for Series A Pref. Stock expiring on 9/17/17	(I)		66,684	100,000	82,270
Warrants for Series A-1 Pref. Stock expiring on 6/30/18	(I)		23,566	34,500	32,132
Loan and Security Agreement with GEO Semiconductor relating to the following assets:					
Warrants for Series A Pref. Stock expiring on 3/1/18	(I)		7,512	10,000	8,007

Warrants for Series A-1 Pref. Stock expiring on 6/29/18	(I)		7,546	10,000	8,478
			105,308		130,887
Mersana Therapeutics, Inc. (5)(8)(9)(10)(13)		Life Sciences			
Developing antibody drug conjugates					
for cancer therapy					
Series A-1 Convertible Preferred Stock	(M)		443,038	411,630	443,038
Common Stock	(M)		3,875,395	350,539	108,667
			4,318,433		551,705
Molecular Imprints, Inc. (5)(8)(10)(14)(15)		Electronics			
Manufacturing nanoimprint					
lithography capital equipment					
Series B Convertible Preferred Stock	(I)		2,000,000	1,333,333	1,876,501
Series C Convertible Preferred Stock	(I)		2,406,595	1,285,071	2,359,061
Non-Convertible Bridge Note	(I)		0	$0	4,043,381
			4,406,595		8,278,943

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

21

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2013

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	Shares/ Principal	Value
Investments in Unaffiliated Companies (3) – 31.2% of net assets at value (Cont.)					
Private Placement Portfolio (Illiquid) (4) – 23.8% of net assets at value (Cont.)					
Nanosys, Inc. (5)(8)		Energy			
Developing inorganic nanowires and quantum dots for use in LED-backlit devices					
Series C Convertible Preferred Stock	(M)		$1,500,000	803,428	$1,098,762
Series D Convertible Preferred Stock	(M)		3,000,003	1,016,950	2,196,781
Series E Convertible Preferred Stock	(M)		496,573	433,688	705,827
Unsecured Convertible Bridge Note, 4%, acquired 7/16/12	(M)		46,385	$43,821	127,016
			5,042,961		4,128,386
Nano Terra, Inc. (5)(9)		Energy			
Developing surface chemistry and nano-manufacturing solutions					
Senior secured debt, 12.0%, maturing on 12/1/15	(I)		663,322	$698,725	680,000
Warrants for Series A-2 Pref. Stock expiring on 2/22/21	(I)		69,168	446,248	21,858
Warrants for Series C Pref. Stock expiring on 11/15/22	(I)		35,403	241,662	90,476
			767,893		792,334
Nantero, Inc. (5)(8)(9)(10)		Electronics			
Developing a high-density, nonvolatile, random access memory chip, enabled by carbon nanotubes					
Series A Convertible Preferred Stock	(M)		489,999	345,070	1,349,224
Series B Convertible Preferred Stock	(M)		323,000	207,051	809,569
Series C Convertible Preferred Stock	(M)		571,329	188,315	736,312
Series D Convertible Preferred Stock	(M)		139,075	35,569	139,075
			1,523,403		3,034,180
OHSO Clean, Inc. (5)(16)		Life Sciences			
Developing natural, hypoallergenic household					

cleaning products enabled by nanotechnology-enabled formulations of thyme oil				
Participation Agreement with Montage Capital relating to the following assets:				
Senior secured debt, 13.00%, maturing on 3/31/15	(I)	527,006	$624,640	592,100
Warrants for Series C Pref. Stock expiring on 3/30/22	(I)	91,742	1,109,333	70,693
		618,748		662,793
Total Unaffiliated Private Placement Portfolio (cost: $29,277,213)				$29,199,564

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

22

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2013

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	Shares/ Principal	Value
Rights to Milestone Payments (Illiquid) (6) – 2.9% of net assets at value					
Amgen, Inc. (8)(10)		Life Sciences			
Rights to Milestone Payments from Acquisition of BioVex Group, Inc.	(I)		$3,291,750	$3,291,750	$3,489,433
Laird Technologies, Inc. (8)(10)		Energy			
Rights to Milestone Payments from Merger & Acquisition of Nextreme Thermal Solutions, Inc.	(I)		0	0	0
Total Unaffiliated Rights to Milestone Payments (cost: $3,291,750)					$3,489,433
Publicly Traded Portfolio (7) – 4.5% of net assets at value					
Solazyme, Inc. (5)(10)(17)		Energy			
Developing algal biodiesel, industrial chemicals and specialty ingredients using synthetic biology					
Common Stock	(M)		$396,564	167,834	$1,827,712
Champions Oncology, Inc. (5)(10)		Life Sciences			
Developing its TumorGraft™ platform for personalized medicine and drug development					
Common Stock	(M)		2,054,446	3,099,651	3,719,582
Warrants for Common Stock expiring 1/29/18	(I)		400	40,000	23,502
			2,054,846		3,743,084
Total Unaffiliated Publicly Traded Portfolio (cost: $2,451,410)					$5,570,796
Total Investments in Unaffiliated Companies (cost: $35,020,373)					$38,259,793

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

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2013

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	Shares/ Principal	Value
Investments in Non-Controlled Affiliated Companies (3) – 44.2% of net assets at value					
Private Placement Portfolio (Illiquid) (18) – 44.2% of net assets at value					
ABSMaterials, Inc. (5)(8)(9)		Energy			
Developing nano-structured absorbent materials for environmental remediation					
Series A Convertible Preferred Stock	(M)		$435,000	390,000	$471,900
Series B Convertible Preferred Stock	(M)		717,644	624,528	755,679
			1,152,644		1,227,579
Adesto Technologies Corporation (5)(8)(19)		Electronics			
Developing low-power, high-performance memory devices					
Series A Convertible Preferred Stock	(M)		2,200,000	6,547,619	1,388,276
Series B Convertible Preferred Stock	(M)		2,200,000	5,952,381	1,262,070
Series C Convertible Preferred Stock	(M)		1,485,531	2,122,187	449,963
Series D Convertible Preferred Stock	(M)		1,393,147	1,466,470	1,070,067
Series D-1 Convertible Preferred Stock	(M)		703,740	987,706	561,291
Series E Convertible Preferred Stock	(M)		2,499,999	3,508,771	9,969,781
			10,482,417		14,701,448
AgBiome, LLC (formerly AgInnovation, LLC) (5)(8)(9)(10)(20)		Life Sciences			
Providing early stage research and discovery for agriculture and utilizing the crop microbiome to identify products that reduce risk and improve yield					
Series A-1 Convertible Preferred Stock	(M)		2,000,000	2,000,000	2,456,834
Series A-2 Convertible Preferred Stock	(M)		521,740	417,392	564,906
			2,521,740		3,021,740
Contour Energy Systems, Inc. (5)(8)(9)(10)(21)		Energy			
Developing batteries using nano-structured materials					
Series A Convertible Preferred Stock	(M)		2,009,995	2,565,798	0

Series B Convertible Preferred Stock	(M)	1,300,000	812,500	0
Series C Convertible Preferred Stock	(M)	1,200,000	1,148,325	90,844
		4,509,995		90,844

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

24

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2013

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	Shares/ Principal	Value
Investments in Non-Controlled Affiliated Companies (3) – 44.2% of net assets at value (Cont.)					
Private Placement Portfolio (Illiquid) (18) – 44.2% of net assets at value (Cont.)					
D-Wave Systems, Inc. (8)(9)(10)(22)		Electronics			
Developing high-performance quantum computing systems					
Series 1 Class B Convertible Preferred Stock	(M)		$1,002,074	1,144,869	$1,399,831
Series 1 Class C Convertible Preferred Stock	(M)		487,804	450,450	550,765
Series 1 Class D Convertible Preferred Stock	(M)		748,473	855,131	1,045,569
Series 1 Class E Convertible Preferred Stock	(M)		248,049	269,280	329,249
Series 1 Class F Convertible Preferred Stock	(M)		238,323	258,721	316,338
Series 2 Class D Convertible Preferred Stock	(M)		736,019	678,264	829,313
Series 2 Class E Convertible Preferred Stock	(M)		659,493	513,900	628,345
Series 2 Class F Convertible Preferred Stock	(M)		633,631	493,747	603,704
Warrants for Common Stock expiring 6/30/15	(I)		98,644	153,890	37,617
			4,852,510		5,740,731
EchoPixel, Inc. (5)(8)(9)(10)(23)		Life Sciences			
Developing algorithms and software to improve visualization of data for life science and healthcare applications					
Series Seed Convertible Preferred Stock	(M)		750,000	2,516,778	750,000
Enumeral Biomedical Corp. (5)(8)(9)(10)		Life Sciences			
Developing therapeutics and diagnostics through functional assaying of single cells					
Series A Convertible Preferred Stock	(M)		1,026,832	957,038	690,538
Series A-1 Convertible Preferred Stock	(M)		750,000	576,923	425,939
Series A-2 Convertible Preferred Stock	(M)		1,050,001	724,138	566,027
			2,826,833		1,682,504
HZO, Inc. (5)(8)(9)		Electronics			
Developing novel industrial coatings that protect electronics against damage from liquids					

