

EQUUS TOTAL RETURN, INC.  
Form 10-Q  
August 14, 2012

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended June 30, 2012

or

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

For the transition period \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 814-00098

\_\_\_\_\_  
**EQUUS TOTAL RETURN, INC.**

(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

76-0345915  
(I.R.S. Employer  
Identification No.)

Eight Greenway Plaza, Suite 930 Houston, Texas  
(Address of principal executive offices)

77046  
(Zip Code)

**Registrant's telephone number, including area code: (713) 529-0900**

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller Reporting Company   
Indicate by check mark whether the registrant is a shell company. Yes  No

There were 10,561,646 shares of the registrant's common stock, \$.001 par value, outstanding, as of August 14, 2012.

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EQUUS TOTAL RETURN, INC.

(A Delaware Corporation)

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Table of ContentsEQUUS TOTAL RETURN, INC.BALANCE SHEETS**Item 1. Financial Statements****Part I. Financial Information**

(in thousands, except per share amounts)	June 30, 2012	December 31, 2011
	(Unaudited)	
Assets		
Investments in portfolio securities at fair value:		
Control investments (cost at \$8,540 and \$23,353 respectively)	\$ 553	\$13,298
Affiliate investments (cost at \$350 and \$350 respectively)	150	150
Non-affiliate investments (cost at \$13,178 and \$12,878 respectively)	5,699	5,734
Total investments in portfolio securities at fair value	6,402	19,182
Cash and cash equivalents	27,039	16,813
Restricted cash and temporary cash investments	—	6,060
Accounts receivable and other	155	91
Accrued interest receivable	217	2,155
Total assets	33,813	44,301
Liabilities and net assets		
Accounts payable and accrued liabilities	347	114
Accounts payable to related parties	48	39
Borrowing under margin account	—	6,000
Total liabilities	395	6,153
Commitments and contingencies		
Net assets	\$ 33,418	\$38,148
Net assets consist of:		
Common stock, par value	\$ 10	\$10
Capital in excess of par value	59,104	64,292
Undistributed net investment losses	(10,030 )	(8,755 )
Unrealized depreciation of portfolio securities, net	(15,666 )	(17,399 )
Total net assets	\$ 33,418	\$38,148
Shares of common stock issued and outstanding, \$.001 par value, 50,000 shares authorized	10,562	10,562
Shares of preferred stock issued and outstanding, \$.001 par value, 5,000 shares authorized	—	—
Net asset value per share	\$3.16	\$3.61

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

Table of ContentsEQUUS TOTAL RETURN, INC.STATEMENTS OF OPERATIONS

(Unaudited)

(in thousands, except per share amounts)	Three months ended June 30,		Six months ended June 30,	
	2012	2011	2012	2011
Investment income:				
Interest income:				
Control investments	\$ 180	\$ 354	\$ 320	\$ 670
Affiliate investments	—	—	—	4
Non-affiliate investments	31	29	118	141
Total interest income	211	383	438	815
Interest from temporary cash investments	1	9	1	16
Total investment income	212	392	439	831
Expenses:				
Compensation expense	370	335	569	827
Professional fees	388	424	671	763
Director fees and expenses	110	126	250	208
Mailing, printing and other expenses	92	45	117	86
General and administrative expense	25	42	97	93
Taxes	4	121	9	121
Interest expense	—	1	1	1
Offering costs	—	300	—	300
Settlement expense	—	200	—	320
Total expenses	989	1,594	1,714	2,719
Net investment loss	(777 )	(1,202 )	(1,275 )	(1,888 )
Net realized gain (loss):				
Control investments	(5,187 )	(10,074 )	(5,187 )	(10,074 )
Affiliate investments	—	—	—	138
Non-affiliate investments	—	—	—	(992 )
Temporary cash investments	(1 )	—	(1 )	(1 )
Net realized loss	(5,188 )	(10,074 )	(5,188 )	(10,929 )
Net unrealized depreciation of portfolio securities:				
End of period	(15,666)	(15,727)	(15,666)	(15,727)
Beginning of period	(17,398)	(27,477)	(17,399)	(27,300)
Net change in unrealized depreciation of portfolio securities	1,732	11,750	1,733	11,573
Net increase (decrease) in net assets resulting from operations	\$(4,233 )	\$474	\$(4,730 )	\$(1,244 )
Net increase (decrease) in net assets resulting from operations per share:				
Basic and diluted	\$(0.40 )	\$0.05	\$(0.45 )	\$(0.13 )
Weighted average shares outstanding:				
Basic and diluted	10,562	10,188	10,562	9,528

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



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EQUUS TOTAL RETURN, INC.

STATEMENTS OF CHANGES IN NET ASSETS

(Unaudited)

(in thousands)	Six Months Ended	
	June 30, 2012	2011
Net decrease in net assets resulting from operations	\$(4,730 )	\$(1,244 )
Capital share transactions:		
Shares issued for portfolio securities	—	4,625
Net increase in net assets resulting from capital share transactions	—	4,625
Increase (decrease) in net assets	(4,730 )	3,381
Net assets at beginning of period	38,148	38,051
Net assets at end of period	\$33,418	\$41,432

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

Table of ContentsEQUUS TOTAL RETURN, INC.STATEMENTS OF CASH FLOWS

(Unaudited)

(in thousands)	Six Months Ended June 30,	
	2012	2011
Reconciliation of decrease in net assets resulting from operations to net cash provided by operating activities:		
Net decrease in net assets resulting from operations	\$(4,730 )	\$(1,244 )
Adjustments to reconcile net decrease in net assets resulting from operations to net cash provided by operating activities:		
Net realized loss	5,188	10,929
Net change in unrealized depreciation of portfolio securities	(1,733 )	(11,573)
Offering costs expense	—	300
Changes in operating assets and liabilities:		
Purchase of portfolio securities	—	(254 )
Net proceeds from dispositions of portfolio securities	4,008	9,731
Principal payments received from portfolio securities	5,618	157
Cash settlement of collateral	—	1,610
Sales of temporary cash investments, net	6,060	—
(Increase) decrease in accounts receivable and other	(64 )	231
Decrease in accrued interest receivable	1,637	23
Deferred offering costs	—	(165 )
Increase in accounts payable and accrued liabilities	233	230
Increase (decrease) in accounts payable-related parties	9	(24 )
Net cash provided by operating activities	16,226	9,951
Cash flows from financing activities:		
Borrowings under margin account	8,000	21,000
Repayments under margin account	(14,000)	(21,000)
Net cash used in financing activities	(6,000 )	—
Net increase in cash and cash equivalents	10,226	9,951
Cash and cash equivalents at beginning of period	16,813	7,382
Cash and cash equivalents at end of period	\$27,039	\$17,333
Non-cash operating and financing activities:		
Shares issued for portfolio securities	\$—	\$4,625
Accrued interest or dividends exchanged for portfolio securities	\$301	\$—
Supplemental disclosure of cash flow information:		
Interest paid	\$1	\$5

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





Table of ContentsEQUUS TOTAL RETURN, INC.SUPPLEMENTAL INFORMATION—SELECTED PER SHARE DATA AND RATIOS

(Unaudited)

	Six months ended June 30, 2012		2011	
Investment income	\$	0.04	\$	0.09
Expenses		0.16		0.29
Net investment loss		(0.12)		(0.20)
Net realized loss		(0.49)		(1.14)
Net change in unrealized depreciation		0.16		1.21
Net decrease in net assets resulting from operations		(0.45)		(0.13)
Capital transactions:				
Shares issued for portfolio securities		—		(0.17)
Dilutive effect of shares issued		—		(0.07)
Net decrease in net assets resulting from capital transactions		—		(0.24)
Net decrease in net assets		(0.45)		(0.37)
Net assets at beginning of period	\$	3.61	\$	4.29
Net assets at end of period, basic and diluted	\$	3.16	\$	3.92
Weighted average number of shares outstanding during period, in thousands		10,562		9,528
Market price per share:				
Beginning of period	\$	2.24	\$	2.50
End of period	\$	2.44	\$	2.40
Selected information and ratios:				
Ratio of expenses to average net assets		4.79		6.84
		(3.56)		(4.75)
		%		%
		%		%

Ratio of net investment loss to average net assets				
Ratio of net decrease in net assets resulting from operations to average net assets	(13.22	%)	(3.13	%)
Total return on market price <sup>(1)</sup>	8.93	%	(4.00	%)

(1) Total return = [(ending market price per share - beginning price per share) / beginning market price per share].

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

Table of Contents**EQUUS TOTAL RETURN, INC.****SCHEDULE OF INVESTMENTS****June 30, 2012****(Unaudited)***(in thousands, except share data)*

Name and Location of Portfolio Company	Industry	Date of Initial Investment	Investment	Principal	Cost of Investment	Fair Value (1)
<b>Control investments: Majority-owned (3):</b>						
Equus Energy, LLC Houston, TX	Energy	December 2011	Member interest (100%)		\$ 250	\$ 128
Equus Media Development Company, LLC Houston, TX	Media	January 2007	Member interest (100%)		3,000	147
Spectrum Management, LLC Carrolton, TX	Business products and services	December 1999	285,000 units of Class A member interest (92.1%/82.5% fully diluted)		2,850	-
			16% subordinated promissory notes due 11/11(2)	\$ 2,440	2,440	278
					5,290	278
<b>Total Control investments: Majority-owned (represents 8.7% of total investments at fair value)</b>					<b>\$ 8,540</b>	<b>\$ 553</b>
<b>Affiliate Investments (4):</b>						
PalletOne, Inc. Bartow, FL	Shipping products and services	October 2001	350,000 shares of common stock (18.70%)		\$ 350	\$ 150
<b>Total Affiliate Investments (represents 2.3% of total investments at fair value)</b>					<b>\$ 350</b>	<b>\$ 150</b>
<b>Non-Affiliate Investments (less than 5% owned):</b>						
The Bradshaw Group Richardson, TX	Business products and services	May 2000	576,828 Class B shares (12.25%) preferred stock		1,795	-
			38,750 Class C shares preferred stock		-	-
			788,649 Class D shares 15% preferred stock		-	-
			2,218,109 Class E shares 8% preferred stock		-	-

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			Warrant to buy 2,229,450 shares of common stock through 5/16	-	-
				1,795	-
Infinia Corporation Ogden, UT	Alternative energy	June 2007	115,180 shares common stock (0.13%)	8,000	-
			Option to purchase 16,000 shares of common stock at \$6.50 per share through 12/12	-	-
				8,000	-
Orco Property Group Paris, France	Real estate	April 2011	1,102,445 shares common stock	1,877	3,149
			471,170 shares common stock	802	1,271
			10% promissory note due 2018 (5)	\$ 704	1,279
				3,383	5,699
Trulite, Inc. Columbia, SC	Alternative energy	August 2008	Warrants to buy 8,934,211 shares of common stock at \$0.01 - \$0.38 per share through 11/15	-	-
<b>Total Non-Affiliate Investments (represents 89.0% of total investments at fair value)</b>				<b>\$ 13,178</b>	<b>\$5,699</b>
<b>Total Investment in Portfolio Securities</b>				<b>\$ 22,068</b>	<b>\$6,402</b>

(1) See Note 3 to the financial statements, Valuation of Investments.

