CSX CORP
Form 10-K
February 18, 2011

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

FORM 10-K

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

For the fiscal year ended December 31, 2010

OR

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

For the transition period from __________ to __________
Commission File Number 1-8022

CSX CORPORATION
(Exact name of registrant as specified in its charter)

Virginia		62-1051971
(State or other jurisdiction of incorporation or organization)		(I.R.S. Employer Identification No.)
500 Water Street, 15th Floor, Jacksonville, FL	32202	(904) 359-3200
(Address of principal executive offices)	(Zip Code)	(Telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of exchange on which registered
Common Stock, $1 Par Value	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer (as defined in Rule 405 of the Securities Act).
Yes (X) No ( )

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.
Yes ( ) No (X)

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. (X)

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer (as defined in Exchange Act Rule 12b-2).

Large Accelerated Filer (X) Accelerated Filer ( ) Non-accelerated Filer ( )

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

Yes ( ) No (X)

On June 25, 2010 (which is the last day of the second quarter and the required date to use), the aggregate market value of the Registrant's voting stock held by non-affiliates was approximately $17 billion (based on the New York Stock Exchange closing price on such date).

There were 370,373,995 shares of Common Stock outstanding on January 28, 2011 (the latest practicable date that is closest to the filing date).

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's Definitive Proxy Statement (the "Proxy Statement") to be filed no later than 120 days after the end of the fiscal year with respect to its annual meeting of shareholders scheduled to be held on May 4, 2011.

CSX CORPORATION
FORM 10-K
TABLE OF CONTENTS

Table of Contents

CSX CORPORATION
PART I

Item 1. Business

CSX Corporation ("CSX"), and together with its subsidiaries (the "Company"), based in Jacksonville, Florida, is one of the nation's leading transportation suppliers. The Company provides rail-based transportation services including traditional rail service and the transport of intermodal containers and trailers.

CSX Transportation, Inc.

CSX's principal operating subsidiary, CSX Transportation, Inc. ("CSXT"), provides an important link to the transportation supply chain through its approximately 21,000 route mile rail network, which serves major population centers in 23 states east of the Mississippi River, the District of Columbia and the Canadian provinces of Ontario and Quebec. It serves over 70 ocean, river and lake ports along the Atlantic and Gulf Coasts, the Mississippi River, the Great Lakes and the St. Lawrence Seaway. CSXT also serves thousands of production and distribution facilities through track connections to approximately 240 short-line and regional railroads.

Lines of Business

During 2010, CSXT's transportation services generated $10.6 billion of revenue and served three primary lines of business:

- The merchandise business shipped nearly 2.6 million carloads and generated approximately 54% of revenue and 40% of volume in 2010. The Company's merchandise business is the most diverse market and transports aggregates (which includes crushed stone, sand and gravel), metal, phosphate, fertilizer, food, consumer (manufactured goods and appliances), agricultural, automotive, paper and chemical products.

- The coal business shipped 1.6 million carloads and accounted for 31% of revenue and 25% of volume in 2010. The Company transports utility, industrial and export coal to electricity-generating power plants, steel manufacturers, industrial plants and deep-water port facilities. Roughly three of every four tons of domestic coal and almost half of the export coal that the Company transports is used for generating electricity.

- The intermodal business accounted for approximately 12% of revenue and 35% of volume in 2010. The intermodal line of business combines the superior economics of rail transportation with the short-haul flexibility of trucks and offers a competitive cost advantage over long-haul trucking. Through its network of more than 50 terminals, the intermodal business serves all major markets east of the Mississippi and transports mainly manufactured consumer goods in containers, providing customers with truck-like service for longer shipments.

Table of Contents

CSX CORPORATION
PART I

Other revenue accounted for 3% of the Company's total revenue in 2010. This revenue category includes revenue from regional subsidiary railroads, demurrage, revenue for customer volume commitments not met, switching and other incidental charges. Revenue from regional railroads includes shipments by railroads that the Company does not directly operate. Demurrage represents charges assessed when freight cars are held beyond a specified period of time. Switching revenue is generated when CSXT switches cars between trains for a customer or another railroad.

Other Entities

In addition to CSXT, the Company's subsidiaries include CSX Intermodal Terminals, Inc. ("CSX Intermodal Terminals"), Total Distribution Services, Inc. ("TDSI"), Transflo Terminal Services, Inc. ("Transflo"), CSX Technology, Inc. ("CSX Technology") and other subsidiaries. The Company's intermodal business links customers to railroads via trucks and terminals. CSX Intermodal Terminals owns and operates a system of intermodal terminals, predominantly in the eastern United States and also performs drayage services (the pickup and delivery of intermodal shipments) and trucking dispatch operations. TDSI serves the automotive industry with distribution centers and storage locations. Transflo connects non-rail served customers to the many benefits of rail by transferring products, such as ethanol and minerals, from rail to trucks. CSX Technology and other subsidiaries provide support services for the Company.

CSX's other holdings include CSX Real Property, Inc., a subsidiary responsible for the Company's real estate sales, leasing, acquisition and management and development activities. These activities are classified in other income because they are not considered by the Company to be operating activities. Results of these activities fluctuate with the timing of non-operating real estate sales.

CSX Intermodal, Inc. ("Intermodal") was a subsidiary of CSX until it merged with CSXT during 2010. Prior to the merger, Intermodal was the parent company of CSX Intermodal Terminals, and conducted the sales and marketing activities associated with intermodal transportation service now provided by CSXT. The Company no longer reflects the intermodal business as a separate segment. CSX's president views intermodal similarly to merchandise and coal. Intermodal revenue will continue to be viewed as a separate revenue group; however, a separate income statement and operating ratio are no longer prepared and business segment disclosures are no longer required. All prior period disclosures have been revised to reflect this change.

This change was a result of certain management realignments, a strategic business review and a change in the Company's intermodal service associated with the start of the UMAX program. The UMAX program, which began during 2010, is a domestic interline container program jointly marketed by CSX and Union Pacific Corporation. Through the UMAX program, the Company provides 53 foot containers to customers for local domestic shipments or transcontinental service provided jointly by CSX and Union Pacific Corporation.

Table of Contents

CSX CORPORATION
PART I

Financial Information

See Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations for operating revenue, operating income and total assets for each of the last three fiscal years.

Company History

A leader in freight rail transportation for more than 180 years, the Company's heritage dates back to the early nineteenth century when The Baltimore and Ohio Railroad Company ("B&O") – the nation's first common carrier – was chartered in 1827. Since that time, the Company has built on this foundation to create a railroad that could safely and reliably service the ever-increasing demands of a growing nation.

Since its founding, numerous railroads have combined with the former B&O through merger and consolidation to create what has become CSX. Each of the railroads that combined into the CSX family brought unique and valuable geographical reach to new markets, gateways, cities, ports and transportation corridors.

CSX was incorporated in 1978 under Virginia law. In 1980, the Company completed the merger of the Chessie System ("Chessie") and Seaboard Coast Line Industries ("Seaboard") into CSX. The merger allowed the Company to connect northern population centers and Appalachian coal fields to growing southeastern markets. Later, the Company's acquisition of key portions of Conrail, Inc. allowed CSXT to link the northeast, including New England and the New York metropolitan area, with Chicago and midwestern markets as well as the growing areas in the southeast already served by CSXT. This current rail network allows the Company to directly serve every major market in the eastern United States with safe, dependable, environmentally responsible and fuel efficient freight transportation and intermodal service.

Competition

The business environment in which the Company operates is highly competitive. Shippers typically select transportation providers that offer the most compelling combination of service and price. Service requirements, both in terms of transit time and reliability, vary by shipper and commodity. As a result, the Company's primary competition varies by commodity, geographic location and mode of available transportation.

CSXT's primary rail competitor is Norfolk Southern Railway, which operates throughout much of the Company's territory. Other railroads also operate in parts of the Company's territory. Depending on the specific market, competing railroads and deregulated motor carriers may exert pressure on price and service levels. For further discussion on the risk of competition to the Company, see Item 1A. Risk Factors.

Table of Contents

CSX CORPORATION
PART I

Regulatory Environment

The Company's operations are subject to various federal, state and local laws and regulations, generally applicable to many businesses in the United States. The railroad operations conducted by the Company's subsidiaries, including CSXT, are subject in many respects to the regulatory jurisdiction of the Surface Transportation Board ("STB"), the Federal Railroad Administration ("FRA"), and its sister agency within the U.S. Department of Transportation ("DOT"), the Pipeline and Hazardous Materials Safety Administration ("PHMSA"). Together, FRA and PHMSA have broad jurisdiction over railroad operating standards and practices, including track, freight cars and locomotives, and hazardous materials requirements. Additionally, the Transportation Security Administration ("TSA"), a component of the Department of Homeland Security ("DHS"), has broad authority over railroad operating practices that may have homeland security implications.

Although the Staggers Act of 1980 significantly deregulated rail rates and much of the rail traffic of the Company's subsidiaries is currently exempt from rate regulation by agency decision, the STB has broad jurisdiction over railroad commercial practices, including some railroad rates, routes, fuel surcharges, conditions of service and the extension or abandonment of rail lines. This includes jurisdiction over freight car charges, the transfer, extension or abandonment of rail lines, rates charged on certain regulated rail traffic and any acquisition of control over rail common carriers.

In 2008, Congress enacted the Rail Safety Improvement Act (the "RSIA"). The legislation includes a mandate that all Class I freight railroads implement a positive train control system ("PTC") by December 31, 2015. PTC must be installed on all main lines with passenger and commuter operations as well as those over which toxic-by-inhalation hazardous materials ("TIH") are transported. Implementation of a PTC system is designed to prevent train-to-train collisions, over-speed derailments, incursions into established work-zone limits, and a train from diverting off-course onto another set of tracks through a switch left in a wrong position. Significant capital costs are anticipated with the implementation of PTC as well as ongoing operating expenses. Currently, CSX estimates that the total multi-year cost of PTC implementation will be at least $1.2 billion for the Company.

In December 2009, a proposed bill called the "Surface Transportation Board Reauthorization Act of 2009" was introduced in the Senate but not advanced. In January 2011, the bill now referred to as the Surface Transportation Board Reauthorization Act of 2011 ("STB Reauthorization Bill") was reintroduced. The STB Reauthorization Bill, if adopted, could increase government involvement in railroad pricing, service and operations. The proposed legislation also includes provisions that would reduce the ability to price at market levels, and open a carrier's privately-owned and maintained rail network to competitors where certain conditions are met.

If adopted as proposed, this bill could have a material adverse effect on the Company's revenue and operations, as well as the ability to invest in enhancing and maintaining vital infrastructure. Prior to the reintroduction of the STB Reauthorization Bill, the STB had already announced two new hearings; one on February 24, 2011 to review the utility of boxcar, intermodal, automotive and other exemptions, and the other on June 22, 2011 to explore the current state of competition in the railroad industry.

For further discussion on regulatory risks to the Company, see Item 1A. Risk Factors.

Table of Contents

CSX CORPORATION
PART I

Other Information

CSX makes available on its website www.csx.com, free of charge, its annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports as soon as reasonably practicable after such reports are filed with or furnished to the Securities and Exchange Commission ("SEC"). The information on the CSX website is not part of this annual report on Form 10-K. Additionally, the Company has posted its code of ethics on its website, which is also available to any shareholder who requests it. This Form 10-K and other SEC filings made by CSX are also accessible through the SEC's website at www.sec.gov.

CSX has included the certifications of its Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO") required by Section 302 of the Sarbanes-Oxley Act of 2002 ("the Act") as Exhibit 31, as well as Section 906 of the Act as Exhibit 32 to this Form 10-K report. Additionally, on June 2, 2010, CSX filed its annual CEO certification with the New York Stock Exchange ("NYSE") confirming CSX's compliance with the NYSE Corporate Governance Listing Standards. The CEO was not aware of any violations of these standards by CSX as of February 14, 2011 (the latest practicable date that is closest to the filing of this Form 10-K). This certification is also included as Exhibit 99 to this Form 10-K.

The Company's annual average number of employees was approximately 30,000 in 2010, which includes approximately 26,000 union employees. Most of the Company's employees provide or support transportation services. The information set forth in Item 6. Selected Financial Data is incorporated herein by reference.

For additional information concerning business conducted by the Company during 2010, see Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Item 1A. Risk Factors

The following risk factors could have a materially adverse effect on the Company's financial condition, results of operations or liquidity, and could cause those results to differ materially from those expressed or implied in the Company's forward-looking statements. Additional risks and uncertainties not currently known to the Company or that the Company currently does not deem to be material also may materially impact the Company's financial condition, results of operations or liquidity.

New legislation or regulatory changes could impact the Company's earnings or restrict its ability to independently negotiate prices.

Legislation passed by Congress or new regulations issued by federal agencies can significantly affect the revenues, costs and profitability of the Company's business. For instance, legislation proposed in the Senate in December 2009, and reintroduced in January 2011 (see Regulatory Environment in Part I for further details), if adopted, could significantly change the federal regulatory framework of the railroad industry. Several of the changes under consideration could have a significant negative impact on the Company's ability to determine prices for rail services, meet service standards and could force a reduction in capital spending. Statutes imposing price constraints or affecting rail-to-rail competition could adversely affect the Company's profitability.

Government regulation and compliance risks may adversely affect the Company's operations and financial results.

The Company is subject to the jurisdiction of various regulatory agencies, including the STB, the FRA and other state and federal regulatory agencies for a variety of economic, health, safety, labor, environmental, tax, legal and other matters. New rules or regulations by these agencies could increase the Company's operating costs or reduce operating efficiencies. For example, the RSIA mandated the installation by December 31, 2015 of Positive Train Control (PTC) on main lines that carry certain hazardous materials and on lines that have commuter or passenger operations. The FRA issued its final rule in January 2010 on the design, operational requirements and implementation of the new technology. The final rule is expected to impose significant new costs on the Company and the rail industry. Noncompliance with these and other applicable laws or regulations could erode public confidence in the Company and can subject the Company to fines, penalties and other legal or regulatory sanctions.

Climate change legislation and regulation could adversely affect the Company's operations and financial results.

Climate change legislation or regulation has been proposed and, in some cases adopted, on the federal, state, provincial (Canada) and local levels. These final and proposed laws and regulations take the form of restrictions, caps, taxes or other controls on greenhouse gas ("GHG") emissions. In particular, the U.S. Environmental Protection Agency ("EPA") has issued various regulations targeting GHG emissions, including rules and standards governing GHG emissions from certain stationary sources and from vehicles.

Any of these pending or proposed laws or regulations could adversely affect CSX and its customers' business, operations and financial results by, among other things: (1) increasing energy costs generally, making it difficult for the Company's customers in the U.S. and Canada to produce products in a cost competitive manner (particularly in the absence of similar regulations in countries like India and China); (2) increasing the Company's fuel and other operating costs and negatively affecting operating and fuel efficiencies; and (3) reducing the consumption of coal as a viable energy resource in the United States. Any of these factors could reduce the amount of traffic the Company handles and have a material adverse effect on the Company's financial condition, results of operations or liquidity.

Capacity constraints could have a negative impact on service and operating efficiency.

CSXT may experience rail network difficulties related to: (i) increased passenger activities, including high-speed rail, in capacity-constrained areas, or (ii) regulatory changes impacting when CSXT can transport freight or service routes that could have a negative effect on CSXT's operational fluidity, leading to deterioration of service, asset utilization and overall efficiency.

General economic conditions could negatively affect demand for commodities and other freight.

The economic recession adversely affected demand for rail and intermodal services. Although traffic improved in 2010, a decline in general domestic and global economic conditions that affect demand for the commodities the Company carries could reduce revenues or have other adverse effects.

CSXT, as a common carrier by rail, is required by law to transport hazardous materials, which could expose the Company to significant costs and claims.

Under federal regulations, CSXT is required to transport hazardous materials under its common carrier obligation. A train accident involving the transport of hazardous materials could result in significant claims arising from personal injury, property or natural resource damage, and environmental penalties and remediation obligations. Such claims, if insured, could exceed existing insurance coverage or insurance may not continue to be available at commercially reasonable rates. CSXT is also required to comply with regulations regarding the handling of hazardous materials.

In November 2008, the TSA issued final rules placing significant new security and safety requirements on passenger and freight railroad carriers, rail transit systems, and facilities that ship hazardous materials by rail. Noncompliance with these rules can subject the Company to significant penalties and could be a factor in litigation arising out of a train accident. Finally, legislation preventing the transport of hazardous materials through certain cities could result in network congestion and increase the length of haul for hazardous substances, which could result in increased operating costs, reduced operating efficiency or increase the risk of an accident involving the transport of hazardous materials.

The Company is subject to environmental laws and regulations that may result in significant costs.

The Company is subject to wide-ranging federal, state, provincial (Canada) and local environmental laws and regulations concerning, among other things, emissions into the air, ground and water, the handling, storage, use, generation, transportation and disposal of waste and other materials, the clean-up of hazardous material and petroleum releases, and the health and safety of our employees. If we violate or fail to comply with these laws and regulations, we could be fined or otherwise sanctioned by regulators. We can also be held liable for consequences arising out of human exposure to any hazardous substances for which we are responsible. In certain circumstances, environmental liability can extend to formerly owned or operated properties, leased properties, adjacent properties and properties owned by third parties or Company predecessors, as well as to properties currently owned, leased or used by the Company.

Table of Contents

CSX CORPORATION
PART I

The Company has been, and may in the future, be subject to, allegations or findings to the effect that it has violated, or is strictly liable under, environmental laws or regulations, and such violations can result in the Company's incurring fines, penalties or costs relating to the clean-up of environmental contamination. Although the Company believes it has appropriately recorded current and long-term liabilities for known and estimable future environmental costs, it could incur significant costs that exceed reserves or require unanticipated cash expenditures as a result of any of the foregoing. The Company also may be required to incur significant expenses to investigate and remediate known, unknown or future environmental contamination.

The Company relies on the stability and availability of its technology systems to operate its business.

The Company relies on information technology in all aspects of its business. A significant disruption or failure of the Company's information technology systems, including computer hardware, software and communications equipment, could result in a service interruption, process failure, security breach or other operational difficulties. The performance and reliability of the Company's technology systems are critical to its ability to operate and compete safely and effectively.

Disruption of the supply chain could negatively affect operating efficiency and increase costs.

The capital intensive nature and sophistication of core rail equipment (including rolling stock equipment, locomotives, rail, and ties) limits the number of railroad equipment suppliers. If any of the current manufacturers stops production or experiences a supply shortage, CSXT could experience a significant cost increase or material shortage. In addition, a few critical railroad suppliers are foreign and, as such, adverse developments in international relations, new trade regulations, disruptions in international shipping, or increases in global demand could make procurement of these supplies more difficult or increase CSXT's operating costs.

Additionally, if a fuel supply shortage were to arise, whether due to the Organization of the Petroleum Exporting Countries or other production restrictions, lower refinery outputs, a disruption of oil imports or otherwise, the Company would be negatively impacted.

Failure to complete negotiations on collective bargaining agreements could result in strikes and/or work stoppages.

Most of CSXT's employees are represented by labor unions and are covered by collective bargaining agreements. Generally speaking, these agreements are bargained nationally by the National Carriers Conference Committee. In the rail industry, negotiations have generally taken place over a number of years and previously have not resulted in any extended work stoppages. If CSXT is unable to negotiate acceptable agreements, however, it could result in strikes by the affected workers, loss of business and increased operating costs as a result of higher wages or benefits paid to union members. Under the Railway Labor Act's procedures (which include mediation, cooling-off periods and the possibility of Presidential intervention), neither party may take action until the procedures are exhausted.

Table of Contents

CSX CORPORATION
PART I

The Company faces competition from other transportation providers.

The Company experiences competition in the form of pricing, service, reliability and other factors from various transportation providers including railroads and motor carriers that operate similar routes across its service area and, to a less significant extent, barges, ships and pipelines. Transportation providers such as motor carriers and barges utilize public rights-of-way that are built and maintained by governmental entities while CSXT and other railroads must build and maintain rail networks using largely internal resources. Any future improvements or expenditures materially increasing the quality or reducing the cost of alternative modes of transportation, or legislation providing for less stringent size or weight restrictions on trucks, could negatively impact the Company's competitive position.

Future acts of terrorism, war or regulatory changes to combat the risk of terrorism may cause significant disruptions in the Company's operations.

Terrorist attacks, along with any government response to those attacks, may adversely affect the Company's financial condition, results of operations or liquidity. CSXT's rail lines or other key infrastructure may be direct targets or indirect casualties of acts of terror or war. This risk could cause significant business interruption and result in increased costs and liabilities and decreased revenues. In addition, premiums charged for some or all of the insurance coverage currently maintained by the Company could increase dramatically or the coverage may no longer be available.

Furthermore, in response to the heightened risk of terrorism, federal, state and local governmental bodies are proposing and, in some cases, have adopted legislation and regulations relating to security issues that impact the transportation industry. For example, the Department of Homeland Security adopted regulations that require freight railroads to implement additional security protocols when transporting hazardous materials. Complying with these regulations could continue to increase the Company's operating costs and reduce operating efficiencies.