Series A Convertible Preferred Stock	(M)	666,667	4,057,294	1,130,362
Series B Convertible Preferred Stock	(M)	5,502,838	21,879,365	6,095,592
		6,169,505		7,225,954

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

25

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2013

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	Shares/ Principal	Value
Investments in Non-Controlled Affiliated Companies (3) – 44.2% of net assets at value (Cont.)					
Private Placement Portfolio (Illiquid) (18) – 44.2% of net assets at value (Cont.)					
Kovio, Inc. (5)(8)(9)(24)		Electronics			
Developing semiconductor products using printed electronics and thin-film technologies					
Series A' Convertible Preferred Stock	(M)		$5,242,993	2,160,000	$0
Series B' Convertible Preferred Stock	(M)		2,006,540	3,015,493	0
Secured Subordinated Convertible Bridge Note, 7%, acquired 6/7/13	(M)		50,000	$50,000	0
			7,299,533		0
Laser Light Engines, Inc. (5)(8)(9)		Energy			
Manufacturing solid-state light sources for digital cinema and large-venue projection displays					
Series A Convertible Preferred Stock	(I)		2,000,000	7,499,062	0
Series B Convertible Preferred Stock	(I)		3,095,802	13,571,848	0
Secured Convertible Bridge Note, 12%, acquired 10/7/11	(I)		200,000	$200,000	0
Secured Convertible Bridge Note, 12%, acquired 11/17/11	(I)		95,652	$95,652	0
Secured Convertible Bridge Note, 12%, acquired 12/21/11	(I)		82,609	$82,609	0
Secured Convertible Bridge Note, 12%, acquired 3/5/12	(I)		434,784	$434,784	0
Secured Convertible Bridge Note, 12%, acquired 7/26/12	(I)		186,955	$186,955	0
Secured Convertible Bridge Note, 20%, acquired 4/29/13	(I)		166,667	$166,667	0
Secured Convertible Bridge Note, 20%, acquired 7/22/13	(I)		166,667	$166,667	0
	(I)		82,061	$80,669	164,122

Secured Convertible Bridge Note, 10%, acquired 10/30/13					
			6,511,197		164,122
Metabolon, Inc. (5)(8)(10)		Life Sciences			
Developing service and diagnostic products through the use of a metabolomics, or biochemical, profiling platform					
Series B Convertible Preferred Stock	(M)		2,500,000	371,739	2,997,991
Series B-1 Convertible Preferred Stock	(M)		706,214	148,696	1,199,196
Series C Convertible Preferred Stock	(M)		1,000,000	1,000,000	2,756,500
Series D Convertible Preferred Stock	(M)		1,499,999	835,882	2,304,109
Series E Convertible Preferred Stock	(M)		1,225,000	444,404	1,225,000
Warrants for Series B-1 Convertible Preferred Stock expiring 3/25/15	(I)		293,786	74,348	216,408
			7,224,999		10,699,204
OpGen, Inc. (8)		Life Sciences			
Developing tools for genomic sequence assembly and analysis					
Series A Convertible Preferred Stock	(M)		245,000	245,000	245,000
Common Stock	(M)		3,260,000	29,883	0
			3,505,000		245,000

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

26

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2013

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	Shares/ Principal	Value
Investments in Non-Controlled Affiliated Companies (3) – 44.2% of net assets at value (Cont.)					
Private Placement Portfolio (Illiquid) (18) – 44.2% of net assets at value (Cont.)					
Produced Water Absorbents, Inc. (5)(8)(9)		Energy			
Developing nano-structured absorbent materials for environmental remediation of contaminated water in the oil and gas industries					
Series A Convertible Preferred Stock	(M)		$1,000,000	1,000,000	$125,000
Series B Convertible Preferred Stock	(M)		1,626,641	6,506,564	1,751,641
Secured Convertible Bridge Note, 8%, acquired 11/14/13	(M)		832,789	$824,119	832,789
			3,459,430		2,709,430
Senova Systems, Inc. (5)(8)(9)		Life Sciences			
Developing next-generation sensors to measure pH					
Series B Convertible Preferred Stock	(M)		1,218,462	1,350,000	540,000
Series B-1 Convertible Preferred Stock	(M)		583,960	1,509,902	603,960
Warrants for Series B Preferred Stock expiring 10/15/17	(I)		131,538	164,423	65,753
Warrants for Series B Preferred Stock expiring 4/24/18	(I)		20,000	25,000	9,997
			1,953,960		1,219,710
SiOnyx, Inc. (5)(8)(9)		Electronics			
Developing silicon-based optoelectronic products enabled by its proprietary Black Silicon					
Series A Convertible Preferred Stock	(M)		750,000	233,499	43,781
Series A-1 Convertible Preferred Stock	(M)		890,000	2,966,667	556,250
Series A-2 Convertible Preferred Stock	(M)		2,445,000	4,207,537	788,913
Series B-1 Convertible Preferred Stock	(M)		1,169,561	1,892,836	451,903
Series C Convertible Preferred Stock	(M)		1,171,316	1,674,030	970,526
Secured Convertible Bridge Note, 8%, acquired 7/22/13	(M)		433,209	$418,066	859,729

Secured Convertible Bridge Note, 8%, acquired 10/2/13	(M)		426,520	$418,066	859,729
Warrants for Series B-1 Convertible Preferred Stock expiring 2/23/17	(I)		130,439	247,350	18,165
Warrants for Common Stock expiring 3/28/17	(I)		84,207	418,507	21,387
			7,500,252		4,570,383
Ultora, Inc. (5)(8)(9)		Energy			
Developing energy-storage devices enabled by carbon nanotubes					
Series A Convertible Preferred Stock	(M)		886,830	17,736	1,788
Series B Convertible Preferred Stock	(M)		236,603	2,347,254	236,603
			1,123,433		238,391
Total Non-Controlled Private Placement Portfolio (cost: $71,843,448)					$54,287,040
Total Investments in Non-Controlled Affiliated Companies (cost: $71,843,448)					$54,287,040

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

27

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2013

(Unaudited)

	Method of Valuation (1)	Primary Industry (2)	Cost	Shares/ Principal	Value
Investments in Controlled Affiliated Companies (3) – 1.1% of net assets at value					
Private Placement Portfolio (Illiquid) (25) – 1.1% of net assets at value					
SynGlyco, Inc. (5)(8)(9)(26)		Life Sciences			
Developing synthetic carbohydrates for pharmaceutical applications					
Common Stock	(I)		$2,729,817	57,463	$0
Series A' Convertible Preferred Stock	(I)		4,855,627	4,855,627	0
Senior Secured Debt, 12.00%, maturing on 12/11/14	(I)		436,637	$500,000	831,828
Secured Convertible Bridge Note, 8%, acquired 1/23/13	(I)		376,312	$350,000	91,389
Secured Convertible Bridge Note, 8%, acquired 4/25/13	(I)		316,504	$300,000	78,334
			8,714,897		1,001,551
ProMuc, Inc. (5)(8)(9)(22)		Life Sciences			
Developing synthetic mucins for the nutritional, food and healthcare markets					
Common Stock	(M)		1	1,000	1
Secured Convertible Bridge Note, 8%, acquired 12/18/13	(M)		351,074	$350,000	351,074
			351,075		351,075
Total Controlled Private Placement Portfolio (cost: $9,065,972)					$1,352,626
Total Investments in Controlled Affiliated Companies (cost: $9,065,972)					$1,352,626
Total Private Placement and Publicly Traded Portfolio (cost: $115,929,793)					$93,899,459

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

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2013

(Unaudited)

	Method of Valuation (1)	Cost	Shares/ Principal	Value
U.S. Government Securities (27) – 15.5% of net assets at value				
U.S. Treasury Bill — due date 01/23/14	(M)	$18,999,765	$19,000,000	$18,999,810
Total Investments in U.S. Government Securities (cost: $18,999,765)				$18,999,810
Total Investments (cost: $134,929,558)				$112,899,269

	Method of Valuation (1)	Number of Contracts	Value
Written Call Options (22) – (0.1)% of net assets at value			
Solazyme, Inc. — Strike Price $12.50, March 22, 2014	(M)	1,500	$103,500
Total Written Call Options (Premiums Received $112,382)			$(103,500)

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

29

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2013

(Unaudited)

Notes to Consolidated Schedule of Investments

(1) See "Footnote to Consolidated Schedule of Investments" on page 32 for a description of the "Valuation Procedures."