(2) Non-income producing.

(3) Majority owned investments are generally defined under the Investment Company Act of 1940 as companies in which we own more than 50% of the voting securities of the company.

(4) Affiliate investments are generally defined under the Investment Company Act of 1940 as companies in which we own at least 5% but not more than 25% voting securities of the company.

(5) Income producing.

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

Table of Contents**EQUUS TOTAL RETURN, INC.****SCHEDULE OF INVESTMENTS – (Continued)****June 30, 2012****(Unaudited)**

Except for our holding of 1,102,455 ordinary shares of Orco Property Group S.A. (“OPG”), substantially all of our portfolio securities are restricted from public sale without prior registration under the Securities Act of 1933 or other relevant foreign regulatory authority. We negotiate certain aspects of the method and timing of the disposition of our investment in each portfolio company, including registration rights and related costs.

As defined in the Investment Company Act of 1940, all of our investments, except for our holding in OPG and its controlled subsidiary, Orco Germany S.A., are in eligible portfolio companies. We provide significant managerial assistance to portfolio companies that comprise 11% of the total value of the investments in portfolio securities as of June 30, 2012

Our investments in portfolio securities consist of the following types of securities as of June 30, 2012 (in thousands):

Type of Securities	Cost	Fair Value	Fair Value as Percentage of Net Assets	
Common stock	\$ 11,029	\$4,570	13.7	%
Secured and subordinated debt	3,144	1,557	4.7	%
Limited liability company investments	6,100	275	0.8	%
Preferred stock	1,795	—	—	
Total	\$ 22,068	\$6,402	19.2	%

Accrued interest has been impaired on notes receivable included in secured and subordinated debt with a fair value of \$0.3 million.

The following is a summary by industry of the Fund’s investments in portfolio securities as of June 30, 2012 (in thousands):

Industry	Fair Value	Fair Value as Percentage of Net Assets	
Real estate	\$5,699	17.1	%
Business products and services	278	0.8	%
Shipping products and services	150	0.5	%
Media	147	0.4	%
Energy	128	0.4	%
Total	\$6,402	19.2	%

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

Table of Contents**EQUUS TOTAL RETURN, INC.****SCHEDULE OF INVESTMENTS****DECEMBER 31, 2011***(in thousands, except share data)*

Name and Location of Portfolio Company	Industry	Date of Initial Investment	Investment	Principal	Cost of Investment	Fair Value <u>(1)</u>
<b>Control investments:</b>						
<b>Majority-owned <sup>(5)</sup>:</b>						
Equus Energy, LLC Houston, TX	Energy	December 2011	Member interest (100%)		\$250	\$236
Equus Media Development Company, LLC Houston, TX	Media	January 2007	Member interest (100%)		3,000	163
Sovereign Business Forms, Inc. Houston, TX	Business products and services	August 1996	1,214,630 shares of common stock (64.67% / 55.00% fully diluted)		5,080	4,488
			12% subordinated promissory notes due 5/13 <sup>(2)</sup>	\$2,363	2,363	2,363
					7,443	6,851
Spectrum Management, LLC Carrolton, TX	Business products and services	December 1999	285,000 units of Class A member interest (92.1% / 82.5% fully diluted)		2,850	-
			16% subordinated promissory notes due 11/11 <sup>(3)(4)</sup>	\$2,440	2,440	319
					5,290	319
<b>Total Control investments: Majority-owned (represents 30.1% of total investments at fair value)</b>					<b>\$15,983</b>	<b>\$7,569</b>
<b>Control Investments: Non-majority owned<sup>(6)</sup>:</b>						
ConGlobal Industries Holding, Inc. San Ramon, CA	Shipping products and services	February 1997	24,397,303 shares of common stock (34.2%)		\$1,370	\$-
			7% subordinated promissory note due 12/12 <sup>(3)</sup>	\$6,000	6,000	5,729



				7,370	5,729
<b>Total Control Investments: Non-majority owned (represents 22.7% of total investments at fair value)</b>				<b>\$7,370</b>	<b>\$5,729</b>
Total Control Investments: (represents 52.8% of total investments at fair value)				\$23,353	\$13,298
Affiliate Investments					
(7):					
PalletOne, Inc. Bartow, FL	Shipping products and services	October 2001	350,000 shares of common stock (18.70%)	\$350	\$150
<b>Total Affiliate Investments (represents 0.6% of total investments at fair value)</b>				<b>\$350</b>	<b>\$150</b>

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

Table of Contents**EQUUS TOTAL RETURN, INC.****SCHEDULE OF INVESTMENTS—(Continued)****DECEMBER 31, 2011***(in thousands, except share data)*

Name and Location of		Date of Initial		Cost of	Fair	
Portfolio Company	Industry	Investment	Investment	Principal Investment	Value (1)	
Non-Affiliate Investments (less than 5% owned):						
The Bradshaw Group Richardson, TX	Business products and services	May 2000	576,828 Class B shares (12.25%) preferred stock	\$ 1,795	\$-	
			38,750 Class C shares preferred stock	-	-	
			788,649 Class D shares 15% preferred stock	-	-	
			2,218,109 Class E shares 8% preferred stock	-	-	
			Warrant to buy 2,229,450 shares of common stock through 5/16	-	-	
				1,795	-	
Infinia Corporation Ogden, UT	Alternative energy	June 2007	115,180 shares common stock (0.13%)	8,000	-	
			Option to purchase 16,000 shares of common stock at \$6.50 per share through 12/12	-	-	
				8,000	-	
Orco Germany S.A. Berlin, Germany	Real estate	April 2011	8,890 4% Corporate Bonds due 5/12	\$8,113	\$3,083	\$5,734
Trulite, Inc. Columbia, SC	Alternative energy	August 2008	Warrants to buy 8,934,211 shares of common stock at \$0.01 - \$0.38 per share through 11/15	-	-	-
<b>Total Non-Affiliate Investments (represents 22.8% of total investments at fair value)</b>				<b>\$12,878</b>	<b>\$5,734</b>	
<b>Total Investment in Portfolio</b>				<b>\$36,581</b>	<b>\$19,182</b>	
<b>Securities</b>						
Temporary Cash Investments						
U.S. Treasury Bill (8)	Government	December 2011	UST 0% due 3/12	\$6,000	\$6,000	\$6,000
<b>Total Temporary Cash Investments (represents 23.8% of total investments at fair value)</b>				<b>\$6,000</b>	<b>\$6,000</b>	
<b>Total Investments</b>				<b>\$42,581</b>	<b>\$25,182</b>	

(1) See Note 3 to the financial statements, Valuation of Investments.

(2) Income-producing.

(3) Income on these securities is accrued to maturity.

(4) Non-income producing.

(5) Majority owned investments are generally defined under the Investment Company Act of 1940 as companies in which we own more than 50% of the voting securities of the company.

(6) Non-majority owned control investments are generally defined under the Investment Company Act of 1940 as companies in which we own more than 25% but not more than 50% of the voting securities of the company.

(7) Affiliate investments are generally defined under the Investment Company Act of 1940 as companies in which we own at least 5% but not more than 25% voting securities of the company.

(8) The Fund has included U.S. Treasury Bills in "Restricted Cash and Temporary Cash Investments" on the balance sheet.

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

Table of Contents**EQUUS TOTAL RETURN, INC.****SCHEDULE OF INVESTMENTS – (Continued)****DECEMBER 31, 2011***(in thousands, except share data)*

Except for our holding of 8,890 4% bonds issued by Orco Germany S.A., substantially all of our portfolio securities are restricted from public sale without prior registration under the Securities Act of 1933. We negotiate certain aspects of the method and timing of the disposition of our investment in each portfolio company, including registration rights and related costs.

As defined in the Investment Company Act of 1940, all of our investments, except for our holding of 8,840 Orco Germany bonds, are in eligible portfolio companies. We provide significant managerial assistance to portfolio companies that comprise 70.1% of the total value of the investments in portfolio securities as of December 31, 2011.

Our investments in portfolio securities consist of the following types of securities as of December 31, 2011 (in thousands):

Type of Securities	Cost	Fair Value	Fair Value as Percentage of Net Assets	
Secured and subordinated debt	\$13,886	\$14,145	37.1	%
Common stock	14,800	4,638	12.1	%
Limited liability company investments	6,100	399	1.0	%
Preferred stock	1,795	—	—	
Total	\$36,581	\$19,182	50.2	%

Cash payments of interest are currently being received and/or accrued on notes aggregating \$13.8 million in fair value, while accrued interest has been impaired on notes receivable included in secured and subordinated debt with a fair value of \$0.3 million.

The following is a summary by industry of our investments in portfolio securities as of December 31, 2011 (in thousands):

Industry	Fair Value	Fair Value as Percentage of Net Assets	
Business products and services	\$7,170	18.8	%
Shipping products and services	5,879	15.4	%
Real estate	5,734	15.0	%
Energy	236	0.6	%
Media	163	0.4	%
Total	\$19,182	50.2	%

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

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EQUUS TOTAL RETURN, INC.

NOTES TO FINANCIAL STATEMENTS

June 30, 2012

(Unaudited)

**(1) Description of Business and Basis of Presentation**

**Description of Business**—Equus Total Return, Inc. (“we,” “us,” “our,” “Equus” the “Company” and the “Fund”), a Delaware corporation, was formed by Equus Investments II, L.P. (the “Partnership”) on August 16, 1991. On July 1, 1992, the Partnership was reorganized and all of the assets and liabilities of the Partnership were transferred to the Fund in exchange for shares of common stock of the Fund. Our shares trade on the New York Stock Exchange under the symbol EQS. On August 11, 2006, our shareholders approved the change of the Fund’s investment strategy to a total return investment objective. This new strategy seeks to provide the highest total return, consisting of capital appreciation and current income. In connection with this strategic investment change, the shareholders also approved the change of name from Equus II Incorporated to Equus Total Return, Inc.

We attempt to maximize the return to stockholders in the form of current investment income and long-term capital gains by investing in the debt and equity securities of companies with a total enterprise value of between \$15.0 million and \$75.0 million, although we may engage in transactions with smaller or larger investee companies from time to time. We seek to invest primarily in companies pursuing growth either through acquisition or organically, leveraged buyouts, management buyouts and recapitalizations of existing businesses or special situations. Our income-producing investments consist principally of debt securities including bonds, subordinate debt, debt convertible into common or preferred stock, or debt combined with warrants and common and preferred stock. Debt and preferred equity financing may also be used to create long-term capital appreciation through the exercise and sale of warrants received in connection with the financing. We seek to achieve capital appreciation by making investments in equity and equity-oriented securities issued by privately-owned companies in transactions negotiated directly with such companies. Given market conditions over the past several years and the performance of our portfolio, our Management and board of directors believe it prudent to continue to review alternatives to refine and further clarify the current strategies.