Severe weather or other natural occurrences could result in significant business interruptions and expenditures in excess of available insurance coverage.

The Company's operations may be affected by external factors such as severe weather and other natural occurrences, including floods, fires, hurricanes and earthquakes. As a result, the Company's rail network may be damaged, its workforce may be unavailable, fuel costs may rise and significant business interruptions could occur. In addition, the performance of locomotives and railcars could be adversely affected by extreme weather conditions. Insurance maintained by the Company to protect against loss of business and other related consequences resulting from these natural occurrences is subject to coverage limitations, depending on the nature of the risk insured. This insurance may not be sufficient to cover all of the Company's damages or damages to others and this insurance may not continue to be available at commercially reasonable rates. Even with insurance, if any natural occurrence leads to a catastrophic interruption of service, the Company may not be able to restore service without a significant interruption in operations.

Table of Contents

The Company may be subject to various claims and lawsuits that could result in significant expenditures.

The Company is subject to various claims and lawsuits, including putative class action litigation alleging violations of antitrust laws. The Company may experience material judgments or incur significant costs to defend existing and future lawsuits. Additionally, existing litigation may suffer adverse developments not currently reflected in the Company's reserve estimates as the ultimate outcome of existing litigation is subject to numerous factors outside of the Company's control. Final judgments or settlement amounts may differ materially from the recorded reserves.

Increases in the number and magnitude of property damage and personal injury claims could adversely affect the Company's operating results.

The Company faces inherent business risk from exposure to occupational and personal injury claims, property damage, including storm damage, and claims related to train accidents. The Company may incur significant costs to defend such claims.

Existing claims may suffer adverse developments not currently reflected in reserve estimates, as the ultimate outcome of existing claims is subject to numerous factors outside of the Company's control. Although the Company establishes reserves and maintains insurance to cover these types of claims, final amounts determined to be due on any outstanding matters may differ materially from the recorded reserves and exceed the Company's insurance coverage.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

The Company's properties primarily consist of track and its related infrastructure, locomotives and freight cars and equipment. These categories and the geography of the network are described below.

Track and Infrastructure

Serving 23 states, the District of Columbia, and the Canadian provinces of Ontario and Quebec, the CSXT rail network serves, among other markets, New York, Philadelphia and Boston in the northeast and mid-Atlantic, the southeast markets of Atlanta, Miami and New Orleans, and the midwestern cities of St. Louis, Memphis and Chicago.

Table of Contents

CSX CORPORATION

PART I

CSXT's track structure includes main thoroughfares, connecting terminals and yards (known as mainline track), track within terminals and switching yards, track adjacent to the mainlines used for passing trains, track connecting the mainline track to customer locations and track that diverts trains from one track to another known as turnouts. Total track miles are greater than CSXT's approximately 21,000 route miles, which reflect the size of CSXT's network that connects markets, customers and western railroads. At December 2010, the breakdown of track miles was as follows:

	Track Miles
Mainline track	26,642
Terminals and switching yards	9,561
Passing sidings and turnouts	928
Total	37,131

In addition to its physical track structure, CSXT operates numerous yards and terminals. These serve as the hubs between CSXT and its local customers and as sorting facilities where rail cars often are received, re-sorted and placed onto new outbound trains.

The Company's ten largest yards and terminals based on annual volume (number of rail cars or intermodal containers processed) are listed below:

Yards and Terminals	Annual Volume (number of units processed)
Chicago, IL	904,451
Waycross, GA	644,415
Selkirk, NY	552,865
Willard, OH	529,872
Indianapolis, IN	499,977
Cincinnati, OH	497,611
Nashville, TN	496,085
Hamlet, NC	473,045
Birmingham, AL	368,774
Louisville, KY	350,467

Table of Contents

CSX CORPORATION
PART I

Network Geography

CSXT's operations are primarily focused on four major transportation networks and corridors which are defined geographically and by commodity flows below.

Coal Network – The CSXT coal network connects the coal mining operations in the Appalachian mountain region with industrial areas in the Northeast and Mid-Atlantic, as well as many river, lake, and deep water port facilities. CSXT's coal network is well positioned to supply utility markets in both the Northeast and Southeast and to transport coal shipments for exports outside of the U.S. Roughly three of every four tons of domestic coal and almost half of the export coal that the Company transports is used for generating electricity.

Interstate 90 (I-90) Corridor – This CSXT corridor links Chicago and the Midwest to metropolitan areas in New York and New England. This route, also known as the "waterlevel route," has minimal hills and grades and nearly all of it has two main tracks (referred to as double track). These superior engineering attributes permit the corridor to support consistent, high-speed intermodal, automotive and merchandise service. This corridor is a primary route for import traffic coming from the far east through western ports moving eastward across the country, through Chicago and into the population centers in the Northeast. The I-90 Corridor is also a critical link between ports in New York, New Jersey, and Pennsylvania and consumption markets in the Midwest. This route carries consumer goods from all three of the Company's major markets – merchandise, coal and intermodal.

Interstate 95 (I-95) Corridor – The CSXT I-95 Corridor connects Charleston, Jacksonville, Miami and many other cities throughout the Southeast with the heavily populated northeastern cities of Baltimore, Philadelphia and New York. CSXT primarily transports food and consumer products, as well as metals and chemicals along this line. It is the only rail corridor along the eastern seaboard south of Washington, D.C., and provides access to major eastern ports.

Southeastern Corridor – This critical part of the network runs between CSXT's western gateways of Chicago, St. Louis and Memphis through the cities of Nashville, Birmingham, and Atlanta and markets in the Southeast. The Southeastern Corridor is the premier rail route connecting these key cities, gateways, and markets and positions CSXT to efficiently handle projected traffic volumes of intermodal, automotive and general merchandise traffic. The corridor also provides direct rail service between the coal reserves of the southern Illinois basin and the increasing demand for coal in the Southeast.

See the following page for a map of the CSX Rail Network.

Table of Contents

CSX CORPORATION
PART I

CSX Rail Network

Table of Contents

CSX CORPORATION
PART I

Locomotives

CSXT operates more than 4,000 locomotives, of which over 95% are owned by CSXT. Freight locomotives are the power source used primarily to pull trains. Switching locomotives are used in yards to sort railcars so that the right railcar is attached to the right train in order to deliver it to its final destination. Auxiliary units are typically used to provide extra traction for heavy trains in hilly terrain. At December 2010, CSXT's fleet of owned and long-term leased locomotives consisted of the following types of locomotives:

	Locomotives	%	Average Age (years)
Freight	3,533	87%	20
Switching	314	8%	32
Auxiliary Units	225	5%	50
Total	4,072	100%	22

As of December 2010, approximately 500 locomotives or 12% were held in temporary storage. As volume continues to return, these locomotives will be placed back into service after restorative maintenance procedures are performed. Of these, over 200 locomotives can be brought back immediately.

Equipment

In 2010, the average daily fleet of cars on line consisted of approximately 211,000. At any time over half of the railcars on the CSXT system are not owned or leased by the Company. Examples of these are: railcars owned by other railroads (which are utilized by CSXT), shipper-furnished or private cars (which are generally used only in that shipper's service) and multi-level railcars used to transport automobiles (which are shared between railroads).

Table of Contents

The Company's equipment consists of freight cars, containers and chassis.

Gondolas – Support CSXT's metals markets and provide transport for woodchips and other bulk commodities. Some gondolas are equipped with special hoods for protecting products like coil and sheet steel.

Open-top hoppers – Transport heavy dry bulk commodities such as coal, coke, stone, sand, ores and gravel that are resistant to weather conditions.

Box cars – Include a variety of tonnages, sizes, door configurations and heights to accommodate a wide range of finished products, including paper, auto parts, appliances and building materials. Insulated box cars deliver food products, canned goods, beer and wine.

Covered hoppers – Have a permanent roof and are segregated based upon commodity density. Lighter bulk commodities such as grain, fertilizer, flour, salt, sugar, clay and lime are shipped in large cars called jumbo covered hoppers. Heavier commodities like cement, ground limestone and glass sand are shipped in small cube covered hoppers.

Multi-level flat cars – Transport finished automobiles and are differentiated by the number of levels: bi-levels for large vehicles such as pickup trucks and SUVs and tri-levels for sedans and smaller automobiles.

Flat cars – Used for shipping intermodal containers and trailers or bulk and finished goods, such as lumber, pipe, plywood, drywall and pulpwood.

Containers - Weather-proof boxes used for bulk shipment of freight.

Chassis - Wheeled support framework for a container that allows it to be attached to a tractor. All of the Company's chassis are leased.

Other cars owned or leased on the network include, but are not limited to, center beam cars for transporting lumber and building products. The Company also has other types of equipment such as lift equipment and doublestack railcars, which allow for two containers to be mounted one above the other.

CSX CORPORATION
PART I

At December 2010, the Company's owned and long-term leased equipment consisted of the following:

Equipment		Number of Units	%
	Gondolas	25,558	32%
	Open-top hoppers	14,440	18%
	Box cars	11,660	14%
	Covered hoppers	11,097	14%
	Multi-level flat cars	10,089	12%
	Flat cars	6,965	9%
	Other cars	493	1%
Subtotal freight cars		80,302	100%
	Containers	15,198	52%
	Chassis	13,669	47%
	Other	297	1%
Subtotal equipment		29,164	100%
Total equipment		109,466	

As of December 31, 2010, approximately 11,000 freight cars or 14% were held in temporary storage. These freight cars can be placed back into service immediately as volume returns.

Item 3. Legal Proceedings

Fuel Surcharge Antitrust Litigation

Since 2007, 31 putative class action suits have been filed in various federal district courts against CSXT and three other U.S.-based Class I railroads. The class action suits have been consolidated in federal court in the District of Columbia. The court has not yet ruled on whether it is appropriate to certify the case as a class action.

The lawsuits contain substantially similar allegations to the effect that the defendants' fuel surcharge practices relating to contract and unregulated traffic resulted from an illegal conspiracy in violation of antitrust laws. The suits seek unquantified treble damages (three times the amount of actual damages) allegedly sustained by purported class members, attorneys' fees and other relief.

All but three of the lawsuits purport to be filed on behalf of a class of shippers that allegedly purchased rail freight transportation services from the defendants through the use of contracts or through other means exempt from rate regulation during defined periods commencing as early as June 2003 and that were assessed fuel surcharges. Three of the lawsuits purport to be on behalf of indirect purchasers of rail services. The court denied the defendants' motion to dismiss the direct purchasers' claims. The court dismissed all of the indirect purchasers' causes of action seeking money damages, but did not dismiss their request for injunctive relief. The dismissal was upheld on appeal. Plaintiffs then petitioned the United States Supreme Court to hear the case. The Supreme Court denied the petition in December 2010.

One additional lawsuit was filed, but not served, by an individual shipper. CSXT entered into a tolling agreement with this shipper whereby the shipper agreed to dismiss the lawsuit against CSXT without prejudice and CSXT agreed to extend the statute of limitations for the claims asserted until the end of 2010. That agreement has been extended to the end of 2011.

CSXT believes that its fuel surcharge practices are lawful. Accordingly, CSXT intends to vigorously defend itself against the purported class actions, which it believes are without merit. While CSXT cannot predict the outcome of the private lawsuits, or of any government investigations, charges or additional litigation that may be filed in the future, we currently believe that these matters will not have a material adverse effect on any of our results of operations, financial condition and liquidity. Penalties for violating antitrust laws can be severe, involving both potential criminal and civil liability. If a material adverse outcome were to occur and be sustained, it could have a material adverse impact on the Company's financial condition, results of operations or liquidity.

Other Legal Proceedings

In addition to the matters described above, the Company is involved in litigation incidental to its business and is a party to a number of legal actions and claims, various governmental proceedings and private civil lawsuits, including, but not limited to, those related to environmental and hazardous material exposure matters, FELA claims by employees, other personal injury claims and disputes and complaints involving certain transportation rates and charges. Some of the legal proceedings include claims for compensatory as well as punitive damages and others are, or are purported to be, class actions. While the final outcome of these matters cannot be predicted with certainty, considering, among other things, the legal defenses available and liabilities that have been recorded along with applicable insurance, it is currently the opinion of CSX management that none of these pending items will have a material adverse effect on the Company's financial condition, results of operations or liquidity. An unexpected adverse resolution of one or more of these items, however, could have a material adverse effect on the Company's financial condition, results of operations or liquidity in that particular period.

Item 4. (Removed and Reserved)

Table of Contents

CSX CORPORATION
PART I

Executive Officers of the Registrant

Executive officers of the Company are elected by the CSX Board of Directors and generally hold office until the next annual election of officers. There are no family relationships or any arrangement or understanding between any officer and any other person pursuant to which such officer was elected. As of the date of this filing, the executive officers' names, ages and business experience are:

Name and Age	Business Experience During Past 5 Years
Michael J. Ward, 60 Chairman, President and Chief Executive Officer	A 33-year veteran of the Company, Ward has served as Chairman, President and Chief Executive Officer of CSX since January 2003. Ward's distinguished railroad career has included key executive positions in nearly all aspects of the Company's business, including sales and marketing, operations and finance.
Oscar Munoz, 52 Executive Vice President and Chief Financial Officer	Munoz has served as Executive Vice President and Chief Financial Officer of CSX and CSXT since May 2003 and is responsible for management and oversight of all financial, strategic planning, information technology, purchasing and real estate activities of CSX. Munoz brings to the Company more than 25 years of experience from a variety of industries. Before joining CSX in 2003, Munoz served as Chief Financial Officer and Vice President of AT&T Consumer Services. He has also held key executive positions within the telecommunication and beverage industries, including the Coca-Cola Company and Pepsico Corporation.

Table of Contents

CSX CORPORATION
PART I

Name and Age	Business Experience During Past 5 Years
David A. Brown, 51 Executive Vice President and Chief Operating Officer	Brown has been the Executive Vice President and Chief Operating Officer of CSXT since January 2010. He manages all aspects of the Company's operations across its 21,000-mile network, including transportation, service design, customer service, engineering and mechanical. Brown served as Chief Transportation Officer of CSXT from 2006-2009. Prior to joining CSXT in 2006, Brown spent 24 years at Norfolk Southern Railway where he served as Vice President of Strategic Planning from 2005 – 2006.
Clarence W. Gooden, 59 Executive Vice President of Sales and Marketing and Chief Commercial Officer	Gooden has been the Executive Vice President and Chief Commercial Officer of CSX and CSXT since April 2004. He is responsible for generating customer revenue, forecasting business trends and developing CSX's model for future revenue growth. A member of the Company for 40 years, Gooden has held key executive positions in both operations and sales and marketing.
Ellen M. Fitzsimmons, 50 Senior Vice President of Law and Public Affairs, General Counsel and Corporate Secretary	Fitzsimmons has been the Senior Vice President of Law and Public Affairs, General Counsel, and Corporate Secretary since December 2003. She serves as the Company's chief legal officer and oversees all government relations and public affairs activities. During her 19-year tenure with the Company, her broad responsibilities have included key roles in major risk and corporate governance-related areas.

Table of Contents

CSX CORPORATION
PART I

Name and Age	Business Experience During Past 5 Years
Lisa A. Mancini, 51 Senior Vice President of Human Resources and Labor Relations	Mancini has been the Senior Vice President of Human Resources and Labor Relations since January 2009. She is responsible for employee compensation and benefits, labor relations, organizational development and transformation, recruitment, training and various administrative activities. She previously served as Vice President-Strategic Infrastructure Initiatives from 2007 to 2009 and, prior to that, Vice President – Labor Relations. Prior to joining CSX in 2003, Mancini served as Chief Operating Officer of the San Francisco Municipal Railway.
Carolyn T. Sizemore, 48 Vice President and Controller	Sizemore has served as Vice President and Controller of CSX and CSXT since April 2002. She is responsible for financial and regulatory reporting, freight billing and collections, payroll for the Company's 30,000 employees, accounts payable and various other accounting processes. Sizemore's responsibilities during her 21-year tenure with the Company have included roles in finance and audit-related areas including a variety of positions in accounting, finance strategies, budgets and performance analysis.

Table of Contents

CSX CORPORATION
PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Market Information

CSX's common stock is listed on the NYSE, which is its principal trading market, and is traded over-the-counter and on exchanges nationwide. The official trading symbol is "CSX."

Description of Common and Preferred Stock

A total of 600 million shares of common stock are authorized, of which 370,342,302 shares were outstanding as of December 2010. Each share is entitled to one vote in all matters requiring a vote of shareholders. There are no pre-emptive rights, which are privileges extended to select shareholders that allow them to purchase additional shares before other members of the general public in the event of an offering. At January 28, 2011, the latest practicable date, there were 37,585 common stock shareholders of record. The weighted average of common shares outstanding, which was used in the calculation of diluted earnings per share, was approximately 386 million as of December 31, 2010. (See Note 2, Earnings Per Share.)

A total of 25 million shares of preferred stock is authorized, none of which is currently outstanding.

The following table sets forth, for the quarters indicated, the dividends declared and the high and low share prices of CSX common stock as required by SEC Regulation S-K.

	Quarter				
	1st	2nd	3rd	4th	Year
2010					
Dividends	$0.24	$0.24	$0.24	$0.26	$0.98
Common Stock Price					
High	$52.83	$62.00	$56.80	$64.80	$64.80
Low	$42.05	$48.00	$46.51	$53.95	$42.05
2009					
Dividends	$0.22	$0.22	$0.22	$0.22	$0.88
Common Stock Price					
High	$36.82	$36.57	$48.85	$50.80	$50.80
Low	$20.70	$25.09	$30.25	$40.67	$20.70

Table of Contents

CSX CORPORATION
PART II

Stock Performance Graph

The cumulative shareholder returns, assuming reinvestment of dividends, on $100 invested at December 31, 2005 are illustrated on the graph below. The Company references the Standard & Poor 500 Stock Index ("S&P 500") and the Dow Jones U.S. Transportation Average Index, which provide comparisons to a broad-based market index and other companies in the transportation industry. As shown in the graph, CSX's five-year stock returns significantly outpaced those of the S&P 500.

* The S&P 500 is a registered trademark of the McGraw-Hill Companies, Inc.

Table of Contents

CSX CORPORATION
PART II

CSX Purchases of Equity Securities

CSX is required to disclose any purchases of its own common stock for the most recent quarter. CSX purchases its own shares for two primary reasons: to further its goals under its share repurchase program and to fund the Company's contribution required to be paid in CSX common stock under a 401(k) plan which covers certain union employees.

Since March 2008, CSX has completed approximately $2.7 billion of its current $3 billion share repurchase program. During fourth quarter 2010, CSX completed approximately $347 million of total share repurchases. The Company expects to repurchase approximately $300 million of its shares in the first quarter of this year, which will complete the remainder of its current program.

CSX Purchases of Equity Securities
for the Quarter

Fourth Quarter	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs
Beginning Balance				$645,208,174
October				
(September 25, 2010 - October 22, 2010)	849,400	$59.27	849,400	594,868,312
November				

(October 23, 2010 - November 26, 2010)	2,840,481	61.06	2,840,481	421,433,217
December				
(November 27, 2010 - December 31, 2010)	1,951,670	63.10	1,951,670	298,286,880
Ending Balance	5,641,551	$61.49	5,641,551	$298,286,880

Note: There were no share repurchases during fourth quarter 2010 to fund the Company's contribution to a 401(k) plan that covers certain union employees.

Table of Contents

CSX CORPORATION
PART II

Item 6. Selected Financial Data

Selected financial data and significant events related to the Company's financial results for the last five fiscal years are listed below.

	Fiscal Years(a)				
(Dollars in Millions, Except Per Share Amounts)	2010	2009	2008	2007	2006
Financial Performance					
Revenue	$10,636	$9,041	$11,255	$10,030	$9,566
Expense	7,565	6,771	8,504	7,784	7,429
Operating Income	$3,071	$2,270	$2,751	$2,246	$2,137
Net Earnings from Continuing Operations	$1,563	$1,128	$1,485	$1,227	$1,311
Earnings Per Share:					
From Continuing Operations, Basic	$4.10	$2.88	$3.71	$2.86	$2.98
From Continuing Operations, Assuming Dilution	4.06	2.85	3.64	2.75	2.82
Average Common Shares Outstanding	381,108	392,127	400,740	430,270	440,084
Average Common Shares Outstanding, Assuming Dilution	384,509	395,686	408,620	448,280	465,934
Operating Ratio	71.1%	74.9%	75.6%	77.6%	77.7%
Financial Position					
Cash, Cash Equivalents and Short-term Investments	$1,346	$1,090	$745	$714	$900
Total Assets	28,141	26,887	26,154	25,417	25,026
Long-term Debt	8,051	7,895	7,512	6,470	5,362
Shareholders' Equity	8,700	8,768	7,985	8,612	8,878
Dividend Per Share	$0.98	$0.88	$0.77	$0.54	$0.33
Additional Data					
Capital Expenditures (Dollars in Billions) (b)	$1.8	$1.6	$1.8	$1.7	$1.4
Employees -- Annual Averages	29,916	30,088	34,363	35,443	36,005

(a) Certain amounts have been adjusted for the retrospective change in accounting policy for rail grinding, see Note 1, Nature of Operations and Significant Accounting Policies.