(2) We classify "Energy" companies as those that seek to improve performance, productivity or efficiency, and to reduce environmental impact, waste, cost, energy consumption or raw materials. We classify "Electronics" companies as those that address problems in electronics-related industries, including semiconductors. We classify "Life Sciences" companies as those that address problems in life sciences-related industries, including biotechnology, agriculture, advanced materials and chemicals, healthcare, bioprocessing, water, industrial biotechnology, food, nutrition and energy.

(3) Investments in unaffiliated companies consist of investments in which we own less than five percent of the voting shares of the portfolio company. Investments in non-controlled affiliated companies consist of investments in which we own five percent or more, but less than 25 percent, of the voting shares of the portfolio company, or where we hold one or more seats on the portfolio company’s Board of Directors but do not control the company. Investments in controlled affiliated companies consist of investments in which we own 25 percent or more of the voting shares of the portfolio company or otherwise control the company.

(4) The aggregate cost for federal income tax purposes of investments in unaffiliated privately held companies is $29,277,213. The gross unrealized appreciation based on the tax cost for these securities is $6,909,761. The gross unrealized depreciation based on the tax cost for these securities is $6,987,410.

(5) All or a portion of the investments or instruments are pledged as collateral under our loan facility.

(6) The aggregate cost for federal income tax purposes of investments in unaffiliated rights to milestone payments is $3,291,750. The gross unrealized appreciation based on the tax cost for these securities is $197,683. The gross unrealized depreciation based on the tax cost for these securities is $0.

(7) The aggregate cost for federal income tax purposes of investments in unaffiliated publicly traded companies is $2,451,410. The gross unrealized appreciation based on the tax cost for these securities is $3,119,386. The gross unrealized depreciation based on the tax cost for these securities is $0.

(8) We are subject to legal restrictions on the sale of our investment(s) in this company.

(9) These investments are development-stage companies. A development-stage company is defined as a company that is devoting substantially all of its efforts to establishing a new business, and either it has not yet commenced its planned principal operations, or it has commenced such operations but has not realized significant revenue from them.

(10) Represents a non-income producing security. Investments that have not paid dividends or interest within the last 12 months are considered to be non-income producing.

(11) Cobalt Technologies, Inc., also does business as Cobalt Biofuels.

(12) With our investments in convertible bridge notes issued by Ensemble Therapeutics Corporation, we received warrants to purchase a number of shares of the class of stock sold in the next financing of Ensemble Therapeutics Corporation equal to $260,989 divided by the price per share of the class of stock sold in the next financing of Ensemble Therapeutics Corporation. The ability to exercise these warrants is, therefore, contingent on Ensemble Therapeutics Corporation completing successfully a subsequent round of financing. These warrants shall expire and no longer be exercisable on dates ranging from September 10, 2015, through July 8, 2020. The cost basis of these warrants is $157.

The accompanying unaudited notes are an integral part of this consolidated schedule.

HARRIS & HARRIS GROUP, INC.

CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2013

(Unaudited)

(13) With our investment in the Mersana Therapeutics, Inc., Series A-1 financing, we received a warrant to purchase 277,760 shares of Series A-2 Convertible Preferred Stock. The ability to exercise the warrant is contingent upon Mersana's achievement of certain milestones. Mersana has not achieved those milestones as of December 31, 2013, and, therefore, this warrant is a contingent asset as of that date. The warrant will expire on July 27, 2022.

(14) As part of a loan the Company made to Molecular Imprints in the second quarter of 2011, we received a liquidation preference payable upon a sale of the company equal to three times the principal of the loan, or $4,044,450. This preference is senior to the preferences of the outstanding preferred stock. While the loan has since been repaid, this liquidation preference remains outstanding as of December 31, 2013.

(15) On February 13, 2014, Molecular Imprints, Inc., announced that it had signed an agreement to sell its semiconductor lithography equipment business to Canon, Inc. See "Note 13. Subsequent Events" in the 2013 Annual Report on Form 10-K.

(16) OHSO Clean, Inc. also does business as CleanWell Company.

(17) A portion of this security is held in connection with written call option contracts: 150,000 shares, having a fair value of $1,633,500, have been pledged to brokers.

(18) The aggregate cost for federal income tax purposes of investments in non-controlled affiliated privately held companies is $71,843,448. The gross unrealized appreciation based on the tax cost for these securities is $10,212,841. The gross unrealized depreciation based on the tax cost for these securities is $27,769,249.

(19) Adesto Technologies Corporation's Series E shares have certain rights and preferences in a sale or IPO that are not ascribed to the other classes of stock.

(20) On January 29, 2013, AgInnovation, LLC, changed its name to AgBiome, LLC.

(21) On February 27, 2014, the board of directors of Contour Energy Systems, Inc., adopted a plan of complete liquidation and dissolution. See "Note 13. Subsequent Events" in the 2013 Annual Report on Form 10-K.

(22)

D-Wave Systems, Inc., is located and is doing business primarily in Canada. We invested in D-Wave Systems, Inc., through Parallel Universes, Inc., a Delaware company. Our investment is denominated in Canadian dollars and is subject to foreign currency translation. See "Note 2. Summary of Significant Accounting Policies" in the 2013 Annual Report on Form 10-K.

(23) Initial investment was made in 2013.

(24) On January 21, 2014, substantially all of Kovio's assets were sold to Thin Film Electronics ASA. See "Note 13. Subsequent Events" in the 2013 Annual Report on Form 10-K.

(25) The aggregate cost for federal income tax purposes of investments in controlled affiliated companies is $9,065,972. The gross unrealized appreciation based on the tax cost for these securities is $0. The gross unrealized depreciation based on the tax cost for these securities is $7,713,346.

(26) On October 31, 2013, Ancora sold a substantial portion of its assets, including the use of its corporate name, to Corden Pharma International US, Inc. ("Corden"). The remaining assets formed a new company, SynGlyco, Inc., of which we continue to own shares. SynGlyco may receive future royalty payments based upon certain sales targets and other terms of the Corden acquisition.

(27) The aggregate cost for federal income tax purposes of our U.S. government securities is $18,999,765. The gross unrealized appreciation on the tax cost for these securities is $45. The gross unrealized depreciation on the tax cost of these securities is $0.

The accompanying unaudited notes are an integral part of this consolidated schedule.

HARRIS & HARRIS GROUP, INC.

FOOTNOTE TO CONSOLIDATED SCHEDULE OF INVESTMENTS

VALUATION PROCEDURES

I. Determination of Net Asset Value

The 1940 Act requires periodic valuation of each investment in the portfolio of the Company to determine its net asset value. Under the 1940 Act, unrestricted securities with readily available market quotations are to be valued at the current market value; all other assets must be valued at "fair value" as determined in good faith by or under the direction of the Board of Directors.

The Board of Directors is also responsible for (1) determining overall valuation guidelines and (2) ensuring that the investments of the Company are valued within the prescribed guidelines.

The Valuation Committee, comprised of all of the independent Board members, is responsible for determining the valuation of the Company’s assets within the guidelines established by the Board of Directors. The Valuation Committee receives information and recommendations from management. An independent valuation firm also reviews select portfolio company valuations. The independent valuation firm does not provide proposed valuations.

The fair values assigned to these investments are based on available information and do not necessarily represent amounts that might ultimately be realized when that investment is sold, as such amounts depend on future circumstances and cannot reasonably be determined until the individual investments are actually liquidated or become readily marketable.

The Deal Team meets at the end of each quarter to discuss portfolio companies and propose fair valuations for all private securities. The Valuation Committee book is prepared with the use of data from primary sources whenever reasonably practicable. Proposed valuations for each portfolio company are communicated to the Valuation Committee in the Valuation Committee book and at the Valuation Committee meeting after the end of each quarter. The Valuation Committee determines the fair value of each private security and publicly traded securities without reliable market quotations. All valuations are then reported to the full Board of Directors along with the Chief Financial Officer’s calculation of net asset value.

II. Approaches to Determining Fair Value

Accounting Standards Codification Topic 820, "Fair Value Measurements and Disclosures," ("ASC 820") defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). It applies fair value terminology to all valuations whereas the 1940 Act applies market value terminology to readily marketable assets and fair value terminology to other assets.

The main approaches to measuring fair value utilized are the market approach and the income approach.

- Market Approach (M): The market approach may use quantitative inputs such as prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities and the values of market multiples derived from a set of comparable companies. The market approach may also use qualitative inputs such as progress toward milestones, the long-term potential of the business, current and future financing requirements and the rights and preferences of certain securities versus those of other securities. The selection of the relevant inputs used to derive value under the market approach requires judgment considering factors specific to the significance and relevance of each input to deriving value.