We elected to be treated as a business development company under the Investment Company Act of 1940 (“1940 Act”). We currently qualify as a regulated investment company (“RIC”) for federal income tax purposes and, therefore, are not required to pay corporate income taxes on any income or gains that we distribute to our stockholders. We have certain wholly owned taxable subsidiaries (“Taxable Subsidiaries”) each of which holds one or more portfolio investments listed on our Schedules of Investments. The purpose of these Taxable Subsidiaries is to permit us to hold portfolio companies organized as limited liability companies, or LLCs, (or other forms of pass-through entities) and still satisfy the RIC tax requirement that at least 90% of our gross revenue for income tax purposes must consist of investment income. Absent the Taxable Subsidiaries, a portion of the gross income of any LLC (or other pass-through entity) portfolio investment would flow through directly to us for the 90% test. To the extent that such income did not consist of investment income, it could jeopardize our ability to qualify as a RIC and, therefore, cause us to incur significant federal income taxes. The income of the LLCs (or other pass-through entities) owned by Taxable Subsidiaries is taxed to the Taxable Subsidiaries and does not flow through to us, thereby helping us preserve our RIC status and resultant tax advantages. We do not consolidate the Taxable Subsidiaries for income tax purposes and they may generate income tax expense because of the Taxable Subsidiaries’ ownership of the portfolio companies. We reflect any such income tax expense on our Statements of Operations.

**Basis of Presentation**—In accordance with Article 6 of Regulation S-X under the Securities Act of 1933 and Securities Exchange Act of 1934, we do not consolidate portfolio company investments, including those in which we have a controlling interest. Our interim unaudited financial statements were prepared in accordance with accounting principles generally accepted in the United States of America, or GAAP, for interim financial information and in accordance with the requirements of reporting on Form 10-Q and Article 10 of Regulation S-X, under the Securities Exchange Act of 1934, as amended. Accordingly, they are unaudited and exclude some disclosures required for annual financial statements. Management believes it has made all adjustments, consisting solely of normal recurring accruals, necessary for the fair presentation of these interim financial statements.

The results of operations for the six months ended June 30, 2012 are not necessarily indicative of results that ultimately may be achieved for the year. The interim unaudited financial statements and notes thereto should be read in conjunction with the financial statements and notes thereto included in the Fund's Form 10-K for the fiscal year ended December 31, 2011, as filed with the Securities and Exchange Commission ("SEC").

**(2) Liquidity and Financing Arrangements**

**Liquidity**—There are several factors that may materially affect the Fund's liquidity during the reasonably foreseeable future. The Fund views this period as the twelve month period from the date of the financial statements in this Form 10-Q, *i.e.*, the period through June 30, 2013.

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We are evaluating the impact of current market conditions on our portfolio company valuations and their ability to provide current income. We have followed valuation techniques in a consistent manner; however, we are cognizant of current market conditions that might affect future valuations of portfolio securities. We believe that our operating cash flow and cash on hand will be sufficient to meet operating requirements and to finance routine capital expenditures through the next twelve months.

**Cash and Temporary Cash Investments**—As of June 30, 2012, we had cash and cash equivalents of \$27.0 million. We had \$6.4 million of our net assets of \$33.4 million invested in portfolio securities.

As of December 31, 2011, we had cash and cash equivalents of \$16.8 million. We had \$19.2 million of our net assets of \$38.1 million invested in portfolio securities. We also had \$6.1 million of restricted cash and temporary cash investments, including primarily the proceeds of a quarter-end margin loan that we incurred to maintain the diversification requirements applicable to a RIC to maintain our pass-through tax treatment. Of this amount, \$6.0 million was invested in U.S. Treasury bills and \$0.1 million represented a required 1% brokerage margin deposit. These securities were held by a securities brokerage firm and pledged along with other assets to secure repayment of the margin loan. The U.S. Treasury bills were sold and the margin loan was repaid to the brokerage firm on January 3, 2012.

**Dividends**— We will pay out net investment income and/or realized capital gains, if any, on an annual basis as required under the Investment Company Act of 1940.

**Investment Commitments**—As of June 30, 2012, we had no outstanding commitments to our portfolio company investments.

Under certain circumstances, we may be called on to make follow-on investments in certain portfolio companies. If we do not have sufficient funds to make follow-on investments, the portfolio company in need of the investment may be negatively impacted. Also, our equity interest in the estimated fair value of the portfolio company could be reduced.

**RIC Borrowings, Restricted Cash and Temporary Cash Investments**—We may periodically borrow sufficient funds to maintain the Fund's RIC status by utilizing a margin account with a securities brokerage firm. There is no assurance that such arrangement will be available in the future. If we are unable to borrow funds to make qualifying investments, we may no longer qualify as a RIC. We would then be subject to corporate income tax on the Fund's net investment income and realized capital gains, and distributions to stockholders would be subject to income tax as ordinary dividends. Failure to continue to qualify as a RIC could be materially adverse to us and our stockholders.

We had no RIC borrowings or restricted cash as of June 30, 2012.

As of March 31, 2012, we borrowed \$8.0 million to make qualifying investments to maintain our RIC status by utilizing a margin account with a securities brokerage firm. We collateralized such borrowings with restricted cash and temporary cash investments in U.S. Treasury bills of \$8.1 million. The U.S. Treasury bills were sold and the margin loan was repaid on April 2, 2012.

As of December 31, 2011, we borrowed \$6.0 million to make qualifying investments to maintain our RIC status by utilizing a margin account with a securities brokerage firm. We collateralized such borrowings with restricted cash and temporary cash investments in U.S. Treasury bills of \$6.1 million. The U.S. Treasury bills were sold on January 3, 2012 and the margin loan was repaid at that time.

**Certain Risks and Uncertainties**— Economic conditions during the previous three and a half years and resulting market dislocations have resulted in a significant decline in the availability of debt and equity capital declining



significantly. Generally, the limited amount of available debt financing has shorter maturities, higher interest rates and fees, and more restrictive terms than debt facilities available in the past. In addition, during these years and continuing into the first six months of 2012, the price of our common stock continued to fall well below our net asset value, thereby making it undesirable to issue additional shares of our common stock. Because of these challenges, our near-term strategies shifted from originating debt and equity investments to preserving liquidity necessary to meet our operational needs. Key initiatives that we have previously undertaken to provide necessary liquidity include monetizations, the suspension of dividends and the internalization of management. Although we cannot assure you that such initiatives will be sufficient, we believe we have sufficient liquidity to meet our 2012 operating requirements.

**(3) Significant Accounting Policies**

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

**Use of Estimates**—The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America (“GAAP”) requires us to make estimates and assumptions that affect the reported amounts and disclosures in the financial statements. Although we believe the estimates and assumptions used in preparing these financial statements and related notes are reasonable in light of known facts and circumstances, actual results could differ from those estimates.

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**Valuation of Investments**—Portfolio investments are carried at fair value with the net change in unrealized appreciation or depreciation included in the determination of net assets. Valuations of portfolio securities are performed in accordance with accounting principles generally accepted in the United States of America and the financial reporting policies of the Securities and Exchange Commission (“SEC”). The applicable methods prescribed by such principles and policies are described below:

*Publicly-traded portfolio securities*—Investments in companies whose securities are publicly traded are generally valued at their quoted market price at the close of business on the valuation date.

*Privately-held portfolio securities*—The fair value of investments for which no market exists is determined on the basis of procedures established in good faith by our Board of Directors. As a general principle, the current “fair value” of an investment would be the amount we might reasonably expect to receive for it upon its current sale, in an orderly manner. Appraisal valuations are necessarily subjective and the estimated values arrived at by the Fund may differ materially from amounts actually received upon the disposition of portfolio securities.

During the first twelve months after an investment is made, the original investment value is utilized to determine the fair value unless significant developments have occurred during this twelve month period which would indicate a material effect on the portfolio company (such as results of operations or changes in general market conditions). After the twelve month period, or if material events have occurred within the twelve month period, Fund management considers a two step process when appraising investments of privately held companies. The first step involves determining the enterprise value of the portfolio company. During this step, Fund management considers three different valuation approaches: a market approach, an income approach, and an asset approach. The particular facts and circumstances of each portfolio company determine which approach, or combination of approaches, will be utilized. The second step when appraising equity investments of privately held companies involves allocating value to the various debt and equity securities of the company. Fund management allocates value to these securities based on their relative priorities. For equity securities such as warrants, the Fund may also incorporate alternative methodologies including the Black-Scholes Option Pricing Model.

**Market approach**—The market approach typically employed by Fund management calculates the enterprise value of a company as a multiple of earnings before interest, taxes, depreciation and amortization (“EBITDA”) generated by the company for the trailing twelve month period. Adjustments to the company’s EBITDA, including those for non-recurring items, may be considered. Multiples are estimated based on current market conditions and past experience in the private company marketplace and are subjective in nature. The Fund will apply liquidity and other discounts it deems appropriate to equity valuations where applicable. The Fund may also use, when available, third-party transactions in a portfolio company’s securities as the basis of valuation (the “private market method”). The private market method will be used only with respect to completed transactions or firm offers made by sophisticated, independent investors.

**Income approach**—The income approach typically utilized by Fund management calculates the enterprise value of a company utilizing a discounted cash flow model incorporating projected future cash flows of the company. Projected future cash flows consider the historical performance of the company as well as current and projected market participant performance. Discount rates are estimated based on current market conditions and past experience in the private company marketplace and are subjective in nature. The Fund will apply liquidity and other discounts it deems appropriate to equity valuations where applicable.

**Asset approach**—The Fund considers the asset approach to determine the fair value of significantly deteriorated investments demonstrating circumstances indicative of a liquidation analysis. This situation may arise when a portfolio company: 1) cannot generate adequate cash flow to meet the principal and interest payments on its

indebtedness; 2) is not successful in refinancing its debt upon maturity; 3) Fund management believes the credit quality of a loan has deteriorated due to changes in the business and underlying asset or market conditions which may result in the company's inability to meet future obligations; or 4) the portfolio company's reorganization or bankruptcy. Consideration is also given as to whether a liquidation event would be orderly or forced.

The Fund bases adjustments upon such factors as the portfolio company's earnings, cash flow and net worth, the market prices for similar securities of comparable companies, an assessment of the company's current and future financial prospects and various other factors and assumptions. In the case of unsuccessful operations, the Fund may base a portfolio company's fair value upon the company's estimated liquidation value. Fair valuations are necessarily subjective, and management's estimate of fair value may differ materially from amounts actually received upon the disposition of its portfolio securities. Also, any failure by a portfolio company to achieve its business plan or obtain and maintain its financing arrangements could result in increased volatility and result in a significant and rapid change in its value.

Fund management considers that the Fund's general intent is to hold its loans to maturity when appraising its privately held debt investments. As such, Fund management believes that the fair value will not exceed the cost of the investment. However, in addition to the previously described analysis involving allocation of value to the debt instrument, the Fund performs a yield analysis to determine if a debt security has been impaired.

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Certificates of deposit purchased by the Fund generally will be valued at their face value, plus interest accrued to the date of valuation.

The Audit Committee of the Board of Directors may engage independent, third-party valuation firms to conduct independent appraisals and review management's preliminary valuations of each privately-held investment in order to make their own independent assessment. Any third-party valuation data would be considered as one of many factors in a fair value determination. The Audit Committee then would recommend the fair values for all privately-held securities based on all relevant factors to the Board of Directors for final approval.