(b) Capital Expenditures - In addition to property additions of $1,427 million and $1,719 million in 2009 and 2008, respectively, shown in investing activities on the consolidated cash flow statements, capital expenditures included cash payments for purchases of new assets using seller financing of approximately $160 million and $54 million, respectively. These payments are included in other financing activities on the consolidated cash flow statements.

Significant Events

2006	-- Two-for-one split of the Company's common stock effective 2006.

-- Recognized gains of \$168 million pre-tax, or \$104 million after-tax, on insurance recoveries from claims related to Hurricane Katrina.

-- Recognized an income tax benefit of \$151 million primarily related to the resolution of certain tax matters, including resolution of ordinary course federal income tax audits for 1994 – 1998.

Table of Contents

CSX CORPORATION
PART II

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

STRATEGIC OVERVIEW

The Company and the rail industry provide customers with access to an expansive and interconnected transportation network that plays a key role in North American commerce. The Company’s network is positioned to reach more than two-thirds of Americans, who account for about three-quarters of the nation’s consumption of goods. Through this network, the Company transports a broad portfolio of products, ranging from coal and new energy sources, like biodiesel and ethanol, to automobiles, chemicals, and consumer products.

CSX remains highly committed to delivering value to shareholders through a balanced approach to deploying capital that includes investments in infrastructure, dividend improvements and share repurchases. In 2011, the Company plans to invest $2.0 billion to sustain core infrastructure and rolling stock, support various strategic investments and fund Positive Train Control (“PTC”) implementation costs. Key terminal expansions and infrastructure projects are important components of CSX’s investment strategy. Strategic investments through public-private partnerships, including the National Gateway initiative and the Massachusetts and Florida projects will provide enhanced transit times and improved service for customers.

The National Gateway is a multi-year infrastructure initiative which will increase intermodal capacity on key corridors between Mid-Atlantic ports and the Midwest. Total project costs are approximately $850 million, of which the Company expects to contribute approximately $400 million. A key component of this initiative is the Company’s new Northwest Ohio intermodal terminal that is scheduled to become operational in the first half of 2011. This high-capacity terminal will expand service offerings to customers as well as improve market access to east coast ports. Once complete, the new terminal will be the most environmentally friendly, technologically advanced intermodal terminal in existence.

These long-term investments provide a foundation for volume growth, productivity as well as safe and reliable operations. To continue these types of investments, the Company must be able to operate in an environment in which it can generate adequate returns and drive shareholder value. CSX will continue to advocate for a fair and balanced regulatory environment to ensure that the value of the Company’s rail service will be reflected in any potential new legislation and policy.

In addition to investing in its network, CSX increased its quarterly cash dividend twice from 22 cents to 26 cents per share during 2010. These were the seventh and eighth dividend increases over a five-year period and represents a 35 percent compounded annual growth rate. CSX also expects to repurchase approximately $300 million in shares by the end of the first quarter, representing the remainder of its existing $3 billion share repurchase program.

Table of Contents

CSX CORPORATION
PART II

2010 HIGHLIGHTS

- Revenue increased $1.6 billion or 18% to $10.6 billion primarily driven by increases in volume and core pricing gains.
- Expenses increased $794 million or 12% to $7.6 billion driven primarily by higher labor-related costs, an increase in volume-related costs and higher fuel prices.
- Operating income increased $801 million or 35% to $3.1 billion and operating ratio improved to 71.1%, both being all-time annual records.

	Fiscal Years		
(in thousands)	2010	2009	2008
Volume	6,384	5,793	6,827
(in millions)			
Revenue	$10,636	$9,041	$11,255
Expense	7,565	6,771	8,504
Operating Income	$3,071	$2,270	$2,751
Operating Ratio	71.1%	74.9%	75.6%

2010 results reflect strong year-over-year volume and revenue growth as a result of the improving economy. Revenue increased 18% from the prior year, to nearly $10.6 billion, with gains across all of the Company's markets with particular growth in automotive and metals. Overall gains were driven by a 10% increase in volume, continued pricing above rail inflation and higher fuel recovery associated with the increase in fuel prices. The Company achieved pricing gains primarily due to improved service and the overall cost advantages that rail-based solutions provide to customers versus other modes of transportation.

As volume increased, expenses increased by $794 million, or only 12%, from the prior year. This increase was driven primarily by higher labor-related costs including inflation and incentive compensation, an increase in volume-related costs and higher fuel expense due to a rise in fuel prices. Although expenses increased year-over-year, CSX was able to achieve a record operating ratio of 71.1% due to the Company's continued focus on cost control and productivity initiatives. Fiscal year 2010 results include an extra week of activity as compared to fiscal year 2009. This activity did not have a material impact on the Company's full year results of operations.

For additional information, refer to Results of Operations discussed on pages 35 through 39.

In addition to the financial highlights described above, the Company measures and reports safety and service performance. Over the last five years, CSX has improved its safety and service measures by more than 50% and generated nearly $1 billion in total productivity gains. In effect, CSX has worked to create a culture of accountability, which focuses on delivering enhanced performance by communicating a focus on leadership, discipline and execution.

During 2010, the Company again demonstrated great improvements related to safety and operating performance. For 2010, the Federal Railroad Administration ("FRA") personal injury rate improved 17% to 1.01, compared to 1.20 in 2009. This is a record full-year personal injury performance for the full year at CSX. The 2010 reported FRA train accident frequency rate improved 9% to 2.68, compared to 2.94 in 2009. These excellent results were achieved through a sustained commitment to safety.

Key service metrics in 2010 declined slightly as volume increased 10% from last year. On-time train originations and arrivals declined to 75% and 69%, respectively. Dwell time increased to 25.0 hours from 24.1 hours in 2009. Average train velocity declined 4% to 21.0 miles per hour. While these key measures declined, they remain within the ranges experienced over the last several years and continue to support efficient and reliable train operations for CSX's customers.

Table of Contents

CSX CORPORATION
PART II

Operating Statistics (Estimated)

		Fiscal Years		Improvement/
		2010	2009	(Decline) %
Safety and Service Measurements	FRA Personal Injury Frequency Index	1.01	1.20	16%
	FRA Train Accident Rate	2.68	2.94	9
	On-Time Train Originations	75%	81%	(7)
	On-Time Destination Arrivals	69%	80%	(14)
	Dwell	25.0	24.1	(4)
	Cars-On-Line	210,984	216,013	2
	Train Velocity	21.0	21.8	(4)
				Increase/ (Decrease)
Resources	Route Miles	21,084	21,190	- %
	Locomotives (owned and long-term leased)	4,072	4,071	-
	Freight Cars (owned and long-term leased)	80,302	84,282	(5)%

Definitions

FRA Personal Injury Frequency Index – Number of FRA-reportable injuries per 200,000 man-hours.

FRA Train Accident Rate – Number of FRA-reportable train accidents per million train-miles.

On-Time Train Originations – Percent of scheduled road trains that depart the origin yard on-time or ahead of schedule.

On-Time Destination Arrivals – Percent of scheduled road trains that arrive at the destination yard on-time to two hours late (30 minutes for intermodal trains).

Dwell – Average amount of time in hours between car arrival at and departure from the yard. It does not include cars moving through the yard on the same train.

Cars-On-Line – An average count of all cars on the network (does not include locomotives, cabooses, trailers, containers or maintenance equipment).

Train Velocity – Average train speed between terminals in miles per hour (does not include locals, yard jobs, work trains or passenger trains).

30

Table of Contents

CSX CORPORATION
PART II

Capital Expenditures

In addition to producing strong financial, safety and service results, CSX continued to invest in its business to create long-term value for shareholders. In 2010 capital expenditures increased to $1.8 billion from $1.6 billion in 2009. (The 2009 amount includes $160 million of cash payments for new assets purchased in the prior year using seller financing. These payments are reflected in the financing section of the consolidated cash flow statement.) The Company is committed to maintaining and improving its existing infrastructure and to positioning itself for long-term growth through expanding network and terminal capacity.

Free Cash Flow (Non-GAAP Measure)

Free cash flow is considered a non-GAAP financial measure under SEC Regulation G, Disclosure of Non-GAAP Measures. Management believes, however, that free cash flow is important in evaluating the Company's financial performance. Free cash flow should be considered in addition to, rather than a substitute for, cash provided by operating activities. Free cash flow is calculated by using net cash from operations and adjusting for property additions and certain other investing activities. As described below, free cash flow before dividends increased $823 million to $1.5 billion.

The following table reconciles cash provided by operating activities (GAAP measure) to free cash flow (non-GAAP measure).

	Fiscal Years		
	2010	2009	2008
(Dollars in Millions)			
Net cash provided by operating activities	$3,246	$2,040	$2,893
Property additions (a)	(1,825)	(1,427)	(1,719)
Other investing activities (b)	69	54	36
Free Cash Flow (before payment of dividends)	$1,490	$667	$1,210

(a) In addition to property additions of $1,427 million and $1,719 million in 2009 and 2008, respectively, total capital expenditures included cash payments for purchases of new assets using seller financing of approximately $160 million and $54 million, respectively. There were none in 2010. These payments are shown in financing activities on the consolidated cash flow statement. Property additions are shown in investing activities on the consolidated cash flow statement.

(b) Other investing activities no longer include Conrail free cash flow as these amounts are immaterial.

Table of Contents

CSX CORPORATION
PART II

FORWARD-LOOKING STATEMENTS

Certain statements in this report and in other materials filed with the SEC, as well as information included in oral statements or other written statements made by the Company, are forward-looking statements. The Company intends for all such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 and the provisions of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These forward-looking statements within the meaning of the Private Securities Litigation Reform Act may contain, among others, statements regarding:

- projections and estimates of earnings, revenues, volumes, rates, cost-savings, expenses, taxes or other financial items;
- expectations as to results of operations and operational initiatives;
- expectations as to the effect of claims, lawsuits, environmental costs, commitments, contingent liabilities, labor negotiations or agreements on the Company's financial condition, results of operations or liquidity;
- management's plans, strategies and objectives for future operations, capital expenditures, share repurchases, proposed new services and other similar expressions concerning matters that are not historical facts, and management's expectations as to future performance and operations and the time by which objectives will be achieved; and
- future economic, industry or market conditions or performance and their effect on the Company's financial condition, results of operations or liquidity.

Forward-looking statements are typically identified by words or phrases such as "believe," "expect," "anticipate," "project," "estimate," "preliminary" and similar expressions. The Company cautions against placing undue reliance on forward-looking statements, which reflect its good faith beliefs with respect to future events and are based on information currently available to it as of the date the forward-looking statement is made. Forward-looking statements should not be read as a guarantee of future performance or results and will not necessarily be accurate indications of the timing when, or by which, such performance or results will be achieved.

Forward-looking statements are subject to a number of risks and uncertainties and actual performance or results could differ materially from those anticipated by any forward-looking statements. The Company undertakes no obligation to update or revise any forward-looking statement. If the Company does update any forward-looking statement, no inference should be drawn that the Company will make additional updates with respect to that statement or any other forward-looking statements. The following important factors, in addition to those discussed in Part II, Item 1A (Risk Factors) of this annual report on Form 10-K and elsewhere in this report, may cause actual results to differ materially from those contemplated by any forward-looking statements:

- legislative, regulatory or legal developments involving transportation, including rail or intermodal transportation, the environment, hazardous materials, taxation, including the outcome of tax claims and litigation, the potential enactment of initiatives to further regulate the rail industry and the ultimate outcome of shipper and rate claims subject to adjudication;

- the outcome of litigation and claims, including, but not limited to, those related to fuel surcharge, environmental contamination, taxes, personal injuries and occupational illnesses;

- changes in domestic or international economic, political or business conditions, including those affecting the transportation industry (such as the impact of industry competition, conditions, performance and consolidation) and the level of demand for products carried by CSXT;

- unanticipated conditions in the financial markets that may affect timely access to capital markets and the cost of capital, as well as management's decisions regarding share repurchases;

- availability of insurance coverage at commercially reasonable rates or insufficient insurance coverage to cover claims or damages;

- changes in fuel prices, surcharges for fuel and the availability of fuel;

- the impact of increased passenger activities in capacity-constrained areas, including potential effects of high speed rail initiatives, or regulatory changes affecting when CSXT can transport freight or service routes;

- natural events such as severe weather conditions, including floods, fire, hurricanes and earthquakes, a pandemic crisis affecting the health of the Company's employees, its shippers or the consumers of goods, or other unforeseen disruptions of the Company's operations, systems, property or equipment;

- the cost of compliance with laws and regulations that differ from expectations (including those associated with PTC implementation) and costs, penalties and operational impacts associated with noncompliance with applicable laws or regulations;

Table of Contents

CSX CORPORATION
PART II

- the inherent business risks associated with safety and security, including the availability and vulnerability of information technology, adverse economic or operational effects from actual or threatened war or terrorist activities and any governmental response;
- labor and benefit costs and labor difficulties, including stoppages affecting either the Company's operations or the customers' ability to deliver goods to the Company for shipment;
- competition from other modes of freight transportation, such as trucking and competition and consolidation within the transportation industry generally;
- the Company's success in implementing its strategic, financial and operational initiatives;
- changes in operating conditions and costs or commodity concentrations; and
- the inherent uncertainty associated with projecting economic and business conditions.

Other important assumptions and factors that could cause actual results to differ materially from those in the forward-looking statements are specified elsewhere in this report and in CSX's other SEC reports, accessible on the SEC's website at www.sec.gov and the Company's website at www.csx.com. The information on the CSX website is not part of this annual report on Form 10-K.

Table of Contents

CSX CORPORATION
PART II

FINANCIAL RESULTS OF OPERATIONS

2010 vs. 2009 Results of Operations

	Fiscal Years			
	2010	2009 (Adjusted) (a)	$ Change	% Change
Revenue	$10,636	$9,041	$1,595	18%
Expense				
Labor and Fringe	2,957	2,629	328	12
Materials, Supplies and Other	2,075	1,999	76	4
Fuel	1,212	849	363	43
Depreciation	947	903	44	5
Equipment and Other Rents	374	391	(17)	(4)
Total Expense	7,565	6,771	794	12
Operating Income	$3,071	$2,270	$801	35
Interest Expense	(557)	(558)	1	-
Other Income - Net	32	34	(2)	(6)
Income Tax Expense	(983)	(618)	(365)	59
Earnings From Continuing Operations	1,563	1,128	435	39
Discontinued Operations	-	15	(15)	(100)
Net Earnings	$1,563	$1,143	$420	37
Earnings Per Diluted Share:				
From Continuing Operations	$4.06	$2.85	$1.21	42
Discontinued Operations	-	0.04	(0.04)	(100)
Net Earnings	$4.06	$2.89	$1.17	40%
Operating Ratio	71.1%	74.9%		380 bps

(a) Certain amounts have been adjusted for the retrospective change in accounting policy for rail grinding, see Note 1, Nature of Operations and Significant Accounting Policies.

Volume and Revenue (Unaudited)
Volume (Thousands of units); Revenue (Dollars in millions); Revenue Per Unit (Dollars)
Fiscal Years

	Volume			Revenue			Revenue Per Unit		
	2010	2009	% Change	2010	2009	% Change	2010	2009	% Change
Agricultural									
Agricultural Products	446	428	4 %	$1,056	$960	10 %	$2,368	$2,243	6%
	313	289	8	465	373	25	1,486	1,291	15

Phosphates and Fertilizers											
Food and Consumer	102	100	2		245	233	5		2,402	2,330	3
Industrial											
Chemicals	461	424	9		1,485	1,267	17		3,221	2,988	8
Automotive	340	234	45		800	511	57		2,353	2,184	8
Metals	243	200	22		520	399	30		2,140	1,995	7
Housing and Construction											
Emerging Markets	418	405	3		615	585	5		1,471	1,444	2
Forest Products	265	258	3		600	547	10		2,264	2,120	7
Total Merchandise	2,588	2,338	11		5,786	4,875	19		2,236	2,085	7
Coal	1,573	1,553	1		3,267	2,727	20		2,077	1,756	18
Intermodal(b)	2,223	1,902	17		1,291	1,184	9		581	623	(7)
Other	-	-	-		292	255	15		-	-	-
Total	6,384	5,793	10	%	$10,636	$9,041	18 %		$1,666	$1,561	7 %

(a) CSX follows a 52/53 week fiscal reporting calendar and 2010 included 53 weeks. The revenue impact for the extra week was $171 million.

(b) The revenue-per-unit decline was primarily driven by the continued impact of terminating the prior purchased transportation agreement. See the explanation for intermodal variances for further information.

2010 vs. 2009 Results of Operations

CSX full year results reflect continued strong year-over-year volume and revenue growth as a result of the improving economy. Ongoing emphasis on pricing above rail inflation, along with higher fuel recovery associated with the increase in fuel prices, drove revenue-per-unit increases in most markets. Fiscal year 2010 results include an extra week of activity as compared to fiscal year 2009.

Volume and Revenue

Merchandise

Agricultural

Agricultural Products – Volume grew with increased shipments of feed grains and ethanol. Shipments of feed grains improved with expanded meat production and lower wheat imports. Ethanol shipments grew as the amount of ethanol in fuel continued to increase.

Phosphates and Fertilizers – Volume increased as a result of strength in demand for domestic fertilizers due to a strong planting season and due to replenishment of low inventories.

Food and Consumer – Volume increased slightly as strength in refrigerated products, primarily fruits and vegetables, and alcoholic beverages were partially offset by weakness in demand for appliances.

Industrial

Chemicals – Growth occurred across most markets reflecting improvement in demand for intermediate products used in manufacturing automobiles and consumer goods. Many plastics and chemicals are key inputs in the production of both durable and nondurable goods, as well as packaging.

Automotive – Strong growth was driven by an increase in North American light-vehicle production in response to increased demand in the improving economy.

Metals – Volume growth was driven by increased shipments of sheet steel for auto production, increases in scrap steel resulting from higher steel production and increases in energy-related products.

Housing and Construction

Emerging Markets – Shipments increased in limestone, transportation equipment and aggregates (which include crushed stone, sand and gravel) as a result of overall market growth due to the improving economy.

Forest Products – Volume increased with strength in shipments of pulp board and paper used in packaging for consumer products. Volume also increased slightly in construction-related markets.

Table of Contents

Coal

Volume was basically flat as increased export shipments were offset by weakness in utility shipments. Higher export shipments were due to greater demand for U.S. metallurgical coal in Asia and steam coal in Europe. Shipments to utility customers were down as high utility stockpiles were reduced throughout the year and are approaching targeted levels. The increase in revenue per unit was driven by improved yield, higher fuel recovery and longer length of haul. Total coal volume is expected to increase as the Company expects to ship approximately 35 – 40 million tons of export coal and projects increases in utility coal volume in 2011.

Intermodal

International and domestic shipment growth resulted from U.S. inventory replenishment, improved U.S. exports, new business, truckload conversions, and new UMAX and door-to-door service offerings.

The revenue-per-unit decline was driven by the impact of switching from a purchased transportation arrangement to a domestic interline program at the start of second quarter. This program, known as UMAX, provides customers with containers for local shipments or transcontinental service provided jointly by CSX and Union Pacific Corporation. This revenue-per-unit decline was partly offset by increased fuel recovery and an improved pricing environment.

Other

Revenue gains were primarily driven by benefits for contract volume commitments not met.

Expense

Total expenses for 2010 increased 12% or $794 million to $7.6 billion compared to the prior year. Descriptions of each expense category as well as significant year-over-year changes are described below.

Labor and Fringe expenses include employee wages and related payroll taxes, health and welfare costs, pension, other post-retirement benefits and incentive compensation. These expenses increased $328 million primarily driven by inflation and higher incentive compensation.

Materials, Supplies and Other expenses consist primarily of materials and contracted services to maintain infrastructure and equipment and for terminal services at automotive facilities. This category also includes costs related to casualty claims, environmental remediation, train accidents, utilities, property and sales taxes and professional services. In addition, this category includes amounts paid to other transportation companies. Total materials, supplies and other expense increased by $76 million in 2010. This increase was primarily driven by the following:

Table of Contents

- Volume increases drove higher operating and maintenance costs at automotive facilities, coal piers and intermodal terminals. In addition, maintenance expenses increased as locomotives previously held in storage during 2009 due to lower volume were placed back into service during 2010. Higher travel costs for train crews and other volume-related expenses also contributed to this increase.

- As safety and occupational claim trends have continued to improve, changes in estimate were recorded in both years - $49 million in 2010 and $105 million in 2009. This resulted in a year-over-year increase in casualty expense of $56 million.

- An operating property transaction with the Commonwealth of Massachusetts closed during 2010 and resulted in a $30 million net book loss on a pre-tax basis. This property is a former Conrail-acquired property. The Company received $50 million of cash related to this transaction.

- The above increases to expense were offset by $126 million of reduced purchased transportation costs as a result of switching from a purchased transportation agreement to the UMAX domestic interline program during 2010 in the intermodal business.

Fuel expense includes locomotive diesel fuel as well as non-locomotive fuel. This expense is driven by the market price and locomotive consumption of diesel fuel. Fuel expense increased $363 million primarily due to higher fuel prices and higher volume. Average fuel price per gallon increased $0.55 or 32% from $1.71 in 2009 to $2.26 in 2010.