- Income Approach (I): The income approach uses valuation techniques to convert future amounts (for example, cash flows or earnings) to a single present value amount (discounted). The measurement is based on the value indicated by current market expectations about those future amounts. Those valuation techniques include present value techniques; option-pricing models, such as the Black-Scholes-Merton formula (a closed-form model) and a binomial model (a lattice model), which incorporate present value techniques; and the multi-period excess earnings method, which is used to measure the fair value of certain assets.

- Hybrid Approach (H): The hybrid approach uses elements of both the market approach and the income approach. The hybrid approach calculates values using the market and income approach, individually. The resulting values are then distributed among the share classes based on probability of exit outcomes.

ASC Topic 820 classifies the inputs used to measure fair value by these approaches into the following hierarchy:

- Level 1: Unadjusted quoted prices in active markets for identical assets or liabilities.

- Level 2: Quoted prices in active markets for similar assets or liabilities, or quoted prices for identical or similar assets or liabilities in markets that are not active, or inputs other than quoted prices 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 our own assumptions that market participants would use to price the asset or liability based upon the best available information.

Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement and are not necessarily an indication of risks associated with the investment.

III. Investment Categories

The Company’s investments can be classified into five broad categories for valuation purposes:

- Equity-related securities;
- Long-term fixed-income securities;
- Short-term fixed-income securities;
- Investments in intellectual property, patents, research and development in technology or product development; and
- All other securities.

The Company applies the methods for determining fair value discussed above to the valuation of investments in each of these five broad categories as follows:

A. EQUITY-RELATED SECURITIES

Equity-related securities, including options or warrants, are fair valued using the market or income approaches. The following factors may be considered when the market approach is used to fair value these types of securities:

§ Readily available public market quotations;

§ The cost of the Company’s investment;

§ Transactions in a company's securities or unconditional firm offers by responsible parties as a factor in determining valuation;

§ The financial condition and operating results of the company;

§ The company's progress towards milestones;

§ The long-term potential of the business and technology of the company;

§ The values of similar securities issued by companies in similar businesses;

§ Multiples to revenue, net income or EBITDA that similar securities issued by companies in similar businesses receive;

§ The proportion of the company's securities we own and the nature of any rights to require the company to register restricted securities under applicable securities laws; and

§ The rights and preferences of the class of securities we own as compared with other classes of securities the portfolio company has issued.

When the income approach is used to value warrants, the Company uses the Black-Scholes-Merton formula.

B. LONG-TERM FIXED-INCOME SECURITIES

1. **Readily Marketable.** Long-term fixed-income securities for which market quotations are readily available are valued using the most recent bid quotations when available.

2. **Not Readily Marketable**. Long-term fixed-income securities for which market quotations are not readily available are fair valued using the income approach. The factors that may be considered when valuing these types of securities by the income approach include:

- Credit quality;
- Interest rate analysis;
- Quotations from broker-dealers;
- Prices from independent pricing services that the Board believes are reasonably reliable; and
- Reasonable price discovery procedures and data from other sources.

C. SHORT-TERM FIXED-INCOME SECURITIES

Short-term fixed-income securities are valued in the same manner as long-term fixed-income securities until the remaining maturity is 60 days or less, after which time such securities may be valued at amortized cost if there is no concern over payment at maturity.

D. INVESTMENTS IN INTELLECTUAL PROPERTY, PATENTS, RESEARCH AND DEVELOPMENT IN TECHNOLOGY OR PRODUCT DEVELOPMENT

Such investments are fair valued using the market approach. The Company may consider factors specific to these types of investments when using the market approach including:

- The cost of the Company's investment;

- Investments in the same or substantially similar intellectual property or patents or research and development in technology or product development or offers by responsible third parties;
- The results of research and development;
- Product development and milestone progress;
- Commercial prospects;
- Term of patent;
- Projected markets; and
- Other subjective factors.

35

E. ALL OTHER SECURITIES

All other securities are reported at fair value as determined in good faith by the Valuation Committee using the approaches for determining valuation as described above.

For all other securities, the reported values shall reflect the Valuation Committee's judgment of fair values as of the valuation date using the outlined basic approaches of valuation discussed in Section II. They do not necessarily represent an amount of money that would be realized if we had to sell such assets in an immediate liquidation. Thus, valuations as of any particular date are not necessarily indicative of amounts that we may ultimately realize as a result of future sales or other dispositions of investments we hold.

IV. Frequency of Valuation

The Valuation Committee shall value the Company’s investment assets (i) as of the end of each calendar quarter at the time sufficiently far in advance of filing of the Company’s reports on Form 10-Q and Form 10-K to enable preparation thereof, (ii) as of within 48 hours of pricing any common stock of the Company by the Company (exclusive of Sundays and holidays) unless the proposed sale price is at least 200 percent of any reasonable net asset value of such shares, and (iii) as of any other time requested by the Board of Directors.

V. Regular Review

The Chief Operating Officer and Chief Financial Officer shall review these Valuation Procedures on an annual basis to determine the continued appropriateness and accuracy of the methodologies used in valuing the Company’s investment assets, and will report any proposed modifications to these Valuation Procedures to the Board of Directors for consideration and approval.

The Chief Executive Officer, the Chief Operating Officer and the individuals responsible for preparing the Valuation Committee book shall meet quarterly before each Valuation Committee meeting to review the methodologies for the valuation of each security, and will highlight any changes to the Valuation Committee.

VI. Other Assets

Non-investment assets, such as fixtures and equipment, shall be valued using the cost approach less accumulated depreciation at rates determined by management and reviewed by the Audit Committee. Valuation of such assets is not the responsibility of the Valuation Committee.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1. THE COMPANY

Harris & Harris Group, Inc. (the "Company," "us," "our" and "we"), is a non-diversified management investment company operating as a business development company ("BDC") under the Investment Company Act of 1940 (the "1940 Act") that specializes in making investments in companies commercializing and integrating products enabled by nanotechnology and microsystems. We operate as an internally managed investment company whereby our officers and employees, under the general supervision of our Board of Directors, conduct our operations.

H&H Ventures Management, Inc.SM ("Ventures") is a 100 percent wholly owned subsidiary of the Company. Ventures is taxed under Subchapter C (a "C Corporation") of the Internal Revenue Code of 1986 (the "Code"). Harris Partners I, L.P, is a limited partnership and, from time to time, may be used to hold certain interests in portfolio companies. The partners of Harris Partners I, L.P., are Ventures (sole general partner) and the Company (sole limited partner). Ventures pays taxes on income generated by its operations as well as on any non-passive investment income generated by Harris Partners I, L.P. For the period ended June 30, 2014, there was no non-passive investment income generated by Harris Partners I, L.P. Ventures, as the sole general partner, consolidates Harris Partners I, L.P. for financial reporting purposes. The Company consolidates its wholly owned subsidiary, Ventures, for financial reporting purposes.

NOTE 2. INTERIM FINANCIAL STATEMENTS

Our interim financial statements have been prepared in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X and in conformity with accounting principles generally accepted in the United States of America ("GAAP") applicable to interim financial information. Accordingly, they do not include all information and disclosures necessary for a fair statement of our financial position, results of operations and cash flows in conformity with GAAP for annual financial statements. In the opinion of management, these financial statements reflect all adjustments, consisting of valuation adjustments and normal recurring accruals, necessary for a fair statement of our financial position, results of operations and cash flows for such periods. The results of operations for any interim period are not necessarily indicative of the results for the full year. These financial statements should be read in conjunction with the financial statements and notes thereto contained in our Annual Report on Form 10-K for the fiscal year ended December 31, 2013.

NOTE 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The following is a summary of significant accounting policies followed in the preparation of the consolidated financial statements:

Principles of Consolidation. The consolidated financial statements have been prepared in accordance with GAAP and include the accounts of the Company and its wholly owned subsidiary. In accordance with GAAP and Regulation S-X, the Company may only consolidate its interests in investment company subsidiaries and controlled operating companies whose business consists of providing services to the Company. Our wholly owned subsidiary, Ventures, is a controlled operating company that provides services to us and is, therefore, consolidated. All significant inter-company accounts and transactions have been eliminated in consolidation. Certain prior period amounts have been reclassified to conform to the current period presentation.

Use of Estimates. The preparation of the consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and contingent assets and liabilities and the reported amounts of revenues and expenses. Actual results could differ from these estimates, and the differences could be material. The most significant estimates relate to the fair valuations of our investments.

