

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

OMB APPROVAL
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SCHEDULE 13D

Under the Securities Exchange Act of 1934

(Amendment No. \_\_)\*

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KCAP Financial, Inc.

(Name of Issuer)

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Common Stock, \$0.01 par value per share

(Title of Class of Securities)

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48668E101

(CUSIP Number)

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Dov Gertzulin  
DG Capital Management, LLC  
460 Park Avenue, 22nd Floor  
New York, NY 10022  
Tel. No.: 646-942-5700

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(Name, Address and Telephone Number of Person Authorized to  
Receive Notices and Communications)

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October 6, 2015

(Date of Event Which Requires Filing of this Statement)

If the filing person has previously filed a statement on Schedule 13G to report the acquisition that is the subject of this Schedule 13D, and is filing this schedule because of §§240.13d-1(e), 240.13d-1(f) or 240.13d-1(g), check the following box. [ ]

**Note:** Schedules filed in paper format shall include a signed original and five copies of the schedule, including all exhibits. See Rule 13d-7 for other parties to whom copies are to be sent.

\* The remainder of this cover page shall be filled out for a reporting person's initial filing on this form with respect to the subject class of securities, and for any subsequent amendment containing information which would alter disclosures provided in a prior cover page.

The information required on the remainder of this cover page shall not be deemed to be "filed" for the purpose of Section 18 of the Securities Exchange Act of 1934 ("Act") or otherwise subject to the liabilities of that section of the Act but shall be subject to all other provisions of the Act (however, see the Notes).

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1 Names of Reporting Persons.

DG Capital Management, LLC

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2 Check the Appropriate Box if a Member of a Group (See Instructions)

(a)

(b)

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3 SEC Use Only

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4 Source of Funds (See Instructions):

WC

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5 Check if disclosure of legal proceedings is required pursuant to Items 2(d) or 2(e):

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6 Citizenship or Place of Organization.

Delaware

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Number of Shares Beneficially Owned by Each Reporting Person With	7 Sole Voting Power
	0
	8 Shared Voting Power
	1,151,334 shares (See Item 2 below)
	9 Sole Dispositive Power
	0
	10 Shared Dispositive Power
	1,151,334 shares (See Item 2 below)

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11 Aggregate Amount Beneficially Owned by Each Reporting Person

1,151,334 shares (See Item 2 below)

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12 Check if the Aggregate Amount in Row (11) Excludes Certain Shares (See Instructions)

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13 Percent of Class Represented by Amount in Row (11)

3.1%

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14 Type of Reporting Person (See Instructions)

IA, OO (Limited Liability Company)

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1 Names of Reporting Persons.

Dov Gertzulin

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2 Check the Appropriate Box if a Member of a Group (See Instructions)

(a)

(b)

---

3 SEC Use Only

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4 Source of Funds (See Instructions):

AF

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5 Check if disclosure of legal proceedings is required pursuant to Items 2(d) or 2(e):

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6 Citizenship or Place of Organization.

United States

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Number of Shares Beneficially Owned by Each Reporting Person With	7 Sole Voting Power
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	8 Shared Voting Power
	1,151,334 shares (See Item 2 below)
	9 Sole Dispositive Power
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13 Percent of Class Represented by Amount in Row (11)

3.1%

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14 Type of Reporting Person (See Instructions)

HC, IN

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## **SCHEDULE 13D**

### **Item 1. Security and Issuer**

This Schedule 13D relates to shares of Common Stock, \$0.01 par value per share (the "Common Stock"), of KCAP Financial, Inc., a Delaware corporation (the "Issuer"). The address of the principal executive offices of the Issuer is 295 Madison Avenue, 6th Floor, New York, New York 10017.

### **Item 2. Identity and Background**

(a) This Schedule 13D is being filed jointly by and on behalf of DG Capital Management, LLC ("DG Capital") and Dov Gertzulin (together, the "Reporting Persons").