Depreciation expense primarily relates to recognizing the cost of a capital asset, such as locomotives, railcars and track structure, over its useful life. This expense is impacted primarily by the capital expenditures made each year. Depreciation expense increased $44 million in 2010 primarily due to a larger asset base.

Equipment and Other includes rent paid for freight cars owned by other railroads or private companies, net of rents received by CSXT for use of its equipment. This category of expenses also includes lease expenses for locomotives, railcars, containers and trailers, office and other rentals. These expenses decreased $17 million primarily due to cost savings associated with improved asset utilization and lower lease expense, partially offset by volume-related increases.

Other

Interest Expense

Interest expense decreased $1 million to $557 million primarily due to lower average debt balances during 2010.

Table of Contents

Other Income – Net

Other income decreased $2 million to $32 million primarily related to lower interest income caused by lower cash and investment balances and lower interest rates in 2010.

Income Tax Expense

Income tax expense increased $365 million to $983 million primarily due to higher earnings during 2010.

Net Earnings

Net earnings increased $420 million to $1.6 billion and earnings per diluted share increased $1.17 to $4.06 in 2010. This increase was primarily due to higher operating income net of income taxes in 2010.

Table of Contents

CSX CORPORATION
PART II

2009 vs. 2008 Results of Operations (a)

	Fiscal Years 2009 (Adjusted)	2008 (Adjusted)	$ Change	% Change
Revenue	$9,041	$11,255	$(2,214)	(20)%
Expense				
Labor and Fringe	2,629	2,955	(326)	(11)
Materials, Supplies and Other	1,999	2,407	(408)	(17)
Fuel	849	1,817	(968)	(53)
Depreciation	903	900	3	-
Equipment and Other Rents	391	425	(34)	(8)
Total Expense	6,771	8,504	(1,733)	(20)
Operating Income	2,270	2,751	(481)	(17)
Interest Expense	(558)	(519)	(39)	8
Other Income - Net	34	100	(66)	(66)
Income Tax Expense	(618)	(847)	229	(27)
Earnings From Continuing Operations	1,128	1,485	(357)	(24)
Discontinued Operations	15	(130)	145	(112)
Net Earnings	$1,143	$1,355	$(212)	(16)
Earnings Per Diluted Share:				
Continuing Operations	$2.85	$3.64	$(0.79)	(22)
Discontinued Operations	0.04	(0.32)	0.36	(113)
Net Earnings	$2.89	$3.32	$(0.43)	(13)%
Operating Ratio	74.9%	75.6%		70 bps

(a) Certain amounts have been adjusted for the retrospective change in accounting policy for rail grinding, see Note 1, Nature of Operations and Significant Accounting Policies.

Volume and Revenue (Unaudited)
Volume (Thousands of units); Revenue (Dollars in millions); Revenue Per Unit (Dollars)
Fiscal Years

	Volume 2009	Volume 2008	Volume % Change	Revenue 2009	Revenue 2008	Revenue % Change	Revenue Per Unit 2009	Revenue Per Unit 2008	Revenue Per Unit % Change
Agricultural									
Agricultural Products	428	432	(1) %	$960	$1,010	(5) %	$2,243	$2,338	(4)%
Phosphates and Fertilizers	289	334	(13)	373	461	(19)	1,291	1,380	(6)
Food and Consumer	100	109	(8)	233	281	(17)	2,330	2,578	(10)
Industrial									
Chemicals	424	493	(14)	1,267	1,454	(13)	2,988	2,949	1
Automotive	234	343	(32)	511	784	(35)	2,184	2,286	(4)
Metals	200	337	(41)	399	752	(47)	1,995	2,231	(11)

Housing and Construction									
Emerging Markets	405	487	(17)	585	714	(18)	1,444	1,466	(2)
Forest Products	258	344	(25)	547	793	(31)	2,120	2,305	(8)
Total Merchandise	2,338	2,879	(19)	4,875	6,249	(22)	2,085	2,171	(4)
Coal	1,553	1,879	(17)	2,727	3,285	(17)	1,756	1,748	-
Intermodal(b)	1,902	2,069	(8)	1,184	1,466	(19)	623	709	(12)
Other	-	-	-	255	255	-	-	-	-
Total	5,793	6,827	(15) %	$9,041	$11,255	(20) %	$1,561	$1,649	(5) %

Prior periods have been reclassified to conform to the current presentation.

40

Table of Contents

CSX CORPORATION
PART II

2009 vs. 2008 Results of Operations

Volume and Revenue

Revenue decreased $2.2 billion, or 20%, to $9.0 billion from the prior year driven by a 15% decline in volume and lower fuel cost recovery associated with the sharp decline in fuel prices. The broad-based economic recession drove year-over-year volume declines across all major markets. In the 2009 challenging environment, the Company continued to achieve pricing gains primarily due to improved service and the overall cost advantages that rail-based solutions provide to customers versus other modes of transportation.

Merchandise

Agricultural

Agricultural Products – Volume was down slightly as the growth in ethanol and export grain was more than offset by lower poultry production which negatively impacted the feed grain and ingredient markets.

Phosphates and Fertilizers – International and domestic shipments declined due to lower phosphate and potash soil application by farmers in reaction to lower prices for grain and the tight credit environment.

Food and Consumer –Weakness in residential construction caused reduced shipments of appliances and other consumer goods. Yet, basic needs markets such as food products were less severely impacted by the economic conditions.

Industrial

Chemicals – Volume declined as weakness in the housing, automotive and consumer goods markets significantly reduced demand for chemical products related to those markets. Revenue per unit was flat as yield management efforts were offset by lower fuel recovery.

Automotive – Volume declined due to a reduction in light vehicle production, several plant closures and lower vehicle sales driven by the weak economy and a tight credit environment. However, volume improved in the second half of the year as inventories stabilized and the Cash for Clunkers program helped spur sales. Revenue per unit was negatively impacted by lower fuel recovery associated with the sharp decline in fuel prices.

Metals – The largest decline in volume was experienced in metals driven by weak global and domestic steel demand in the automotive and construction industries. The decline in demand moderated during the year due to replenishment of low inventories and an improvement in automotive production.

Housing and Construction

Emerging Markets – Volume was down as a result of declines in aggregate shipments, such as crushed stone, sand and gravel, caused by a continued weakness in both residential and non-residential construction.

Table of Contents

CSX CORPORATION
PART II

Forest Products – A weak housing market drove the decline in lumber and building products. Paper volume continued to be soft due to electronic media substitution and less packaging being used as a result of lower consumer spending.

Coal

Volume declines were driven by lower demand from electric utilities and a decrease in exports compared to 2008. Domestic coal demand for generating electricity was down due to natural gas substitution and lower industrial production, resulting in continued high stock pile levels. The 2009 export market decline was a result of both lower steel production in Europe reducing the need for metallurgical coal (used to produce steel) and less expensive alternative global sources for European utilities. Overall revenue per unit for the coal market improved as yield management efforts more than offset lower fuel recovery.

Intermodal

Volume decline was driven by a decrease in international traffic due to the economy which was partially offset by domestic growth in railroad provided container shipments, over-the-road truckload conversions, and expanded service offerings. Revenue per unit was lower primarily due to decreased fuel recovery and competitive truck pricing.

Expense

Total expenses for 2009 decreased 20% or $1.7 billion to $6.8 billion compared to the prior year. Significant year-over-year changes are described below.

Labor and Fringe expenses decreased $326 million primarily driven by labor productivity initiatives, such as employee furloughs and reduced crew overtime. Lower incentive compensation was partially offset by inflation and other items.

Materials, Supplies and Other expenses decreased by $408 million in 2009. This decrease is driven by several items:

- Volume-related expenses decreased as a result of lower operating costs at automotive facilities and terminals. In addition, maintenance expenses decreased as locomotives were placed into storage as a result of reduced shipments during 2009. Lower travel costs for train crews and other volume-related expenses also contributed to this decrease.

- As safety and occupational claim trends have continued to improve, changes in estimate were recorded in both years - $105 million in 2009 and $10 million in 2008. This resulted in a year-over-year reduction in casualty expense of $95 million.

    - Prior year storm and proxy-related items not repeated in the current year accounted for approximately $74 million of this decrease.

- Improved collections and a stabilizing economic environment caused a $25 million decrease in bad debt expense.

- The decreases described above were partially offset by an increase in inflation-related items in 2009.

Fuel expense decreased $968 million primarily due to sharply lower fuel prices and lower volume. Average fuel prices per gallon decreased $1.37 or 44% from $3.08 in 2008 to $1.71 in 2009.

Depreciation expense increased $3 million primarily due to a slightly larger asset base. This increase was largely offset by lower depreciation rates resulting from periodic asset life studies.

Equipment and Other Rents expense decreased $34 million mainly due to lower volume and fewer locomotive leases.

Other

Interest Expense

Interest expense increased $39 million to $558 million due to higher average debt balances in 2009.

Other Income – Net

Other income decreased $66 million to $34 million in 2009. 2008 results included a $30 million non-cash adjustment to correct equity earnings from a non-consolidated subsidiary that was not repeated in 2009. Reduced interest income as a result of lower average cash and investment balances also contributed to this decrease. In addition, real estate sales declined during 2009.

Income Tax Expense

Income tax expense decreased $229 million to $618 million primarily due to lower earnings in 2009.

Net Earnings

Net earnings decreased $212 million to $1.1 billion and earnings per diluted share decreased $0.43 to $2.89 in 2009. This decrease was primarily due to the following factors:

- Operating income decreased $481 million primarily due to lower revenue.

- Offsetting this decrease was a $145 million increase in income from discontinued operations as 2008 included an impairment loss related to The Greenbrier as well as a $229 million decrease in tax expense.

Table of Contents

CSX CORPORATION
PART II

LIQUIDITY AND CAPITAL RESOURCES

Liquidity is a company's ability to generate adequate amounts of cash to meet both current and future needs for obligations as they mature and to provide for planned capital expenditures, including those to implement regulatory and legislative initiatives. In order to have a complete picture of a company's liquidity, its balance sheet, sources and uses of cash flow and external factors should be reviewed.

Material Changes in the Consolidated Balance Sheets and Significant Cash Flows

Consolidated Balance Sheets

CSX's balance sheet reflects its strong capital base and the impact of CSX's balanced approach in deploying its capital for the benefit of its shareholders, which includes investments in infrastructure, dividend improvement and share repurchases.

Total assets increased $1.3 billion from the previous year. This was driven by net properties which increased $735 million since December 2009 due to planned capital expenditures. Other long-term assets increased $188 million as a result of cash consideration paid in the exchange of debt securities (see Note 9, Debt and Credit Agreements). On the liability side, the Company increased net debt by $656 million due to additional borrowings. Deferred income tax liability also increased by $525 million due to the impact of accelerated depreciation and bonus depreciation. Bonus depreciation increased from 50% to 100% due to legislative changes that became effective in September 2010 and will continue in 2011. Finally, shareholders' equity decreased $68 million as a result of $1.5 billion of share repurchases since December 2009 which was offset by increased earnings during 2010.

Sources of Cash

The Company has multiple sources of cash. First, the Company generates cash from operations. In 2010, the Company generated $3.2 billion of cash from operating activities which represented a $1.2 billion increase from the prior year. This increase was primarily driven by higher earnings in 2010. Second, CSX has access to numerous financing sources including a $1.25 billion five-year unsecured revolving credit facility that expires in May 2012. This facility can be increased by an additional $500 million to $1.75 billion with the approval of the lending banks. As of the date of this filing, the Company has not drawn on this facility. See Note 9, Debt and Credit Agreements for more information.

CSX filed its shelf registration statement with the SEC in February 2010. This shelf registration statement is unlimited as to amount and may be used, subject to market conditions and CSX Board authorization, to issue debt or equity securities at CSX's discretion. While CSX seeks to give itself flexibility with respect to cash requirements, there can be no assurance that market conditions would permit CSX to sell such debt securities on acceptable terms at any given time, or at all.

Table of Contents

CSX CORPORATION
PART II

Uses of Cash

Net cash used in investing activities during 2010 was driven by $1.8 billion of property additions. Funds used for property additions are further described below.

	Fiscal Years		
Capital Expenditures (Dollars in millions) (a)	2010	2009	2008
Track	$777	$748	$701
Bridges, Signals and Other	475	363	401
Total Infrastructure	1,252	1,111	1,102
Capacity and Commercial Facilities	258	169	189
Locomotives	25	19	247
Freight Cars	157	71	160
Regulatory (including PTC)	133	57	21
Total Property Additions	1,825	1,427	1,719
Cash paid for new assets purchased using seller financing (b)	-	160	54
Total Capital Expenditures	$1,825	$1,587	$1,773

(a) Certain amounts have been adjusted for the retrospective change in accounting policy for rail grinding, see Note 1, Nature of Operations and Significant Accounting Policies.

(b) Cash paid for new assets purchased using seller financing are included in other financing activities on the consolidated cash flow statements.

Among other things, the Company uses cash for scheduled payments of debt and leases and to pay dividends to shareholders. CSX paid dividends of $372 million in 2010, which was $27 million more than prior year. This increase was primarily due to an increase in the quarterly dividend to $0.24 per share at the beginning of 2010 and then to $0.26 in fourth quarter 2010. Net cash used in financing activities was $1.3 billion which increased $920 million primarily as a result of $1.5 billion of share repurchases offset by net debt in 2010.

Capital spending programs are and have been designed to assure the ability to provide safe, efficient and reliable transportation services. For 2011, CSX plans to spend $2.0 billion of capital of which over half will be used to sustain the core infrastructure. Approximately $260 million (including PTC), or 13%, of 2011 total capital spending will be applied toward the implementation of unfunded required regulatory projects. CSX intends to fund these capital investments through cash generated from operations. The remaining amounts will be allocated to locomotives, freight cars and high return and growth or productivity investments such as the new intermodal terminal located in Northwest Ohio.

Table of Contents

CSX CORPORATION
PART II

CSX is continually evaluating market and regulatory conditions that could affect the Company's ability to generate sufficient returns on capital investments. CSX may revise its future estimates for capital spending as a result of changes in business conditions, tax legislation or the enactment of new laws or regulations. Although new legislation or regulations, such as the STB Reauthorization Bill or climate change legislation, could have a material adverse effect on the Company's operations and financial performance in the future (see Risk Factors under Item 1A of this Form 10-K), it is too early to predict the manner or severity of such impact. However, the Company continues to take steps and explore opportunities to reduce the impact of its operations on the environment, including investments in new technologies, reducing fuel consumption and increasing fuel efficiency and lowering emissions.

Liquidity and Working Capital

Currently, CSX is well positioned from a liquidity standpoint. The Company ended the year with over $1.3 billion of cash, cash equivalents and short-term investments. CSX also has a $1.25 billion credit facility with a diverse syndicate of banks that was not drawn on. Additionally, in 2010, the Company issued $800 million of new long-term debt.

The Company also has a $250 million receivables securitization facility with a 364-day term and expires in December 2011. The purpose of this facility is to provide an alternative to commercial paper and a low cost source of short-term liquidity. As of the date of this filing, the Company has no outstanding balances drawn on this facility. Under the terms of this facility, CSXT transfers eligible third-party receivables to CSX Trade Receivables, a bankruptcy-remote special purpose subsidiary. A separate subsidiary of CSX will service the receivables. Upon transfer, the receivables become assets of CSX Trade Receivables and are not available to the creditors of CSX or any of its other subsidiaries. In the event CSX Trade Receivables draws under this facility, the Company will record an equivalent amount of debt on its consolidated financial statements.

Working capital can also be considered a measure of a company's ability to meet its short-term needs. CSX had a working capital surplus of $318 million and $705 million at December 2010 and 2009, respectively. The decline since December 2009 is primarily due to a $500 million reclassification from long-term debt to current maturities of long-term debt for amounts due within the next twelve months.

The Company's working capital balance varies due to factors such as the timing of scheduled debt payments and changes in cash and cash equivalent balances as discussed above. Although the Company currently has a surplus, a working capital deficit is not unusual for CSX or other companies in the industry and does not indicate a lack of liquidity. The Company continues to maintain adequate current assets to satisfy current liabilities and maturing obligations when they come due. Furthermore, the Company has sufficient financial capacity, including its revolving credit facility and shelf registration statement, to manage its day-to-day cash requirements and any anticipated obligations. The Company from time to time accesses the credit markets for additional liquidity.

CSX CORPORATION
PART II

Credit Ratings

Credit ratings reflect an independent agency's judgment on the likelihood that a borrower will repay a debt obligation at maturity. The ratings reflect many considerations, such as the nature of the borrower's industry and its competitive position, the size of the company, its liquidity and access to capital and the sensitivity of a company's cash flows to changes in the economy. The two largest rating agencies, Standard & Poor's ("S&P") and Moody's Investors Service ("Moody's"), use alphanumeric codes to designate their ratings. The highest quality rating for long-term credit obligations is AAA+ and Aaa1 for S&P and Moody's, respectively. A credit rating is not a recommendation to buy, sell or hold securities and may be subject to revision or withdrawal at any time by the assigning rating agency.

Ratings of BBB- and Baa3 or better by S&P and Moody's, respectively, reflect ratings on debt obligations that fall within a band of credit quality considered to be investment grade. Currently, CSX's long-term ratings fall at the lower end of this category. If CSX's credit ratings were to decline to lower levels, the Company could experience significant increases in its interest cost for new debt. In addition, a decline in CSX's credit ratings could adversely affect the market's demand, and thus the Company's ability to readily issue new debt.

SCHEDULE OF CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS

The following tables set forth maturities of the Company's contractual obligations and other commitments:

Type of Obligation	2011	2012	2013	2014	2015	Thereafter	Total
(Dollars in Millions) (Unaudited)							
Contractual Obligations							
Long-term Debt (See Note 9)	$613	$507	$780	$526	$628	$5,610	$8,664
Purchase Obligations (See Note 7)	429	330	319	309	319	3,850	5,556
Operating Leases - Net (See Note 7) (a)	77	67	38	21	21	154	378
Agreements with Conrail (a)	2	3	3	4	1	1	14
Total Contractual Obligations	$1,121	$907	$1,140	$860	$969	$9,615	$14,612
Other Commitments(b)	$ 125	$ -	$ -	$ -	$ -	$ -	$ 125

(a) Agreements with Conrail represent minimum future lease payments of $14 million for freight cars and locomotives (see Note 13, Related Party Transactions). This amount plus total operating leases-net of $378 million above equals total net lease commitments of $392 million disclosed in Note 7, Commitments and Contingencies.

(b) Other commitments of $125 million consisted of surety bonds and letters of credit. Surety bonds are issued by a third-party as an assurance that CSX will fulfill certain obligations and are typically a contract, state, federal or court requirement.

OFF-BALANCE SHEET ARRANGEMENTS

For detailed information about the Company's guarantees, operating leases and purchase obligations, see Note 7, Commitments and Contingencies.

There are no off-balance sheet arrangements that are reasonably likely to have a material effect on the Company's financial condition, results of operations or liquidity.

Table of Contents

CSX CORPORATION
PART II

CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires that management make estimates in reporting the amounts of certain assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and certain revenues and expenses during the reporting period. Actual results may differ from those estimates. These estimates and assumptions are discussed with the Audit Committee of the Board of Directors on a regular basis. Consistent with the prior year, significant estimates using management judgment are made for the following areas:

- casualty, environmental and legal reserves;
- pension and post-retirement medical plan accounting;
- depreciation policies for assets under the group-life method; and
- income taxes

Casualty, Environmental and Legal Reserves

Casualty

Casualty reserves represent accruals for personal injury, occupational injury claims and asbestos. During 2010 the Company increased its self-insured retention amount for these claims from $25 million to $50 million per injury for claims occurring on or after June 1, 2010. Currently, no individual claim is expected to exceed the Company's self-insured retention amount. In accordance with the Contingencies Topic in the ASC, to the extent the value of an individual claim exceeds the self-insured retention amount, the Company would present the liability on a gross basis with a corresponding receivable for insurance recoveries. These reserves fluctuate based upon the timing of payments as well as changes in independent third-party estimates, which are reviewed by management. Most of the claims relate to CSXT unless otherwise noted below. Defense and processing costs, which historically have been insignificant and are anticipated to be insignificant in the future, are not included in the recorded liabilities.

As of December 2010, the Company had $375 million in casualty reserves. See below for details regarding changes in estimate for casualty reserves.

Table of Contents

CSX CORPORATION
PART II

Critical Accounting Estimates, continued

Personal Injury

Personal injury reserves represent liabilities for employee work-related and third-party injuries. Work-related injuries for CSXT employees are primarily subject to the Federal Employers' Liability Act ("FELA"). In addition to FELA liabilities, employees of other CSX subsidiaries are covered by various state workers' compensation laws, the Federal Longshore and Harbor Workers' Compensation Program or the Maritime Jones Act.

CSXT retains an independent actuarial firm to assist management in assessing the value of personal injury claims and cases. An analysis is performed by the independent actuarial firm semi-annually and is reviewed by management. The methodology used by the actuary includes a development factor to reflect growth or reduction in the value of these personal injury claims. It is based largely on CSXT's historical claims and settlement experience. Actual results may vary from estimates due to the number, type and severity of the injury, costs of medical treatments and uncertainties in litigation.