Portfolio Investment Valuations. Investments are stated at "value" as defined in the 1940 Act and in the applicable regulations of the Securities and Exchange Commission ("SEC") and in accordance with GAAP. Value, as defined in Section 2(a)(41) of the 1940 Act, is (i) the market price for those securities for which a market quotation is readily available and (ii) the fair value as determined in good faith by, or under the direction of, the Board of Directors for all other assets. (See "Valuation Procedures" in the "Footnote to Consolidated Schedule of Investments.") As of June 30, 2014, our financial statements include privately held investments fair valued at $93,009,936. The fair values of our privately held investments and warrants of Champions Oncology, Inc., a publicly traded company, were determined in good faith by, or under the direction of, the Board of Directors. Upon sale of investments, the values that are ultimately realized may be different from what is presently estimated. The difference could be material.

Cash. Cash includes demand deposits. Cash is carried at cost, which approximates fair value.

Unaffiliated Rights to Milestone Payments. At June 30, 2014, and December 31, 2013, the outstanding potential milestone payments from Amgen, Inc.’s acquisition of BioVex Group, Inc., were valued at $3,496,847 and $3,489,433, respectively. The milestone payments are derivatives and valued using the probability-adjusted, present value of proceeds from future payments that would be due upon successful completion of certain regulatory and sales milestones. If all remaining milestones are met, we would receive $9,526,393. There can be no assurance as to how much of this amount we will ultimately realize or when it will be realized, if at all. At June 30, 2014, the outstanding potential milestone payments from Canon, Inc.'s acquisition of Molecular Imprints, Inc., were valued at $630,257. If all remaining milestones are met, we would receive $1,735,582. There can be no assurance as to how much of this amount we will ultimately realize or when it will be realized, if at all. At June 30, 2014, and December 31, 2013, the outstanding potential milestone payments from Laird Technologies, Inc.’s acquisition of Nextreme Thermal Solutions, Inc., were valued at $0.

Receivable from Sales of Investments. At June 30, 2014, we had no receivables from sales of investments. At December 31, 2013, we had a receivable totaling $448,886 from the sales of 43,073 shares of Solazyme, Inc., which settled on January 2 and January 6, 2014, and 2,075 shares of Champions Oncology, Inc., which settled on January 3, 2014.

Funds Held in Escrow from Sale of Investment. At June 30, 2014, and December 31, 2013, there were funds held in escrow fair valued at $1,447,933 and $1,786,390, respectively, relating to the sales of Xradia, Inc., to Carl Zeiss AG and Molecular Imprints, Inc., to Canon, Inc. Funds held in escrow are valued using certain discounts applied to the amounts withheld. Funds held in escrow totaling $1,235,312 and $1,139,515 from the Xradia transaction were released in January and July of 2014, respectively. Funds held in escrow valued at $308,418 from the Molecular Imprints transaction are expected to be released in April of 2016 and April of 2017, net of any settlement of any indemnity claims and expenses related to the transaction. If the funds held in escrow for this transaction are released in full, we would receive $625,000 and realize a gain of $316,582.

Prepaid Expenses. We include prepaid insurance premiums and deferred financing charges in "Prepaid expenses." Prepaid insurance premiums are recognized over the term of the insurance contract and are included in "Insurance expense" in the Consolidated Statements of Operations. Deferred financing charges consist of fees and expenses paid in connection with the closing of loan facilities and are capitalized at the time of payment. Deferred financing charges are amortized over the term of the loan facility discussed in "Note 5. Debt." Amortization of the financing charges is included in "Interest and other debt expense" in the Consolidated Statements of Operations.

Property and Equipment. Property and equipment are included in "Other assets" and are carried at $220,754 and $246,138 at June 30, 2014, and December 31, 2013, respectively, representing cost, less accumulated depreciation of $394,678 and $375,600, respectively. Depreciation is provided using the straight-line method over the estimated useful lives of the property and equipment. We estimate the useful lives to be five to ten years for furniture and fixtures, three years for computer equipment, and the lesser of ten years or the remaining life of the lease for leasehold improvements. All of our fixed assets are pledged as collateral under the Company's four-year $20,000,000 Multi-Draw Term Loan Facility Credit Agreement, by and among the Company, as borrower, Orix Corporate Capital, Inc., as administrative agent and lender and the other lenders party thereto from time to time (the "Loan Facility").

Post Retirement Plan Liabilities. The Company provides a Retiree Medical Benefit Plan for employees who meet certain eligibility requirements. Until it was terminated on May 5, 2011, the Company also provided an Executive Mandatory Retirement Benefit Plan for certain individuals employed by us in a bona fide executive or high policy-making position. The net periodic postretirement benefit cost for the year is determined as the sum of service cost for the year and interest on the accumulated postretirement benefit obligation. Unrecognized actuarial gains and losses are recognized as net periodic benefit cost pursuant to the Company's historical accounting policy. The impact of plan amendments are amortized over the service period as a component of "Accumulated other comprehensive income."

Interest Income Recognition. Interest income, including amortization of premium and accretion of discount, is recorded on an accrual basis. When accrued interest is determined to not be recoverable, the Company ceases accruing interest and writes off any previously accrued interest. Securities are deemed to be non-income producing if, on their last interest or dividend date, no cash was paid or no cash or in-kind dividends were declared. These write-offs are reversed through interest income. During the three months and six months ended June 30, 2014, the Company earned $71,029 and $144,592, respectively, in interest on U.S. government securities, senior secured debt, participation agreements, subordinated secured debt, non-convertible promissory notes and interest-bearing accounts. During the three months and six months ended June 30, 2013, the Company earned $80,608 and $175,817, respectively, in interest on U.S. government securities, senior secured debt, participation agreements, subordinated secured debt, non-convertible promissory notes and interest-bearing accounts. During the three months and six months ended June 30, 2014, the Company recorded, on a net basis, $62,806 and $135,534, respectively, of bridge note interest. The total for the six months ended June 30, 2014, includes a partial write-off of previously accrued bridge note interest of $1,392. During the three months and six months ended June 30, 2013, the Company recorded $79,355 and $139,236, respectively, of bridge note interest.

Loan Fees. Loan fees received in connection with our venture debt investments are deferred. The unearned fee income is accreted into income based on the effective interest method over the life of the investment. Total loan fees accreted into investment income were $16,757 and $32,262 for the three months and six months ended June 30, 2014, respectively. Total loan fees accreted into investment income were $15,140 and $27,467 for the three months and six months ended June 30, 2013, respectively.

Call Options. The Company writes covered call options on publicly traded securities with the intention of earning option premiums. Option premiums may increase the Company's realized gains and, therefore, may help increase distributable income, but may limit the realized gains on the security. When a Company writes (sells) an option, an amount equal to the premium received by the Company is recorded in the Consolidated Statements of Assets and Liabilities as a liability. The amount of the liability is subsequently marked-to-market to reflect the current market value of the option written. When an option expires, the Company realizes a gain on the option to the extent of the premiums received. Premiums received from writing options that are exercised or closed are added to the proceeds or offset against the amount paid on the transaction to determine the realized gain or loss. At June 30, 2014, and December 31, 2013, the Company had 50,000 and 150,000 shares, respectively, of Solazyme, Inc., covered by call option contracts. In the event these contracts are exercised, the Company would be required to deliver those shares to the counterparty.

Stock-Based Compensation. The Company has a stock-based employee compensation plan. The Company accounts for the Amended and Restated Harris & Harris Group, Inc. 2012 Equity Incentive Plan (the "Stock Plan") by determining the fair value of all share-based payments to employees, including the fair value of grants of employee stock options and restricted stock awards, and records these amounts as an expense in the Consolidated Statements of Operations over the vesting period with a corresponding increase to our additional paid-in capital. At June 30, 2014, and December 31, 2013, the increase to our operating expenses was offset by the increase to our additional paid-in capital, resulting in no net impact to our net asset value. Additionally, the Company does not record the potential tax benefits associated with the expensing of stock options or restricted stock because the Company currently intends to qualify as a regulated investment company ("RIC") under Subchapter M of the Code, and the deduction attributable to such expensing, therefore, is unlikely to provide any additional tax savings. The amount of non-cash, stock-based compensation expense recognized in the Consolidated Statements of Operations is based on the fair value of the awards the Company expects to vest, recognized over the vesting period on a straight-line basis for each award, and adjusted for actual awards vested and pre-vesting forfeitures. The forfeiture rate is estimated at the time of grant and revised, if necessary, in subsequent periods if the actual forfeiture rate differs from the estimated rate and is accounted for in the current period and prospectively. See "Note 9. Stock-Based Compensation" for further discussion.

Rent expense. Our lease at 1450 Broadway, New York, New York, commenced on January 21, 2010. The lease expires on December 31, 2019. The base rent is $36 per square foot with a 2.5 percent increase per year over the 10 years of the lease, subject to a full abatement of rent for four months and a rent credit for six months throughout the lease term. Certain leasehold improvements were also paid for on our behalf by the landlord, the cost of which is accounted for as property and equipment and "Deferred rent" in the accompanying Consolidated Statements of Assets and Liabilities. These leasehold improvements are depreciated over the lease term. We also lease office space in California and North Carolina. We apply these rent abatements, credits, escalations and landlord payments on a straight-line basis in the determination of rent expense over the lease term.

