Oxford Lane Capital Corp.
Form N-CSRS
November 29, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM N-CSR

CERTIFIED SHAREHOLDER REPORT OF REGISTERED MANAGEMENT INVESTMENT COMPANIES

Investment Company Act file number 811-22432

Oxford Lane Capital Corp.

(Exact name of registrant as specified in charter)

8 Sound Shore Drive, Suite 255
Greenwich, CT 06830

(Address of principal executive offices)

Jonathan H. Cohen
Chief Executive Officer
Oxford Lane Capital Corp.

8 Sound Shore Drive, Suite 255
Greenwich, CT 06830

(Name and address of agent for service)

Registrant s telephone number, including area code: (203) 983-5275

Date of fiscal year end: March 31

Date of reporting period: September 30, 2012

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Item 1. Reports to Shareholders.

The semi-annual report to shareholders for the six months ended September 30, 2012 is filed herewith pursuant to rule 30e-1 under the Investment Company Act of 1940.

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Oxford Lane Capital Corp.

Semi-Annual Report

September 30, 2012

oxfordlanecapital.com

OXFORD LANE CAPITAL CORP.

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Oxford Lane Capital Corp.

November 29, 2012

To Our Shareholders:

We are pleased to submit to you the report of Oxford Lane Capital Corp. (the Fund or Oxford Lane) for the six months ended September 30, 2012. The net asset value of our shares at that date was $17.13 per common share. The Fund s common stock is traded on the NASDAQ Global Select Market and its share price can differ from its net asset value; at period end, the Fund s closing price on the NASDAQ Global Select Market was $15.30, up from $14.60 at March 31, 2012. The total return for Oxford Lane, for the six months ended September 30, 2012, as reflected in the Fund s financial highlights, was 12.79%. This return reflects the change in market price for the period, as well as the positive impact of $1.10 per share in dividends declared and paid.

We should also draw your attention to our dividend policy, which has been discussed in earlier reports, as we believe that the Fund is in an unusual position. Oxford Lane is subject to significant differences between its accounting income and its taxable income particularly as it relates to our CLO equity investments. We invest in CLO entities which generally constitute passive foreign investment companies and are subject to complex tax rules; the calculation of taxable income attributed to a CLO equity investment can be dramatically different from the calculation of income for financial reporting purposes. Taxable income is based upon the distributable share of earnings as determined under tax regulations for each CLO equity investment, while accounting income is currently based upon an effective yield calculation. In general, we currently expect the taxable income to be higher than reportable accounting income on the basis of actual cash received, and our dividend decisions will be based upon our expectations for that taxable income (as is required for a regulated investment company). While reportable accounting income from our CLO equity class investments for the six months ended September 30, 2012 was approximately $2.7 million, we received or were entitled to receive approximately $5.9 million in distributions. Our dividend policy is based upon the $5.9 million in distributions.

Investment Review

The Fund s investment objective is to maximize its portfolio s risk adjusted total return. Our current focus is to seek current income by investing in structured finance investments, specifically CLO vehicles which own debt securities. We may also seek to make direct investment in corporate debt securities. As of September 30, 2012, we held debt investments in 16 different CLO structures, and equity investments in 11different CLO structures.

The Fund has implemented its investment objective by purchasing in both the primary and secondary markets the income notes (sometimes referred to as equity) and junior debt tranches of various CLO vehicles. Structurally, CLO vehicles are entities formed to purchase and manage a portfolio of loans. The loans within a CLO vehicle are limited to loans which meet established credit criteria. They are subject to concentration limitations in order to limit a CLO vehicle s exposure to individual credits. The CLO vehicles which the Fund focuses on are collateralized primarily by senior loans, and generally have minimal exposure to real estate, mortgage loans or to pools of consumer-based debt, such as credit card receivables or auto loans. Thus far, we are satisfied with the quality of our investment portfolio and the income stream that it is producing.

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Investment Outlook

Despite strength across the credit markets broadly, we believe that the market for CLO-related assets continues to provide us with the opportunity to generate attractive risk adjusted returns within our strategy. We believe that a number of factors support this conclusion, including:

- We believe that the long-term and relatively low-cost capital that many CLO vehicles have secured, compared with current asset spreads and associated LIBOR floors have created opportunities to purchase certain CLO equity and junior debt instruments that may produce attractive risk-adjusted returns. Although Senior Loan yields have generally decreased since mid-2010, we believe that CLO equity and junior debt instruments still offer attractive risk-adjusted returns.
- We believe that CLO equity and junior debt have generally become more liquid since mid-2009. From late 2007 through mid-2009, these assets traded infrequently. We believe that greater liquidity in this market has created more opportunities to select among various CLO debt and equity instruments.
- We believe that investing in CLO securities, and CLO equity instruments in particular, requires a high level of expertise and analysis. We believe that typically this analysis can only be adequately conducted by knowledgeable market participants since that analysis tends to be highly specialized.
- We believe that a stronger credit market for Senior Loans has reduced the risk of collateral coverage test violations across many CLO structures, thereby reducing the risk that current cash distributions otherwise payable to junior debt and/or equity tranches will be diverted under the priority of payments to pay down the more senior obligations in various CLO structures.
- We believe that the US CLO market is relatively large with total assets under management of approximately $252 billion managed by 627 different CLO vehicles[(1)]. We estimate that the amount outstanding of the junior-most debt tranches (specifically the tranches originally rated BB) and equity tranches together are in excess of $25 billion.

In addition to reviewing the junior debt and equity tranches of pre-2008 vintage CLOs, we have analyzed post-2010 CLOs (in both the primary and secondary markets) given the recent increase in new CLO issuance. Through October 2012, CLO issuance stood at approximately $41.5 billion across approximately 95 deals (compared to approximately $12 billion for 2011)[(2)].

While the post-2010 CLOs generally have a higher cost of capital (which may result in a lower return for the equity investors in those CLOs) compared to pre-2008 CLOs, they offer certain attractive structural features (including, in certain cases, better credit enhancement and lower leverage) and stronger collateral packages. We believe there are a significant number of these investment opportunities to consider.

We have and continue to review a large number of CLO investment vehicles in the current market environment, and we expect that the majority of our portfolio holdings, over the near to intermediate-term, will continue to be focused on CLO debt and equity securities.

Jonathan H. Cohen
Chief Executive Officer

1. As of September 2012. Source: Thomson Reuters LPC.
2. As of November 2012. Source: Nomura Securities International, Inc.

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OXFORD LANE CAPITAL CORP.

TOP TEN LONG-TERM HOLDINGS AS OF SEPTEMBER 30, 2012 (Unaudited)

Investment	Maturity	Fair Value	% of Net Assets
ACA CLO 2007-1A income notes	June 15, 2022	$11,357,625	13.16%
Carlyle Global Market Strategies CLO 2011-1X income notes	August 10, 2021	6,600,000	7.65 %
Waterfront CLO 2007 secured notes Class D	August 2, 2020	6,356,250	7.36 %
CIFC Funding 2006-1X CLO secured notes Class B2L	October 20, 2020	4,370,080	5.06 %
Harbourview CLO 2006-1 income notes	December 27, 2019	4,215,750	4.88 %
ACA CLO 2007-1A secured notes Class E	June 15, 2022	4,069,574	4.71 %
Mountain Capital CLO IV, Ltd 2005-4X secured notes Class B2L	March 15, 2018	3,660,965	4.24 %
Sargas CLO I Ltd secured notes Class D	August 27, 2020	3,577,500	4.14 %
Hewett's Island CLO III secured notes Class D	August 9, 2017	3,195,832	3.70 %
Jersey Street CLO 2006-1A income notes	October 20, 2018	3,185,000	3.69 %

Portfolio Investment Breakdown (Excludes cash and other net assets)

FAIR VALUE BY ASSET TYPE

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OXFORD LANE CAPITAL CORP.