During 2010 and 2009, the Company reduced personal injury reserves by $24 million and $84 million respectively. These reductions were based on management's review of the actuarial analysis performed by an independent actuarial firm. In recent years, the Company has experienced a continued downward trend in the number of injuries which has resulted in a continued reduction of the CSXT's Federal Railroad Administration ("FRA") personal injury rate. These reductions in reserves are a direct result of the Company's improvement in safety and were included in materials, supplies and other in the consolidated income statements.

Occupational & Asbestos

Occupational claims arise from allegations of exposures to certain materials in the workplace, such as solvents, soaps, chemicals (collectively referred to as "irritants") and diesel fuels or allegations of chronic physical injuries resulting from work conditions, such as repetitive stress injuries, carpal tunnel syndrome and hearing loss.

The Company is also party to a number of asbestos claims by employees alleging exposure to asbestos in the workplace. The heaviest possible exposure for employees resulted from work conducted in and around steam locomotive engines that were largely phased out beginning around the 1950s. Other types of exposures, however, including exposure from locomotive component parts and building materials, continued until these exposures were substantially eliminated by 1985. Additionally, the Company has retained liability for asbestos claims filed against its previously owned international container shipping business. Diseases associated with asbestos typically have long latency periods (amount of time between exposure to a disease and the onset of the disease) which can range from 10 to 40 years after exposure.

Critical Accounting Estimates, continued

CSXT retains a third-party specialist to assist management in assessing the value of the Company's occupational and asbestos reserves. The analysis is performed by the specialist semi-annually and is reviewed by management. The objective of the analysis is to determine the number of incurred but not reported ("IBNR") claims. With the exception of carpal tunnel, management and third-party specialists have determined that seven years is the most probable time period in which unasserted claim filings and claim values can be estimated. Carpal tunnel claims use a three-year period to estimate the reserve due to the shorter latency period for these types of injuries.

The third party specialist analyzes CSXT's historical claim filings, settlement amounts, and dismissal rates to determine future anticipated claim filing rates and average settlement values. The potentially exposed population is estimated by using CSX employment records and industry data from the Railroad Retirement 2009 report. From this analysis, the specialist provides an estimate of the IBNR claims liability.

The estimated future filing rates and estimated average claim values are the most sensitive assumptions for this reserve. A 1% increase or decrease in either the forecasted number of occupational and asbestos IBNR claims or the average claim values would result in approximately a $1 million increase or decrease in the liability recorded for unasserted occupational and asbestos claims.

During 2010 and 2009, the Company reduced occupational reserves by $12 million and $19 million respectively. The 2010 reduction is primarily attributable to a decrease in the number of repetitive stress injury claims and lower settlement values for irritant claims. The 2009 reduction is attributable to a decrease in the number of carpal tunnel and repetitive stress injury claims. This reduction was included in materials, supplies and other in the consolidated income statements.

During 2010 and 2009, the Company reduced its reserves for asbestos claims by $13 million and $24 million, respectively. The 2010 reduction was primarily related to some claims that were determined to have no value due to lack of sufficient medical evidence as well as a decrease in the estimate of future claim filings. The 2009 reduction was also primarily related to a significant number of claims that were determined to have no value due to lack of sufficient medical evidence. These reductions in reserves were included in materials, supplies and other in the consolidated income statements.

CSX CORPORATION
PART II

Critical Accounting Estimates, continued

Environmental

The Company is a party to various proceedings related to environmental issues, including administrative and judicial proceedings involving private parties and regulatory agencies. The Company has been identified as a potentially responsible party at approximately 247 environmentally impaired sites. Many of these are, or may be, subject to remedial action under the federal Comprehensive Environmental Response, Compensation and Liability Act of 1980, or CERCLA, also known as the Superfund Law, or similar state statutes. Most of these proceedings arose from environmental conditions on properties used for ongoing or discontinued railroad operations. A number of these proceedings, however, are based on allegations that the Company, or its predecessors, sent hazardous substances to facilities owned or operated by others for treatment, recycling or disposal. In addition, some of the Company's land holdings were leased to others for commercial or industrial uses that may have resulted in releases of hazardous substances or other regulated materials onto the property and could give rise to proceedings against the Company.

In any such proceedings, the Company is subject to environmental clean-up and enforcement actions under the Superfund Law, as well as similar state laws that may impose joint and several liability for clean-up and enforcement costs on current and former owners and operators of a site without regard to fault or the legality of the original conduct. These costs could be substantial.

In accordance with the Asset Retirement and Environmental Obligations Topic in the ASC, the Company reviews its role with respect to each site identified at least quarterly, giving consideration to a number of factors such as:

- type of clean-up required;
- nature of the Company's alleged connection to the location (e.g., generator of waste sent to the site or owner or operator of the site);
- extent of the Company's alleged connection (e.g., volume of waste sent to the location and other relevant factors); and
- number, connection and financial viability of other named and unnamed potentially responsible parties at the location.

As of December 2010, the Company had $107 million in environmental reserves. These recorded liabilities for estimated future environmental costs are undiscounted and include future costs for remediation and restoration of sites as well as any significant ongoing monitoring costs, but exclude any anticipated insurance recoveries. Based on the review process, the Company has recorded amounts to cover contingent anticipated future environmental remediation costs with respect to each site to the extent such costs are estimable and probable. Payments related to these liabilities are expected to be made over the next several years. Environmental remediation costs are included in materials, supplies and other on the consolidated income statement.

Table of Contents
CSX CORPORATION
PART II

Critical Accounting Estimates, continued

Currently, the Company does not possess sufficient information to reasonably estimate the amounts of additional liabilities, if any, on some sites until completion of future environmental studies. In addition, conditions that are currently unknown could, at any given location, result in additional exposure, the amount and materiality of which cannot presently be reliably estimated. Based upon information currently available, however, the Company believes its environmental reserves are adequate to fund remedial actions to comply with present laws and regulations, and that the ultimate liability for these matters, if any, will not materially affect its overall financial condition, results of operations or liquidity.

Legal

In accordance with the Contingencies Topic in the ASC, an accrual for a loss contingency is established if information available prior to issuance of the financial statements indicates that it is probable that an asset has been impaired or a liability has been incurred at the date of the financial statements, and the amount of loss can be reasonably estimated. If no accrual is made for a loss contingency because one or both of these conditions are not met, or if an exposure to loss exists in excess of the amount accrued, disclosure of the contingency is made when there is at least a reasonable possibility that a loss or an additional loss may have been incurred.

The Company evaluates all exposures relating to legal liabilities at least quarterly and adjusts reserves when appropriate under the guidance noted above. The amount of a particular reserve may be influenced by factors that include official rulings, newly discovered or developed evidence, or changes in laws, regulations and evidentiary standards.

Pension and Post-retirement Medical Plan Accounting

The Company sponsors defined benefit pension plans principally for salaried, management personnel. The plans provide eligible employees with retirement benefits based predominantly on years of service and compensation rates near retirement. For employees hired in 2003 or thereafter, benefits are determined based on a cash balance formula, which provides benefits by utilizing interest and pay credits based upon age, service and compensation. As of December 2010, the projected benefit obligation for the Company's pension plans was $2.5 billion. CSX made pension plan contributions of $250 million to its qualified defined benefit pension plans in 2009 and none in 2010.

In addition to these plans, the Company sponsors a self-insured post-retirement medical plan and a life insurance plan that provide benefits to full-time, salaried, management employees, hired prior to January 1, 2003, upon their retirement if certain eligibility requirements are met. Prior to 2011, the post-retirement medical plan was partially funded by all participating retirees, with retiree contributions adjusted annually. Beginning in 2011, Medicare-eligible retirees will be covered by a health reimbursement arrangement, which is an employer-funded account that can be used for reimbursement of eligible medical expenses. Non-Medicare eligible retirees will continue to be covered by the existing self-insured program. The life insurance plan is non-contributory.

Table of Contents

CSX CORPORATION
PART II

Critical Accounting Estimates, continued

For information related to the funded status of the Company's pension and other post-retirement benefit plans, see Note 8, Employee Benefit Plans.

The accounting for these plans is subject to the guidance provided in the Compensation—Retirement Benefits Topic in the ASC. This rule requires that management make certain assumptions relating to the following:

- discount rates used to measure future obligations and interest expense;
- long-term rate of return on plan assets;
- salary scale inflation rates;
- health care cost trend rates; and
- other assumptions.

The Company engages independent, external actuaries to compute the amounts of liabilities and expenses relating to these plans subject to the assumptions that the Company selects. The Company reviews the discount, long-term rate of return, salary scale inflation and health care cost trend rates on an annual basis and makes modifications to the assumptions based on current rates and trends as appropriate.

Discount Rates

Discount rates affect the amount of liability recorded and the interest expense component of pension and post-retirement expense. Discount rates reflect the rates at which pension and other post-retirement benefits could be effectively settled, or in other words, how much it would cost the Company to buy enough high quality bonds to generate cash flow equal to the Company's expected future benefit payments. The Company determines the discount rate based on the market yield as of year end for high quality corporate bonds whose maturities match the plans' expected benefit payments.

The discount rates used by the Company to value its 2010 pension and post-retirement obligations are 5.0% and 4.5%, respectively. For 2009, the discount rate used by the company to value its pension and post-retirement obligations was 5.25% and 4.75%, respectively. Discount rates may differ for pension and post-retirement benefits due to the different time horizons of future payments for each of the plans. As of December 2010, the time horizon for pensions is approximately 11 years, while, for post-retirement, the time horizon is approximately 7 years.

Each year, these discount rates are reevaluated and adjusted to reflect the best estimate of the current effective settlement rates. If interest rates generally decline or rise, the assumed discount rates will change.

CSX CORPORATION
PART II

Critical Accounting Estimates, continued

Long-term Rate of Return on Plan Assets

The expected long-term average rate of return on plan assets reflects the average rate of earnings expected on the funds invested, or to be invested, to provide for benefits included in the projected benefit obligation. In estimating that rate, the Company gives appropriate consideration to the returns being earned by the plan assets in the funds and the rates of return expected to be available for reinvestment as well as the current and projected asset mix of the funds. Management balances market expectations obtained from various investment managers and economists with both market and actual plan historical returns to develop a reasonable estimate of the expected long-term rate of return on assets. As this assumption is long-term, it is adjusted less frequently than other assumptions used in pension accounting. The long-term rate of return on plan assets used by the Company to value its pension obligation was 8.25% and 8.5% in 2010 and 2009, respectively.

Salary Scale Inflation Rates

Salary scale inflation rates are based on current trends and historical data accumulated by the Company. The Company reviews recent wage increases and management incentive compensation payments over the past five years in its assessment of salary scale inflation rates. The Company used a salary scale rate of 4.0% to value its 2010 and 2009 pension obligations.

Health Care Cost Trend Rates

Health care cost trend rates are based on recent plan experience and industry trends. The Company uses actuarial data to substantiate the inflation assumption for health care costs, representing increases in total plan costs (which include claims and administrative fee cost components). The 2010 and 2009 assumed health care cost trend rate for benefit obligations was 8.5% for non-Medicare-eligible participants and 8.0% for Medicare-eligible participants which is expected to decrease gradually until reaching 5% in 2018, based upon current actuarial projections. However, the year-to-year comparisons may fluctuate.

Other Assumptions

The calculations made by the actuaries also include assumptions relating to mortality rates, turnover and retirement age. These assumptions are based upon historical data and are selected by management.

Table of Contents

CSX CORPORATION
PART II

Critical Accounting Estimates, continued

2011 Estimated Pension and Post-retirement Expense

Net pension and post-retirement benefits expense for 2011 is expected to be approximately $75 million and $26 million, respectively, compared to $54 million and $32 million, respectively, in 2010. The increase in the pension expense is primarily related to additional amortization of the losses incurred by the pension plan assets during 2008 and the decrease in the discount rate (which causes expense to increase).

The following sensitivity analysis illustrates the effect of changes in certain assumptions like discount rates, salaries and health care costs on the 2010 estimated pension and post-retirement expense:

(Dollars in Millions)	Pension	OPEB
Discount Rate 1% decrease	$ 23	$ 1
Discount Rate 1% increase	$ (22)	$ (1)
Long-term Rate of Return 1% decrease	$ 19	N/A
Long-term Rate of Return 1% increase	$ (19)	N/A
Salary Inflation 1% decrease	$ (9)	N/A
Salary Inflation 1% increase	$ 10	N/A
Health Care Cost 1% change	N/A	$ 0

Depreciation Policies for Assets Utilizing the Group-Life Method

The Company depreciates its rail assets, including main-line track, locomotives and freight cars, using the group-life method of accounting. Assets depreciated under the group-life method comprise over 87% of total fixed assets of $32 billion on a gross basis at December 2010. All other assets of the Company are depreciated on a straight-line basis. The group-life method aggregates assets with similar lives and characteristics into groups and depreciates each of these groups as a whole. When using the group-life method, an underlying assumption is that each group of assets, as a whole, is used and depreciated to the end of its recoverable life.

The Company currently utilizes more than 130 different depreciable asset categories to account for depreciation expense for the railroad assets that are depreciated under the group-life method of accounting. Examples of depreciable asset categories include 18 different categories for crossties due to the different combinations of density classifications and asset types. By utilizing various depreciable categories, the Company can more accurately account for the use of its assets.

Table of Contents

CSX CORPORATION
PART II

Critical Accounting Estimates, continued

The Company believes the group-life method of depreciation closely approximates the straight-line method of depreciation. Additionally, due to the nature of most of its assets (e.g., track is one contiguous, connected asset), the Company believes that this is the most effective way to properly depreciate its assets.

Under the group-life method of accounting, the service lives and salvage values for each group of assets are determined by completing periodic life studies and applying management's assumptions regarding the service lives of its properties. A life study is the periodic review of asset lives for group assets conducted by a third-party specialist, analyzed by the Company's management and approved by the Surface Transportation Board ("STB"), the regulatory board that has broad jurisdiction over railroad practices. The STB requires life studies be performed for equipment assets every three years and for road (e.g. bridges and signals) and track (e.g., rail, ties and ballast) assets every six years. The Company believes the frequency currently required by the STB provides adequate review of asset lives and that a more frequent review would not result in a material change due to the long-lived nature of most of the assets.

Changes in asset lives due to the results of the life studies are applied on a prospective basis and could significantly impact future periods' depreciation expense, and thus, the Company's results of operations.

There are several factors taken into account during the life study and they include:

- statistical analysis of historical life and salvage data for each group of property;
- statistical analysis of historical retirements for each group of property;
- evaluation of current operations;
- evaluation of technological advances and maintenance schedules;
- previous assessment of the condition of the assets and outlook for their continued use;
- expected net salvage to be received upon retirement; and
- comparison of assets to the same asset groups with other companies.

Table of Contents

CSX CORPORATION
PART II

Critical Accounting Estimates, continued

For retirements or disposals of depreciable rail assets that occur in the ordinary course of business, the asset cost (net of salvage value or sales proceeds) is charged to accumulated depreciation and no gain or loss is recognized. As individual assets within a specific group are retired, resulting gains and losses are recorded in accumulated depreciation. As part of the life study, an assessment of the recorded amount of accumulated depreciation is made to determine if it is deficient (or in excess) of the appropriate amount indicated by the study. Any such deficiency (or excess), including any deferred gains or losses, is amortized as a component of depreciation expense over the remaining useful life of the asset group until the next required life study. Since the overall assumption with group-life is that the assets within the group on average have the same life and characteristics, it is therefore concluded that the deferred gains and losses offset over time.

In the event that large groups of assets are removed from service as a result of unusual acts or sales, resulting gains and losses are recognized immediately. These acts are not considered to be in the normal course of business and are therefore recognized when incurred. Examples of such acts would be the major destruction of assets due to significant storm damage (e.g., major hurricanes), the sale of a rail line segment to another railroad or the disposal of an entire class of assets (e.g., disposal of all refrigerated freight cars).

Recent experience with life studies has resulted in depreciation rate changes, which did not materially affect the Company's annual depreciation expense of $947 million and $903 million for 2010 and 2009, respectively. A 1% change in the average life of all group-life assets would result in a $9 million change to the Company's annual depreciation expense. The Company completed life studies for its equipment assets in 2009 and concluded life studies for its road, track and equipment assets in 2008 resulting in a reduction in depreciation expense of $11 million in 2010 and $18 million in 2009.

Income Taxes

CSX accounts for income taxes in accordance with the Income Taxes Topic in the ASC that addresses how tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. Under this topic, the Company must recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate resolution.

Table of Contents

CSX CORPORATION
PART II

Critical Accounting Estimates, continued

CSX files a consolidated federal income tax return, which includes its principal domestic subsidiaries. Examinations of the federal income tax returns of CSX have been completed through 2008. The federal income tax return for 2009 currently is under review. During 2010, the Company participated in a contemporaneous Internal Revenue Service ("IRS") audit of tax year 2010. Management believes adequate provision has been made for any adjustments that might be assessed. While the final outcome of these matters cannot be predicted with certainty, it is the opinion of CSX management that none of these items will have a material adverse effect on the financial condition, results of operations or liquidity of CSX. An unexpected adverse resolution of one or more of these items, however, could have a material adverse effect on the results of operations in a particular fiscal quarter or fiscal year. As of December 2010, the Company's uncertain tax positions were $20 million.

New Accounting Pronouncements and Change in Accounting Policy

See Note 1, Nature of Operations and Significant Accounting Policies under the caption, "New Accounting Pronouncements and Changes in Accounting Policy."

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

CSX does not hold or issue derivative financial instruments for trading purposes. Historically, the Company has used derivative financial instruments to address market risk exposure to fluctuations in interest rates and the risk of volatility in its fuel costs. As of December 2010, the Company had $10 million outstanding in interest rate swap agreements. A 1% fluctuation in interest rates on these swaps would cause less than a $1 million change in interest expense.

At December 2010, CSX had $67 million of outstanding floating rate debt obligations outstanding. A 1% fluctuation in interest rates on these notes would cause a $1 million change in interest expense.

Table of Contents

CSX CORPORATION
PART II

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

Table of Contents

CSX CORPORATION
PART II
REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and Board of Directors of CSX Corporation

We have audited the accompanying consolidated balance sheets of CSX Corporation as of December 31, 2010 and December 25, 2009, and the related consolidated statements of income, cash flows, and changes in shareholders' equity for each of the three fiscal years in the period ended December 31, 2010. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of CSX Corporation at December 31, 2010 and December 25, 2009, and the consolidated results of its operations and its cash flows for each of the three fiscal years in the period ended December 31, 2010, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), CSX Corporation's internal control over financial reporting as of December 31, 2010, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 18, 2011 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP
Certified Public Accountants

Jacksonville, Florida
February 18, 2011

Table of Contents

CSX CORPORATION
PART II

CONSOLIDATED INCOME STATEMENTS
(Dollars in Millions, Except Per Share Amounts)

	Fiscal Years		
	2010	2009 (Adjusted) (a)	2008 (Adjusted) (a)
Revenue	$10,636	$9,041	$11,255
Expense			
Labor and Fringe	2,957	2,629	2,955
Materials, Supplies and Other	2,075	1,999	2,407
Fuel	1,212	849	1,817
Depreciation	947	903	900
Equipment and Other Rents	374	391	425
Total Expense	7,565	6,771	8,504
Operating Income	3,071	2,270	2,751
Interest Expense	(557)	(558)	(519)
Other Income - Net (Note 10)	32	34	100
Earnings From Continuing Operations Before Income Taxes	2,546	1,746	2,332
Income Tax Expense (Note 12)	(983)	(618)	(847)
Earnings From Continuing Operations	1,563	1,128	1,485
Discontinued Operations (Note 14)	-	15	(130)
Net Earnings	$1,563	$1,143	$1,355
Per Common Share (Note 2)			
Net Earnings Per Share, Basic			
Continuing Operations	$4.10	$2.88	$3.71
Discontinued Operations	-	0.04	(0.32)
Net Earnings	$4.10	$2.92	$3.39
Net Earnings Per Common Share, Assuming Dilution			
Continuing Operations	$4.06	$2.85	$3.64
Discontinued Operations	-	0.04	(0.32)
Net Earnings	$4.06	$2.89	$3.32
Average Common Shares Outstanding (Thousands)	381,108	392,127	400,740
Average Common Shares Outstanding, Assuming Dilution (Thousands)	384,509	395,686	408,620
Cash Dividends Paid Per Common Share	$0.98	$0.88	$0.77

(a) Certain amounts have been adjusted for the retrospective change in accounting policy for rail grinding, see Note 1, Nature of Operations and Significant Accounting Policies.