Because of the inherent uncertainty of the valuation of portfolio securities which do not have readily ascertainable market values, amounting to \$6.4 million and \$19.2 million as of June 30, 2012 and December 31, 2011, respectively, our fair value determinations may materially differ from the values that would have been used had a ready market existed for the securities. One of the Fund's portfolio investments, the 1,102,455 ordinary shares of Orco Property Group S.A. ("OPG"), is publicly listed on the NYSE Euronext Paris Exchange. These shares were cleared for trading on July 27, 2012.

On a daily basis, we adjust our net asset value for the changes in the value of our publicly held securities, if applicable, and material changes in the value of private securities, generally determined on a quarterly basis or as announced in a press release, and reports those amounts to Lipper Analytical Services, Inc. Weekly and daily net asset values appear in various publications, including *Barron's* and *The Wall Street Journal*.

**Deferred Offering Costs**—Accumulation of costs related to the offering whereby we will sell additional shares or rights to acquire shares at a market price that may have been below net asset value. The main components of the costs are legal fees and consultant's fees specifically related to the offering.

**Foreign Exchange**—We record temporary changes in foreign exchange rates of portfolio securities denominated in foreign currencies as changes in fair value. These changes are therefore reflected as unrealized gains or losses until realized.

**Investment Transactions**—Investment transactions are recorded on the accrual method. Realized gains and losses on investments sold are computed on a specific identification basis.

We classify our investments in accordance with the requirements of the 1940 Act. Under the 1940 Act, "Control Investments" are defined as investments in companies in which EQS owns more than 25% of the voting securities or maintains greater than 50% of the board representation. Under the 1940 Act, "Affiliate Investments" are defined as those non-control investments in companies in which EQS owns between 5% and 25% of the voting securities. Under the 1940 Act, "Non-affiliate Investments" are defined as investments that are neither Control Investments nor Affiliate Investments.

**Interest Income Recognition**—We record interest income, adjusted for amortization of premium and accretion of discount, on an accrual basis to the extent that we expect to collect such amounts. We stop accruing interest on investments when we determine that interest is no longer collectible. We may also impair the accrued interest when we determine that all or a portion of the current accrual is uncollectible. If we receive any cash after determining that interest is no longer collectible, we treat such cash as payment on the principal balance until the entire principal balance has been repaid, before we recognize any additional interest income. We accrete or amortize discounts and premiums on securities purchased over the life of the respective security using the effective yield method. The amortized cost of investments represents the original cost adjusted for the accretion of discount and/or amortization of premium on debt securities.

**Payment in Kind Interest (PIK)**—We have loans in our portfolio that may pay PIK interest. We add PIK interest, if any, computed at the contractual rate specified in each loan agreement, to the principal balance of the loan and record it as interest income. To maintain our status as a RIC, we must pay out to stockholders this non-cash source of income in the form of dividends even if we have not yet collected any cash in respect of such investments.

**Cash Flows**—For purposes of the Statements of Cash Flows, we consider all highly liquid temporary cash investments purchased with an original maturity of three months or less to be cash equivalents. We include our investing activities within cash flows from operations. We exclude “Restricted Cash & Temporary Cash Investments” used for purposes of complying with RIC requirements from cash equivalents. See Note 2 for further discussion of the Fund’s RIC borrowings.

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**Income Taxes**—We intend to comply with the requirements of the Code necessary for us to qualify as a RIC. So long as we comply with these requirements, we generally will not be subject to corporate-level federal income taxes on otherwise taxable income (including net realized capital gains) distributed to stockholders. Therefore, we did not record a provision for federal income taxes in our financial statements. We borrow money from time to time to maintain our tax status under the Internal Revenue Code as a RIC. See Note 2 for further discussion of the Fund's RIC borrowings.

Texas margin tax applies to legal entities conducting business in Texas. The margin tax is based on our Texas sourced taxable margin. The tax is calculated by applying a tax rate to a base that considers both revenue and expenses and therefore has the characteristics of an income tax. As a result, we did not owe state income tax for the year ended December 31, 2011.

**Fair Value Measurement**—Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. We have categorized all investments recorded at fair value based upon the level of judgment associated with the inputs used to measure their fair value. Hierarchical levels, directly related to the amount of subjectivity associated with the inputs to fair valuation of these assets and liabilities, are as follows:

Level 1—Inputs are unadjusted, quoted prices in active markets for identical assets at the measurement date. The types of assets carried at Level 1 fair value generally are equities listed in active markets.

Level 2—Inputs (other than quoted prices included in Level 1) are either directly or indirectly observable for the asset in connection with market data at the measurement date and for the extent of the instrument's anticipated life. Fair valued assets that are generally included in this category are warrants held in a public company.

Level 3—Inputs reflect management's best estimate of what market participants would use in pricing the asset at the measurement date. It includes prices or valuations that require inputs that are both significant to the fair value measurement and unobservable. Generally, assets carried at fair value and included in this category are debt, warrants and/or other equity investments held in a private company. As previously described, Fund management considers a two step process when appraising investments of privately held companies. The first step involves determining the enterprise value of the portfolio company. During this step, Fund management considers three different valuation approaches: a market approach, an income approach, and a cost approach. The particular facts and circumstances of each portfolio company determine which approach, or combination of approaches, will be utilized. The second step when appraising equity investments of privately held companies involves allocating value to the various debt and equity securities of the company. Fund management allocates value to these securities based on their relative priorities. For equity securities such as warrants, the Fund may also incorporate alternative methodologies including the Black-Scholes Option Pricing Model. Yield analysis is also employed to determine if a debt security has been impaired.

We will record unrealized depreciation on investments when we determine that the fair value of a security is less than its cost basis, and will record unrealized appreciation when we determine that the fair value is greater than its cost basis.

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As of June 30, 2012, investments measured at fair value on a recurring basis are categorized in the tables below based on the lowest level of significant input to the valuations:

(in thousands)	Total	Fair Value Measurements As of June 30, 2012		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets				
Investments:				
Control investments	\$553	\$—	\$—	\$ 553
Affiliate investments	150	—	—	150
Non-affiliate investments	5,699	—	3,149	2,550
Total investments	6,402	—	3,149	3,253
Temporary cash investments	—	—	—	—
Total investments and temporary cash investments	\$6,402	\$—	\$ 3,149	\$ 3,253

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As of December 31, 2011, investments measured at fair value on a recurring basis are categorized in the tables below based on the lowest level of significant input to the valuations:

(in thousands)	Total	Fair Value Measurements As of December 31, 2011		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets				
Investments:				
Control investments	\$13,298	\$—	\$ —	\$ 13,298
Affiliate investments	150	—	—	150
Non-affiliate investments	5,734	—	—	5,734
Total investments	19,182	—	—	19,182
Temporary cash investments	6,000	6,000	—	—
Total investments and temporary cash investments	\$25,182	\$6,000	\$ —	\$ 19,182

The following table provides a reconciliation of fair value changes during the six months ended June 30, 2012 for all investments for which we determine fair value using unobservable (Level 3) factors:

(in thousands)	Fair value measurements using significant unobservable inputs (Level 3)			
	Control Investments	Affiliate Investments	Non-affiliate Investments	Total
Fair value as of December 31, 2011	\$13,298	\$ 150	\$ 5,734	\$19,182
Realized gains (losses)	(5,187 )	—	—	(5,187 )
Change in unrealized appreciation (depreciation)	2,069	—	(336 )	1,733
Purchases of portfolio securities	—	—	301	301
Proceeds from sales/dispositions	(9,627 )	—	—	(9,627 )
Transfers in (out) of Level 3	—	—	(3,149 )	(3,149 )
Fair value as of June 30, 2012	\$553	\$ 150	\$ 2,550	\$3,253

The following table provides a reconciliation of fair value changes during the six months ended June 30, 2011 for all investments for which we determine fair value using unobservable (Level 3) factors:



(in thousands)	Fair value measurements using significant unobservable inputs (Level 3)			
	Control Investments	Affiliate Investments	Non-affiliate Investments	Total
Fair value as of December 31, 2010	\$17,576	\$ 762	\$ 9,324	\$27,662
Realized gains (losses)	(10,074)	139	(992 )	(10,927)
Change in unrealized appreciation (depreciation)	8,302	(139 )	3,410	11,573
Purchases of portfolio securities	186	—	3,083	3,269
Proceeds from sales/dispositions	(158 )	(712 )	(9,020 )	(9,890 )
Fair value as of June 30, 2011	\$15,832	\$ 50	\$ 5,805	\$21,687

#### **(4) Related Party Transactions and Agreements**

Except as noted below, as compensation for services to the Fund, each Independent Director receives an annual fee of \$20,000 paid quarterly in arrears, a fee of \$2,000 for each meeting of the Board of Directors attended in person, a fee of \$1,000 for participation in each telephonic meeting of the Board and a fee of \$1,000 for each committee meeting attended, and reimbursement of all out-of-pocket expenses relating to attendance at such meetings. A quarterly fee of \$15,000 is paid to the Chairman of the Audit Committee and a quarterly fee of \$3,750 is paid to the Independent Chairman of the Board. We may also pay other one-time or recurring fees to members of our Board of Directors in special circumstances. During 2011 and the six months ended June 30, 2012, we paid Fraser Atkinson a fee of \$60,000 and \$30,000, respectively, in lieu of his standard compensation as Chairman of the Audit Committee for additional duties undertaken in connection with the Fund's review and analysis of its portfolio holdings for the year. Neither Mr. Bertrand des Pallieres, an Independent Director, nor any of our interested directors, receive annual fees for their service

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on the Board of Directors. The Fund incurred \$250,366 and \$207,943 in fees to our directors for the six months ended June 30, 2012 and 2011, respectively.

In June 2010, the Fund ratified and approved the use of A+ Filings, LLC ("A+ Filings") to file its reports with the Securities and Exchange Commission. Mr. Kenneth I. Denos, Secretary of the Fund, holds a majority of the voting shares of A+ Filings. The Fund incurred approximately \$5,000 and \$11,000 in services rendered by A+ Filings for the six months ended June 30, 2012 and 2011, respectively.

On December 20, 2010, the Fund approved a consulting agreement ("Consulting Agreement") with John A. Hardy, the Fund's Chief Executive Officer. The Consulting Agreement provides for base compensation to Mr. Hardy of \$200,000 per annum and an annual bonus based upon achievement of certain criteria. The bonus is subject to an annual payout cap of \$150,000, and any bonus earned that exceeds the payout cap will be carried over into subsequent fiscal years. If the Consulting Agreement is terminated without cause, as defined therein, Mr. Hardy will be entitled to receive one year's base consulting fee, together with all bonuses earned and unpaid up to the date of termination. Mr. Hardy is not entitled to participate in any employee-related benefits, including health, life and disability plans, of the Fund. During the six months ended June 30, 2012, Mr. Hardy was principally responsible for the disposition of two of the Fund's legacy portfolio investments, the gross proceeds of which totaled \$11,611,143. These dispositions were the principal trigger for an annual bonus payment to Mr. Hardy for the fiscal year ended December 31, 2012 of \$150,000. For the six months ended June 30, 2012, the Fund incurred compensation expense of \$250,000, relating to Mr. Hardy's Consulting Agreement, which amount includes the bonus described above. Mr. Hardy has further waived his right to \$672,585 of earned but unpaid bonus in connection with activities of the Fund during the six months ended June 30, 2012. As of June 30, 2011, the Fund incurred compensation expense of \$250,000 relating to Mr. Hardy's Consulting Agreement which included the \$150,000 cash bonus for fiscal 2011 in connection with the disposal of certain investments in January 2011 where the Fund received \$10,000,000 in cash. Mr. Hardy has further permanently waived his right to \$633,302 of earned but unpaid bonus in connection with activities of the Fund during the first six months of 2011.