Shares reported herein for DG Capital represent shares beneficially owned by private investment funds for which DG Capital serves as investment adviser. Mr. Gertzulin serves as Managing Member of DG Capital.

(b) The address of the principal business office of each reporting person is 460 Park Avenue, 22nd Floor, New York, NY 10022.

(c) The principal business of DG Capital is acting as an investment adviser to private investment funds and other accounts. The principal occupation of Mr. Gertzulin is serving as Managing Member of DG Capital.

(d) None of the Reporting Persons has, during the last five years, been convicted in a criminal proceeding (excluding traffic violations or similar misdemeanors).

(e) None of the Reporting Persons has, during the last five years, been a party to a civil proceeding of a judicial or administrative body of competent jurisdiction and as a result of such proceeding was or is subject to a judgment, decree or final order enjoining future violations of, or prohibiting or mandating activities subject to, federal or State securities laws or finding any violation with respect to such laws.

(f) See Item 6 of the cover pages.

### **Item 3. Source and Amount of Funds or Other Consideration**

The shares of Common Stock reported herein were acquired in open-market transactions occurring from April 9, 2015 and through October 5, 2015 for an aggregate of \$5,733,463 and were purchased using working capital of the private investment funds advised by DG Capital.

### **Item 4. Purpose of Transaction**

The Reporting Persons acquired the shares of Common Stock reported herein based on the Reporting Persons' belief that such shares represent an attractive investment opportunity. However, the Reporting Persons intend to engage in discussions with the Board of Directors of the Issuer (the "Board") regarding strategies to enhance shareholder value. The Reporting Persons may also engage in discussions with the Board and/or members of the Issuer's management team concerning, without limitation, the performance of management, potential business combinations and strategic alternatives and other matters concerning the Issuer.

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On October 6, 2015, the Reporting Persons delivered to the Board of Directors of the Issuer a copy of the letter attached hereto as Exhibit 7.1, the contents of which are incorporated herein.

The Reporting Persons also may consider, formulate, discuss and seek to cause the Issuer to implement various plans or proposals intended to enhance the value of their current or future investment in the Issuer, enhance stockholder value or enhance the value of the Issuer's assets, including plans or proposals that may involve extraordinary matters relating to the Issuer. Any such action may be taken or advocated by the Reporting Persons alone or in conjunction with other shareholders, potential acquirers, financing sources and/or other third parties, and could include one or more purposes, plans or proposals that relate to or would result in any of the transactions, matters or effects enumerated in Items 4(a) through (j) of Schedule 13D.

The Reporting Persons review their holdings in the Issuer on a continuing basis and as part of this ongoing review, evaluate various alternatives that are or may become available with respect to the Issuer and its securities. The Reporting Persons may from time to time acquire or cause to be acquired, additional equity or debt securities or other instruments of the Issuer, its subsidiaries or affiliates, or dispose or cause to be disposed, such equity or debt securities or other instruments, in any amount that the Reporting Persons may determine in their sole discretion, through open market transactions, privately negotiated transactions or otherwise.

From time to time, the Reporting Persons or entities to which they provide investment advice may, from time to time, (i) enter into derivative securities transactions or other hedging arrangements with respect to securities held for their accounts, (ii) hold shares of Common Stock in margin accounts or lend portfolio securities to brokers, banks or other financial institutions, or (iii) take other actions with respect to securities of the Issuer. Loans of portfolio securities typically would obligate the borrower to return the securities, or an equal amount of securities of the same class, to the lender and may provide that the borrower is entitled to exercise voting rights and retain dividends during the term of the loan. From time to time, to the extent permitted by applicable law, the Reporting Persons or entities to which they provide investment advice may borrow securities, including shares of Common Stock, for the purpose of effecting, and may effect, short sale transactions, and may purchase securities for the purpose of closing out short sale positions in such securities.

The information set forth in this Item 4 is subject to change, and there can be no assurances that the discussions or activities described in this Item 4 will continue or occur or that any of the Reporting Persons will or will not take, or cause to be taken, any of the actions described above or any similar actions.