See accompanying Notes to Consolidated Financial Statements

Table of Contents

CSX CORPORATION
PART II

CONSOLIDATED BALANCE SHEETS
(Dollars in Millions)

	December 2010	December 2009 (Adjusted) (a)
ASSETS		
Current Assets:		
Cash and Cash Equivalents (Note 1)	$1,292	$1,029
Short-term Investments	54	61
Accounts Receivable - Net (Note 1)	993	995
Materials and Supplies	218	203
Deferred Income Taxes	192	158
Other Current Assets	106	124
Total Current Assets	2,855	2,570
Properties	32,065	30,907
Accumulated Depreciation	(8,266)	(7,843)
Properties - Net (Note 6)	23,799	23,064
Investment in Conrail (Note 13)	673	650
Affiliates and Other Companies	461	438
Other Long-term Assets (Note 11)	353	165
Total Assets	$28,141	$26,887
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities:		
Accounts Payable	$1,046	$967
Labor and Fringe Benefits Payable	520	383
Casualty, Environmental and Other Reserves (Note 5)	176	190
Current Maturities of Long-term Debt (Note 9)	613	113
Income and Other Taxes Payable	85	112
Other Current Liabilities	97	100
Total Current Liabilities	2,537	1,865
Casualty, Environmental and Other Reserves (Note 5)	502	547
Long-term Debt (Note 9)	8,051	7,895
Deferred Income Taxes (Note 12)	7,053	6,528
Other Long-term Liabilities (Note 11)	1,298	1,284
Total Liabilities	19,441	18,119
Shareholders' Equity:		
Common Stock, $1 Par Value (Note 3)	370	393
Other Capital	-	80

Retained Earnings (Note 1)	9,087	9,090
Accumulated Other Comprehensive Loss (Note 1)	(771)	(809)
Noncontrolling Minority Interest	14	14
Total Shareholders' Equity	8,700	8,768
Total Liabilities and Shareholders' Equity	$28,141	$26,887

(a) Certain amounts have been adjusted for the retrospective change in accounting policy for rail grinding, see Note 1, Nature of Operations and Significant Accounting Policies

See accompanying Notes to Consolidated Financial Statements

Table of Contents

CSX CORPORATION
PART II

CONSOLIDATED CASH FLOW STATEMENTS
(Dollars in Millions)

	Fiscal Years
	2010
OPERATING ACTIVITIES	
Net Earnings	$
Adjustments to Reconcile Net Earnings to Net Cash Provided by Operating Activities:	
Depreciation	
Deferred Income Taxes	
Non-cash Discontinued Operations (Note 14)	

In early May 2008, Gas Solutions II Ltd purchased a series of propane puts at $0.10 out of the money and at prices of $1.5
gallon and $1.394 per gallon covering the periods May 1, 2008, through April 30, 2009, and May 1, 2009, through Apr
2010, respectively. These hedges were executed at close to the highest market propane prices ever achieved on an hist
basis; such hedges preserve the upside of Gas Solutions II Ltd to benefit from potential future increases in commodity p
GSHI generated approximately $26,172 of EBITDA for the fiscal year ending December 31, 2008, an increase of 67%
2007 results. Despite the volatility in commodity prices over the last year, GSHI generated approximately $25,816 of EB
for the fiscal year ending December 31, 2009.

In determining the value of GSHI, we have utilized several valuation techniques to determine the value of the investment.
techniques offer a wide range of values. Our Board of Directors has determined the value to be $85,187 for our debt and e
positions at December 31, 2009 based upon a combination of a discounted cash flow analysis and a public compar
analysis. At December 31, 2009 and June 30, 2009, GSHI was valued $50,184 above its amortized cost.

Integrated Contract Services, Inc.

ICS is an investment that we made in April 2007. Prior to January 2009, ICS owned the assets of ESA Environm
Specialists, Inc. ("ESA") and 100% of the stock of The Healing Staff ("THS"). ESA originally defaulted under our co
governing our investment in ESA, prompting us to commence foreclosure actions with respect to certain ESA assets in re
of which we have a priority lien. In response to our actions, ESA filed voluntarily for reorganization under the bankruptcy
on August 1, 2007. On September 20, 2007, the U.S. Bankruptcy Court approved a Section 363 Asset Sale from ESA to u

complete this transaction, we contributed our ESA debt to a newly-formed entity, ICS, and provided funds for working capital on October 9, 2007. In return for the debt, we received senior secured debt in ICS of equal amount to our ESA debt, preferred stock of ICS, and 49% of th common stock. ICS subsequently ceased operations and assigned the collateral back to us. ICS is in default of both paymer financial covenants. During September and October 2007, we provided $1,170 to THS for working capital.

In January 2009, we foreclosed on the real and personal property of ICS. Through this foreclosure process, we gained ownership of THS and certain ESA assets. Based upon an analysis of the liquidation value of the ESA assets and the ente value of THS, our Board of Directors affirmed the fair value of our investment in ICS at $5,275 at December 31, 20 reduction of $11,377 from its amortized cost, compared to the $11,652 unrealized loss recorded at June 30, 2009.

Iron Horse Coiled Tubing, Inc.

Iron Horse is an investment that we made in April 2006. Iron Horse had been a provider of coiled tubing subcontractor se prior to making a strategic decision in late 2007 to directly service natural gas and oil producers in the Western Can Sedimentary Basin ("WCSB") as a fracturing services provider. As a result of the business transition, the Company's financial performance declined significantly from 2007 levels. Iron Horse completed its transition from a subcontracto direct service provider in 2009, but natural gas prices fell to trough levels due to the recession and heightened natura inventory levels. Since November 2009, Iron Horse has seen increased activity in the WCSB and is now completing wel several large producers in the WCSB.

Prior to December 31, 2007, we owned 8.5% of the common stock in Iron Horse. On December 31, 2007, we receiv additional 50.3% of the common stock in Iron Horse, which increased our total ownership to 58.8%. Through a ser subsequent loans that were used to construct equipment and facilitate the transition from a subcontractor to a direct se provider, we secured an additional 21.0% of the common stock in Iron Horse in September 2008, which increased our ownership to 79.8% of the common stock in Iron Horse.

The Board of Directors wrote-down the fair value of our investment in Iron Horse to $12,318 as of December 31, 20 reduction of $8,399 from its amortized cost, compared to the $6,738 unrealized loss recorded at June 30, 2009.

Yatesville Coal Holdings, Inc.

All of our coal holdings have been consolidated under common management in Yatesville. Yatesville began to improvement after the consolidation of the coal holdings, but the company exhausted its permitted reserves in December and has not had any meaningful revenue stream since. We continue to evaluate strategies for Yatesville such as soli indications of interest regarding a transaction involving part or all of recoverable reserves. During the six months December 31, 2009, we provided additional funding of $3,376 to Yatesville to fund ongoing operations including permitting. During the quarter, we discontinued operations at Yatesville. As of December 31, 2009, our Board of Dir determined that consistent with the decision to discontinue operations, the impairment of Yatesville was other than temp and we recorded a realized loss of $51,228 which was the amount that the amortized cost exceeded the fair value at Dec 31, 2009. Our Board of Directors set the value of the remaining Yatesville investment at $1,035, which represents the re value of recoverable reserves, as of December 31, 2009, a reduction of $12,062 from its value as of June 30, 2009.

Capitalization

Our investment activities are capital intensive and the availability and cost of capital is a critical component of our busines
capitalize our business with a combination of debt and equity. Our debt currently consists of a

revolving credit facility availing us of the ability to borrow debt subject to borrowing base determinations and our equity c
is currently comprised entirely of common equity.

On June 25, 2009, we completed a first closing on an expanded $250,000 syndicated revolving credit facility (the "Faci
The new Facility, for which six lenders have closed on $210,000 to date, includes an accordion feature which allows the Fa
to accept up to an aggregate total of $250,000 of commitments for which we continue to solicit additional commitments
other lenders for the additional $40,000. The revolving period of the Facility extends through June 2010, with an addition
year amortization period after the completion of the revolving period. As of December 31, 2009 and June 30, 2009, w
$10,000 and $124,800 of borrowings outstanding under our credit facility, respectively.

Interest on borrowings under the credit facility is one-month Libor plus 400 basis points, subject to a minimum Libor fl
200 basis points after that date. The maintenance of this facility requires us to pay a fee for the amount not drawn upon. Th
assessed at the rate of 100 basis points per annum. The following table shows the facility amounts and outstanding borro
at December 31, 2009 and June 30, 2009:

	As of December 31, 2009		As of June 30, 2009	
	Facility Amount	Amount Outstanding	Facility Amount	Amour Outstand
Revolving Credit Facility	$ 195,000	$ 10,000	$ 175,000	$ 124,80

The following table shows the contractual maturity of our revolving credit facility at December 31, 2009:

	Payments Due By Period		
	Less Than 1 Year	1 - 3 Years	More Than 3 Years
Credit Facility Payable	$ 10,000	$ —	$

During the six months ended December 31, 2009, we completed public and private offerings and raised $97,675 of addi
equity by issuing 11,431,797 shares of our common stock below net asset value diluting shareholder value by $0.75 per
We also issued 8,444,068 shares to acquire Patriot increasing net asset value to shareholders by $0.03 per share. The follo
table shows the calculation of net asset value per share as of December 31, 2009 and June 30, 2009:

	As of December 31, 2009	As of June 30, 2
Net Assets	$ 637,477	$ 532,596
Shares of common stock outstanding	63,349,746	42,943,084
Net asset value per share	$ 10.06	$ 12.40

At December 31, 2009, we had 63,349,746 of our common stock issued and outstanding.

Results of Operations

For the three months ended December 31, 2009 and December 31, 2008, the net (decrease) increase in net assets resulting
operations was ($16,853) and $6,524, respectively, representing ($0.29) and $0.22 per share, respectively. We experienced

realized and unrealized loss of $33,778 or approximately $0.59 per share in the three months ended December 31, 2009
compares with the net realized and unrealized loss of $5,436 during the three months ended December 31, 20
approximately $0.18 per share.

For the six months ended December 31, 2009 and December 31, 2008, the net (decrease) increase in net assets resulting operations was ($23,231) and $20,522, respectively, representing ($0.43) and $0.69 per share, respectively. We experien net realized and unrealized loss of $52,474 or approximately $0.98 per share in the six months ended December 31, 2009 compares with the net realized and unrealized loss of $14,940 during the six months ended December 31, 20 approximately $0.51 per share.

While we seek to maximize gains and minimize losses, our investments in portfolio companies can expose our capital to greater than those we may anticipate as these companies are typically not issuing securities rated investment grade, have li resources, have limited operating history, are generally private companies with limited operating information available an likely to depend on a small core of management talents. Changes in any of these factors can have a significant impact o value of the portfolio company.

Investment Income

We generate revenue in the form of interest income on the debt securities that we own, dividend income on any comm preferred stock that we own, and amortized loan origination fees on the structuring of new deals. Our investments, if in the of debt securities, will typically have a term of one to ten years and bear interest at a fixed or floating rate. To the e achievable, we will seek to collateralize our investments by obtaining security interests in our portfolio companies' asset also may acquire minority or majority equity interests in our portfolio companies, which may pay cash or in-kind dividend recurring or otherwise negotiated basis. In addition, we may generate revenue in other forms including prepayment pen and possibly consulting fees. Any such fees generated in connection with our investments are recognized as earned.

Investment income consists of interest income, including accretion of loan origination fees and prepayment penalty dividend income and other income, including net profits interest, overriding royalties interest and structuring fees following table details the various components of investment income and the related levels of debt investments for the months ended December 31, 2009 and December 31, 2008:

	For The Three Months Ended December 31,		For The Six Months Ended December 31,	
	2009	2008	2009	2008
Interest income	$ 18,539	$ 17,241	$ 33,374	$ 34,7
Dividend income	4,170	4,665	10,388	9,3
Other income	6,174	307	6,638	13,8
Total investment income	$ 28,883	$ 22,213	$ 50,400	$ 58,0
Average debt principal of investments	$ 571,809	$ 537,101	$ 535,069	$ 517,4
Weighted-average interest rate earned	12.86%	12.74%	12.37%	13.

Total investment income increased significantly from $22,213 for the three months ended December 31, 2008 to $28,883 f six months ended December 31, 2009. This $6,670 increase is primarily due to the Patriot acquisition, for which we recog a gain from the acquisition of $5,714 and purchase discount accretion of $5,320 during the three months ended Decemb 2009. The discount accretion includes $4,560 of accelerated accretion from early repayments of ADAPCO, Quartermast Aylward. Total investment income has decreased for the six months ended December 31, 2009 from the amount reported f six months ended December 31, 2008 primarily due to a decrease in other income. This $7,189 decrease in other inco

primarily due to the settlement of our net profit interests in IEC/ARS for $12,576 during the six months ended Decemb
2008, partially offset but gain from the acquisition of Patriot.

Average principal balances of debt investments have increased from $537,101 for the three months ended December 31, 20
$571,809 for the three months ended December 31, 2009. For the six months ended December 31, 2008

---

and 2009, average principal balances of debt investments increased from $517,421 to $535,069, respectively. These incr are primarily due to the Patriot acquisition which resulted in an additional $289,030 of debt principal to our portfolio.

The weighted-average interest rate earned increased from 12.74% for the three months ended December 31, 2008 to 12.86 the three months ended December 31, 2009. This increase is primarily the result of purchase discount accretion of $5,320 the Patriot acquisition. For the six months ended December 31, 2008 and 2009, weighted-average interest rate earned decr from 13.34% to 12.37%, respectively. This decrease is primarily the result of Patriot acquisition purchase discount accr offset by foregone interest on non-accrual loans. During the six month period ended December 31, 2009, interest of $1 was foregone on non-accrual debt investments compared to $4,983 of forgone interest for the three months ended Decemb 2008. Without adjustments for foregone interest and purchase discount accretion from the Patriot acquisition, the wei average interest rates earned on debt investments would have been 15.0% and 15.3% for the three months ended Decemb 2009 and 2008, respectively.

Operating Expenses

Our primary operating expenses consist of investment advisory fees (base management and income incentive fees), facility costs, legal and professional fees and other operating and overhead-related expenses. These expenses incluc allocable portion of overhead under the Administration Agreement with Prospect Administration under which Pro Administration provides administrative services and facilities for us. Our investment advisory fees compensate our Inves Adviser for its work in identifying, evaluating, negotiating, closing and monitoring our investments. We bear all other cos expenses of our operations and transactions in accordance with our Administration Agreement with Prospect Administr Operating expenses were $11,958 and $10,253 for the three months ended December 31, 2009 and December 31, respectively. Operating expenses were $21,157 and $22,550 for the six months ended December 31, 2009 and Decemb 2008, respectively.

The base management fee was $3,176 and $2,940 for the three months ended December 31, 2009 and December 31, respectively. The base management fee was $6,385 and $5,763 for the six months ended December 31, 2009 and Decemb 2008, respectively. The increase in this expense for the three and six months ended December 31, 2009 is directly related growth in total assets.

For the three months ended December 31, 2009 and December 31, 2008, we incurred $4,231 and $2,990, respective income incentive fees. The $1,241 increase in the income incentive fee for the respective three-month period is driven increase in pre-incentive fee net investment income from $14,950 for the three months ended December 31, 2008 to $21,1 the three months ended December 31, 2009, primarily the result of additional investment income from the Patriot acquis For the six months ended December 31, 2009 and December 31, 2008, we incurred $7,311 and $8,865, respectively, of in incentive fees. The $1,554 decrease in the income incentive fee for the respective six-month period is driven by a decre pre-incentive fee net investment income from $44,327 for the six months ended December 31, 2008 to $36,554 for th months ended December 31, 2009, primarily the result of the settlement of net profits interest in IEC/ARS in the 2008 p offset by the income from the Patriot acquisition. No capital gains incentive fee has yet been incurred pursuant to the Inves Advisory Agreement.

During the three and six months ended December 31, 2009, we incurred $1,995 and $3,369 of expenses related to our facility. This compares with expenses of $1,965 and $3,483 incurred during the three and six months ended December 31,

These expenses are related directly to the leveraging capacity put into place for each of those periods and the lev
indebtedness actually undertaken during those quarters. The table below describes the various credit facility expenses ar
related indicators of leveraging capacity and indebtedness during these periods.

	For The Three Months Ended December 31, 2009	2008	For The Six Months Ended December 31, 2009	2008
Interest on borrowings	$ 266	$ 1,712	$ 393	$ 2,942
Amortization of deferred financing costs	1,282	180	2,106	360
Commitment and other fees	447	73	870	181
Total	$ 1,995	$ 1,965	$ 3,369	$ 3,483
Weighted-average debt outstanding	$ 17,609	$ 137,525	$ 13,003	$ 125,845
Weighted-average interest rate on borrowings	6.00 %	4.94 %	6.00 %	4.64
Facility amount at beginning of period	$ 195,000	$ 200,000	$ 195,000	$ 200,000

The increase in our interest rate incurred is primarily due to an increase of 150 basis points in our current borrowin effective June 25, 2009.

As our asset base has grown and we have added complexity to our capital raising activities, due, in part, to our assumpt the sub-administration role from Vastardis, we have commensurately increased the size of our administrative and financial accounting for a significant increase in the overhead allocation from Prospect Administration. Over the last year, Pro Administration has added several additional staff members, including a senior finance professional, a controller, two corp counsels and other finance professionals. As our portfolio continues to grow, we expect to continue to increase the size administrative and financial staff on a basis that provides increasing returns to scale. However, initial investme administrative and financial staff may not provide returns to scale immediately, perhaps not until the portfolio increase greater size. Other allocated expenses from Prospect Administration have, as expected, increased alongside with the incre staffing and asset base.

Legal costs increased from $184 for the three months ended December 31, 2008 to $390 for the three months ended Dece 31, 2009 primarily due to the increased size of our portfolio. Legal costs decreased from $483 for the six months December 31, 2008 to $390 for the six months ended December 31, 2009 as there were legal matters in the prior year that longer active.

Net Investment Income, Net Realized (Loss) Gains, (Decrease) Increase in Net Assets from Net Change in Unrealized Depreciation/Appreciation and Net (Decrease) Increase in Net Assets Resulting from Operations

Net investment income was $16,925 and $11,960 for the three months ended December 31, 2009 and December 31, respectively. This $4,965 increase was due primarily to the Patriot acquisition, for we recognized a gain from the acqui and purchase discount accretion, partially offset by increased advisory fees and forgone interest related to Iron Hors investment income was $29,243 and $35,462 for the six months ended December 31, 2009 and December 31, respectively. This $6,219 decrease is due primarily to the settlement of our net profit interests in IEC/ARS during t months ended December 31, 2008, offset by the Patriot acquisition, increased advisory fees and forgone interest related t Horse for the six months ended December 31, 2009.

Net realized (loss) gains were ($51,229) and $16 for the three months ended December 31, 2009 and December 31, respectively. Net realized (loss) gains were ($51,229) and $1,661 for the six months ended December 31, 2009 and Dece 31, 2008, respectively. The net realized loss of $51,229 for the three and six months ended December 31, 2009 wa primarily to the impairment of Yatesville. See Investment Valuations for further discussion.

Net increase (decrease) in net assets from changes in unrealized appreciation/depreciation was $17,451 and ($5,452) f three months ended December 31, 2009 and December 31, 2008, respectively. For the three months ended

December 31, 2009, the $17,451 increase in net assets from the net change in unrealized appreciation/depreciation was d
primarily by our impairment of Yatesville which resulted in $40,856 being reversed out of unrealized, partially offs
write-downs of our investments in Ajax, H&M, NRG and R-V. For the three months ended December 31, 2008, the $
decrease in net assets from the net change in unrealized appreciation/depreciation was driven primarily by write-downs
investments in Deb Shops, Iron Horse, Qualitest, RMC, Resco, WEPI, and Yatesville which were partially offset by unre
appreciation of our investment in GSHI.

Net decrease in net assets from changes in unrealized appreciation/depreciation was $1,245 and $16,601 for the six m
ended December 31, 2009 and December 31, 2008, respectively. The $1,245 decrease occurring during the six months e
December 31, 2009 was primarily attributable to unrealized depreciation recognized for our investments in Ajax, Coalbed
Shops, H&M, NRG, and R-V partially offset by the impairment of our investment in Yatesville of $51,228. The $1
decrease occurring during the six months ended December 31, 2008 was attributable to unrealized depreciation recogniz
our investments in Deb Shops, Iron Horse, Qualitest, RMC, Resco, WEPI, and Yatesville partially offset by a write-up o
investment in GSHI.

Financial Condition, Liquidity and Capital Resources

For the six months ended December 31, 2009 and December 31, 2008, our operating activities provided (used) $155,12
($23,126) of cash, respectively. Investing activities for the Patriot acquisition used $106,586 and zero for the six months e
December 31, 2009 and December 31, 2008, respectively. Financing activities provided $54,640 and $25,009 of cash durin
six months ended December 31, 2009 and December 31, 2008, respectively, which included the payments of divider
$36,469 and $22,221, during the six months ended December 31, 2009 and December 31, 2008, respectively.

Our primary uses of funds have been to continue to invest in our investments in portfolio companies, to add new compan
our investment portfolio, acquire Patriot, repay outstanding borrowings and to make cash distributions to holders o
common stock.

We have and may continue to fund a portion of our cash needs through borrowings from banks, issuances of senior securit
secondary offerings. We may also securitize a portion of our investments in mezzanine or senior secured loans or other a
Our objective is to put in place such borrowings in order to enable us to expand our portfolio. At December 31, 2009, w
$10,000 outstanding borrowings on our $195,000 revolving credit facility. Subsequent to December 31, 2009, we compl
closing for an additional $15,000 commitment to the revolving credit facility, increasing total commitments to $210,000.