In November, 2011, Equus Energy, LLC, a wholly-owned subsidiary of the Fund, entered into a consulting agreement with Global Energy Associates, LLC ("Global Energy") to provide consulting services for energy related investments. Henry W. Hankinson, Director, is a managing partner and co-founder of Global Energy. Payments to Global Energy totaled \$37,500 for the six months ended June 30, 2012.

In respect of services provided to the Fund by members of the Board not in connection with their roles and duties as directors, the Fund pays a rate of \$250 per hour for services rendered. In connection with services rendered by Kenneth I. Denos, Secretary and Chief Compliance Officer of the Fund, the Fund incurred \$151,500 which is included in compensation expense for the six months ended June 30, 2012. For the six months ended June 30, 2011, the Fund incurred \$113,800 which is included in compensation expense in the statement of operations and \$117,188 which is included in deferred offering costs on the balance sheet.

**(5) Dividends**

We will pay out net investment income and/or realized capital gains, if any, on an annual basis as required under the Investment Company Act of 1940.

**(6) Portfolio Securities**

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During the six month ended June 30, 2012, we realized capital losses of \$5.2 million, including the following transactions (in thousands):

Portfolio Company	Industry	Type	Transaction Type	Realized Loss
ConGlobal Industries Holdings, Inc.	Shipping products and services	Control	Disposition	\$(4,114)
Sovereign Business Forms Inc.	Business products and services	Control	Disposition	(1,073)
Various others				(1)
				\$(5,188)

Net unrealized depreciation on investments decreased by \$1.7 million during the six months ended June 30, 2012, to a net unrealized depreciation of \$15.7 million. Such decrease in unrealized depreciation is largely due to the following changes:

- (i) Transfer of unrealized loss to realized loss of ConGlobal Industries Holding, Inc. (“ConGlobal”) of \$1.6 million upon the divestiture of the investment.
- (ii) Transfer of unrealized loss to realized loss of Sovereign Business Forms, Inc. (“Sovereign”) of \$0.6 million upon the divestiture of the investment.
- (iii) Restructuring of the Orco Germany, S.A. bonds (“Orco Germany”) with the capitalization of \$0.3 million accrued interest resulting in a corresponding decrease in unrealized gain.

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On May 7, 2012, holders of 72.5% of all Orco Germany bondholders approved a joint restructuring of certain bond debt of Orco Germany and its parent company, Orco Property Group S.A. (“OPG”). Pursuant to such restructuring, approximately 84.5% of the Orco Germany bonds held by each bondholder were converted into *Obligations Convertibles en Actions* (“OCA”) on May 9, 2012. The OCA are expected to be converted into an aggregate of 26,209,613 OPG shares to be delivered in two tranches. The first tranche, consisting of 18,361,540 OPG shares, was delivered in May 2012, of which the Fund received 1,102,455 OPG shares. The second tranche, consisting of 7,848,073 OPG shares, is expected to be received in September 2012. The remaining 15.5% of the Orco Germany bonds held by each bondholder are expected to be converted into newly-issued 6-year OPG notes (“New OPG Notes”) with a face value of €20.0 million bearing cash and PIK interest each at 5% per annum, which interest percentages may be reduced over time upon timely repayments of principal tranches during a four-year period commencing in 2015. Of the total amount of New OPG Notes issued, Equus expects to receive New OPG Notes in the face amount of €1,199,927. Certain terms of the restructuring require approval of the Paris Commercial Court, which is overseeing safeguard proceedings (*procédure de sauvegarde*) with respect to OPG and its assets. As of June 30, 2012, Equus held 1,102,455 OPG shares, OCA that is convertible into an additional 471,170 OPG shares, and 1,378 Orco Germany bonds, or approximately 6.0% of all Orco Germany bonds outstanding, which have yet to be converted into the New OPG Notes.

During the six month ended June 30, 2012, we made no new or follow-on investments. However, the restructuring of the Orco Germany bonds noted above resulted in the capitalization of \$0.3 million accrued interest.

During the six months ended June 30, 2011, we made a follow-on investment of \$0.2 million in Spectrum Management, LLC. On April 27, 2011, we announced that we had entered into two separate transactions involving the purchase of an aggregate of 11,408 bonds (“Bonds”) issued by Orco Germany, a commercial and multi-family residential real estate holding company and developer based in Berlin. The consideration provided to the selling bondholders consisted of an aggregate of 1,700,000 newly issued shares of common stock of the Fund. We received 8,890 of the Bonds on April 27, 2011. On May 9, 2011, one of these agreements was amended and restated to provide for an additional 45 days to deliver the remaining 2,518 of the Bonds in exchange for providing to the Fund approximately \$1.6 million in cash as security for such delivery. As the remaining bonds were not delivered by the specified date, the cash collateral became free and clear property of the Fund on June 23, 2011.

The following table includes significant investment activity during the six months ended June 30, 2011 (in thousands):

Portfolio Company	Investment Activity				Total
	New Investments		Existing Investments		
	Cash	Non-Cash	Follow-On	PIK	
Orco Germany S.A.	\$67	\$ 3,016	\$ —	\$ —	\$3,083
Spectrum Management, LLC	—	—	187	—	187
	\$67	\$ 3,016	\$ 187	\$ —	\$3,270

During the six months ended June 30, 2011, we realized net capital losses of \$10.9 million, including the following significant transactions (in thousands):

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Portfolio Company	Industry	Type	Transaction Type	Realized Gain (Loss)
Riptide Entertainment, LLC	Entertainment and leisure	Control	Disposition	\$(10,074)
London Bridge Entertainment Partners Ltd	Entertainment and leisure	Non-affiliate	Disposition	(992)
RP&C International Investments LLC	Healthcare	Affiliate	Disposition	138
Various others				(1)
				\$(10,929)

During the six months ended June 30, 2011, we received \$0.2 million from Sovereign Business Forms, Inc. (“Sovereign”) in the form of principal payments. During the six months ended June 30, 2011, we sold our promissory notes in 1848 Capital Partners, LLC (“1848”), Big Apple Entertainment Partners, LLC (“Big Apple”), and London Bridge Entertainment Partners, Ltd (“London Bridge”) and certain assets of Riptide Entertainment Partners, LLC (“Riptide”) in which we hold a 64.67% membership interest. All of these assets were sold to Capital Markets Acquisition Partners, LLC for a combined price of \$10 million, with \$9.8 million allocated to the promissory notes held by the Fund and \$0.2 million to Riptide. The Fund allocated the proceeds to the promissory notes resulting in a realized loss of approximately \$0.9 million at London Bridge. In addition, the monies provided to Riptide were sufficient to satisfy its outstanding liabilities, resulting in a value of \$0. We also received \$0.8 million in connection with the sale and redemption of our membership interest in RP&C International Investments LLC (“RP&C”).

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Net unrealized depreciation on investments decreased by \$11.6 million, during the six months ended June 30, 2011, to a net unrealized depreciation of \$15.7 million. Such increase in depreciation resulted from the following changes:

- (i) Decline in fair market value of ConGlobal of \$2.5 million due to lower storage revenue for containers.
- (ii) Transfer of unrealized depreciation to realized depreciation for London Bridge of \$0.8 million due to the sale of the promissory note.
- (iii) Transfer of unrealized depreciation to realized depreciation for Riptide of \$10.1 million due to the sale of the promissory notes and the winding up of the entity.
- (iv) Transfer of unrealized appreciation to realized appreciation for RP&C of \$0.1 million due to the maturity of the investment.
- (v) Increase in fair market value of Sovereign of \$0.6 million due to improved operating performance.
- (vi) Increase in fair market value of Spectrum of \$0.2 million due to the extension of maturity of outstanding debt and the reduction of the risk associated with this potential default.
- (vii) Increase in the fair market value of Orco Germany of \$2.7 million due to the difference in the market price of Equus shares used as consideration for the bonds on the date of acquisition.

(9) Recent Accounting Pronouncements

In May 2011, the FASB issued changes to disclosure requirements for fair value measurements which resulted in a consistent definition of fair value and common requirements for measurement of and disclosure about fair value between GAAP and International Financial Reporting Standards (“IFRS”). These changes become effective for interim and annual periods beginning after December 15, 2011. We adopted this standard beginning on January 1, 2012. Our implementation of this standard did not have a material impact on our process for measuring fair values, our financial position or our results of operations.

(10) Subsequent Events

Management performed an evaluation of the Fund’s activity through the date the financial statements were issued, noting the following subsequent event:

According to press releases issued by Orco Property Group S.A. (“OPG”), on July 19, 2012, a prospectus covering the issuance of 18,361,540 new ordinary shares of OPG to various convertible bondholders was approved by the Commission de Surveillance du Secteur Financier (Luxembourg). These shares, 1,102,455 of which are held by the Fund, were admitted to trading on the NYSE Euronext on July 27, 2012. The OPG shares were received by the Fund in May 2012 as part of a restructuring of certain debts of OPG and its controlled subsidiary, Orco Germany S.A. The

terms of this restructuring are summarized below under Item 2 – “Portfolio Investments.”

**Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations**

**Overview**

Equus Total Return, Inc. (“we,” “us,” “our,” “Equus” the “Company” and the “Fund”), a Delaware corporation, was formed by Equus Investments II, L.P. (the “Partnership”) on August 16, 1991. On July 1, 1992, the Partnership was reorganized and all of the assets and liabilities of the Partnership were transferred to the Fund in exchange for shares of common stock of the Fund. Our shares trade on the New York Stock Exchange under the symbol EQS. On August 11, 2006, our shareholders approved the change of the Fund’s investment strategy to a total return investment objective. This new strategy seeks to provide the highest total return, consisting of capital appreciation and current income. In connection with this strategic investment change, the shareholders also approved the change of name from Equus II Incorporated to Equus Total Return, Inc.

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We attempt to maximize the return to stockholders in the form of current investment income and long-term capital gains by investing in the debt and equity securities of companies with a total enterprise value of between \$15.0 million and \$75.0 million, although we may engage in transactions with smaller or larger investee companies from time to time. We seek to invest primarily in companies pursuing growth either through acquisition or organically, leveraged buyouts, management buyouts and recapitalizations of existing businesses or special situations. Our income-producing investments consist principally of debt securities including subordinate debt, debt convertible into common or preferred stock, or debt combined with warrants and common and preferred stock. Debt and preferred equity financing may also be used to create long-term capital appreciation through the exercise and sale of warrants received in connection with the financing. We seek to achieve capital appreciation by making investments in equity and equity-oriented securities issued by privately-owned companies in transactions negotiated directly with such companies. Given market conditions over the past several years and the performance of our portfolio, our Management and board of directors believe it prudent to continue to review alternatives to refine and further clarify the current strategies.