**Item 5. Interest in Securities of the Issuer**

(a) and (b) See Items 7-11 of the cover pages and Item 2 above.

Pursuant to Rule 13d-4, each of the Reporting Persons expressly declares that this Schedule 13D and any amendments hereto shall not be construed as an admission that such Reporting Person is, for the purposes of Section 13(d) or 13(g) of the Securities Exchange Act of 1934, as amended, the beneficial owner of any securities reported herein, except to the extent that such Reporting Person owns such shares.

The percentage calculations herein are based on information provided by the Issuer in its Quarterly Report for the quarter ended June 30, 2015, as filed with the Securities and Exchange Commission on August 5, 2015.

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(c) The following table lists the Reporting Persons' transactions in the Common Stock that were effected during the sixty day period prior to the filing of this Schedule 13D:

Transaction	Date	No. Shares	Price Per Share
Open market purchase	8/24/2015	400	\$4.28
Open market purchase	8/28/2015	13,975	\$4.72
Open market purchase	9/8/2015	1,521	\$4.75
Open market sale	9/22/2015	4,974	\$4.87
Open market purchase	9/30/2015	20,000	\$4.54
Open market purchase	10/1/2015	386,807	\$4.76
Open market sale	10/1/2015	380,329	\$4.76
Open market purchase	10/2/2015	3,800	\$4.80
Open market purchase	10/2/2015	4,300	\$4.79
Open market purchase	10/5/2015	6,629	\$4.95

(d) Not applicable.

(e) Not applicable.

**Item 6. Contracts, Arrangements, Understandings or Relationships with Respect to Securities of the Issuer**

Not applicable.

**Item 7. Material to Be Filed as Exhibits**

Exhibit 99.1 Letter, dated October 6, 2015, from the Reporting Persons to the Board of Directors of the Issuer.  
Exhibit 99.2 Joint Filing Agreement by and among the Reporting Persons.

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**SIGNATURE**

After reasonable inquiry and to the best of my knowledge and belief, I certify that the information set forth in this statement is true, complete and correct.

Date: October 6, 2015

**DG Capital Management, LLC**

By: /s/ Dov Gertzulin  
Dov Gertzulin, Managing Member

**Dov Gertzulin**

By: /s/ Dov Gertzulin  
Dov Gertzulin, Individually

**Exhibit 99.1**

October 6th, 2015

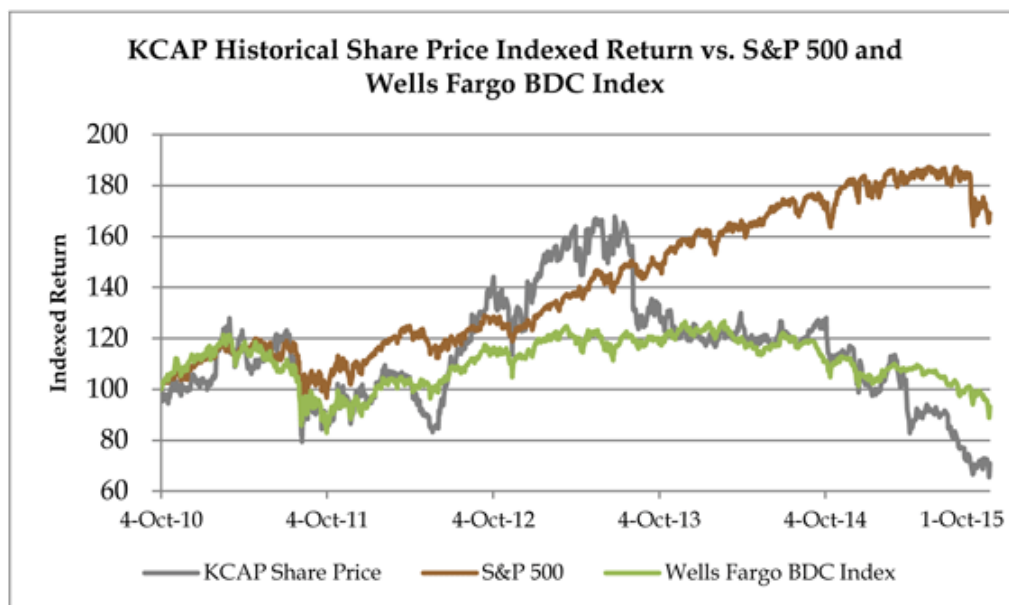
KCAP Financial, Inc.  
295 Madison Avenue, 6th Floor  
New York, NY 10017