40

Realized Gain or Loss and Unrealized Appreciation or Depreciation of Portfolio Investments. Realized gain or loss is recognized when an investment is disposed of and is computed as the difference between the Company's cost basis in the investment at the disposition date and the net proceeds received from such disposition. Realized gains and losses on investment transactions are determined by specific identification. Unrealized appreciation or depreciation is computed as the difference between the fair value of the investment and the cost basis of such investment.

Income Taxes. As we intend to qualify as a RIC under Subchapter M of the Code, the Company does not accrue for income taxes. The Company has capital loss carryforwards that can be used to offset net realized capital gains. The Company recognizes interest and penalties in income tax expense. We pay federal, state and local income taxes on behalf of our wholly owned subsidiary, Ventures, which is a C corporation. See "Note 10. Income Taxes" for further discussion.

Foreign Currency Translation. The accounting records of the Company are maintained in U.S. dollars. All assets and liabilities denominated in foreign currencies are translated into U.S. dollars based on the rate of exchange of such currencies against U.S. dollars on the date of valuation. The Company does not isolate the portion of the results of operations that arises from changes in foreign currency rates on investments held on its Consolidated Statements of Operations. For the three months ended June 30, 2014, included in the net decrease in unrealized depreciation on investments was an unrealized gain of $206,811 resulting from foreign currency translation. For the six months ended June 30, 2014, included in the net decrease in unrealized depreciation on investments was an unrealized loss of $9,162 resulting from foreign currency translation. For the three months and six months ended June 30, 2013, included in the net decrease in unrealized depreciation on investments was an unrealized loss of $197,041 and $310,047, respectively, resulting from foreign currency translation.

Securities Transactions. Securities transactions are accounted for on the date the transaction for the purchase or sale of the securities is entered into by the Company (i.e., trade date).

Concentration of Credit Risk. The Company places its cash and cash equivalents with financial institutions and, at times, cash held in depository accounts may exceed the Federal Deposit Insurance Corporation insured limit.

Recent Accounting Pronouncements. In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers (Topic 606)," which is the new comprehensive revenue recognition standard that will supersede all existing revenue recognition guidance under GAAP. The standard's core principle is that a company will recognize revenue when it transfers promised goods or services to a customer in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. This ASU is effective for annual and interim periods beginning on or after December 15, 2016, and early adoption is not permitted. Entities will have the option of using either a full retrospective approach or a modified approach to adopt the guidance in the ASU. The Company is currently evaluating the impact of adopting this guidance.

In June 2014, the FASB issued ASU 2014-12, "Compensation - Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could be Achieved after the Requisite Service Period." This ASU provides more explicit guidance for treating share-based payment awards that require a specific performance target that affects vesting and that could be achieved after the requisite service period as a performance condition. The new guidance is effective for annual and interim reporting periods beginning after December 15, 2015. The Company does not expect the adoption of this guidance to have a material impact on the consolidated financial statements.

NOTE 4. BUSINESS RISKS AND UNCERTAINTIES

We invest primarily in privately held companies, the securities of which are inherently illiquid. We also have investments in small publicly traded companies. Although these companies are publicly traded, their stock may not trade at high volumes and prices can be volatile, which may restrict our ability to sell our positions. These privately held and publicly traded businesses tend to not have attained profitability, and many of these businesses also lack management depth and have limited or no history of operations. Because of the speculative nature of our investments and the lack of a liquid market for and restrictions on transfers of privately held investments, there is greater risk of loss relative to traditional marketable investment securities.

We do not choose investments based on a strategy of diversification. We also do not rebalance the portfolio should one of our portfolio companies increase in value substantially relative to the rest of the portfolio. Therefore, the value of our portfolio may be more vulnerable to microeconomic events affecting a single sector, industry or portfolio company and to general macroeconomic events that may be unrelated to our portfolio companies. These factors may subject the value of our portfolio to greater volatility than a company that follows a diversification strategy. As of June 30, 2014, and December 31, 2013, our largest 10 investments by value accounted for approximately 79 percent and 75 percent, respectively, of the value of our equity-focused venture capital portfolio, excluding the rights to milestone payments. Our largest three investments, by value, Adesto Technologies Corporation, HZO, Inc., and Metabolon, Inc., accounted for approximately 16 percent, 12 percent and 12 percent, respectively, of our equity-focused venture capital portfolio as of June 30, 2014. Adesto Technologies, HZO and Metabolon are privately held portfolio companies. As of December 31, 2013, our largest three investments, by value, Adesto Technologies Corporation, Metabolon, Inc., and Molecular Imprints, Inc., accounted for approximately 17 percent, 12 percent and 9 percent, respectively, of our equity-focused venture capital portfolio.

Approximately 97 percent of the portion of our equity-focused venture capital portfolio that was fair valued was comprised of securities of 26 privately held companies and warrants of one publicly traded company. Because there is typically no public or readily ascertainable market for our interests in the small privately held companies in which we invest, the valuation of the securities in that portion of our portfolio is determined in good faith by our Valuation Committee, which is comprised of all of the independent members of our Board of Directors. The values are determined in accordance with our Valuation Procedures and are subject to significant estimates and judgments. The fair value of the securities in our portfolio may differ significantly from the values that would be placed on these securities if a ready market for the securities existed. Any changes in valuation are recorded in our Consolidated Statements of Operations as "Net decrease (increase) in unrealized depreciation on investments." Changes in valuation of any of our investments in privately held companies from one period to another may be significant.

NOTE 5. DEBT

On September 30, 2013, the Company terminated the $10,000,000 Revolving Loan Agreement by and between the Company and TD Bank, N.A., dated February 24, 2011. At the date of termination, there was no principal outstanding under this credit facility, and no termination fees were incurred in connection with ending this credit facility.

On September 30, 2013, the Company entered into a four-year $20,000,000 Multi-Draw Term Loan Facility Credit Agreement, by and among the Company, as borrower, Orix Corporate Capital, Inc., as administrative agent and lender and the other lenders party thereto from time to time (the "Loan Facility") that may be used by the Company to fund investments in portfolio companies. The Loan Facility replaces the Company's prior credit facility with TD Bank, NA. The Loan Facility, among other things, matures on September 30, 2017, and bears interest at 10 percent per annum in cash. The Company has the option to have interest accrue at a rate of 13.5 percent per annum if the Company decides not to pay interest in cash monthly. The Company currently plans to pay interest in cash if and when any borrowings are outstanding. The Loan Facility also requires payment of a draw fee on each borrowing equal to 1.0 percent of such borrowing and an unused commitment fee of 1.0 percent per annum. Fee payments under the Loan Facility are made quarterly in arrears. The Company may prepay the loans or reduce the aggregate commitments under the Loan Facility at any time prior to the maturity date, as long as certain conditions are met, including payment of required prepayment or termination fees. The Loan Facility is secured by all of the assets of the Company and its wholly owned subsidiaries, subject to certain customary exclusions. The Loan Facility contains certain affirmative and negative covenants, including without limitation: (a) maintenance of certain minimum liquidity requirements; (b) maintenance of an eligible asset leverage ratio of not less than 4.0:1.0; (c) limitations on liens; (d) limitations on the incurrence of additional indebtedness; and (e) limitations on structural changes, mergers and disposition of assets (other than in the normal course of our business activities).

At June 30, 2014, and December 31, 2013, the Company had no outstanding debt. The weighted average annual interest rate for the three months and six months ended June 30, 2014, was zero percent, exclusive of amortization of closing fees and other expenses. The weighted average debt outstanding for the three months and six months ended June 30, 2014, was $0. The remaining capacity under the Loan Facility was $20,000,000 at June 30, 2014. Fees and expenses of $700,000 related to establishing the Loan Facility have been deferred and included as "Prepaid expenses" as of June 30, 2014. These amounts are amortized over the term of the Loan Facility, and $87,440 was amortized in the six months ended June 30, 2014. At June 30, 2014, the Company was in compliance with all covenants required by the Loan Facility.