STATEMENT OF ASSETS AND LIABILITIES (Unaudited)

	September 30, 2012
ASSETS	
Investments, at fair value (identified cost: $66,927,511)	$82,389,658
Cash and cash equivalents	3,381,748
Dividend receivable	1,025,507
Interest receivable, including accrued interest purchased	417,010
Prepaid expenses and other assets	42,779
Total assets	87,256,702
LIABILITIES	
Investment advisory fee payable to affiliate	368,539
Incentive fees payable	330,724
Directors' fees payable	27,500
Administrator expense payable	30,800
Accrued expenses	178,041
Total liabilities	935,604
NET ASSETS applicable to 5,040,197 shares of $0.01 par value common stock outstanding	$86,321,098
NET ASSETS consist of:	
Paid in capital	76,386,464
Net realized gain (loss) on investments	
Net unrealized appreciation on investments	15,462,147
Distribution in excess of net investment income	(5,527,513)
Total net assets	$86,321,098
Net asset value per common share	$17.13
Market price per share	$15.30
Market price discount to net asset value per share	(10.68%)

See Accompanying Notes

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OXFORD LANE CAPITAL CORP.

SCHEDULE OF INVESTMENTS SEPTEMBER 30, 2012 (Unaudited)

COMPANY[1]	INDUSTRY	INVESTMENT	PRINCIPAL AMOUNT	COST	FAIR VALUE[2]	% of Net Assets
Collateralized Loan Obligation Debt Investments						
ACA CLO 2007-1A	structured finance	CLO secured notes - Class E[3][4][5] (5.21%, due June 15, 2022)	$5,090,786	$3,650,267	$4,069,574	
Bridgeport CLO II	structured finance	CLO secured notes - Class D[3][4][5] (4.64%, due June 18, 2021)	3,391,502	2,461,566	2,653,511	
Canaras Summit CLO 2007-1A	structured finance	CLO secured notes - Class E[3][4][5] (4.73%, due June 19, 2021)	750,000	522,683	602,550	
Cent CDO 15	structured finance	CLO secured notes - Class D[3][4][5] (4.56%, due March 11, 2021)	1,625,000	1,254,644	1,317,713	
CIFC Funding 2006-1X			5,730,501	4,181,268	4,370,080	

	structured finance	CLO secured notes - Class B2L(3)(4)(5) (4.45%, due October 20, 2020)			
Colts 2007-1X	structured finance	CLO secured notes - Class E(3)(4)(5) (4.03%, due March 20, 2021)	3,000,000	1,962,251	2,542,800
Emporia III, Ltd. 2007-3A	structured finance	CLO secured notes - Class E(3)(4)(5) (4.15%, due April 23, 2021)	3,594,000	2,807,615	2,682,921
GSC VIII	structured finance	CLO secured notes - Class D(3)(4)(5) (3.86%, due April 17, 2021)	2,112,137	1,384,371	1,605,224
Hewett's Island CLO III	structured finance	CLO secured notes - Class D(3)(4)(5) (6.19%, due August 09, 2017)	3,486,616	2,838,186	3,195,832
Hewett's Island CLO IV	structured finance	CLO secured notes - Class E(3)(4)(5) (4.99%, due May 09, 2018)	1,500,000	1,327,490	1,245,000
Hewett's CLO V	structured finance	CLO secured notes -	1,707,884	1,116,962	1,349,570

		Class E(3)(4)(5) (6.19%, due August 09, 2017)				
Kingsland V, Ltd. 2007-5X	structured finance	CLO secured notes - Class E(3)(4)(5) (4.71%, due July 14, 2021)	4,000,000	2,872,712	3,000,000	
Mountain Capital CLO IV, Ltd 2005-4X	structured finance	CLO secured notes - Class B2L(3)(4)(5) (5.14%, due March 15, 2018)	4,230,373	3,146,228	3,660,965	
PPM Grayhawk CLO 2007	structured finance	CLO secured notes - Class D(3)(4)(5) (4.06%, due April 18, 2021)	1,869,138	1,413,931	1,361,293	
Sargas CLO I Ltd	structured finance	CLO secured notes - Class D(3)(4)(5) (4.43%, due August 27, 2020)	4,500,000	3,258,217	3,577,500	
Waterfront CLO 2007	structured finance	CLO secured notes - Class D(3)(4)(5) (5.21%, due August 02, 2020)	7,500,000	5,687,886	6,356,250	
Total Collateralized Loan Obligation Debt Investments				$39,886,277	$43,590,783	50.50%

(Continued on next page)

See Accompanying Notes

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OXFORD LANE CAPITAL CORP.

SCHEDULE OF INVESTMENTS (continued) SEPTEMBER 30, 2012 (Unaudited)

COMPANY[1]	INDUSTRY	INVESTMENT	PRINCIPAL AMOUNT	COST	FAIR VALUE[2]	% of Net Assets
Collateralized Loan Obligation Equity Investments						
ACA CLO 2007-1A	structured finance	CLO income notes[4][6] (Estimated yield 15.50%, maturity June 15, 2022)	12,212,500	9,191,429	11,357,625	
Canaras Summit CLO 2007-1X	structured finance	CLO income notes[4][6] (Estimated yield 22.95%, maturity June 19, 2021)	1,500,000	902,036	1,800,000	
Carlyle Global Market Strategies CLO 2011-1X	structured finance	CLO income notes[4][6] (Estimated yield 15.30%, maturity August 10, 2021)	6,000,000	5,290,512	6,600,000	
Gale Force 4 CLO 2007-4A	structured finance	CLO income notes[4][6] (Estimated yield 16.30%,	1,500,000	821,464	1,380,000	

		maturity August 20, 2021)			
Harbourview CLO 2006-1	structured finance	CLO income notes(4)(6) (Estimated yield 22.30%, maturity December 27, 2019)	4,380,000	2,399,320	4,215,750
Hillmark Funding Ltd. 2006-1A	structured finance	CLO income notes(4)(6) (Estimated yield 18.90%, maturity May 21, 2021)	2,000,000	1,218,263	1,800,000
Jersey Street CLO 2006-1A	structured finance	CLO income notes(4)(6) (Estimated yield 20.00%, maturity October 20, 2018)	3,185,000	1,988,319	3,185,000
Kingsland IV, Ltd. 2007-4A	structured finance	CLO income notes(4)(6) (Estimated yield 16.70%, maturity April 16, 2021)	2,350,000	1,712,415	2,655,500
Lightpoint CLO VII, Ltd. 2007-7X	structured finance	CLO income notes(4)(6) (Estimated yield 22.38%, maturity May 15, 2021)	2,000,000	1,096,719	1,800,000
Octagon XI CLO 2007-1A	structured finance	CLO income notes(4)(6)	2,025,000	1,408,771	2,430,000

		(Estimated yield 19.76%, maturity August 25, 2021)				
Rampart CLO 2007-1A	structured finance	CLO income notes(4)(6) (Estimated yield 15.30%, maturity October 25, 2021)	1,500,000	1,011,986	1,575,000	
Total Collateralized Loan Obligation Investments		Equity		$27,041,234	$38,798,875	44.95%
Total Investments				$66,927,511	$82,389,658	95.45%

(1) We do not control and are not an affiliate of any of our portfolio companies, each as defined in the Investment Company Act of 1940 (the 1940 Act). In general, under the 1940 Act, we would be presumed to control a portfolio company if we owned 25% or more of its voting securities and would be an affiliate of a portfolio company if we owned 5% or more of its voting securities.

(2) Fair value is determined in good faith by the Board of Directors of the Company.

(3) Notes bear interest at variable rates.

(4) Cost value reflects accretion of original issue discount or market discount, and amortization of premium.

(5) The CLO secured notes generally bear interest at a rate determined by reference to LIBOR which resets quarterly. For each CLO debt investment, the rate provided is as of September 30, 2012.