Attn: Board of Directors

Dear KCAP's Board of Directors,

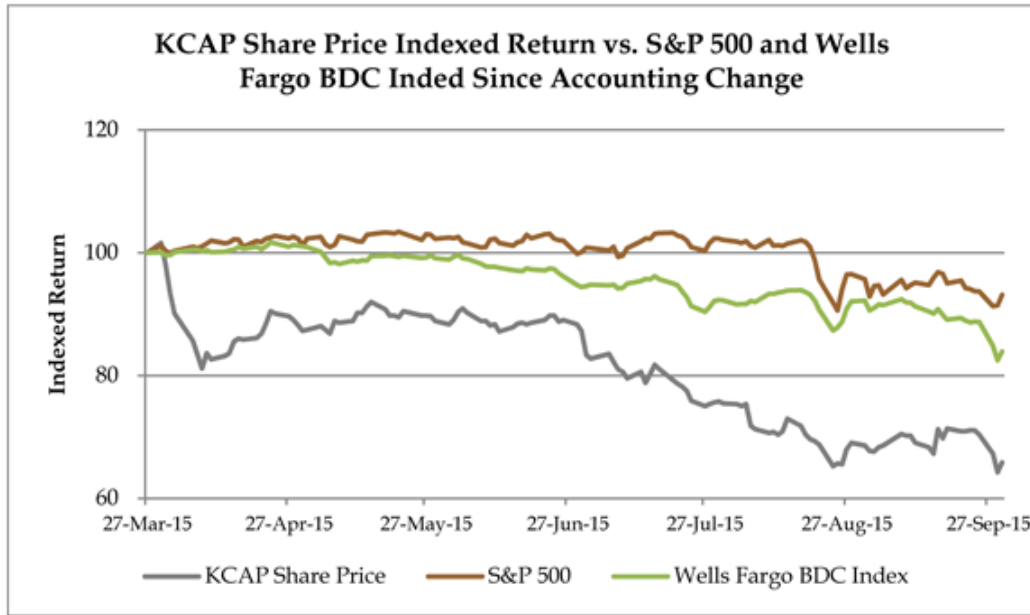
Funds managed by DG Capital Management LLC and its affiliates own 1,151,334 shares of KCAP Financial ("KCAP" or the "Company") or about 3.1% of shares outstanding, making us the Company's third largest shareholder. We believe that KCAP is not well understood by investors and KCAP shares are materially undervalued. The KCAP Board of Directors should undertake actions in order to maximize shareholder value, including a sale of the entire Company, or a sale of certain assets to purchase shares which are trading at a large discount to the Company's estimate of fair value. We believe that a sale of the entire business to another Business Development Company ("BDC") would likely yield the highest return for shareholders.

KCAP stock has underperformed both the S&P 500 and the Wells Fargo BDC Index over the last five years on a total return basis. KCAP has returned 14.5%/2.8% annualized vs. the S&P 500 at 80.0%/12.7% annualized.





We believe a significant factor in KCAP's poor performance is the complex collection of assets that the Company owns, which ultimately resulted in a restatement of their financial results. On March 30, 2015, management announced a "Restatement of Historical Financial Results": "On March 24, 2015, the Audit Committee of the Board of the Directors of KCAP Financial, Inc. concluded that the Company's previously issued audited consolidated financial statements for the years ended December 31, 2010 through 2013 as well as the previously issued unaudited consolidated financial statements for the fiscal quarters ended March 31, 2010 through September 30, 2014 require corrections due to errors related to the accounting for investment income from its equity investments in collateralized loan obligation funds and dividend income from its Asset Manager Affiliates." After the release on March 30, 2015, KCAP stock materially underperformed the S&P 500 and the Wells Fargo BDC Index. Every \$1.00 invested in the S&P on March 27, 2015 would be worth 93 cents as of October 1, 2015 vs. 87 cents in the BDC Index and only 69 cents in KCAP stock.