We elected to be treated as a business development company under the Investment Company Act of 1940 (“1940 Act”). We currently qualify as a regulated investment company (“RIC”) for federal income tax purposes and, therefore, are not required to pay corporate income taxes on any income or gains that we distribute to our stockholders. We have certain wholly owned taxable subsidiaries (“Taxable Subsidiaries”) each of which holds one or more portfolio investments listed on our Schedules of Investments. The purpose of these Taxable Subsidiaries is to permit us to hold portfolio companies organized as limited liability companies, or LLCs, (or other forms of pass-through entities) and still satisfy the RIC tax requirement that at least 90% of our gross revenue for income tax purposes must consist of investment income. Absent the Taxable Subsidiaries, a portion of the gross income of any LLC (or other pass-through entity) portfolio investment would flow through directly to us for the 90% test. To the extent that such income did not consist of investment income, it could jeopardize our ability to qualify as a RIC and, therefore, cause us to incur significant federal income taxes. The income of the LLCs (or other pass-through entities) owned by Taxable Subsidiaries is taxed to the Taxable Subsidiaries and does not flow through to us, thereby helping us preserve our RIC status and resultant tax advantages. We do not consolidate the Taxable Subsidiaries for income tax purposes and they may generate income tax expense because of the Taxable Subsidiaries’ ownership of the portfolio companies. We reflect any such income tax expense on our Statements of Operations.

## **Significant Developments**

The Board and Management believe that market conditions and the performance of the legacy portfolio have dictated the need to pursue a different direction for the Fund and its shareholders. The following are the significant developments that occurred during the 2nd quarter 2012:

- On May 30, 2012, the Fund announced that in exchange for \$5.25 million in cash, it had sold to ConGlobal Industries Holding, Inc. (“ConGlobal”), the Fund’s 34.2% equity interest in ConGlobal, together with the Fund’s promissory note issued by ConGlobal and all interest as accrued. As a result of a number of factors, including a
- (i) decline in EBITDA from historical highs, together with the recent loss of two of ConGlobal’s key customer accounts in the Northwest, ConGlobal had advised Equus that it would be difficult to repay the note held by Equus, due in December 2012, in the principal amount of \$6.0 million plus accrued interest of approximately \$1.9 million.

The Equus note was subordinate to the position of ConGlobal’s senior lender and thus, ConGlobal was not required to pay the Fund until the senior lender had been fully paid. In addition, the Fund had held this position for over 15 years. Principally, as a result of these factors, Equus wished to monetize this position, and did not wish to grant further extensions to the maturity of the note, as it had done in the past. The Fund worked with



ConGlobal to achieve a compromise which resulted in the closing of the transaction.

(ii) On June 21, 2012, the Fund announced that it had sold to Sovereign Business Forms, Inc. ("Sovereign"), the Fund's 55% fully-diluted equity interest in Sovereign, together with the Fund's promissory note issued by Sovereign and all interest as accrued in exchange for \$6.36 million in cash. Having held its interest in Sovereign for approximately 16 years, Equus sought to monetize its investment. In May 2011 an investment banking firm was retained to canvas potential strategic buyers, determine market interest and explore a possible sale of the company. No formal offers in a valuation range acceptable to the Fund were received. Subsequently, Sovereign's Management, with the cooperation of the Fund, refinanced operations to obtain the capital to buy out the position held by Equus.

(iii) On May 7, 2012, holders of 72.5% of all Orco Germany bondholders approved a joint restructuring of certain bond debt of Orco Germany and its parent company, Orco Property Group S.A. ("OPG"). Pursuant to such restructuring, approximately 84.5% of the Orco Germany bonds held by each bondholder were converted into *Obligations Convertibles en Actions* ("OCA") on May 9, 2012. The OCA are expected to be converted into an aggregate of 26,209,613 OPG shares to be delivered in two tranches. The first tranche, consisting of 18,361,540 OPG shares, is expected to be received in September 2012. The remaining 15.5% of the Orco Germany bonds held by each bondholder are expected to be converted into newly-issued 6-year OPG notes ("New OPG Notes") with a face value of €20.0 million bearing cash and PIK interest each at 5% per annum, which interest percentages may be reduced over

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time upon timely repayments of principal tranches during a four-year period commencing in 2015. Of the total amount of New OPG Notes issued, Equus expects to receive New OPG Notes in the face amount of €1,199,927. Certain terms of the restructuring require approval of the Paris Commercial Court, which is overseeing safeguard proceedings (*procédure de sauvegarde*) with respect to OPG and its assets. As of June 30, 2012, Equus held 1,102,455 OPG shares, OCA that is convertible into an additional 471,170 OPG shares, and 1,378 Orco Germany bonds, or approximately 6.0% of all Orco Germany bonds outstanding, which have yet to be converted into the New OPG Notes.

## **Critical Accounting Policies**

Our financial statements are based on the selection and application of significant accounting policies, which require management to make significant estimates and assumptions. We believe that the following are some of the more critical judgment areas in the application of our accounting policies that currently affect our financial condition and results of operations.

**Valuation of Investments**— Portfolio investments are carried at fair value with the net change in unrealized appreciation or depreciation included in the determination of net assets. Valuations of portfolio securities are performed in accordance with accounting principles generally accepted in the United States of America and the financial reporting policies of the SEC. The applicable methods prescribed by such principles and policies are described below:

*Publicly-traded portfolio securities*—Investments in companies whose securities are publicly traded are generally valued at their quoted market price at the close of business on the valuation date.

*Privately-held portfolio securities*—The fair value of investments for which no market exists is determined on the basis of procedures established in good faith by our Board of Directors. As a general principle, the current “fair value” of an investment would be the amount we might reasonably expect to receive for it upon its current sale, in an orderly manner. Appraisal valuations are necessarily subjective and the estimated values arrived at by the Fund may differ materially from amounts actually received upon the disposition of portfolio securities.

During the first twelve months after an investment is made, the original investment amount is utilized to determine the fair value unless significant developments have occurred during this twelve month period which would indicate a material effect on the portfolio company (such as results of operations or changes in general market conditions). After the twelve month period, or if material events have occurred within the twelve month period, Fund management considers a two step process when appraising investments of privately held companies. The first step involves determining the enterprise value of the portfolio company. During this step, Fund management considers three different valuation approaches: a market approach, an income approach, and an asset approach. The particular facts and circumstances of each portfolio company determine which approach, or combination of approaches, will be utilized. The second step when appraising equity investments of privately held companies involves allocating value to the various debt and equity securities of the company. Fund management allocates value to these securities based on their relative priorities. For equity securities such as warrants, the Fund may also incorporate alternative methodologies including the Black-Scholes Option Pricing Model.

**Market approach** – The market approach typically employed by Fund management calculates the enterprise value of a company as a multiple of earnings before interest, taxes, depreciation and amortization (“EBITDA”) generated by the company for the trailing twelve month period. Adjustments to the company’s EBITDA, including those for non-recurring items, may be considered. Multiples are estimated based on current market conditions and past experience in the private company marketplace and are subjective in nature. The Fund will apply liquidity and other discounts it deems appropriate to equity valuations where applicable. The Fund may also use, when available, third-party transactions in a portfolio company’s securities as the basis of valuation (the “private market method”). The private market method will be used only with respect to completed transactions or firm offers made by sophisticated, independent investors.

**Income approach** – The income approach typically utilized by Fund management calculates the enterprise value of a company utilizing a discounted cash flow model incorporating projected future cash flows of the company. Projected future cash flows consider the historical performance of the company as well as current and projected market participant performance. Discount rates are estimated based on current market conditions and past experience in the private company marketplace and are subjective in nature. The Fund will apply liquidity and other discounts it deems appropriate to equity valuations where applicable.

**Asset approach** – The Fund considers the asset approach to determine the fair value of significantly deteriorated investments demonstrating circumstances indicative of a liquidation analysis. This situation may arise when a portfolio company: 1) cannot generate adequate cash flow to meet the principal and interest payments on its indebtedness; 2) is not successful in refinancing its debt upon maturity; 3) Fund management believes the credit quality of a loan has deteriorated due to changes in the business and

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underlying asset or market conditions which may result in the company's inability to meet future obligations; or 4) the portfolio company's reorganization or bankruptcy. Consideration is also given as to whether a liquidation event would be orderly or forced.

The Fund bases adjustments upon such factors as the portfolio company's earnings, cash flow and net worth, the market prices for similar securities of comparable companies, an assessment of the company's current and future financial prospects and various other factors and assumptions. In the case of unsuccessful operations, the Fund may base a portfolio company's fair value upon the company's estimated liquidation value. Fair valuations are necessarily subjective, and management's estimate of fair value may differ materially from amounts actually received upon the disposition of its portfolio securities. Also, any failure by a portfolio company to achieve its business plan or obtain and maintain its financing arrangements could result in increased volatility and result in a significant and rapid change in its value.

Fund management considers that the Fund's general intent is to hold its loans to maturity when appraising its privately held debt investments. As such, Fund management believes that the fair value will not exceed the cost of the investment. However, in addition to the previously described analysis involving allocation of value to the debt instrument, the Fund performs a yield analysis to determine if a debt security has been impaired.

Certificates of deposit purchased by the Fund generally will be valued at their face value, plus interest accrued to the date of valuation.

The Audit Committee of the Board of Directors may engage independent, third-party valuation firms to conduct independent appraisals and review management's preliminary valuations of each privately-held investment in order to make their own independent assessment. Any third-party valuation data would be considered as one of many factors in a fair value determination. The Audit Committee then would recommend the fair values for all privately-held securities based on all relevant factors to the Board of Directors for final approval.

Because of the inherent uncertainty of the valuation of portfolio securities which do not have readily ascertainable market values, amounting to \$6.4 million and \$19.2 million as of June 30, 2012 and December 31, 2011, respectively, our fair value determinations may materially differ from the values that would have been used had a ready market existed for the securities. One of the Fund's portfolio investments, the 1,102,455 ordinary shares of Orco Property Group S.A. ("OPG"), is publicly listed on the NYSE Euronext Paris Exchange. These shares were cleared for trading on July 27, 2012.

On a daily basis, we adjust our net asset value for the changes in the value of our publicly held securities, if applicable, and material changes in the value of private securities, generally determined on a quarterly basis or as announced in a press release, and reports those amounts to Lipper Analytical Services, Inc. Weekly and daily net asset values appear in various publications, including Barron's and *The Wall Street Journal*.

### **Federal Income Taxes**

We intend to comply with the requirements of the Internal Revenue Code necessary for us to qualify as a RIC. So long as we comply with these requirements, we generally will not be subject to corporate-level federal income taxes on otherwise taxable income (including net realized capital gains) distributed to stockholders. Therefore, we did not record a provision for federal income taxes in our financial statements. As of December 31, 2011, we had a capital loss carry forward of \$26.5 million which may be used to offset future capital gains. We may borrow money from time to time to maintain our status as a RIC under the Internal Revenue Code. See Note 2 for further discussion of the Fund's RIC borrowings.

### **Interest Income Recognition**

We record interest income, adjusted for amortization of premium and accretion of discount, on an accrual basis to the extent that we expect to collect such amounts. We stop accruing interest on investments when we determine that interest is no longer collectible. We may also impair the accrued interest when we determine that all or a portion of the current accrual is uncollectible. If we receive any cash after determining that interest is no longer collectible, we treat such cash as payment on the principal balance until the entire principal balance has been repaid, before we recognize any additional interest income. We accrete or amortize discounts and premiums on securities purchased over the life of the respective security using the effective yield method. The amortized cost of investments represents the original cost adjusted for the accretion of discount and/or amortization of premium on debt securities.