(6) The CLO income notes are considered equity investments. Equity investments are entitled to recurring distributions which are generally equal to the remaining cash flow of the payments made by the underlying fund's securities less contractual payments to debt holders and fund expenses. The estimated yield indicated is based upon a current projection of the amount and timing of these recurring distributions and the estimated amount of repayment of principal upon termination. Such projections are periodically reviewed and adjusted, and the estimated yield may not ultimately be realized.

See Accompanying Notes

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OXFORD LANE CAPITAL CORP.

STATEMENT OF OPERATIONS
(Unaudited)

	Six Months Ended September 30, 2012
INVESTMENT INCOME	
Interest income	$ 4,426,952
EXPENSES	
Investment advisory fees	700,310
Incentive fees	595,142
Professional fees	205,956
Administrator expense	234,530
Directors' fees	97,000
General and administrative	172,049
Insurance expense	18,300
Transfer agent and custodian fees	23,098
Total expenses	2,046,385
Net investment income	2,380,567
Net change in unrealized appreciation on investments	13,717,732
Net realized gain (loss) on investments	
Net realized and unrealized gain on investments	13,717,732
Net increase in net assets resulting from operations	$ 16,098,299

See Accompanying Notes

OXFORD LANE CAPITAL CORP.

STATEMENT OF CHANGES IN NET ASSETS (Unaudited)

	Six Months Ended September 30, 2012	Year Ended March 31, 2012
Increase in net assets from operations:		
Net investment income	$ 2,380,567	$ 2,630,828
Net realized gain (loss) on investments		
Net change in unrealized appreciation on investments	13,717,732	1,786,915
Net increase in net assets resulting from operations	16,098,299	4,417,743
Distributions from net investment income	(5,481,875)	(4,736,315)
Capital share transaction:		
Issuance of common stock (net of underwriting fees and offering costs)	32,771,348	8,283,284
Reinvestment of dividends	1,054,125	51,693
Net increase in net assets from capital share transactions	33,825,473	8,334,977
Total increase in net assets	44,441,897	8,016,405
Net assets at beginning of period	41,879,201	33,862,796
Net assets at end of period (including distributions in excess of net investment income of $5,527,513 and $2,426,205)	$ 86,321,098	$ 41,879,201

See Accompanying Notes

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OXFORD LANE CAPITAL CORP.

STATEMENT OF CASH FLOWS (Unaudited)

	Six Months Ended September 30, 2012
CASH FLOWS FROM OPERATING ACTIVITIES	
Net increase in net assets resulting from operations	$ 16,098,299
Adjustments to reconcile net increase in net assets resulting from operations to net cash used in operating activities:	
Amortization of discounts and premiums	(3,229,246)
Purchases of investments	(30,878,220)
Repayments of principal and reductions to investment cost value	5,959,907
Net change in unrealized appreciation on investments	(13,717,732)
Decrease in deferred offering costs	149,039
Increase in dividend receivable	(1,025,507)
Increase in interest receivable	(158,455)
Decrease in prepaid expenses and other assets	5,823
Increase in investment advisory fee payable	180,977
Increase in incentive fee payable	125,936
Decrease in directors' fees payable	(13,500)
Increase in administrator expense payable	24,412
Decrease in accrued offering costs	(107,981)
Increase in accrued expenses	8,789
Net cash used in operating activities	(26,577,459)
CASH FLOWS FROM FINANCING ACTIVITIES	
Distributions paid (net of stock issued under dividend reinvestment plan of $1,054,125)	(4,427,750)
Proceeds from the issuance of common stock	34,488,713
Underwriting fees and offering costs for the issuance of common stock	(1,717,365)
Net cash provided by financing activities	28,343,598
Net increase in cash and cash equivalents	1,766,139
Cash and cash equivalents, beginning of period	1,615,609
Cash and cash equivalents, end of period	$ 3,381,748

See Accompanying Notes

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OXFORD LANE CAPITAL CORP.

NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2012

NOTE 1. ORGANIZATION

Oxford Lane Capital Corp. (OXLC , we or the Fund) was incorporated under the General Corporation Laws of the State of Maryland on June 9, 2010 as a non-diversified closed-end management investment company that has registered as an investment company under the Investment Company Act of 1940, as amended (the 1940 Act). In addition, the Fund has elected to be treated for tax purposes as a regulated investment company, or RIC under Subchapter M of the Internal Revenue Code of 1986, as amended (the Code). The Fund s investment objective is to maximize its portfolio s total return and seeks to achieve its investment objective by investing primarily in senior secured loans and the equity and junior debt tranches of collateralized loan obligation (CLO) vehicles.

On January 25, 2011, the Fund closed its initial public offering and sold 1,825,000 shares of its common stock at a price of $20.00 per share, less an underwriting discount of $1.40 per share and offering expenses of approximately $362,000. Certain of OXLC's directors and officers purchased shares at the public offering price. On February 24, 2011, the Fund issued an additional 30,000 shares of its common stock at the same price pursuant to the underwriters' overallotment. The total net proceeds to the Fund from the initial public offering, including the exercise of the overallotment, were approximately $34.1 million.

OXLC s investment activities are managed by Oxford Lane Management LLC, (OXLC Management), a registered investment adviser under the Investment Advisors Act of 1940, as amended. BDC Partners LLC (BDC Partners) is the managing member of OXLC Management and serves as the administrator of OXLC.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

USE OF ESTIMATES

The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America, which require management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

In the normal course of business, the Fund may enter into contracts that contain a variety of representations and provide indemnifications. The Fund s maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet occurred. However, based upon experience, the Fund expects the risk of loss to be remote.

CASH AND CASH EQUIVALENTS

The Fund considers all highly liquid debt instruments with a maturity of three months or less at the time of purchase to be cash equivalents.

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NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2012

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

INVESTMENT VALUATION

The most significant estimates made in the preparation of the Fund s financial statements are the valuation of investments and the related amounts of unrealized appreciation and depreciation of investments recorded. OXLC believes that there is no single definitive method for determining fair value in good faith. As a result, determining fair value requires that judgment be applied to the specific facts and circumstances of each portfolio investment while employing a consistently applied valuation process for the types of investments OXLC makes. The Fund is required to specifically fair value each individual investment on a quarterly basis.

In May 2011, the FASB issued ASU 2011-04, *Fair Value Measurement which represents amendments to achieve common fair value measurement and disclosure requirements in US GAAP and IFRS.* The amendments are of two types: (i) those that clarify the FASB s intent about the application of existing fair value measurement and disclosure requirements and (ii) those that change a particular principle or requirement for measuring fair value or for disclosing information about fair value measurements. The amendments that change a particular principle or requirement for measuring fair value or disclosing information about fair value measurements relate to (i) measuring the fair value of the financial instruments that are managed within a portfolio; (ii) application of premium and discount in a fair value measurement; and (iii) additional disclosures about fair value measurements. The update is effective for interim and annual periods beginning after December 15, 2011 and as such OXLC has adopted this ASU beginning with the six months ended September 30, 2012. OXLC has increased its disclosures related to Level 3 fair value measurement, in addition to other required disclosures. There were no related impacts on OXLC s financial position or results of operations.

The Fund complies with ASC 820-10, *Fair Value Measurements and Disclosure*, which establishes a three-level valuation hierarchy for disclosure of fair value measurements. ASC 820-10 clarified the definition of fair value and requires companies to expand their disclosure about the use of fair value to measure assets and liabilities in interim and annual periods subsequent to initial recognition. ASC 820-10 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820-10 also establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include: Level 1, defined as observable inputs such as quoted prices in active markets; Level 2, which includes inputs such as quoted prices for similar securities in active markets and quoted prices for identical securities in markets that are not active; and Level 3, defined as unobservable inputs for which little or no market data exists, therefore requiring an entity to develop its own assumptions. The Fund has determined that due to the general illiquidity of the market for the Fund s investment portfolio, whereby little or no market data exists, all of the Fund s investments are valued based upon Level 3 inputs as of September 30, 2012. The Fund s Board of Directors determines the value of OXLC s investment portfolio each quarter. The prices used by the Fund to value securities may differ from the value that would be realized if the securities were sold, and these differences could be material to the Fund s financial statements.