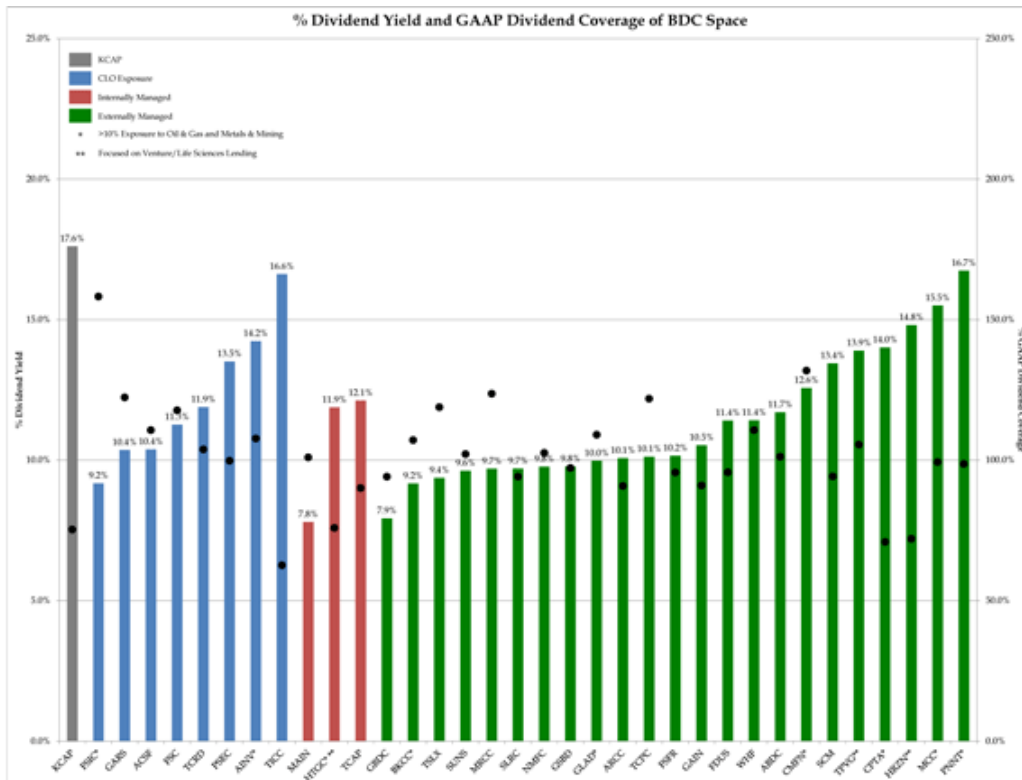
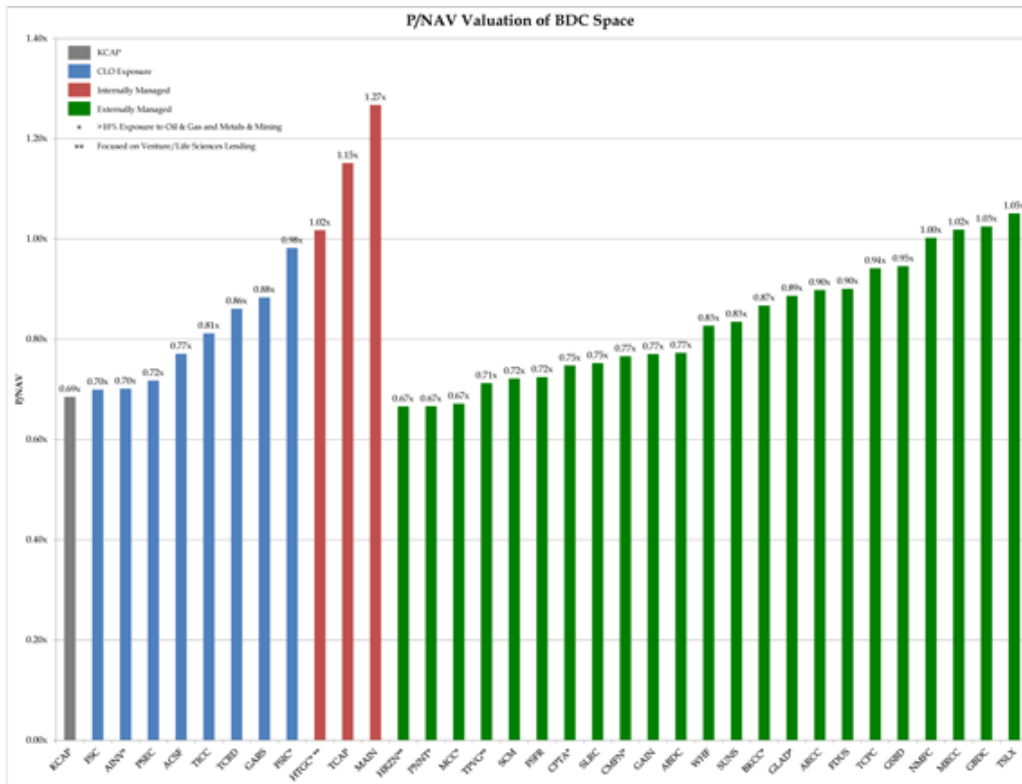
Sell-side analysts have also reflected this negatively in their analysis of the company, e.g.:

"We believe investors continue to have some uncertainty about the sustainability of the core dividend; (...) following the company's restatement of historical results and the change in accounting for income from CLO equity investments. Furthermore, we believe this uncertainty will continue as BDC investors have commonly used NII as a proxy for distributions. A dividend shortfall from NII/share was evident in 1Q15 as NII/ share of \$0.18 was \$0.03/share less than the quarterly distribution. KCAP management expects the dividend to be regularly supported by non-GAAP cash measures through a "resources available for distribution" metric." JMP Securities, July 8, 2015

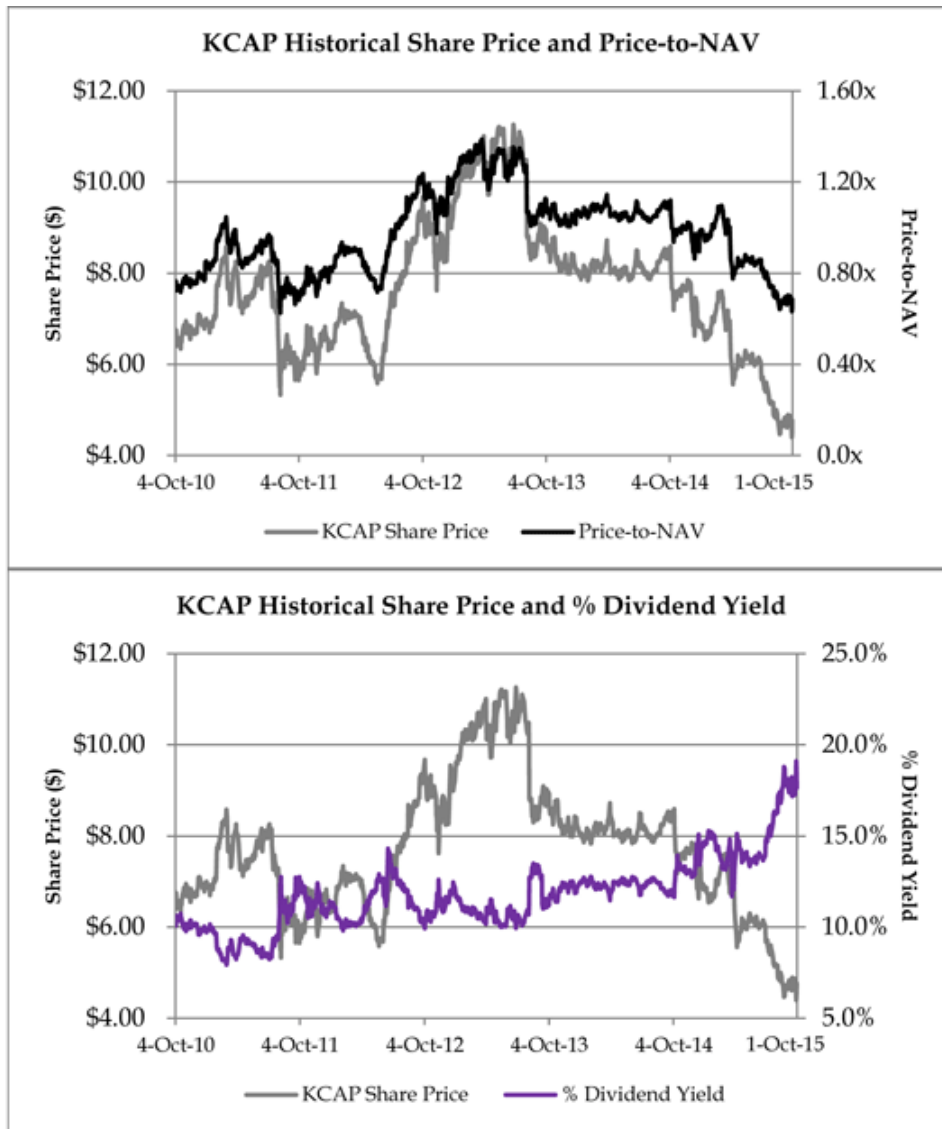
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"While we are big fans of the asset management platform because of the contractual long-term profile of the income streams and high return on invested capital, the complexity of the cash flows makes KCAP more difficult to understand and volatility related to payment speeds in the structured finance portfolios can be an issue. This came to the forefront in 4Q14 when KCAP had two separate accounting issues and had to restate historical financials." Keefe, Bruyette & Woods, August 14, 2015

This view has become consensus and as such KCAP trades at a material discount to peers (see below). On a P/NAV Basis, the company trades at 0.69X P/NAV, where the comps trade at 0.85X on average. Stripping out BDCs with material exposure to Oil & Gas and Venture Cap credits, the peer group trades at 0.88X on