NOTE 6. FAIR VALUE OF INVESTMENTS

At June 30, 2014, our financial assets were categorized as follows in the fair value hierarchy:

		Fair Value Measurement at Reporting Date Using:		
Description	June 30, 2014	Unadjusted Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Privately Held Portfolio Companies:				
Preferred Stock	$ 82,918,390	$ 0	$ 0	$ 82,918,390
Bridge Notes	2,514,976	0	0	2,514,976
Warrants	921,633	0	0	921,633
Rights to Milestone Payments	4,127,104	0	0	4,127,104
Common Stock	546,767	0	0	546,767
Senior Secured Debt	1,305,901	0	0	1,305,901
Participation Agreement	675,165	0	0	675,165
Publicly Traded Portfolio Companies:				
Common Stock	$ 3,112,895	$ 3,112,895	$ 0	$ 0
Total Investments:	$ 96,122,831	$ 3,112,895	$ 0	$ 93,009,936
Funds Held in Escrow From Sales of Investments:	$ 1,447,933	$ 0	$ 0	$ 1,447,933
Total Financial Assets:	$ 97,570,764	$ 3,112,895	$ 0	$ 94,457,869
Liabilities:				
Written Call Options	$ 47,500	$ 47,500	$ 0	$ 0
Total Liabilities:	$ 47,500	$ 47,500	$ 0	$ 0

Significant Unobservable Inputs

The table below presents the valuation technique and quantitative information about the significant unobservable inputs utilized by the Company in the fair value measurements of Level 3 assets. Unobservable inputs are those inputs for which little or no market data exists and, therefore, require an entity to develop its own assumptions.

	Fair Value at June 30, 2014	Valuation Technique(s)	Unobservable Input	Range (Weighted Average[a])
Preferred Stock	$3,749,795	Hybrid Approach	Private Offering Price Probability of Exit Outcomes Probability of Achieving Milestones	$1.38 ($1.38) 25% - 75% ([b]) 26% - 80% ([b])
Preferred Stock	0	Income Approach	Probability of Exit Outcomes Probability of Achieving Milestones	0% - 100% ([b]) 0% - 100% ([b])
Preferred Stock	79,168,595	Market Approach	Private Offering Price Non-Performance Risk Revenue Multiples Illiquidity Discounts Probability of Exit Outcomes	$0.10 - $3.91 ($1.74) 0% - 94% (2.1%) 1.26 - 8.80 (2.94) 20% - 30% (23.1%) 0% - 100% ([b])
Bridge Notes	1,293,877	Income Approach	Private Offering Price	$1.00 ($1.00)
	1,221,099	Market Approach	Non-Performance Risk	0% (0%)
Common Stock	546,767	Market Approach	Private Offering Price Non-Performance Risk	$0.001 - $1.076 ($0.92) 0% (0%)
Warrants	921,633	Black-Sholes-Merton Model	Stock Price Volatility Expected Term	$0.00 - $2.76 ($1.17) 64.3% - 107% (104%) 0.16 - 9.60 Years (4.0)
Rights to Milestone Payments	4,127,104	Probability Weighted Discounted Cash Flow	Probability of Achieving Independent Milestones Probability of Achieving Dependent Milestones	0% - 80% ([b]) 0% - 30% ([b])
Participation Agreements[c]	675,165	Income Approach	Warrant Adjusted Effective Yield Effective Yield Non-Performance Risk Participation Payment Risk Stock Price Volatility	22.8% (22.8%) 22.8% (22.8%) 0% (0%) 0% (0%) $0.09 - $0.50 ($0.46) 107% (107%)

			Expected Term	3.22 - 7.75 Years (3.89)
Senior Secured Debt	1,305,901	Income Approach	Effective Yield Non-Performance Risk	15.8% (6.7%) 0% (0%)
Funds Held in Escrow From Sales of Investments	1,447,933		Escrow Discounts	0 - 50% (11%)
Total	**$94,457,869**			

(a) Weighted average based on fair value at June 30, 2014.

(b) Weighted average has not been disclosed owing to the wide range of possible values.

(c) In connection with our investments in participation agreements in GEO Semiconductor, Inc., and OHSO Clean, Inc., we received warrants to purchase stock. See "Warrants" for a discussion of the valuation methodology used.

Valuation Methodologies and Inputs for Level 3 Assets

The following sections describe the valuation techniques and significant unobservable inputs used to measure Level 3 assets.

45

Preferred Stock, Bridge Notes and Common Stock

Preferred stock, bridge notes and common stock are valued by either a market, income or hybrid approach using internal models with inputs, most of which are not market observable. Common inputs for valuing Level 3 preferred stock, bridge note and private common stock investments include: prices from recently executed private transactions in a company’s securities or unconditional firm offers, revenue multiples of comparable publicly traded companies, M&A transactions consummated by comparable companies, discounts for lack of marketability, rights and preferences of the class of securities we own as compared with other classes of securities the portfolio company has issued, particularly related to potential liquidity scenarios of an IPO or an acquisition transaction, and management’s best estimate of risk attributable to non-performance risk. Certain securities are valued using the present value of future cash flows. We define non-performance risk as the risk that the price per share (or implied valuation of a portfolio company) or the effective yield of a debt security of a portfolio company, as applicable, does not appropriately represent the risk that a portfolio company with negative cash flow will be: (a) unable to raise capital, will need to be shut down and will not return our invested capital; or (b) able to raise capital, but at a valuation significantly lower than the implied post-money valuation of the last round of financing. We assess non-performance risk for each private portfolio company quarterly. Our assessment of non-performance risk typically includes an evaluation of the financial condition and operating results of the company, the company's progress towards milestones, and the long-term potential of the business and technology of the company and how this potential may or may not affect the value of the shares owned by us. An increase to the non-performance risk or a decrease in the private offering price of a future round of financing from that of the most recent round would result in a lower fair value measurement and/or a change in the distribution of value among the classes of securities we own.

Bridge notes commonly contain terms that provide for the conversion of the full amount of principal, and sometimes interest, into shares of preferred stock at a defined price per share and/or the price per share of the next round of financing. The use of a discount for non-performance risk in the valuation of bridge notes would indicate the potential for conversion of only a portion of the principal, plus interest when applicable, into shares of preferred stock or the potential that a conversion event will not occur and that the likely outcome of a liquidation of assets would result in payment of less than the remaining principal outstanding of the note. An increase in non-performance risk would result in a lower fair value measurement.

Warrants

We use the Black-Scholes-Merton option-pricing model to determine the fair value of warrants held in our portfolio. Option pricing models, including the Black-Scholes-Merton model, require the use of subjective input assumptions, including expected volatility, expected life, expected dividend rate, and expected risk-free rate of return. In the Black-Scholes-Merton model, variations in the expected volatility or expected term assumptions have a significant impact on fair value. Because certain securities underlying the warrants in our portfolio are not publicly traded, many of the required input assumptions are more difficult to estimate than they would be if a public market for the underlying securities existed.

46

An input to the Black-Scholes-Merton option-pricing model is the value per share of the type of stock for which the warrant is exercisable as of the date of valuation. This input is derived according to the methodologies discussed in "Preferred Stock, Bridge Notes and Common Stock."

Rights to Milestone Payments

Rights to milestone payments are valued using a probability-weighted discounted cash flow model. As part of Amgen Inc.'s acquisition of our former portfolio company, BioVex Group, Inc., we are entitled to potential future milestone payments based upon the achievement of certain regulatory and sales milestones. We are also entitled to future milestone payments from Laird Technologies Inc.'s acquisition of our former portfolio company, Nextreme Thermal Solutions, Inc., and from Canon, Inc.'s acquisition of Molecular Imprints, Inc. We assign probabilities to the achievements of the various milestones. Milestones identified as independent milestones can be achieved irrespective of the achievement of other contractual milestones. Dependent milestones are those that can only be achieved after another, or series of other, milestones are achieved. The interest rates used in these models are observable inputs from sources such as the Federal Reserve published interest rates.

Participation Agreements and Senior Secured Debt

We invest in venture debt investments through participation agreements and senior secured debt. We value these securities using an income approach. The income approach uses valuation techniques to convert future amounts (for example, cash flows or earnings) to a single present value amount (discounted). The measurement is based on the value indicated by current market expectations about those future amounts. Common inputs for valuing Level 3 debt investments include: the effective yield of the debt investment or, in the case where we have received warrant coverage, the warrant-adjusted effective yield of the security, adjustments for changes in the yields of comparable publicly traded high-yield debt funds and risk-free interest rates and an assessment of non-performance risk. For those debt investments made through participation agreements, we include discounts for the risk of breach of the participation agreements. For venture debt investments, an increase in yields would result in a lower fair value measurement. Furthermore, yields would decrease, and value would increase, if the company is exceeding targets and risk has been substantially reduced from the level of risk that existed at the time of investment. Yields would increase, and values would decrease, if the company is failing to meet its targets and risk has been increased from the level of risk that existed at the time of investment.

The following chart shows the components of change in the financial assets categorized as Level 3 for the three months ended June 30, 2014.