### **Payment in Kind Interest**

We have loans in our portfolio that may pay PIK interest. We add PIK interest, if any, computed at the contractual rate specified in each loan agreement, to the principal balance of the loan and record it as interest income. To maintain the Fund's status as a RIC, we must pay out to our stockholders this non-cash source of income in the form of dividends even if we have not yet collected any cash in respect of such investments.

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**Current Market Conditions**

Overall economic conditions in the United States have improved, albeit marginally, during 2011 and the first six months of 2012. However, the economic recovery has been hampered by slower growth, persistent high unemployment levels and lingering softness in certain housing markets. Further, the banking industry continues to experience additional bank failures as regulators continue to impose strict capital requirements. Additionally, future economic expansion and business investment is threatened by perceptions of higher taxes and healthcare costs, as well as the high levels of government deficit spending.

Consistent with other companies in the financial services sector, our performance has been adversely affected. Between December 31, 2009 and June 30, 2012 our net asset value declined from \$5.74 per share to \$3.16 per share. This further impacted the closing price of our common stock, as it declined approximately 21.9% during 2010 and further declined 10.4% during 2011. As of June 30, 2012, our common stock is trading at a 22.9% discount to our net asset value.

Since 2010, we have executed certain initiatives to enhance liquidity, achieve a lower operational cost structure, provide more assistance to portfolio companies and realize certain of our portfolio investments. Specifically, we changed the composition of our Board of Directors and Management, terminated certain of our follow-on investments, internalized the management of the Fund, suspended our managed distribution policy, modified our investment strategy to pursue shorter term liquidation opportunities, pursued non-cash investment opportunities, and sold certain of our underperforming investment holdings. We believe these actions continue to be necessary to protect capital and liquidity during this turbulent economic period in order to preserve and enhance shareholder value. We also expect that, because of management internalization, certain expenses of the Fund will not increase commensurate with an increase in the size of the Fund and, therefore, we can achieve efficiencies in our cost structure if we are able to grow the Fund.

**Liquidity and Capital Resources**

We generate cash primarily from maturities, sales of securities and borrowings, as well as capital gains realized upon the sale of portfolio investments. We use cash primarily to make additional investments, either in new companies or as follow-on investments in the existing portfolio companies and to pay the dividends to our stockholders.

Because of the nature and size of the portfolio investments, we may periodically borrow funds to make qualifying investments to maintain its tax status as a RIC. During the six months ended June 30, 2012 and 2011, we borrowed such funds by utilizing a margin account with a securities brokerage firm. There is no assurance that such arrangement will be available in the future. If the Fund is unable to borrow funds to make qualifying investments, it may no longer qualify as a RIC. The Fund would then be subject to

corporate income tax on its net investment income and realized capital gains, and distributions to stockholders would be subject to income tax as ordinary dividends.

The Fund has the ability to borrow funds and issue forms of senior securities representing indebtedness or stock, such as preferred stock, subject to certain restrictions. Net taxable investment income and net taxable realized gains from the sales of portfolio investments are intended to be distributed at least annually, to the extent such amounts are not

reserved for payment of expenses and contingencies or to make follow-on or new investments.

The Fund reserves the right to retain net long-term capital gains in excess of net short-term capital losses for reinvestment or to pay contingencies and expenses. Such retained amounts, if any, will be taxable to the Fund as long-term capital gains and stockholders will be able to claim their proportionate share of the federal income taxes paid on such gains as a credit against their own federal income tax liabilities. Stockholders will also be entitled to increase the adjusted tax basis of their Fund shares by the difference between their undistributed capital gains and their tax credit.

We are evaluating the impact of current market conditions on our portfolio company valuations and their ability to provide current income. We have followed valuation techniques in a consistent manner; however, we are cognizant of current market conditions that might affect future valuations of portfolio securities. We believe that our operating cash flow and cash on hand will be sufficient to meet operating requirements and to finance routine capital expenditures through the next twelve months.

## **Results of Operations**

### **Investment Income and Expense**

Net investment loss declined to \$1.3 million for the six months ended June 30, 2012 from \$1.9 million for the six months ended June 30, 2011, as the decline in total investment income was offset by a similar decline in total expenses.

Total income from portfolio securities was \$0.4 million and \$0.8 million for the six months ended June, 2012 and 2011, respectively. The \$0.4 million decrease was primarily due to the decline in income producing investments and the impairment of accrued interest receivable of Spectrum Management, LLC.

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Compensation expense was \$0.6 million and \$0.8 million for the six months ended June 30, 2012 and 2011, respectively. The \$0.2 million decrease was due to salary and accrued bonus for the Chief Investment Officer for the six months ended June 30, 2011.

Settlement expense was \$0.3 million for the six months ended June 30, 2011 in connection with the settlement of a lease agreement dispute with American General Insurance Company.

Offering costs were \$0.3 million for the six months ended June 30, 2011 due to the write-off of deferred offering costs.

**Realized Gains and Losses on Sales of Portfolio Securities**

During the six months ended June 30, 2012, we realized capital losses of \$5.2 million including the following transactions (in thousands):

Portfolio Company	Industry	Type	Transaction Type	Realized Loss
ConGlobal Industries Holdings, Inc.	Shipping products and services	Control	Disposition	\$(4,114)
Sovereign Business Forms Inc.	Business products and services	Control	Disposition	(1,073)
Various others				(1)
				\$(5,188)

During the six months ended June 30, 2011, we realized net capital losses of \$10.9 million, including the following transactions (in thousands):

Portfolio Company	Industry	Type	Transaction Type	Realized Gain (Loss)
Riptide Entertainment, LLC	Entertainment and leisure	Control	Disposition	\$(10,074)
London Bridge Entertainment Partners Ltd	Entertainment and leisure	Non-affiliate	Disposition	(992)
RP&C International Investments LLC	Healthcare	Affiliate	Disposition	138
Various others				(1)
				\$(10,929)

**Changes in Unrealized Appreciation/Depreciation of Portfolio Securities**

Net unrealized depreciation on investments decreased by \$1.7 million during the six months ended June 30, 2012, to a net unrealized depreciation of \$15.7 million. Such decrease in unrealized depreciation is largely due to the following changes:

- (i) Transfer of unrealized loss to realized loss of ConGlobal of \$1.6 million upon the divestiture of the investment.
- (ii) Transfer of unrealized loss to realized loss of Sovereign of \$0.6 million upon the divestiture of the investment.



- (iii) Restructuring of Orco Germany bonds with the capitalization of \$0.3 million accrued interest resulting in a corresponding decrease in unrealized gain.

Net unrealized depreciation on investments decreased by \$11.6 million, during the six months ended June 30, 2011, to a net unrealized depreciation of \$15.7 million. Such decrease in depreciation resulted from the following changes:

- (i) Decline in fair market value of ConGlobal of \$2.5 million due to lower storage revenue for containers.
- (ii) Transfer of unrealized depreciation to realized depreciation for London Bridge of \$0.8 million due to the sale of the promissory note.
- (iii) Transfer of unrealized depreciation to realized depreciation for Riptide of \$10.1 million due to the sale of the promissory notes and the winding up of the entity.
- (iv) Transfer of unrealized appreciation to realized appreciation for RP&C of \$0.1 million due to the maturity of the investment.
- (v) Increase in fair market value of Sovereign of \$0.6 million due to improved operating performance.
- (vi) Increase in fair market value of Spectrum of \$0.2 million due to the extension of maturity of outstanding debt and the reduction of the risk associated with this potential default.
- (vii) Increase in the fair market value of Orco Germany of \$2.7 million due to the difference in the market price of Equus shares used as consideration for the bonds on the date of acquisition.

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**Dividends**

We will pay out net investment income and/or realized capital gains, if any, on an annual basis as required under the Investment Company Act of 1940.

**Portfolio Investments**

During the six months ended June 30, 2012, we received \$6.4 million from the disposal of the Fund's 55% fully-diluted equity interest in Sovereign, together with the Fund's promissory note and all interest as accrued interest.

During the six months ended June 30, 2012, we received \$5.3 million from the disposal of the Fund's 34.2% fully equity interest in ConGlobal, together with the Fund's promissory note and all interest as accrued interest.

On May 7, 2012, holders of 72.5% of all Orco Germany bondholders approved a joint restructuring of certain bond debt of Orco Germany and its parent company, Orco Property Group S.A. ("OPG"). Pursuant to such restructuring, approximately 84.5% of the Orco Germany bonds held by each bondholder were converted into Obligations Convertibles en Actions ("OCA") on May 9, 2012. The OCA are expected to be converted into an aggregate of 26,209,613 OPG shares to be delivered in two tranches. The first tranche, consisting of 18,361,540 OPG shares, was delivered in May 2012, of which the Fund received 1,102,455 OPG shares. The second tranche, consisting of 7,848,073 OPG shares, is expected to be received in September 2012. The remaining 15.5% of the Orco Germany bonds held by each bondholder are expected to be converted into newly-issued 6-year OPG notes ("New OPG Notes") with a face value of €20.0 million bearing cash and PIK interest each at 5% per annum, which interest percentages may be reduced over time upon timely repayments of principal tranches during a four-year period commencing in 2015. Of the total amount of New OPG Notes issued, Equus expects to receive New OPG Notes in the face amount of €1,199,927. Certain terms of the restructuring require approval of the Paris Commercial Court, which is overseeing safeguard proceedings (procédure de sauvegarde) with respect to OPG and its assets. As of June 30, 2012, Equus held 1,102,455 OPG shares, OCA that is convertible into an additional 471,270 OPG shares, and 1,378 Orco Germany bonds, or approximately 6.0% of all Orco Germany bonds outstanding, which have yet to be converted into the New OPG Notes.

During the six month ended June 30, 2012, we made no new or follow-on investments. However, the restructuring of the Orco Germany bonds noted above resulted in the capitalization of \$0.3 million accrued interest.

During the six months ended June 30, 2011, we received \$0.2 million from Sovereign Business Forms, Inc. in the form of principal payments. We sold our promissory notes in 1848 Capital Partners, LLC ("1848"), Big Apple Entertainment Partners, LLC ("Big Apple"), and London Bridge Entertainment Partners, Ltd ("London Bridge") and certain assets of Riptide Entertainment Partners, LLC ("Riptide") in which we hold a 64.67% membership interest. All of these assets were sold to Capital Markets Acquisition Partners, LLC for a combined price of \$10 million, with \$9.8 million allocated to the promissory notes held by the Fund and \$0.2 million to Riptide. The Fund allocated the proceeds to the promissory notes resulting in a realized loss of approximately \$0.9 million at London Bridge. In addition, the monies provided to Riptide were sufficient to satisfy its outstanding liabilities, resulting in a value of \$0. We also received \$0.8 million in connection with the sale and redemption of our membership interest in RP&C International Investments LLC.