average. Even the sub-group with CLO exposure trades at 0.8X. Looking at Dividend Yields, KCAP trades at a 17.6% Yield, where the comps trade at 11.5% on average. Stripping out BDCs with material exposure to Oil & Gas and Venture Cap credits, the peer group trades at 10.8% on average and the sub-group with CLO exposure trades at 12.2% on average.



And KCAP's valuation has contracted to post financial-crisis lows on both a Price/NAV and Dividend Yield basis.



We believe free cash flow, which is similar to the cash "Available for Distribution" measure, is reflective of economic reality, KCAP can substantially cover its dividend and KCAP shares are materially undervalued. While management has made an effort to explain the accounting complexity (e.g. in the company's April 2015 Investor Presentation) and has made the case that the dividend is well-covered, we are deeply disappointed that management and the Board has not acted with a sense of urgency to correct the valuation discrepancy. To that end, on the Company's second quarter call, management seemed reluctant to consider taking measures to take advantage of the price to value dislocation and even seemed to argue against the long-term benefits of a share-buyback:

<Andrew Palmer, Analyst>: Good morning and thank you for taking my question. With the stock trading at 0.74 times book value per share, and an internal management structure that is more align(ed) with the shareholders, what has prevented you and the Board from implementing a share buyback program to drive value for shareholders?