During the past several quarters, OXLC has acquired a number of debt and equity positions in collateralized loan obligation (CLO) investment vehicles, which are special purpose financing vehicles. In valuing such investments, OXLC considers the operating metrics of the specific investment vehicle, including compliance with collateralization tests, defaulted and restructured securities, and payment defaults, if any. In addition, OXLC considers indicative prices provided by a recognized industry pricing service as well as the indicative prices provided by the broker who arranges transactions in such investment vehicles, to the extent available, as well as any available information on other relevant transactions including trades, if any, and firm bids and offers in the market. OXLC Management or the Valuation Committee may request an additional

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NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2012

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

analysis by a third-party firm to assist in the valuation process of CLO investment vehicles. All information is presented to the Board for its determination of fair value of these investments.

The Fund may also invest directly in senior secured loans (either in the primary or secondary markets). In valuing such investments, OXLC Management will prepare an analysis of each loan, including a financial summary, covenant compliance review, recent trading activity in the security, if known, and other business developments related to the portfolio company. All available information, including non-binding indicative bids obtained from a recognized industry pricing service and large agent banks which may not be considered reliable, will be presented to the Valuation Committee of the Board to consider in its determination of fair value. In some instances, there may be limited trading activity in a security even though the market for the security is considered not active. In such cases the Board will consider the number of trades, the size and timing of each trade and other circumstances around such trades, to the extent such information is available, in its determination of fair value. At September 30, 2012, the Fund did not have any direct investments in senior secured loans.

ASC 820-10-35, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly*, provides guidance on factors that should be considered in determining when a previously active market becomes inactive and whether a transaction is orderly. In accordance with ASC 820-10-35, the Fund s valuation procedures specifically provide for the review of indicative quotes supplied by the brokers or large agent banks that make a market for each CLO investment or senior secured loan, respectively.

The Fund s assets measured at fair value on a recurring basis subject to the disclosure requirements of ASC 820-10-35 at September 30, 2012, were as follows:

($ in millions)	Fair Value Measurements at Reporting Date Using			
Assets	Quoted Prices in Active Markets for Identical Assets	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total

	(Level 1)			
CLO debt	$	$	$ 43.6	$ 43.6
CLO equity			38.8	38.8
Total	$	$	$ 82.4	$ 82.4

Significant Unobservable Inputs for Level 3 Investments

In accordance with ASU 2011-04, the following table provides quantitative information about the Company s Level 3 fair value measurements as of September 30, 2012. The Company s valuation policy, as described above, establishes parameters for the sources and types of valuation analysis, as well as the methodologies and inputs that the Company uses in determining fair value. If the Valuation Committee or OXLC Management determines that additional techniques, sources or inputs are appropriate or necessary in a given situation, such additional work will be undertaken. The table, therefore, is not all-inclusive, but provides information on the significant Level 3 inputs that are pertinent to the Company s fair value measurements. The weighted average calculations in the table below are based on principal balances for all CLO debt and equity investments.

($ in millions)	Quantitative Information about Level 3 Fair Value Measurements				
Assets	Fair Value as of September 30, 2012	Valuation Techniques/Methodologies	Unobservable Input	Range/Weighted Average	
CLO debt	$43.6	market quotes	NBIB [(1)]	72.83%	91.66%/80.59%
CLO equity	38.8	market quotes	NBIB [(1)]	90.0%	120.0%/100.38%
Total Fair Value for Level 3 Investments	$82.4				

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OXFORD LANE CAPITAL CORP.

NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2012

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(1) The Company generally uses prices provided by an independent pricing service or broker or agent bank non-binding indicative bid prices (NBIB) on or near the valuation date as the primary basis for the fair value determinations for CLO debt and equity investments. These bid prices are non-binding, and may not be determinative of fair value. Each bid price is evaluated by the Valuation Committee in conjunction with additional information compiled by OXLC Management, including actual trades and firm bids and offers, if any, financial performance, recent business developments, and, in the case of CLO debt and equity investments, performance and covenant compliance information as provided by the independent trustee.

Significant increases or decreases in any of the unobservable inputs in isolation may result in a significantly lower or higher fair value measurement.

A rollforward of the fair value of investments for the six months ended September 30, 2012, utilizing significant unobservable inputs, is as follows:

($ in millions)	Collateralized Loan Obligation Debt Investments	Collateralized Loan Obligation Equity Investments	Total
Balance at March 31, 2012	$ 23.3	$ 17.2	$40.5
Realized gains included in earnings	0.0	0.0	0.0
Unrealized appreciation (depreciation) included in earnings	4.8	8.9	13.7
Amortization of discounts and premiums	0.5	2.7	3.2
Purchases	15.0	15.9	30.9
Repayments, sales of principal and reductions to investment cost value	0.0	(5.9)	(5.9)
Transfers in and/or out of level 3	0.0	0.0	0.0
Balance at September 30, 2012	$ 43.6	$ 38.8	$82.4
The amount of total gains for the period included in earnings attributable to the change in unrealized gains or losses related to our Level 3 assets still held at the reporting date and reported within the net change in unrealized gains or losses on investments in our Statement of Operations	$ 4.8	$ 8.9	$13.7

The Fund s policy is to recognize transfers in and transfers out of valuation levels as of the beginning of the reporting period. There were no transfers between Level 1, Level 2 and Level 3 during the six months ended September 30, 2012.

PREPAID EXPENSES

Prepaid expenses consist primarily of insurance costs.

INVESTMENT INCOME RECOGNITION

Interest income from debt positions in CLO investment vehicles is recorded on the accrual basis to the extent that such amounts are expected to be collected. Amortization of premium or accretion of discount is recognized on the effective yield method.

Interest income from investments in the equity class of security of CLO investment vehicles (typically income notes or subordinated notes) is recorded based upon an estimation of an effective yield to maturity utilizing assumed cash flows. The Fund monitors the expected cash flows from its CLO equity investments, including the expected residual payments, and the effective yield is determined and updated periodically.

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OXFORD LANE CAPITAL CORP.

NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2012

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

FEDERAL INCOME TAXES

The Fund intends to operate so as to qualify to be taxed as a RIC under Subchapter M of the Internal Revenue Code and, as such, to not be subject to federal income tax on the portion of its taxable income and gains distributed to stockholders. To qualify for RIC tax treatment, OXLC is required to distribute at least 90% of its investment company taxable income, as defined by the Code.

Because federal income tax regulations differ from accounting principles generally accepted in the United States, distributions in accordance with tax regulations may differ from net investment income and realized gains recognized for financial reporting purposes. Differences may be permanent or temporary. Permanent differences are reclassified among capital accounts in the financial statement to reflect their tax character. Temporary differences arise when certain items of income, expense, gain or loss are recognized at some time in the future. Differences in classification may also result from the treatment of short-term gains as ordinary income for tax purposes.

The tax basis components of distributable earnings differ from the amounts reflected in the Statement of Assets and Liabilities due to temporary book/tax differences primarily arising from investments in equity CLOs and permanent book/tax differences attributable to non-deductible excise taxes. These amounts will be finalized before filing the federal tax return.

At September 30, 2012, net unrealized appreciation for tax purposes is $8,022,843, which includes aggregate gross unrealized appreciation of $8,697,214; and aggregate gross unrealized depreciation of $674,371. For tax purposes, the cost basis of the portfolio investments at September 30, 2012 was approximately $74,366,815.

DIVIDENDS AND DISTRIBUTIONS

Dividends from net investment income and capital gain distributions are determined in accordance with U.S. federal income tax regulations, which differ from GAAP. Dividends from net investment income, if any, are expected to be declared and paid quarterly. Net realized capital gains, unless offset by any available capital loss carry-forward, are typically distributed to shareholders annually. Dividends and distributions to shareholders are recorded on the ex-dividend date and are automatically reinvested in full and fractional shares of the Fund in accordance with the Fund s dividend reinvestment plan unless the shareholder has elected to have them paid in cash.