	Beginning Balance 4/1/2014	Total Realized Gains (Losses) Included in Changes in Net Assets	Transfers		Total Unrealized (Depreciation) Appreciation Included in Changes in Net Assets	Investments in Portfolio Companies, Interest on Bridge Notes, and Amortization of Loan Fees, Net	Disposals	Ending Balance 6/30/2014	Amount of T (Depreciatior Appreciation the Period Included in Changes in N Assets Attributable to the Change in Unrealized G or Losses Relati to Assets Still H at the Reporting Date
Preferred Stock	$70,633,956	$4,263,420	$1,897,462	1,2	$5,720,997	$6,889,016	$(6,486,461)	$82,918,390	$5,549,964
Bridge Notes	5,402,815	0	(3,653,987)	1	68,236	697,912	0	2,514,976	68,236
Common Stock	108,668	0	436,605	1	1,494	0	0	546,767	1,494
Warrants	740,070	0	65,250	1	72,946	43,367	0	921,633	72,946
Rights to Milestone Payments	3,491,600	0	629,670	1	5,834	0	0	4,127,104	5,834
Participation Agreements	757,797	0	0		(40,708)	1,276	(43,200)	675,165	(40,708)
Senior Secured Debt	1,466,451	0	0		(92,510)	15,481	(83,521)	1,305,901	(92,510)
	551,294	271,639	625,000	2	0	0	0	1,447,933	0

Funds Held in Escrow From Sales of Investments								
Total	$83,152,651	$4,535,059	$0	$5,736,289	$7,647,052	$(6,613,182)	$94,457,869	$(5,565,256)

[1] Transfers among asset classes are owing to conversions at financing events. These do not represent transfers in or out of Level 3.

[2] There was a $625,000 transfer from "Preferred Stock" into "Funds Held in Escrow From Sales of Investments" owing to the sale of Molecular Imprints, Inc., to Canon, Inc.

We elected to use the beginning of period values to recognize transfers in and out of Level 3 investments. For the three months ended June 30, 2014, there were no transfers out of Level 3.

48

The following chart shows the components of change in the financial assets categorized as Level 3 for the six months ended June 30, 2014.

	Beginning Balance 1/1/2014	Total Realized Gains (Losses) Included in Changes in Net Assets	Transfers	Total Unrealized (Depreciation) Appreciation Included in Changes in Net Assets	Investments in Portfolio Companies, Interest on Bridge Notes, and Amortization of Loan Fees, Net	Disposals	Ending Balance 6/30/2014	Amount o (Deprecia Appreciat the Period Included i Changes i Assets Attributab to the Change in Unrealize or Losses Re to Assets Sti at the Repor Date
Preferred Stock	$71,577,059	$(2,986,113)	$2,746,327 [1,2]	$10,226,545	$7,841,033	$(6,486,461)	$82,918,390	$2,805,97
Bridge Notes	6,044,114	(50,000)	(4,502,852)[1]	(1,124,325)	2,148,039	0	2,514,976	(1,174,3
Common Stock	108,668	0	436,605 [1]	1,494	0	0	546,767	1,494
Warrants	800,487	0	65,250 [1]	(45,038)	100,934	0	921,633	(45,038
Rights to Milestone Payments	3,489,433	0	629,670 [1]	8,001	0	0	4,127,104	8,001
Participation Agreements	777,195	0	0	(18,231)	2,601	(86,400)	675,165	(18,231
Senior Secured Debt	1,511,828	0	0	(97,276)	29,660	(138,311)	1,305,901	(97,276
	1,786,390	271,858	625,000 [2]	0	0	(1,235,315)	1,447,933	0

Funds Held in Escrow From Sales of Investments								
Total	$86,095,174	$(2,764,255)	$0	$8,951,170	$10,122,267	$(7,946,487)	$94,457,869	$1,480,6

[1] Transfers among asset classes are owing to conversions at financing events. These do not represent transfers in or out of Level 3.

[2] There was a $625,000 transfer from "Preferred Stock" into "Funds Held in Escrow From Sales of Investments" owing to the sale of Molecular Imprints, Inc., to Canon, Inc.

For the six months ended June 30, 2014, there were no transfers out of Level 3.

49

At December 31, 2013, our financial assets were categorized as follows in the fair value hierarchy:

		Fair Value Measurement at Reporting Date Using:		
Description	December 31, 2013	Unadjusted Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
U.S. Government Securities:	$18,999,810	$ 18,999,810	$ 0	$ 0
Privately Held Portfolio Companies:				
Preferred Stock	$71,577,059	$ 0	$ 0	$ 71,577,059
Bridge Notes	6,044,114	0	0	6,044,114
Warrants	800,487	0	0	800,487
Rights to Milestone Payments	3,489,433	0	0	3,489,433
Common Stock	108,668	0	0	108,668
Senior Secured Debt	1,511,828	0	0	1,511,828
Participation Agreement	777,195	0	0	777,195
Non-Convertible Promissory Note	4,043,381	0	4,043,381	0
Publicly Traded Portfolio Companies:				
Common Stock	$5,547,294	$ 5,547,294	$ 0	$ 0
Total Investments:	$112,899,269	$ 24,547,104	$ 4,043,381	$ 84,308,784
Funds Held in Escrow From Sales of Investments:	$1,786,390	$ 0	$ 0	$ 1,786,390
Total Financial Assets:	$114,685,659	$ 24,547,104	$ 4,043,381	$ 86,095,174
Liabilities:				
Written Call Options	$103,500	$ 103,500	$ 0	$ 0
Total Liabilities:	$103,500	$ 103,500	$ 0	$ 0

The following chart shows the components of change in the financial assets categorized as Level 3 for the twelve months ended December 31, 2013.

	Beginning Balance 1/1/2013	Total Realized Gains (Losses) Included in Changes in Net Assets	Transfers	Total Unrealized (Depreciation) Appreciation Included in Changes in Net Assets	Investments in Portfolio Companies, Interest on Bridge Notes, and Amortization of Loan Fees, Net	Disposals	Ending Balance 12/31/2013	Am (De Ap the Per Inc Ch Ass Att to t Ch Un or Los to Ass at the Dat
Preferred Stock	$78,615,582	$10,006,915	$1,817,476 [1]	$(17,635,033)	$12,779,034	$(14,006,915)	$71,577,059	$(9
Bridge Notes	4,152,634	0	(1,822,831) [1]	(1,078,514)	4,792,825	0	6,044,114	(1
Common Stock	108,667	(4,384,762)	0	4,384,762	1	0	108,668	0
Warrants	586,320	0	5,355 [1]	188,412	20,400	0	800,487	18
Rights to Milestone Payments	3,400,734	0	0	88,699	0	0	3,489,433	88
Participation Agreements	1,138,148	90,255	0	(22,807)	5,966	(434,367)	777,195	39
Subordinated Secured Debt	120,410	15,058	0	(10,836)	368	(125,000)	0	0
Senior Secured Debt	1,075,870	0	0	397,325	339,907	(301,274)	1,511,828	39

Non-Convertible Promissory Note	3,033,338	0	(3,033,338)	0	0	0	0	0
Publicly Traded Common Stock	1,348,227	0	(1,547,827)	0	199,600	0	0	0
Funds Held in Escrow From Sales of Investments	1,052,345	766,448	0	0	1,168,671	(1,201,074)	1,786,390	0
Total	$94,632,275	$6,493,914	$(4,581,165)	$(13,687,992)	$19,306,772	$(16,068,630)	$86,095,174	$(9

[1] Transfers among asset classes are owing to conversions at financing events. These do not represent transfers in or out of Level 3.

We elected to use the beginning of period values to recognize transfers in and out of Level 2 and Level 3 investments. For the year ended December 31, 2013, there were transfers out of Level 3 totaling $4,581,165. Our shares of Champions Oncology, Inc., transferred from a Level 3 investment to a Level 1 investment owing to the market for the shares becoming active with increased and sustained trading volume and the lapse of restrictions on 626,523 shares that were previously restricted. Our non-convertible promissory note in Molecular Imprints, Inc., transferred from a Level 3 investment to a Level 2 investment owing to an acquisition offer.

The following chart shows the components of change in the financial assets categorized as Level 3 for the three months ended June 30, 2013.

	Beginning Balance 4/1/2013	Total Realized Gains (Losses) Included in Changes in Net Assets	Transfers	Total Unrealized (Depreciation) Appreciation Included in Changes in Net Assets	Investments in Portfolio Companies, Interest on Bridge Notes, and Amortization of Loan Fees, Net	Disposals	Ending Balance 6/30/2013	Amount of Total (Depreciation) Appreciation for the Period Included in Changes in Net Assets Attributable to the Change in Unrealized Gains or Losses Relating to Assets Still Held at the Reporting Date
Preferred Stock	$79,279,756	$ 0	$352,838 [1]	$(1,505,819)	$3,836,373	$ 0	$81,963,148	$(1,505,819)
Bridge Notes	5,213,314	0	(352,838)[1]	1,129,927	815,430	0	6,805,833	1,129,927
Common Stock	108,667	0						