During the six months ended June 30, 2011, we made a follow-on investment of \$0.2 million in Spectrum Management, LLC. On April 27, 2011, we announced that we had entered into two separate transactions involving the purchase of an aggregate of 11,408 4% bonds due May 2012 ("Bonds") issued by Orco Germany, a commercial and multi-family residential real estate holding company and developer based in Berlin. The consideration provided to the selling bondholders consisted of an aggregate of 1,700,000 newly issued shares of common stock of the Fund. We

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received 8,890 of the Bonds on April 27, 2011. On May 9, 2011, one of these agreements was amended and restated to provide for an additional 45 days to deliver 2,518 of the Bonds in exchange for providing to the Fund approximately \$1.6 million in cash as security for such delivery. As the remaining bonds were not delivered by the specified date, the cash collateral became free and clear property of the Fund on June 23, 2011.

The following table includes significant investment activity during the six months ended June 30, 2011 (in thousands):

Portfolio Company	Investment Activity				Total
	New		Existing		
	Cash	Non-Cash	Follow-On	DK	
Orco Germany S.A.	\$67	\$ 3,016	\$ —	\$ —	\$3,083
Spectrum Management, LLC	—	—	187	—	187
	\$67	\$ 3,016	\$ 187	\$ —	\$3,270

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**Subsequent Events**

Management performed an evaluation of the Fund's activity through the date the financial statements were issued, noting the following subsequent event:

According to press releases issued by Orco Property Group S.A. ("OPG"), on July 19, 2012, a prospectus covering the issuance of 18,361,540 new ordinary shares of OPG to various convertible bondholders was approved by the Commission de Surveillance du Secteur Financier (Luxembourg). These shares, 1,102,455 of which are held by the Fund, were admitted to trading on the NYSE Euronext on July 27, 2012. The OPG shares were received by the Fund in May 2012 as part of a restructuring of certain debts of OPG and its controlled subsidiary, Orco Germany S.A. The terms of this restructuring are summarized above under Item 2 – "Portfolio Investments."

**Item 3. Quantitative and Qualitative Disclosure about Market Risk**

We are subject to financial market risks, including changes in interest rates with respect to investments in debt securities and outstanding debt payable, as well as changes in marketable equity security prices. The Fund has invested in a company outside of the United States which has given rise to exposure to foreign currency value fluctuations. We do not use derivative financial instruments to mitigate any of these risks. The return on investments is generally not affected by foreign currency fluctuations.

Our investments in portfolio securities consist of some fixed-rate debt securities. Since the debt securities are generally priced at a fixed rate, changes in interest rates do not directly affect interest income. In addition, changes in market interest rates are not typically a significant factor in the determination of fair value of these debt securities, since the securities are generally held to maturity. We determine their fair values based on the terms of the relevant debt security and the financial condition of the issuer.

A portion of our investment portfolio consists of debt and equity investments in private companies. Modest changes in public market equity prices generally do not significantly impact the estimated fair value of these investments. However, volatility in stock markets, particularly as such fluctuations may affect Orco Property Group and other European issuers, may affect the quoted price for such stock and may therefore impact their estimated fair value. In addition, significant changes in market equity prices can have a longer-term effect on valuations of private companies, which could affect the carrying value and the amount and timing of gains or losses realized on these investments.

We are classified as a "non-diversified" investment company under the Investment Company Act, which means we are not limited in the proportion of our assets that may be invested in the securities of a single user. The value of one segment called Real Estate includes one portfolio company and was 17.1% of the net asset value and 89% of our investments in portfolio company securities (at fair value) as of June 30, 2012. Changes in business or industry trends or in the financial condition, results of operations, or the market's assessment of any single portfolio company will affect the net asset value and the market price of our common stock to a greater extent than would be the case if we were a "diversified" company holding numerous investments.

**Item 4. Controls and Procedures**

The Fund maintains disclosure controls and other procedures that are designed to ensure that information required to be disclosed by the Fund in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is

accumulated and communicated to the Fund's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

The Fund's management, with the participation of the Fund's Chief Executive Officer and Chief Financial Officer, have evaluated the effectiveness of the design and operations of the Fund's "disclosure controls and procedures" (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934) as of June 30, 2012. Based on their evaluation, the Fund's Chief Executive Officer and Chief Financial Officer concluded that the Fund's disclosure controls and procedures were effective at a reasonable assurance level. There has been no change in the Fund's internal control over financial reporting during the quarter ended June 30, 2012, that has materially affected, or is reasonably likely to materially affect, the Fund's internal control over financial reporting.

## **Part II. Other Information**

### **Item 1. Legal Proceedings**

On April 26, 2010, the Securities and Exchange Commission ("SEC") subpoenaed records of the Fund in connection with certain trades in the Fund's shares by SPQR Capital LLP, SAE Capital Ltd., Versatile Systems Inc., Mobiquity Investments Limited, and anyone associated with those entities. The Fund has fully cooperated with the SEC's request.

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In January 2006, Equus sold its 31.5% ownership interest in Champion Window, Inc. (“Champion”), a portfolio company of the Fund, to Atrium Companies Inc. (“Atrium”) pursuant to a Stock Purchase Agreement (“SPA”) dated December 22, 2005. The SPA contained certain limited rights of indemnification for Atrium in connection with its purchase of such ownership interest.

Atrium filed suit in the District Court of Harris County, Texas against two former officers of Atrium’s subsidiary, Champion, alleging, amongst other matters, that the former officers breached their fiduciary duties to Champion by hiring undocumented workers. This action was commenced primarily as a result of an investigation by the U.S. Immigration and Customs Enforcement agency (“ICE”) into Atrium’s hiring practices. On March 12, 2012, to protect its interests, Equus filed a Petition in Intervention in the State Court Action seeking a declaration from the Court that Equus did not owe any obligation to indemnify Atrium or Champion for any penalties, costs or fees associated with the investigation by ICE.

On March 16, 2012, Atrium and Champion filed a claim with the American Arbitration Association in Dallas, Texas, against Equus and a number of the other sellers under the SPA.

In the Arbitration Action, Atrium and Champion seek damages arising from Equus’ and the other sellers’ indemnity obligations set forth in the SPA. Atrium claims it is entitled to indemnification under the SPA for costs it has incurred in responding to an ongoing investigation by ICE. Atrium entered into a Non-Prosecution Agreement with ICE. It appears that one condition of the Non-Prosecution Agreement required Atrium to pay ICE \$2,000,000. Atrium and Champion asserted two counts of breach of contract against Equus, both arising out of the alleged obligation to indemnify Atrium and Champion pursuant to certain provisions of the SPA. Atrium and Champion also asserted claims for fraudulent inducement against two former officers and directors of Champion. Through the arbitration, Atrium and Champion seek to recover an unspecified amount in the form of alleged “losses, damages, assessments, penalties, interest, reasonable attorneys’ and accountants’ fees, settlement costs, and other costs and expenses arising directly or indirectly out of or incident to,” the alleged breach of the indemnity provisions in the SPA. As a consequence of their fraudulent inducement claim against the two former officers and directors, Atrium and Champion alternatively seek equitable rescission of the SPA and exemplary damages from the two former officers and directors.

Atrium and Champion have yet to specify the amount of damages they seek from Equus or the other sellers pursuant to the alleged indemnity obligations under the SPA. Atrium and Champion have disclosed the payment of \$2 million to ICE to resolve the investigation and avoid prosecution for their hiring practices.

Equus intends to vigorously contest the claims and denies that it owes any indemnity obligations to Atrium or Champion and further denies that it is in any way liable to Atrium or Champion. To the extent Atrium and Champion are able to establish a right to an indemnity, Equus will contest the amount of the claimed indemnity, inasmuch as we believe (among other defenses) that the indemnity obligation can only exist, if at all, with respect to damages arising as a direct and proximate result of employees who were hired prior to the closing date of the 2006 sale of Champion and remained in continuous employment after the 2006 sale, and not to any employee who may have been hired in the six years after the sale.

While the Fund believes the Atrium claim is without merit and the Fund intends to vigorously dispute the claim, there is a reasonable possibility of an adverse ruling which may require the Fund to indemnify Atrium. If Equus is required to indemnify Atrium and Champion, we estimate that such indemnity obligation could vary from \$2.0 - \$3.0 million. Pursuant to the SPA, the indemnification obligation of Equus and the other sellers is several and not joint, and any such indemnity, however uncertain, would likely be reduced proportionately to the Fund’s percentage ownership in Champion at the time of sale, which was 31.5% of Champion’s shares outstanding.

From time to time, the Fund is also a party to certain legal proceedings incidental to the normal course of our business including the enforcement of our rights under contracts with our portfolio companies. While the outcome of these legal proceedings cannot at this time be predicted with certainty, the Fund does not expect that these proceedings will have a material effect upon the Fund's financial condition or results of operations.

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**Item 1A. Risk Factors**

There have been no material changes in the Fund's risk factors from the disclosure set forth in the Annual Report on Form 10-K for the year ended December 31, 2011.

Readers should carefully consider these risks and all other information contained in the annual report on Form 10-K, including the Fund's financial statements and the related notes thereto. The risks and uncertainties described below are not the only ones facing the Fund. Additional risks and uncertainties not presently known to the Fund, or not presently deemed material by the Fund, may also impair its operations and performance.

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**Item 6. Exhibits**

3. Articles of Incorporation and by-laws.
- (a) Restated Certificate of Incorporation of the Fund, as amended. [Incorporated by reference to Exhibit 3(a) to Registrant's Annual Report on Form 10-K for the year ended December 31, 2007.]
- (b) Certificate of Merger dated June 30, 1993, between the Fund and Equus Investments Incorporated. [Incorporated by reference to Exhibit 3(b) to Registrant's Annual Report on Form 10-K for the year ended December 31, 2007.]
- (c) Amended and Restated Bylaws of the Fund. [Incorporated by reference to Exhibit 3(b) to Registrant's Current Report on Form 8-K filed on December 16, 2010.]
10. Material Contracts.
- (c) Safekeeping Agreement between the Fund and Amegy Bank dated August 16, 2008. [Incorporated by reference to Exhibit 10(g) to Registrant's Annual Report on Form 10-K for the year ended December 31, 2008.]
- (d) Form of Indemnification Agreement between the Fund and certain of its directors and officers. [Incorporated by reference to Exhibit 10(d) to Registrant's Annual Report on Form 10-K for the year ended December 31, 2011]
- (e) Form of Release Agreement between the Fund and certain of its officers and former officers. [Incorporated by reference to Exhibit 10(h) to Registrant's Annual Report on Form 10-K for the year ended December 31, 2004.]
- (f) Code of Ethics of the Fund (Rule 17j-1) [Incorporated by reference to Exhibit 10(f) to Registrant's Annual Report on Form 10-K for the year ended December 31, 2009.]
31. Rule 13a-14(a)/15d-14(a) Certifications
- (1) Certification by Chief Executive Officer
- (2) Certification by Chief Financial Officer
32. Section 1350 Certification
- (1) Certification by Chief Executive Officer
- (2) Certification by Chief Financial Officer

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SIGNATURE

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has caused this report to be signed by the undersigned, thereunto duly authorized.

EQUUS TOTAL RETURN, INC.

/s/ John A. Hardy

Date: August 14, 2012

John A. Hardy  
Chief Executive Officer

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