Amounts required to be distributed reflect estimates made by the Fund. Dividends paid by the Fund are subject to re-characterization for tax purposes.

CONCENTRATION OF CREDIT RISK

At September 30, 2012, the Fund maintained a cash balance with State Street Bank and Trust Co. The Fund is subject to credit risk arising should State Street Bank and Trust Co. be unable to fulfill its obligations. In addition, the Fund s portfolio may be concentrated in a limited number of investments in CLO vehicles, which will subject the Fund to a risk of significant loss if that sector experiences a market downturn.

SECURITIES TRANSACTIONS

Securities transactions are recorded on trade date. Realized gains and losses on investments sold are recorded on the basis of specific identification.

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OXFORD LANE CAPITAL CORP.

NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2012

NOTE 3. RELATED PARTY TRANSACTIONS

Effective September 9, 2010, the Fund entered into an Investment Advisory Agreement with OXLC Management, a registered investment adviser under the Investment Advisers Act of 1940, as amended. BDC Partners is the managing member of OXLC Management and serves as the administrator of OXLC. Pursuant to the Investment Advisory Agreement, the Fund has agreed to pay OXLC Management a fee for advisory and management services consisting of two components a base management fee and an incentive fee. The base-management fee is calculated at an annual rate of 2.00% of the Fund s gross assets. For services rendered under the Investment Advisory Agreement, the base management fee is payable quarterly in arrears.

The base management fee is calculated based on the average value of the Fund s gross assets, which means all assets of any type, at the end of the two most recently completed calendar quarters, and appropriately adjusted for any share issuances or repurchases during the current calendar quarter. Base management fees for any partial month or quarter will be appropriately pro-rated.

The incentive fee is calculated and payable quarterly in arrears based on the pre-incentive fee net investment income for the immediately preceding calendar quarter. For this purpose, pre-incentive fee net investment income means interest income, dividend income and any other income (including any other fees, such as commitment, origination, structuring, diligence and consulting fees or other fees that are received from an investment) accrued during the calendar quarter, minus our operating expenses for the quarter (including the base management fee, expenses payable under the Administration Agreement to BDC Partners, and any interest expense and dividends paid on any issued and outstanding preferred stock, but excluding the incentive fee). Pre-incentive fee net investment income includes accrued income that the Fund has not yet received in cash. Pre-incentive fee net investment income does not include any realized or unrealized capital gains or losses, and the Fund could incur incentive fees in periods when there is a net decrease in net assets from operations. Pre-incentive fee net investment income, expressed as a rate of return on the value of the Fund s net assets at the end of the immediately preceding calendar quarter, is compared to a hurdle of 1.75% per quarter (7.00% annualized). Our undistributed net investment income used to calculate the incentive fee is also included in the amount of the Fund s gross assets used to calculate the 2.00% base management fee. The incentive fee with respect to the Fund s pre-incentive fee net investment income in each calendar quarter is calculated as follows:

no incentive fee in any calendar quarter in which the Fund s pre-incentive fee net investment income does not exceed the hurdle of 1.75%;

100% of pre-incentive fee net investment income with respect to that portion of such pre-incentive fee net investment income, if any, that exceeds the hurdle but is less than 2.1875% in any calendar quarter (8.75% annualized). The Fund refers to this portion of the pre-incentive fee net investment income (which exceeds the hurdle but is less than 2.1875%) as the catch-up. The catch-up is meant to provide the investment adviser with 20% of the pre-incentive fee net investment income as if a hurdle did not apply if the net investment income exceeds 2.1875% in any calendar quarter; and

20% of the amount of pre-incentive fee net investment income, if any, that exceeds 2.1875% in any calendar quarter (8.75% annualized) is payable to OXLC Management (once the hurdle is reached and the catch-up is achieved, 20% of all pre-incentive fee net investment income thereafter is allocated to OXLC Management).

There is no offset in subsequent quarters for any quarter in which an incentive fee is not earned. For the six months ended September 30, 2012, the Fund accrued incentive fee expenses of approximately $595,000. At September 30, 2012, the Fund has an incentive fee payable of approximately $331,000.

Effective September 9, 2010 the Fund entered into an administration agreement with BDC Partners to serve as its administrator. Under the administration agreement, BDC Partners performs, or oversees the performance of, the Fund s required administrative services, which include, among other things, being

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OXFORD LANE CAPITAL CORP.

NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2012

NOTE 3. RELATED PARTY TRANSACTIONS (continued)

responsible for the financial records which the Fund is required to maintain and preparing reports to the Fund s stockholders. In addition, BDC Partners assists the Fund in determining and publishing the Fund s net asset value, oversees the preparation and filing of the Fund s tax returns and the printing and dissemination of reports to the Fund s stockholders, and generally oversees the payment of the Fund s expenses and the performance of administrative and professional services rendered to the Fund by others. Payments under the administration agreement are equal to an amount based upon the Fund s allocable portion of BDC Partners overhead in performing its obligations under the administration agreement, including rent, the fees and expenses associated with performing compliance functions and the Fund s allocable portion of the compensation of the Fund s chief financial officer, chief compliance officer, controller and treasurer, and any administrative support staff. The administration agreement may be terminated by either party without penalty upon 60 days written notice to the other party.

The independent directors receive an annual fee of $35,000. In addition, the independent directors receive $2,000 plus reimbursement of reasonable out-of-pocket expenses incurred in connection with attending each Board meeting, $1,500 plus reimbursement of reasonable out-of-pocket expenses incurred in connection with attending each Valuation Committee meeting and $1,000 plus reimbursement of reasonable out-of-pocket expenses incurred in connection with attending each Audit Committee meeting. The Chairman of the Audit Committee also receives an additional annual fee of $5,000. No compensation will be paid to directors who are interested persons of the Fund as defined in the 1940 Act.

Certain directors, officers and other related parties, including members of OXLC Management, own 6.8% of the Fund at September 30, 2012.

NOTE 4. OTHER INCOME

Other income includes closing fees, or origination fees, associated with investments in portfolio companies. Such fees are normally paid at closing of the Fund s investments, are fully earned and non-refundable, and are generally non-recurring. The Fund had no such income for the six months ended September 30, 2012.

NOTE 5. RIGHTS OFFERING

On April 11, 2012 (the Record Date) the Fund issued non-transferable rights to purchase common stock to its stockholders of record (Record Date Stockholders). Record Date Stockholders received four rights for each outstanding share of common stock owned on the record date. The rights entitled the holders to purchase one new share of common stock for every one right held. On April 27, 2012, the Fund closed its rights offering and sold 2,508,270 shares of its common stock at a price of $13.75 per share, less underwriting fees and offering costs of approximately $1.7 million. The total net proceeds to the Fund from the issuance of non-transferable rights to common stock to Record Date Stockholders were approximately $32.8 million.

NOTE 6. PURCHASES AND SALES OF SECURITIES

Purchases and sales of securities, excluding short-term investments and prepayments, for the six months ended September 30, 2012, totaled approximately $30.9 million and $0, respectively.

NOTE 7. COMMITMENTS

In the normal course of business, the Fund enters into a variety of undertakings containing warranties and indemnifications that may expose the Fund to some risk of loss. The risk of future loss arising from such undertakings, while not quantifiable, is expected to be remote.

As of September 30, 2012, the Fund had not issued any commitments to purchase additional debt or equity investments from any portfolio companies.

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OXFORD LANE CAPITAL CORP.

NOTES TO FINANCIAL STATEMENTS SEPTEMBER 30, 2012

NOTE 8. INDEMNIFICATION

Under the Fund s organizational documents, its officers and directors are indemnified against certain liabilities arising out of the performance of their duties to the Fund. In addition, in the normal course of business the Fund enters into contracts that contain a variety of representations which provide general indemnifications. The Fund s maximum exposure under these agreements cannot be known; however, the Fund expects any risk of loss to be remote.