<Dayl Pearson, President and Chief Executive Officer> Well, I think that's a great question, Andy. And I think it's something that we and the Board look at on a regular basis and I think you know mathematically in the short-term, I think share buybacks look like a very attractive alternative. But I think we and the Board manage the business for long-term value not short-term value. First of all, I would say that based on the analysis that we've seen these share buybacks when they've been done had not really had a significant impact on the share price. Number one, number two you know is a closed and effectively a closed in fund with leverage limitations and we're sort of at or slightly above our optimal leverage. And I think Board wants to make sure that the significant cushion in case of unseen events such as what happened in 2008 where you could have a significant sell off in credit markets and all of a sudden, without doing anything, be in violation of your leverage covenants, which would be significantly negative for the business.

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<Andrew Kerai, Analyst>: Yes, good morning. Thank you. Just to take in order to reiterate on the last comment on the stock buyback, it's very -- Dayl, it's very frustrating from a shareholders' point of view seeing where your stock is trading. You have a very high mix relative to other BDCs of liquid debt investments and I can appreciate the comment on the leverage, but the reality is, we both know that, you can sell some of these loans, which are trading I think the weighted average basis about 98 or 99, pay down some of the convert and simultaneously buyback stock. So, I'm not quite clear on the comment of how a stock buyback with a 30% discount to NAV is a temporary benefit. It is truly accretive to now then -- frankly, there is no risky investment that's going to get to 30% accretion. So, if you could maybe just walking through the analysis the board came to -- that's not the best use of shareholder capital at this point in time.

<Dayl Pearson, President and Chief Executive Officer> I'm not going to comment any further. Not going to comment on how the board looks the things in detail. Those are things that are discussed at the board level, and I have given a broad outline of the thoughts of the Board. And I appreciate your comments, but I'm not going to comment any further.

<Andrew Kerai, Analyst> Okay. We'll thank you. Just wanted to reiterate, there are BDCs that are trading at narrower discounts that are now implementing buybacks. So, we'd certainly like to appreciate it and what has a very high mix of liquid loans. So, thank you.

Recently, we've seen a pickup in consolidation in the industry. For example, Pennantpark Floating Rate Capital's acquisition of MCG Capital Corp at 1.0x Price/NAV and TPG Specialty Lending's hostile offer to acquire TICC Capital Corp at 0.9X. We believe that KCAP is an attractive acquisition target for another BDC considering the high-quality of the Company's portfolio and the potential synergies to an acquirer. The Company's internal-management structure could also compel an acquirer to pay a premium multiple. A sale at the book value per share of \$6.96, implies a return of 46%. We believe that the company should engage financial advisors to assist in this process. We are also open to discussing other alternative strategies which could unlock the value of KCAP shares. However, after a period of material underperformance, the Company's Board and management should act with a sense of urgency in correcting the large disconnect between the share price and the underlying value of the Company.

**JOINT FILING AGREEMENT**

This Joint Filing Agreement, dated as of October 6, 2015, is by and among DG Capital Management, LLC and Dov Gertzulin (the "Filers").

Each of the Filers may be required to file with the United States Securities and Exchange Commission a statement on Schedule 13G and/or 13D with respect to shares of Common Stock, par value \$0.01 per share, of KCAP Financial, Inc. beneficially owned by them from time to time.

Pursuant to and in accordance with Rule 13(d)(1)(k) promulgated under the Securities Exchange Act of 1934, as amended, the Filers hereby agree to file a single statement on Schedule 13G and/or 13D (and any amendments thereto) on behalf of each of such parties, and hereby further agree to file this Joint Filing Agreement as an exhibit to such statement, as required by such rule.

This Joint Filing Agreement may be terminated by any of the Filers upon one week's prior written notice (or such lesser period of notice as the Filers may mutually agree) to the other party.

Executed and delivered as of the date first above written.

**DG Capital Management, LLC**

By: /s/ Dov Gertzulin  
Dov Gertzulin, Managing Member

**Dov Gertzulin**

By: /s/ Dov Gertzulin  
Dov Gertzulin, Individually