On September 6, 2007, our Registration Statement on Form N-2 was declared effective by the SEC. At December 31,
under the Registration Statement, we had remaining availability to issue up to approximately $147,500 of our equity secu
over the next eight months.

We also continue to generate liquidity through public and private stock offerings. On July 7, 2009 we completed a public
offering for 5,175,000 shares of our common stock at $9.00 per share, raising $46,575 of gross proceeds. On August 20,
and September 24, 2009, we issued 3,449,686 shares and 2,807,111 shares, respectively, of our common stock at $8.5
$9.00 per share, respectively, in private stock offerings, raising $29,322, and $25,264 of gross proceeds, respect
Concurrent with the sale of these shares, we entered into a registration rights agreement in which we granted the purch

certain registration rights with respect to the shares. Under the terms and conditions of the registration rights agreemen
filed with the SEC a post-effective amendment to the registration statement on Form N-2 on November 6, 2009.
amendment was declared effective by the SEC on November 9, 2009.

On December 2, 2009 we acquired the outstanding shares of Patriot common stock for approximately $201,083. Und
terms of the merger agreement, Patriot common shareholders received 0.363992 shares of our common

---

stock for each share of Patriot common stock, resulting in 8,444,068 shares of common stock being issued by us. In conne
with the transaction, we repaid all the outstanding borrowings of Patriot, in compliance with the merger agreement.

Off-Balance Sheet Arrangements

At December 31, 2009, we did not have any off-balance sheet liabilities or other contractual obligations that are reaso
likely to have a current or future material effect on our financial condition, other than those which originate from
investment advisory and management agreement and the administration agreement and 2) the portfolio companies.

Developments Since the End of the Fiscal Quarter

On January 25, 2010, we issued 236,985 shares of our common stock in connection with the dividend reinvestment plan.

On January 4, 2010, we completed a closing for an additional $15,000 commitment to the Facility, increasing
commitments to $210,000.

Merger Discussions with Allied Capital Corporation

On January 14, 2010, Prospect Capital delivered a proposal letter to the Allied Capital Board (the "First Prospect Capital M
Offer Letter") containing an offer to acquire each outstanding Allied Capital Corporation ("Allied Capital") Share in exc
for 0.385 of a share of Prospect Capital Common Stock (the "First Prospect Capital Merger Offer").

On January 19, 2010, Allied Capital filed a Form 8-K stating that the Allied Capital Board determined that the First Pro
Capital Merger Offer did not constitute a "Superior Proposal" as such term is defined in the Ares Capital Merger Agreeme

On January 20, 2010, Prospect Capital issued a press release containing a copy of a letter it subsequently sent to the A
Capital Board in connection with the First Prospect Capital Merger Offer.

On January 26, 2010, Prospect Capital announced that it delivered another letter to the Allied Capital Board, raising its o
acquire Allied Capital (the "Second Prospect Capital Merger Offer Letter").

On February 3, 2010, Allied Capital informed us and filed a Form 8-K stating that the Allied Capital Board determined th
Second Prospect Capital Merger Offer did not constitute a "Superior Proposal" as such term is defined in the Ares C
Merger Agreement.

On February 9, 2010, Prospect Capital announced that it delivered another letter to the Allied Capital Board, raising its o
acquire Allied Capital (the "Third Prospect Capital Merger Offer Le

On February 11, 2010, Allied Capital informed us and filed a Form 8-K stating that the Allied Capital Board determined th Third Prospect Capital Merger Offer did not constitute a "Superior Proposal" as such term is defined in the Ares Capital M Agreement. Prospect Capital has filed proxy materials to solicit Allied Shareholders to vote against Allied's proposed merg with Ares Capital Corporation. A merger with Allied would be material to Prospect Capital and its shareholders. If Prospe Capital were to negotiate a merger agreement with Allied, Prospect Capital would provide extensive disclosure to its shareholders regarding the terms and conditions of and risks regarding such transaction.

REPORT OF MANAGEMENT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Management is responsible for establishing and maintaining adequate internal control over financial reporting, an
performing an assessment of the effectiveness of internal control over financial reporting as of June 30, 2009. Internal co
over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reportin
the preparation of financial statements for external purposes in accordance with generally accepted accounting principles
Company's internal control over financial reporting includes those policies and procedures that (i) pertain to assets o
Company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of fina
statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Compan
being made only in accordance with authorizations of management and directors of the Company; and (iii) provide reaso
assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company's asset
could have a material effect on the financial statements.

Management performed an assessment of the effectiveness of the Company's internal control over financial reporting as of
30, 2009 based upon criteria in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organiz
the Treadway Commission ("COSO"). Based on our assessment, management determined that the Company's internal co
over financial reporting was effective as of June 30, 2009 based on the criteria on Internal Control — Integrated Framewor
by COSO. There were no changes in our internal control over financial reporting during the quarter ended June 30, 200
have materially affected, or are reasonably likely to affect, our internal control over financial reporting.

Our management's assessment of the effectiveness of our internal control over financial reporting as of June 30, 2009 has
audited by BDO Seidman LLP, an independent registered public accounting firm, as stated in their report which appears
10-K.

USE OF PROCEEDS

Unless otherwise specified in a prospectus supplement, we intend to use the net proceeds from selling Securities pursuant t
prospectus initially to maintain balance sheet liquidity, involving repayment of debt under our credit facility, investme
high quality short-term debt instruments or a combination thereof, and thereafter to make long-term investments in accor
with our investment objective. A supplement to this prospectus relating to each offering will provide additional detail,
extent known at the time, regarding the use of the proceeds from such offering including any intention to utilize proceeds t
expenses in order to avoid sales of long-term assets.

We anticipate that substantially all of the net proceeds of an offering of Securities pursuant to this prospectus will be us
the above purposes within six months, depending on the availability of appropriate investment opportunities consistent wi
investment objective and market conditions. In addition, we expect that there will be several offerings pursuant t
prospectus; we expect that substantially all of the proceeds from all offerings will be used within three years. Pending ou
investments, we plan to invest a portion of net proceeds in cash equivalents, U.S. government securities and other high-q
debt investments that mature in one year or less from the date of investment and other general corporate purposes
management fee payable by us will not be reduced while our assets are invested in such securities. See "Regulation — Te
Investments" for additional information about temporary investments we may make while waiting to make longer
investments in pursuit of our investment objective.

FORWARD-LOOKING STATEMENTS

Our annual report on Form l0-K for the year ended June 30, 2009, any of our quarterly reports on Form 10-Q or current re on Form 8-K, or any other oral or written statements made in press releases or otherwise by or on behalf of Prospect C Corporation including this prospectus may contain forward looking statements within the meaning of the Section 21E Securities Exchange Act of 1934, as amended, which involve substantial risks and uncertainties. Forward looking staten predict or describe our future operations, business plans, business and investment strategies and portfolio management an performance of our investments and our investment management business. These forward-looking statements are not hist facts, but rather are based on current expectations, estimates and projections about our industry, our beliefs, an assumptions. Words such as "intends," "intend," "intended," "goal," "estimate," "estimates," "expects," "expect," "expe "project," "projected," "projections," "plans," "seeks," "anticipates," "anticipated," "should," "could," "may," "will," "des to," "foreseeable future," "believe," "believes" and "scheduled" and variations of these words and similar expression intended to identify forward-looking statements. Our actual results or outcomes may differ materially from those anticip Readers are cautioned not to place undue reliance on these forward looking statements, which speak only as of the da statement was made. We undertake no obligation to publicly update or revise any forward looking statements, whethe result of new information, future events or otherwise. These forward-looking statements do not meet the safe harb forward-looking statements pursuant to Section 27A of the Securities Act. These statements are not guarantees of f performance and are subject to risks, uncertainties, and other factors, some of which are beyond our control and diffic predict and could cause actual results to differ materially from those expressed or forecasted in the forward-looking staten including without limitation:

- our future operating results,
- our business prospects and the prospects of our portfolio companies,
- the impact of investments that we expect to make,
- the dependence of our future success on the general economy and its impact on the industries in which we inv
- the ability of our portfolio companies to achieve their objectives,
- difficulty in obtaining financing or raising capital, especially in the current credit and equity environment,
- the level and volatility of prevailing interest rates and credit spreads, magnified by the current turmoil in the credit markets,
- adverse developments in the availability of desirable loan and investment opportunities whether they are due competition, regulation or otherwise,
- a compression of the yield on our investments and the cost of our liabilities, as well as the level of leverage available to us,
- our regulatory structure and tax treatment, including our ability to operate as a business development compan and a regulated investment company;
- the adequacy of our cash resources and working capital;
- the timing of cash flows, if any, from the operations of our portfolio companies;
-

the ability of our investment adviser to locate suitable investments for us and to monitor and administer our investments,

- authoritative generally accepted accounting principles or policy changes from such standard-setting bodies as Financial Accounting Standards Board, the Securities and Exchange Commission, Internal Revenue Service, New York Stock Exchange, and other authorities that we are subject to, as well as their counterparts in any foreign jurisdictions where we might do business; and
- the risks, uncertainties and other factors we identify in "Risk Factors" and elsewhere in this prospectus and in filings with the SEC.

Although we believe that the assumptions on which these forward-looking statements are based are reasonable, any of assumptions could prove to be inaccurate, and as a result, the forward-looking statements based on those assumptions also be inaccurate. Important assumptions include our ability to originate new loans and investments, certain margins and lev profitability and the availability of additional capital. In light of these and other uncertainties, the inclusion of a project forward-looking statement in this prospectus should not be regarded as a representation by us that our plans and objective be achieved. These risks and uncertainties include those described or identified in "Risk Factors" and elsewhere i prospectus. You should not place undue reliance on these forward-looking statements, which apply only as of the date o prospectus.

DISTRIBUTIONS

We have paid and intend to continue to distribute quarterly distributions to our stockholders out of assets legally availab distribution. Our distributions, if any, will be determined by our Board of Directors. Certain amounts of the qua distributions may from time to time be paid out of our capital rather than from earnings for the quarter as a result o deliberate planning or by accounting reclassifications.

In order to maintain RIC tax treatment, we must distribute at least 90% of our ordinary income and realized net short capital gains in excess of realized net long-term capital losses, if any, out of the assets legally available for distribution. In to avoid certain excise taxes imposed on RICs, we are required to distribute with respect to each calendar year by January the following year an amount at least equal to the sum of

- 98% of our ordinary income for the calendar year,
- 98% of our capital gains in excess of capital losses for the one-year period ending on October 31 of the calen year, and
- any ordinary income and net capital gains for preceding years that were not distributed during such years.

In December 2008, our Board of Directors elected to retain excess profits generated in the quarter ended September 30, and pay a 4% excise tax on such retained earnings. This tax of $533,000 was paid in the quarter ending March 31, 2009.

In addition, although we currently intend to distribute realized net capital gains (which we define as net long-term capital in excess of short-term capital losses), if any, at least annually, out of the assets legally available for such distributions, w decide in the future to retain such capital gains for investment. In such event, the consequences of our retention of net c gains are as described under "Material U.S. Federal Income Tax Considerations." We can offer no assurance that w achieve results that will permit the payment of any cash distributions and, if we issue senior securities, we may be proh from making distributions if doing so causes us to fail to maintain the asset coverage ratios stipulated by the 1940 Ac distributions are limited by the terms of any of our borrowings.

We maintain an "opt out" dividend reinvestment plan for our common stockholders. As a result, if we declare a dividend stockholders' cash dividends will be automatically reinvested in additional shares of our common stock, unless they specif "opt out" of the dividend reinvestment plan so as to receive cash dividends. See "Dividend Reinvestment Plan." To the e prudent and practicable, we intend to declare and pay dividends on a quarterly basis.

With respect to the dividends paid to stockholders, income from origination, structuring, closing, commitment and other u fees associated with investments in portfolio companies were treated as taxable income and accordingly, distribu stockholders. For the fiscal year ended June 30, 2009, we declared total dividends of approximately $56.1 million. For th and second quarters of the fiscal year ending June 30, 2010, we paid total distributions of approximately $22.3 millio $25.9 million, respectively.

Tax characteristics of all distributions will be reported to stockholders, as appropriate, on Form 1099-DIV after the end
year. Our ability to pay distributions could be affected by future business performance, liquidity, capital needs, altern
investment opportunities and loan covenants.

The following table lists the quarterly distributions per share since shares of our common stock began being regularly quot
The NASDAQ Global Select Market:

Date Declared	Record Date	Payment Date		Per Share		Amount
11/11/2004	12/10/2004	12/30/2004	$	0.100	$	705,510
2/9/2005	3/11/2005	3/31/2005	$	0.125	$	881,888
4/21/2005	6/10/2005	6/30/2005	$	0.150	$	1,058,26
9/15/2005	9/22/2005	9/29/2005	$	0.200	$	1,411,02
12/12/2005	12/22/2005	12/29/2005	$	0.280	$	1,975,42
3/15/2006	3/24/2006	3/31/2006	$	0.300	$	2,116,53
6/14/2006	6/23/2006	6/30/2006	$	0.340	$	2,401,06
7/31/2006	9/22/2006	9/29/2006	$	0.380	$	4,858,87
12/15/2006	12/29/2006	1/5/2007	$	0.385	$	7,263,92
3/14/2007	3/23/2007	3/30/2007	$	0.3875	$	7,666,83
6/14/2007	6/22/2007	6/29/2007	$	0.390	$	7,752,90
9/6/2007	9/19/2007	9/28/2007	$	0.3925	$	7,830,00
12/18/2007	12/28/2007	1/7/2008	$	0.395	$	9,369,85
3/6/2008	3/31/2008	4/16/2008	$	0.400	$	10,468,4
6/19/2008	6/30/2008	7/16/2008	$	0.40125	$	11,845,0
9/16/2008	9/30/2008	10/16/2008	$	0.4025	$	11,881,9
12/19/2008	12/31/2008	1/19/2009	$	0.40375	$	11,966,3
3/24/2009	3/31/2009	4/20/2009	$	0.405	$	12,670,8
6/23/2009	7/8/2009	7/20/2009	$	0.40625	$	19,547,9
9/28/2009	10/8/2009	10/19/2009	$	0.4075	$	22,278,9
12/17/2009	12/31/2009	1/25/2010	$	0.40875	$	25,894,2
Total Declared					$	181,845

SENIOR SECURITIES

Information about our senior securities is shown in the following table as of each fiscal year ended June 30 since the Con
commenced operations and as of December 31, 2009, unless otherwise noted. The report of our independent registered p
accounting firm on the senior securities table as of June 30, 2009 is attached as an exhibit to the registration statement of w
this prospectus is a part.

Class and Year	Total Amount Outstanding(1)	Asset Coverage per Unit(2)	Involuntary Liquidating Preference Per Unit(3)	Avera Marke Valu Per Unit(4
Credit Facility				
Fiscal 2010 (as of December 31, 2009, unaudited)	$ 10,000	$ 64,748	–	–
Fiscal 2009 (as of June 30, 2009)	124,800	5,268	–	–
Fiscal 2008 (as of June 30, 2008)	91,167	5,712	–	–
Fiscal 2007 (as of June 30, 2007)	–	N/A	–	–
Fiscal 2006 (as of June 30, 2006)	28,500	4,799	–	–
Fiscal 2005 (as of June 30, 2005)	–	N/A	–	–
Fiscal 2004 (as of June 30, 2004)	–	N/A	–	–

(1) Total amount of each class of senior securities outstanding at the end of the period presented (in 000's).
(2) The asset coverage ratio for a class of senior securities representing indebtedness is calculated as our consolidated assets, less all liabilities and indebtedness not represented by senior securities, divided by senior securities represe indebtedness. This asset coverage ratio is multiplied by $1,000 to determine the Asset Coverage Per Unit.
(3) This column is inapplicable because we have had only bank debt outstanding during the time periods.
(4) This column is inapplicable because we have not had any preferred stock outstanding during any of the time perio

PRICE RANGE OF COMMON STOCK

Our common stock is quoted on The NASDAQ Global Select Market under the symbol "PSEC." The following table sets for the periods indicated, our net asset value per share of common stock and the high and low sales prices per share c common stock as reported on The NASDAQ Global Select Market. Our common stock historically trades at prices both and below its NAV. There can be no assurance, however, that such premium or discount, as applicable, to NAV w maintained.

	NAV(1)	Stock Price High(2)	Low(2)	Premium (Discount) of High to NAV	Premium (Discount) of Low to NAV	Divider Declare
Twelve Months Ending June 30, 2005						
First quarter	$ 13.67	$ 15.45	$ 14.42	13.0 %	5.5 %	—
Second quarter	13.74	15.15	11.63	10.3 %	(15.4)%	$ 0.100
Third quarter	13.74	13.72	10.61	(0.1)%	(22.8)%	0.125
Fourth quarter	14.59	13.47	12.27	(7.7)%	(15.9)%	0.150
Twelve Months Ending June 30, 2006						
First quarter	$ 14.60	$ 13.60	$ 11.06	(6.8)%	(24.2)%	$ 0.200
Second quarter	14.69	15.46	12.84	5.2 %	(12.6)%	0.280
Third quarter	14.81	16.64	15.00	12.4 %	1.3 %	0.300
Fourth quarter	15.31	17.07	15.83	11.5 %	3.4 %	0.340
Twelve Months Ending June 30, 2007						
First quarter	$ 14.86	$ 16.77	$ 15.30	12.9 %	3.0 %	$ 0.380
Second quarter	15.24	18.79	15.60	23.3 %	2.4 %	0.385
Third quarter	15.18	17.68	16.40	16.5 %	8.0 %	0.3875
Fourth quarter	15.04	18.68	16.91	24.2 %	12.4 %	0.390
Twelve Months Ending June 30, 2008						
First quarter	$ 15.08	$ 18.68	$ 14.16	23.9 %	(6.1)%	$ 0.3925
Second quarter	14.58	17.17	11.22	17.8 %	(23.0)%	0.395
Third quarter	14.15	16.00	13.55	13.1 %	(4.2)%	0.400
Fourth quarter	14.55	16.12	13.18	10.8 %	(9.4)%	0.4012
Twelve Months Ending June 30, 2009						
First quarter	$ 14.63	$ 14.24	$ 11.12	(2.7)%	(24.0)%	$ 0.4025
Second quarter	14.43	13.08	6.29	(9.4)%	(56.4)%	0.4037
Third quarter	14.19	12.89	6.38	(9.2)%	(55.0)%	0.405
Fourth quarter	12.40	10.48	7.95	(15.5)%	(35.9)%	0.4062
Twelve Months Ending June 30, 2010						
First quarter	$ 11.11	$ 10.99	$ 8.82	(1.1)%	(20.6)%	$ 0.4075
Second quarter	10.06	12.31	9.93	22.4 %	(1.3)%	0.4087
Third quarter (to 2/25/10)	(3)(4)	13.20	10.45	(4)	(4)	(5

---

(1) Net asset value per share is determined as of the last day in the relevant quarter and therefore may not reflect th asset value per share on the date of the high or low sales price. The NAVs shown are based on outstanding sha the end of each period.

(2) The High/Low Stock Price is calculated as of the closing price on a given day in the applicable quarter.

(3) Our most recently determined NAV per share was $10.06 as of December 31, 2009 ($10.07 on an as adjusted solely to give effect to our issuance of common stock on January 25, 2010 in connection with our divi reinvestment plan). NAV as of March 31, 2010 may be higher or lower than $10.07 based on potential chang valuations as of March 31, 2010.

(4) NAV has not yet been finally determined for any day after December 31, 2009.

(5) The dividend for the third quarter of 2010 will be declared in March 2010.

On February 25, 2010, the last reported sales price of our common stock was $11.66 per share. As of February 25, 2010, w approximately 69 stockholders of record.

BUSINESS

General

We are a financial services company that primarily lends to and invests in middle market privately-held companies. We closed-end investment company that has filed an election to be treated as a business development company und Investment Company Act of 1940, or the 1940 Act. We invest primarily in senior and subordinated debt and equ companies in need of capital for acquisitions, divestitures, growth, development, project financing and recapitalizatio work with the management teams or financial sponsors to seek investments with historical cash flows, asset collate contracted pro-forma cash flows.

On July 27, 2004, we completed our initial public offering, or IPO, and sold 7 million shares of common stock at a pr $15.00 per share, less underwriting discounts and commissions totaling $1.05 per share. An additional 55,000 shares issued through the exercise of an over-allotment option with respect to the IPO on August 27, 2004. Since the IPO an exercise of the related over-allotment option, we have made eleven other share offerings and six related over-allotment op resulting in the issuance of 43,493,836 shares at prices ranging from $7.75 to $17.70. The most recent offering was comp on September 24, 2009 pursuant to which the Company sold 2,807,111 at an unregistered direct price of $9.00 per share.