NOTE 9. FINANCIAL HIGHLIGHTS

Financial highlights for the six months ended September 30, 2012, the year ended March 31, 2012 and for the period January 25, 2011 (Commencement of Operations) to March 31, 2011 are as follows:

	Six Months Ended September 30, 2012	Year Ended March 31, 2012	January 25, 2011 (Commencement of Operations) to March 31, 2011
Per Share Data			
Net asset value at beginning of period[1]	$ 17.05	$ 18.19	$ 16.80
Net investment income[2]	0.52	1.19	0.07
Net realized and unrealized capital gains (loss)	3.00	0.83	(0.03)
Total from investment operations	3.52	2.02	0.04
Less Distributions per share from net investment income	(1.10)	(2.05)	(0.25)
Less Distributions per share based on weighted average share impact[3]	(0.34)	(0.10)	
Total distributions[4]	(1.44)	(2.15)	(0.25)
Effect of shares issued, net of underwriting expense[5]	(1.65)	(0.77)	1.79
Effect of offering costs[5]	(0.35)	(0.24)	(0.19)
Effect of shares issued, net[5]	(2.00)	(1.01)	1.60
Net asset value at end of period	$ 17.13	$ 17.05	$ 18.19
Per share market value at beginning of period	$ 14.60	$ **% of Sales**	
Medical	$ 3,733	7%	$ 2,142 5%

EMS	(1,189)	(3)	(526)	(1)
DSS	9,861	21	(100)	(0)
Other unallocated	(8,939)		(5,523)	
Totals	$ 3,466	3	$ (4,007)	(2)

On a consolidated basis, selling and administrative expenses for the nine months ended March 31, 2010 decreased by approximately $0.2 million, compared to the same period in the prior year, reflecting decreased costs resulting from facility closings and cost reduction activities, legal fees in fiscal 2009 related to Electropac litigation, partially offset by increased expenses related to the Company s short-term incentive plan and stock-based compensation.

Other operating expenses were $1.1 million and $20,000 for the nine months ended March 31, 2010 and 2009, respectively. Current year expenses primarily represent ongoing carrying costs for facilities held for sale.

Restructuring/impairment charges were $2.1 million and $0.7 million for the nine months ended March 31, 2010 and 2009, respectively, of which $1.0 million and $0.6 million were included in the EMS operating results for those periods. For a further discussion of the restructuring activity see Note 11 to the Unaudited Condensed Consolidated Financial Statements.

Interest expense consists of interest and fees on our outstanding debt and revolving credit facility (see Note 6 to the Unaudited Condensed Consolidated Financial Statements), including amortization of financing costs. Interest expense was $0.7 million for the nine months ended March 31, 2010 compared to $1.3 million for the nine months ended March 31, 2009. The decrease primarily reflects the repayment of the Company s line-of-credit and bank term debt with available cash on August 14, 2009.

The fiscal 2010 nine month period reflects a gain on sale of investment of $0.2 million from the sale of part of the Company s interest in Cybernet. See Note 2 to the Unaudited Condensed Consolidated Financial Statements for a further discussion of this sale. Translation adjustments, not related to costs of goods sold, along with gains and losses from foreign currency transactions, in the aggregate, amounted to losses of $24,000 and $1.3 million for the nine months ended March 31, 2010 and 2009, respectively. The Canadian dollar experienced significant volatility against the U.S. dollar during the nine months ended March 31, 2009. With the closure of the Canadian facility, however, the impact in fiscal 2010 has not been significant and it is anticipated that future periods will not be significant. Other income for the nine months ended March 31, 2010 was $0.2 million, versus $9,000 in the same period of fiscal 2009.

The Company is responsible for income taxes within each jurisdiction. The Company recorded an income tax benefit of approximately $2.0 million for the nine months ended March 31, 2010, compared to expense of $0.4 million for the same period in the prior year. The fiscal 2010 benefit reflects the release of $2.3 million of deferred tax asset valuation allowance in relation to recent tax regulation changes. See Note 2 to the Unaudited Condensed Consolidated Financial Statements for a further discussion of income taxes.

Due to the factors described above, the Company reported net income of $5.3 million ($0.54 per share, basic and diluted) for the nine months ended March 31, 2010, compared to a net loss of $6.9 million ($(0.70) per share, basic and diluted) for the corresponding period last year.

Liquidity and Capital Resources

During fiscal 2009, the Company generated $38.2 million of operating cash flows, primarily due to reductions in inventory levels and certain DSS contracts allowing for billings to occur when certain milestones under the applicable program are reached, independent of the amount expended as of that point. These billings reduce the amount of cash that would otherwise be required during the performance of these contracts. As of March 31, 2010 and June 30, 2009, $12.2 million and $25.1 million, respectively, of billings in excess of costs were received. The Company currently expects to meet its liquidity needs through a combination of sources including, but not limited to, operations, its line-of-credit, anticipated continuation of interim billings on certain DSS contracts, the potential proceeds from sales of closed facilities, and improved cash flow from changes in how the Company manages inventory. It is currently anticipated that usage of the line-of-credit and interim government billings will continue to be a component in providing Sparton s working capital. With the above sources providing the expected cash flows, the Company currently believes that it will have sufficient liquidity for our anticipated needs over the next 12 months, but no assurances regarding liquidity can be made.

For the nine months ended March 31, 2010, cash and cash equivalents decreased $20.1 million to $16.1 million. Operating activities provided $5.0 million in fiscal 2010 and $6.5 million in fiscal 2009 in net cash flows. The primary use of cash from operating activities in fiscal 2010 was the payment of accounts payable and accrued liabilities and the funding of production related to U.S. Navy contracts. Payables and accrued liabilities have decreased as a result of the closing of facilities, reduced volume of inventory purchases, cash outlays relating to restructuring activities and pension contributions made in the first quarter of fiscal 2010. A primary source of cash from operating activities in fiscal 2010 was the decrease in accounts receivable, reflective of collections on government milestone contracts, collection of receivables from disengaging customers, income taxes recovered from net operating loss carrybacks, and the large volume of sales during the fourth quarter of fiscal 2009. A second primary source of cash from operating activities in fiscal 2010 was the decrease in inventories, reflecting the Company s continued inventory management efforts. The primary use of cash from operating activities in fiscal 2009 was for the funding of operating losses, while the primary source of cash in fiscal 2009 was the decrease in inventories, primarily due to the Company s focus on reducing the level of inventory carried.

Cash flows used in investing activities in fiscal 2010 and 2009 totaled $4.2 million and $2.1 million, respectively. Fiscal 2010 reflects the utilization of $3.1 million to establish a trust, the Sparton Corporation Financial Assurance Trust, related to environmental remediation activities at one of Sparton s former facilities. The funds are held in Sparton s name and are invested with Sparton receiving the benefit of the investment return. Investment returns on the funds during the nine month period totaled approximately $0.1 million. These funds are available for use to satisfy the $4.7 million of expected remediation liability reflected in the March 31, 2010 balance sheet. For further discussion of this remediation activity, see Commitments and Contingencies below. Both nine month periods reflect the payment of contingent purchase consideration to the prior owners of Astro. Capital expenditures for the nine months ended March 31, 2010 and 2009 were $1.0 million and $1.1 million, respectively. Fiscal 2010 reflects approximately $0.5 million in proceeds from the sale of property, plant and equipment in relation to the closing of its Jackson, Michigan and London, Ontario, Canada plants. In addition, fiscal 2010 reflects the proceeds from the sale of a portion of its interest in Cybernet totaling approximately $0.5 million.

Cash flows used in financing activities in fiscal 2010 and 2009 totaled $20.9 million and $1.1 million, respectively. The primary uses of cash from financing activities in fiscal 2010 and 2009 were the repayment of debt. Fiscal 2010 also reflects the payment of financing fees related to the Company s new revolving credit facility. The primary source of cash from financing activities in fiscal 2009 was from increased borrowings on the Company s bank line-of-credit facility. In the nine months ended March 31, 2010, the Company paid off the existing balance on its line-of-credit facility totaling $15.5 million, and the $3.4 million remaining balance on its term loan, with National City Bank.

As of March 31, 2010, the Company s bank line-of-credit facility totaled $20.0 million, with no borrowings against the available funds. This bank debt is subject to certain customary covenants which were met at March 31, 2010. The maturity date for this line-of-credit is August 14, 2012. There are notes payable totaling $1.0 million outstanding to the former owners of Astro, as well as $1.9 million of industrial revenue bonds. Borrowings are discussed further in Note 6 to the Unaudited Condensed Consolidated Financial Statements.

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During fiscal 2009, management initiated a full evaluation of the Company s operations and long-term business strategy. As a result, in the third fiscal quarter, management began to implement a formal turnaround plan focused on returning Sparton to profitability and the assurance of the Company s viability. These measures have been designed to reduce operating costs, increase efficiencies, and improve our competitive position in response to excess capacity, the prevailing economy and the need to optimize manufacturing resources. These restructuring activities included, among other actions, plant consolidation and closures, workforce reductions, customer contract disengagements, and changes in employee pension and health care benefits. While the majority of these restructuring activities were completed as of March 31, 2010, the Company expects to incur approximately $0.1 million of additional restructuring expenses during the remainder of fiscal 2010, with restructuring related cash payments of approximately $0.9 million in future quarters.

Commitments and Contingencies

Environmental Remediation

One of Sparton s former manufacturing facilities, located in Albuquerque, New Mexico (Coors Road), has been involved with ongoing environmental remediation since the early 1980 s. At March 31, 2010, Sparton had accrued approximately $4.7 million as its best estimate of the remaining minimum future undiscounted financial liability with respect to this matter, of which approximately $0.5 million is classified as a current liability and included on the balance sheet in other accrued liabilities. The Company s minimum cost estimate is based upon existing technology and excludes legal and related consulting costs, which are expensed as incurred. The Company s estimate includes equipment and operating and maintenance costs for onsite and offsite pump and treat containment systems, as well as continued onsite and offsite monitoring. It also includes periodic reporting requirements.

On October 15, 2009, approximately $3.1 million of cash was utilized to establish a trust, the Sparton Corporation Financial Assurance Trust, for remediation activity. The funds are held in Sparton s name and are invested with Sparton receiving the benefit of the investment return. As of March 31, 2010, approximately $3.2 million was held in this trust. These funds are available for use against the $4.7 million expected remediation liability. The trust was established to meet the United States Environmental Protection Agency s (EPA) financial assurance requirements for the fiscal year ending June 30, 2010, with trust funds to be drawn upon only should Sparton not continue to meet its financial remediation requirements. The trust will remain in place until the Company can again satisfy the EPA financial assurance requirements through compliance with financial ratios, as was previously attained on an annual basis until fiscal year 2009. Upon the successful compliance with the financial ratios, the Company will be able to dissolve the trust. The Company s first opportunity, under the annual filing requirements, to again regain compliance with the financial ratios is expected to be upon completion of the June 30, 2010 fiscal year.

In fiscal 2003, Sparton reached an agreement with the United States Department of Energy (DOE) and others to recover certain remediation costs. Under the settlement terms, Sparton received cash and obtained some degree of risk protection as the DOE agreed to reimburse Sparton for 37.5% of certain future environmental expenses in excess of $8.4 million incurred from the date of settlement, if any, of which approximately $3.1 million has been incurred as of March 31, 2010 toward the $8.4 million threshold. Uncertainties associated with environmental remediation contingencies are pervasive and often result in wide ranges of reasonably possible outcomes. Estimates developed in the early stages of remediation can vary significantly. Normally a finite estimate of cost does not become fixed and determinable at a specific point in time. Rather, the costs associated with environmental remediation become estimable over a continuum of events and activities that help to frame and define a liability. Factors which cause uncertainties for the Company include, but are not limited to, the effectiveness of the current work plans in achieving targeted results and proposals of regulatory agencies for desired methods and outcomes. It is possible that cash flows and results of operations could be materially affected by the impact of changes associated with the ultimate resolution of this contingency.

Customer Relationships

The Company had an action before the U.S. Court of Federal Claims to recover damages arising out of an alleged infringement by the U.S. Navy of certain patents held by Sparton and used in the production of sonobuoys. Pursuant to an agreement between the Company and counsel conducting the litigation, a significant portion of the claim will be retained by the Company s counsel in contingent fees if the litigation is successfully concluded. A trial of the matter was conducted by the court in April 2008, with a decision against Sparton filed in August 2009 and published in September 2009. In October 2009, an appeal of this unfavorable decision was filed with the Federal Circuit Court of Appeals. Based on this decision, management believes that the Company s ability to obtain any recovery with respect to the claim is greatly diminished.

Product Issues

Some of the printed circuit boards supplied to the Company for its aerospace sales were discovered in fiscal 2005 to be nonconforming and defective. The defect occurred during production at the raw board supplier s facility, prior to shipment to Sparton for further processing. The Company and our customer, who received the defective boards, contained the defective boards. While investigations were underway, $2.8 million of related product and associated incurred costs were initially deferred and classified in Sparton s balance sheet within other non-current assets.

In August 2005, Sparton Electronics Florida, Inc. filed an action in the U.S. District Court, Middle District of Florida against Electropac Co. Inc. (Electropac) and a related party (the raw board manufacturer) to recover these costs. A trial was conducted in August 2008 and the trial court made a partial ruling in favor of Sparton; however, the court awarded an amount less than the previously deferred $2.8 million. Following this ruling, a provision for a loss of $0.8 million was established in the fourth quarter of fiscal 2008. Court ordered mediation was conducted following the court s ruling and a settlement was reached in September 2008 for payment to the Company of $2.0 million plus interest. The settlement is secured by a mortgage on real property and a consent judgment. In December 2008, a recovery of $0.6 million against the $2.0 million was received with the remaining balance due in September 2009, at which time Electropac failed to make the scheduled payment. In the fourth quarter of fiscal 2009, the Company established a reserve of $0.2 million against the remaining settlement balance. In March of 2010, Sparton and Electropac agreed to amend the settlement reducing the amount due to $1.2 million and providing for an immediate payment of $1.1 million with the remaining $0.1 million due on or before December 31, 2010. As of March 31, 2010 and June 30, 2009, $0.1 million and $1.2 million, respectively, remains in other current assets on the Company s balance sheet.

Litigation

On August 9, 2009, Sparton and certain subsidiaries were named as defendants in a wrongful death suit, alleging that a defective transmission shifter assembly in a 1996 Chrysler automobile caused the July 2007 death of Hunter Magro. The suit also named Chrysler LLC, Dura Automotive Systems, Inc., and Chandler Motors Company as defendants. The suit was filed in Pontotoc County Circuit Court in Mississippi. Sparton has not manufactured automotive shifter assemblies for Chrysler since December 1996, when it sold its KPI Group subsidiary to Dura Automotive Systems, Inc. The plaintiff seeks damages from the defendants for economic loss, pain and suffering, and loss of companionship, as well as punitive damages. Sparton has denied liability, has notified its insurance carriers regarding this claim, and is vigorously defending this matter. At this time, it is not possible to determine or predict the outcome of this suit, and as a result, no amounts have been accrued in the financial statements as of March 31, 2010. While no assurances can be given, the Company does not believe that this litigation, if adversely determined, would have a material adverse affect on the Company s financial position or results of operations.

Other

In addition to the foregoing, from time to time, the Company is involved in various legal proceedings relating to claims arising in the ordinary course of business. The Company is not currently a party to any such legal proceedings, the adverse outcome to which, individually or in the aggregate, is expected to have a material adverse effect on our business, financial condition or results of operations.

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Contractual Obligations and Off-Balance Sheet Arrangements

Information regarding the Company s long-term debt obligations, environmental liability payments, operating lease payments, and other commitments is provided in Part II, Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, of the Company s Annual Report on Form 10-K for the fiscal year ended June 30, 2009. As discussed in Note 6 to the Unaudited Condensed Consolidated Financial Statements in this Quarterly Report, in connection with the replacement credit facility obtained in August, 2009, the Company paid the remaining $3.4 million balance on its bank term loan and $15.5 million outstanding on its revolving credit line. In addition, as of June 30, 2009, there were $24.7 million of non cancelable purchase orders outstanding. This amount has decreased to $15.0 million as of March 31, 2010. Additionally, due primarily to lease cancellations related to the Company s restructuring activities during the nine months ended March 31, 2010, contractual obligations under operating leases are now $754,000, $1,841,000, $811,000, $143,000, $141,000 and $145,000 for fiscal years 2010, 2011, 2012, 2013, 2014 and thereafter, respectively. Other than as noted above, there have been no material changes in the nature or amount of the Company s contractual obligations since June 30, 2009.

Critical Accounting Policies

Our financial statements are prepared in conformity with GAAP and require us to select appropriate accounting policies. The assumptions and judgments we use in applying our accounting policies have a significant impact on our reported amounts of assets, liabilities, revenue and expenses. While we believe that the assumptions and judgments used in our estimates are reasonable, actual results may differ from these estimates under different assumptions or conditions.

We have identified the most critical accounting policies upon which our financial status depends. The critical policies were determined by considering accounting policies that involve the most complex or subjective decisions or assessments. We also have other policies considered key accounting policies; however, these policies do not meet the definition of critical accounting policies because they do not generally require us to make estimates or judgments that are complex or subjective. Our critical accounting policies include the following:

- Environmental contingencies
- Government contract cost estimates
- Inventory valuation allowances
- Allowances for probable losses on receivables
- Pension obligations
- Business combinations
- Valuation of property, plant and equipment
- Goodwill and customer relations
- Deferred costs and claims for reimbursement
- Income taxes
- Restructuring accrual

There have been no significant changes to our critical accounting policies that are described in Part II, Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations section of our Annual Report on Form 10-K for the year ended June 30, 2009.

New Accounting Pronouncements

See Note 2, Summary of Significant Accounting Policies, of the Notes to Unaudited Condensed Consolidated Financial Statements in this Quarterly Report on Form 10-Q for a discussion of new accounting pronouncements.

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Item 3. Quantitative and Qualitative Disclosures About Market Risk.

The Company manufactures its products in the United States and Vietnam, and ceased manufacturing in Canada during the fourth quarter of fiscal 2009. Sales are to the U.S. and Canada, as well as other foreign markets. The Company is potentially subject to foreign currency exchange rate risk relating to intercompany activity and balances and to receipts from customers and payments to suppliers in foreign currencies. Also, adjustments related to the translation of the Company s Canadian and Vietnamese financial statements into U.S. dollars are included in current earnings. As a result, the Company s financial results could be affected by factors such as changes in foreign currency exchange rates or economic conditions in the domestic and foreign markets in which the Company operates. However, minimal third party receivables and payables are denominated in foreign currency and the related market risk exposure is considered to be immaterial. Historically, foreign currency gains and losses related to intercompany activity and balances have not been significant. However, due to the greater volatility of the Canadian dollar, the impact of transaction and translation gains has increased. With the closure of the Canadian facility, however, the impact in fiscal 2010 has not been significant and it is anticipated that future periods will not be significant.

The Company has financial instruments that are subject to interest rate risk, principally long-term debt associated with the SMS acquisition in May, 2006, and the line-of-credit facility with National City Business Credit, Inc. Historically, the Company has not experienced material gains or losses due to such interest rate changes. As interest rates periodically adjust to market values for the majority of our debt, interest rate risk is not considered to be significant.

Item 4T. Controls and Procedures.

Each of our Chief Executive Officer and Chief Financial Officer has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities and Exchange Act of 1934) as of the end of the period covered by this quarterly report. Based on such evaluation, such officers have concluded that, as of the end of the period covered by this quarterly report, our disclosure controls and procedures are effective.

There have been no changes in our internal controls over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended March 31, 2010 that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

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PART II. OTHER INFORMATION

Item 1. Legal Proceedings.

See Management s Discussion and Analysis of Financial Condition and Results of Operations Commitments and Contingencies of this report.

In addition to the above, from time to time, we are involved in various legal proceedings relating to claims arising in the ordinary course of business. We are not currently a party to any such legal proceedings, the outcome of which, individually or in the aggregate, is expected to have a material adverse effect on our business, financial condition or results of operations.

Item 1A. Risk Factors.

You should carefully consider the risks and uncertainties described in Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended June 30, 2009 and the other information in our subsequent filings with the SEC, including this Quarterly Report on Form 10-Q. Our business, financial condition, results of operations and stock price could be materially adversely affected by any of these risks. The risks described in our Annual Report on Form 10-K are not the only ones we face. Additional risks and uncertainties that are currently unknown to us or that we currently consider to be immaterial may also impair our business or adversely affect our financial condition, results of operations and stock price.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

None.

Item 3. Defaults Upon Senior Securities.

None.

Item 5. Other Information.

None.

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Item 6. Exhibits.

Exhibit Number	Description
3.1	By-Laws of the Registrant as amended, incorporated herein by reference from Exhibit 3.1 to the Registrant s Current Report on Form 8-K, filed with the SEC on November 3, 2008.
3.2	Amended Articles of Incorporation of the Registrant, incorporated herein by reference from the Registrant s Quarterly Report on Form 10-Q for the three-month period ended September 30, 2004.
3.3	Amended Code of Regulations of the Registrant, incorporated herein by reference from the Registrant s Quarterly Report on Form 10-Q for the three-month period ended September 30, 2004.
10.1	Amended and Restated Revolving Credit and Security Agreement dated August 14, 2009 among the Company, its subsidiaries and National City Business Credit, Inc., incorporated by reference from Exhibit 10.1 to the Registrant s Current Report on Form 8-K filed with the SEC on August 18, 2009.
10.2	Post-closing Agreement dated August 14, 2009 among the Company, its subsidiaries and National City Business Credit, Inc., incorporated by reference from Exhibit 10.2 to the Registrant s Current Report on Form 8-K filed with the SEC on August 18, 2009.
10.3	Long-Term Stock Option Incentive Plan, incorporated by reference from Exhibit 10.1 to the Registrant s Current Report on Form 8-K filed with the SEC on September 11, 2009.
10.4	Lease Extension and Amendment Agreement dated May 1, 2010 between Sparton Technology, Inc. and 9621 Coors, L.L.C., guaranteed by Albuquerque Motor Company, Inc., incorporated by reference from Exhibit 10.1 to the Registrant s Current Report on Form 8-K filed with the SEC on May 6, 2010.
10.5	Option Agreement dated May 1, 2010 by and between Sparton Technology, Inc. and 9621 Coors, L.L.C., guaranteed by Albuquerque Motor Company, Inc., incorporated by reference from Exhibit 10.2 to the Registrant s Current Report on Form 8-K filed with the SEC on May 6, 2010.
31.1*	Chief Executive Officer certification under Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Chief Financial Officer certification under Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Chief Executive Officer and Chief Financial Officer certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

* Filed herewith.

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SIGNATURES

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

	Sparton Corporation
Date: May 14, 2010	By: /s/ CARY B. WOOD Cary B. Wood President and Chief Executive Officer (Principal Executive Officer)
Date: May 14, 2010	By: /s/ GREGORY A. SLOME Gregory A. Slome Senior Vice President and Chief Financial Officer (Principal Financial Officer)

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