On December 2, 2009, we completed our previously announced acquisition of Patriot under the Agreement and Plan of M dated as of August 3, 2009, by and among, us and Patriot. Pursuant to the terms of the merger agreement, we acquired P for approximately $200 million comprised of our common stock and cash to repay all of Patriot's outstanding debt, amounted to $107.3 million. In the merger, each outstanding share of Patriot common stock was converted into the ri receive 0.363992 shares of common stock of Prospect, representing 8,444,068 shares of the Company's common stock, a payment of cash in lieu of fractional shares of Prospect common stock of less than $200 resulting from the application foregoing exchange ratio.

Our headquarters are located at 10 East 40th Street, 44th Floor, New York, NY 10016, and our telephone number is 448-0702. Our investment adviser is Prospect Capital Management LLC.

Our Investment Objective and Policies

Our investment objective is to generate both current income and long-term capital appreciation through debt and e investments. We focus on making investments in private companies, and many of our investments are in energy companie are a non-diversified company within the meaning of the 1940 Act.

Typically, we concentrate on making investments in companies with annual revenues of less than $500 million and ente values of less than $250 million. Our typical investment involves a secured loan of less than $50 million with some fo equity participation. From time to time, we acquire controlling interests in companies in conjunction with making secure investments in such companies. In most cases, companies in which we invest are privately held at the time we invest in We refer to these companies as "target" or "middle market" companies and these investments as "middle market investmen

We seek to maximize returns and protect risk for our investors by applying rigorous analysis to make and monito
investments. While the structure of our investments varies, we can invest in senior secured debt, senior unsecured
subordinated secured debt, subordinated unsecured debt, mezzanine debt, convertible debt, convertible preferred e
preferred equity, common equity, warrants and other instruments, many of which generate current yield. Our invest
primarily range between approximately $5 million and $50 million each, although this investment size may vary as the s
our capital base changes.

While our primary focus is to seek current income through investment in the debt and/or dividend-paying equity securit eligible privately-held, thinly-traded or distressed companies and long-term capital appreciation by acquiring accompa warrants, options or other equity securities of such companies, we may invest up to 30% of the portfolio in opportu investments in order to seek enhanced returns for stockholders. Such investments may include investments in the deb equity instruments of broadly-traded public companies. We expect that these public companies generally will have securities that are non-investment grade. Within this 30% basket, we may also invest in debt and equity securities of comp located outside of the United States.

Our investments may include other equity investments, such as warrants, options to buy a minority interest in a por company, or contractual payment rights or rights to receive a proportional interest in the operating cash flow or net inco such company. When determined by our Investment Adviser to be in our best interest, we may acquire a controlling intere portfolio company. Any warrants we receive with our debt securities may require only a nominal cost to exercise, and thu portfolio company appreciates in value, we may achieve additional investment return from this equity interest. We structured, and will continue to structure, some warrants to include provisions protecting our rights as a minority-interest applicable, controlling-interest holder, as well as puts, or rights to sell such securities back to the company, upon the occur of specified events. In many cases, we obtain registration rights in connection with these equity interests, which may in demand and "piggyback" registration rights.

We plan to hold many of our investments to maturity or repayment, but will sell our investments earlier if a liquidity event place, such as the sale or recapitalization of a portfolio company, or if we determine a sale of one or more of our investme be in our best interest.

We have qualified and elected to be treated for U.S. Federal income tax purposes as a Registered Investment Company (" under Subchapter M of the Code. As a RIC, we generally do not have to pay corporate-level U.S. Federal income taxes o ordinary income or capital gains that we distribute to our stockholders as dividends. To continue to qualify as a RIC, we among other things, meet certain source-of-income and asset diversification requirements (as described below). In additi qualify for RIC tax treatment we must distribute to our stockholders, for each taxable year, at least 90% of our "inves company taxable income," which is generally our ordinary income plus the excess of our realized net short-term capital over our realized net long-term capital losses.

For a discussion of the risks inherent in our portfolio investments, see "Risk Factors — Risks Relating to our Investments.'

Industry Sectors

We have invested significantly in industrial and energy related companies. However, we continue to widen our focus in sectors of the economy to diversify our portfolio holdings. The energy industry consists of companies in the direct energy chain as well as companies that sell products and services to, or acquire products and services from, the direct energy chain. In this prospectus, we refer to all of these companies as "energy companies" and assets in these companies as "e assets." The categories of energy companies in this chain are described below. The direct energy value chain broadly inc upstream businesses, midstream businesses and downstream businesses:

·

Upstream businesses find, develop and extract energy resources, including natural gas, crude oil and coal, wh are typically from geological reservoirs found underground or offshore, and agricultural products.

· Midstream businesses gather, process, refine, store and transmit energy resources and their by products in a f that is usable by wholesale power generation, utility, petrochemical, industrial and gasoline customers.

- Downstream businesses include the power and electricity segment as well as businesses that process, refine, market or distribute hydrocarbons or other energy resources, such as customer-ready natural gas, propane and gasoline, to end-user customers.

Ongoing Relationships with Portfolio Companies

Monitoring

Prospect Capital Management monitors our portfolio companies on an ongoing basis. Prospect Capital Managemen continue to monitor the financial trends of each portfolio company to determine if it is meeting its business plan and to a the appropriate course of action for each company.

Prospect Capital Management employs several methods of evaluating and monitoring the performance and value o investments, which may include, but are not limited to, the following:

- Assessment of success in adhering to the portfolio company's business plan and compliance with covenants;
- Regular contact with portfolio company management and, if appropriate, the financial or strategic sponsor, to discuss financial position, requirements and accomplishments;
- Attendance at and participation in board meetings of the portfolio company; and
- Review of monthly and quarterly financial statements and financial projections for the portfolio company.

Investment Valuation

Our Board of Directors has established procedures for the valuation of our investment portfolio. These procedures are de below.

Investments for which market quotations are readily available are valued at such market quotations.

For most of our investments, market quotations are not available. With respect to investments for which market quotatio not readily available or when such market quotations are deemed not to represent fair value, our Board of Director approved a multi-step valuation process each quarter, as described below:

1) each portfolio company or investment is reviewed by our investment professionals with the independent valuation engaged by our Board of Directors;

2) the independent valuation firm conducts independent appraisals and makes their own independent assessment;

3) the audit committee of our Board of Directors reviews and discusses the preliminary valuation of our Investment Advis
that of the independent valuation firm; and

4) the Board of Directors discusses the valuations and determines the fair value of each investment in our portfolio in goo
based on the input of our Investment Adviser, the independent valuation firm and the audit committee.

Investments are valued utilizing a market approach, an income approach, or both approaches, as appropriate. The m
approach uses prices and other relevant information generated by market transactions involving identical or comparable
or liabilities (including a business). The income approach uses valuation techniques to convert future amounts (for exa
cash flows or earnings) to a single present value amount (discounted) calculated based on an appropriate discount rate
measurement is based on the net present value indicated by current market expectations about those future amour
following these approaches, the types of factors that we may take into account in fair value pricing our investments inclu
relevant: available current market data, including relevant and applicable market trading and transaction compara
applicable market yields and multiples, security covenants, call protection provisions, information rights, the natur
realizable value of any collateral, the portfolio company's ability to make payments, its earnings and discounted cash flow
markets in which the portfolio company does business, comparisons of financial ratios of peer companies that are public,
comparables, the principal market and enterprise values, among other factors.

In September 2006, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Codification ("AS
"Codification") 820, Fair Value Measurements and Disclosures ("ASC 820"). ASC 820 defines fair value, establis
framework for measuring fair value in GAAP, and expands disclosures about fair value measurements. We adopted ASC 8
a prospective basis beginning in the quarter ended September 30, 2008.

ASC 820 classifies the inputs used to measure these fair values into the following hierarchy:

Level 1: Quoted prices in active markets for identical assets or liabilities, accessible by the Company at the measurement d

Level 2: Quoted prices for similar assets or liabilities in active markets, or quoted prices for identical or similar ass
liabilities in markets that are not active, or other observable inputs other than quoted prices.

Level 3: Unobservable inputs for the asset or liability.

In all cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has
determined based on the lowest level of input that is significant to the fair value measurement. Our assessment o
significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors spec
each investment.

The changes to generally accepted accounting principles from the application of ASC 820 relate to the definition of fair v
framework for measuring fair value, and the expanded disclosures about fair value measurements. ASC 820 applies to fair
measurements already required or permitted by other standards.

In accordance with ASC 820, the fair value of our investments is defined as the price that we would receive upon selli
investment in an orderly transaction to an independent buyer in the principal or most advantageous market in whic
investment is transacted.

In April 2009, the FASB issued ASC 820-10-65, Determining Fair Value When the Volume and Level of Activity for the or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly" ("ASC 820-10-65"). This u provides further clarification for ASC 820 in markets that are not active and provides additional guidance for determining the volume of trading level of activity for an asset or liability has significantly decreased and for identifying circumstance indicate a transaction is not orderly. ASC 820-10-65 is effective for interim and annual reporting periods ending after Ju 2009. The adoption of ASC 820-10-65 for

the three and six months ended December 31, 2009, did not have any effect on our net asset value, financial position or r
of operations as there was no change to the fair value measurement principles set forth in ASC 820.

In January 2010, the FASB issued Accounting Standards Update 2010-06, Fair Value Measurements and Disclosures (
820): Improving Disclosures about Fair Value Measurements ("ASC 2010-06"). ASU 2010-06 amends ASC 820-1
clarifies and provides additional disclosure requirements related to recurring and non-recurring fair value measurement
employers' disclosures about postretirement benefit plan assets. ASU 2010-06 is effective for interim and annual rep
periods beginning after December 15, 2009. Our management does not believe that the adoption of the amended guida
ASC 820-10 will have a significant effect on our financial statements.

For a discussion of the risks inherent in determining the value of securities for which readily available market values c
exist, see "Risk Factors — Risks relating to our business — Most of our portfolio investments are recorded at fai
determined in good faith by our Board of Directors and, as a result, there is uncertainty as to the value of our por
investments."

Valuation of Other Financial Assets and Financial Liabilities

In February 2007, FASB issued ASC Subtopic 820-10-05-1, The Fair Value Option for Financial Assets and Fina
Liabilities ("ASC 820-10-05-1"). ASC 820-10-05-1 permits an entity to elect fair value as the initial and subse
measurement attribute for many of assets and liabilities for which the fair value option has been elected and similar asse
liabilities measured using another measurement attribute. We have adopted this statement on July 1, 2008 and have elect
to value some assets and liabilities at fair value as would be permitted by ASC 820-10-05-1.

The Investment Adviser

Prospect Capital Management manages our investments as our investment adviser. Prospect Capital Management is a Del
limited liability corporation that has been registered as an investment adviser under the Advisers Act since March 31,
Prospect Capital Management is led by John F. Barry III and M. Grier Eliasek, two senior executives with signi
investment advisory and business experience. Both Messrs. Barry and Eliasek spend a significant amount of their time in
roles at Prospect Capital Management working on the Company's behalf. The principal executive offices of Prospect C
Management are 10 East 40th Street, 44th Floor, New York, NY 10016. We depend on the diligence, skill and netwo
business contacts of the senior management of our Investment Adviser. We also depend, to a significant extent, o
Investment Adviser's investment professionals and the information and deal flow generated by those investment professio
the course of their investment and portfolio management activities. The Investment Adviser's senior management
evaluates, negotiates, structures, closes, monitors and services our investments. Our future success depends to a signi
extent on the continued service of the senior management team, particularly John F. Barry III and M. Grier Eliasek
departure of any of the senior managers of our Investment Adviser could have a materially adverse effect on our abil
achieve our investment objective. In addition, we can offer no assurance that Prospect Capital Management will rema
Investment Adviser or that we will continue to have access to its investment professionals or its information and deal
Under our Investment Advisory Agreement, we pay Prospect Capital Management investment advisory fees, which cons
an annual base management fee based on our gross assets as well as a two-part incentive fee based on our performance
Barry currently controls Prospect Capital Management. See "Management — Management Services — Board of Director
of the Investment Advisory Agreement."

As a business development company, we offer, and must provide upon request, managerial assistance to certain of our por
companies. This assistance could involve, among other things, monitoring the operations of our portfolio compa
participating in board and management meetings, consulting with and advising officers of portfolio companies and prov
other organizational and financial guidance. We may receive fees for these

services. Such fees would not qualify as "good income" for purposes of the 90% income test that we must meet each y
qualify as a RIC. Prospect Administration provides such managerial assistance on our behalf to portfolio companies wh
are required to provide this assistance.

Staffing

Mr. John F. Barry III, our chairman and chief executive officer, Mr. Grier Eliasek, our chief operating officer and presiden
Mr. Brian H. Oswald, our chief financial officer, chief compliance officer, treasurer and secretary, comprise our s
management. Over time, we expect to add additional officers and employees. Messrs. Barry and Eliasek each also serves
officer of Prospect Administration and performs his respective functions under the terms of the Administration Agreemen
day-to-day investment operations are managed by Prospect Capital Management. In addition, we reimburse Pro
Administration for our allocable portion of expenses incurred by it in performing its obligations under the Administ
Agreement, including rent and our allocable portion of the costs of our Chief Executive Officer, President, Chief Fina
Officer, Chief Operating Officer, Chief Compliance Officer, Treasurer and Secretary and their respective staffs
"Management — Management Services — Administration Agreement."

Properties

We do not own any real estate or other physical properties materially important to our operation. Our corporate headquarte
located at 10 East 40th Street, 44th Floor, New York, NY 10016, where we occupy an office space pursuant t
Administration Agreement.

Legal Proceedings

On December 6, 2004, Dallas Gas Partners, L.P. ("DGP") served us with a complaint filed November 30, 2004 in the
District for the Southern District of Texas, Galveston Division. DGP alleges that DGP was defrauded and that we breache
fiduciary duty to DGP and tortiously interfered with DGP's contract to purchase Gas Solutions, Ltd. (a subsidiary o
portfolio company, GSHI) in connection with our alleged agreement in September 2004 to loan DGP funds with which
intended to buy Gas Solutions, Ltd. for approximately $26 million. The complaint sought relief not limited to $100 millio
November 30, 2005, U.S. Magistrate Judge John R. Froeschner of the U.S. District Court for the Southern District of T
Galveston Division, issued a recommendation that the court grant our Motion for Summary Judgment dismissing all clai
DGP. On February 21, 2006, U.S. District Judge Samuel Kent of the U.S. District Court for the Southern District of T
Galveston Division issued an order granting our Motion for Summary Judgment dismissing all claims by DGP, against u
May 16, 2007, the Court also granted us summary judgment on DGP's liability to us on our counterclaim for DGP's breac
release and covenant not to sue. On January 4, 2008, the Court, Judge Melinda Harmon presiding, granted our motion to di
all DGP's claims asserted against certain of our officers and affiliates. On August 20, 2008, Judge Harmon entered a
Judgment dismissing all of DGP's claims. DGP appealed to the U.S. Court of Appeals for the Fifth Circuit, which affirm
Final Judgment on June 24, 2009. DGP has moved for rehearing. Our damage claims against DGP remain pending.

In May 2006, based in part on unfavorable due diligence and the absence of investment committee approval, we declin
extend a loan for $10 million to a potential borrower ("plaintiff"). Plaintiff was subsequently sued by its own attorney in a
Texas court for plaintiff's failure to pay fees owed to its attorney. In December 2006, plaintiff filed a cross-action against u
certain of our affiliates (the "defendants") in the same local Texas court, alleging, among other things, tortious interferenc
contract and fraud. We petitioned the United States District Court for the Southern District of New York (the "District C

to compel arbitration and to enjoin the Texas action. In February 2007, our motions were granted. Plaintiff appeale decision. On July 24, 2008, the Second Circuit Court of Appeals affirmed the judgment of the District Court. The arbit commenced in July 2007 and concluded in late November 2007. Post-hearing briefings were completed in February 200 April 14, 2008, the arbitrator rendered an award in our favor, rejecting all of plaintiff's claims. On April 18, 2008, we f petition before the District Court to confirm the award. On October 8, 2008, the District Court granted the Company's

---

petition to confirm the award, confirmed the awards and subsequently entered judgment thereon in favor of the Company
amount of $2.3 million. After filing a defective notice of appeal to the United States Court of Appeals for the Second Circ
November 5, 2008, plaintiff's counsel resubmitted a new notice of appeal on January 9, 2009. The plaintiff subsequ
requested that the Company agree to stipulate to the withdrawal of plaintiff's appeal to the Second Circuit. Such a stipu
was filed with the Second Circuit on or about April 14, 2009. Based on this stipulation, the Second Circuit issued a ma
terminating the appeal, which was transmitted to the District Court on April 23, 2009. Post-judgment discovery against pla
is continuing and we have filed a motion for sanctions against plaintiff's counsel. Argument for the motion for sanction
held on November 19, 2009 and a decision from the court is pending.

We are involved in various investigations, claims and legal proceedings that arise in the ordinary course of our business.
matters may relate to intellectual property, employment, tax, regulation, contract or other matters. The resolution of
matters that may arise out of these investigations, claims and proceedings will be subject to various uncertainties and, e
such matters are without merit, could result in the expenditure of significant financial and managerial resources.

We are not aware of any other material pending legal proceeding, and no such material proceedings are contemplated to
we are a party or of which any of our property is subject.

Management

Our business and affairs are managed under the direction of our Board of Directors. Our Board of Directors currently cons five directors, three of whom are not "interested persons" of the Company as defined in Section 2(a)(19) of the 1940 Ac refer to these individuals as our independent directors. Our Board of Directors elects our officers to serve for a one-year and until their successors are duly elected and qualify, or until their earlier removal or resignation.

Board Of Directors And Executive Officers

Under our charter, our directors are divided into three classes. Directors are elected for a staggered term of three years with a term of office of one of the three classes of directors expiring each year. At each annual meeting of our stockholder successors to the class of directors whose terms expire at such meeting are elected to hold office for a term expiring annual meeting of stockholders held in the third year following the year of their election. Each director holds office for the to which he or she is elected and until his or her successor is duly elected and qualifies.

Directors and Executive Officers

Our directors and executive officers and their positions are set forth below. The address for each director and executive o is c/o Prospect Capital Corporation, 10 East 40th Street, 44th Floor, New York, NY 10016.

Independent Directors

Name and Age	Position(s) Held with the Company	Term of Office(1) and Length of Time Served	Principal Occupation(s) During Past 5 Years	Number of Portfolios in Fund Complex Overseen by Director	Other Directorships Held by Director(2)
Graham D.S. Anderson, 45	Director	Class I Director since September 2008; Term expires 2011	General Partner of Euclid SR Partners from 2000 to present. From 1996 to 2000, Mr. Anderson was a General Partner of Euclid Partners, the predecessor to Euclid SR Partners.	One	None
Eugene S. Stark, 52	Director	Class III Director since September 2008; Term expires 2010	Principal Financial Officer, Chief Compliance Officer and Vice President — Administration of General American Investors Company, Inc. from May 2005 to present. Prior to his role with General American Investors Company, Inc., Mr. Stark served as	One	None

			the Chief Financial Officer of Prospect Capital Corporation from January 2005 to April 2005. From May 1987 to December 2004 Mr. Stark served as Senior Vice President and Vice President with Prudential Financial, Inc.		
Andrew C. Cooper, 48	Director	Class II Director since February 2009; Term expires 2012	Mr. Cooper is an entrepreneur, who over the last 11 years has founded, built, run and sold three companies. He is Co-Chief Executive Officer of Unison Site Management, Inc., a specialty finance company focusing on cell site easements, and Executive Director of Brand Asset Digital, a digital media marketing and distribution company. Prior to that, Mr. Cooper focused on venture capital and investment banking for Morgan Stanley for 14 years.	One	Unison Site Management, LLC, Brand Asset Digital, LLC and Aquatic Energy, LLC

(1) Our Board of Directors is divided into three classes of directors serving staggered three-year terms. Mr. Anderson is a C director with a term that will expire in 2011, Mr. Eliasek and Mr. Cooper are Class II directors with terms that will exp 2012 and Mr. Barry and Mr. Stark are Class III directors with terms that will expire in 2010.

(2) No director otherwise serves as a director of an investment company subject to the 1940 Act.

Interested Directors

Name and Age	Position(s) Held with the Company	Term of Office(1) and Length of Time Served	Principal Occupation(s) During Past 5 Years	Number of Portfolios in Fund Complex Overseen by Director	Other Directorships Held by Director(2)
John F. Barry III,(3) 57	Director, Chairman of the Board of Directors, and Chief Executive Officer	Class III Director since June 2004; Term expires 2010	Chairman and Chief Executive Officer of the Company; Managing Director and Chairman of the Investment Committee of Prospect Capital Management and Prospect Administration since June 2004; Managing Director of Prospect Capital Management.	One	None
M. Grier Eliasek,(3) 36	Director, President and Chief Operating Officer	Class II Director since June 2004; Term expires 2012	President and Chief Operating Officer of the Company, Managing Director of Prospect Capital Management and Prospect Administration	One	None

(1) Our Board of Directors is divided into three classes of directors serving staggered three-year terms. Mr. Anderson is a C director with a term that will expire in 2011, Mr. Eliasek and Mr. Cooper are Class II directors with terms that will exp 2012 and Mr. Barry and Mr. Stark are Class III directors with terms that will expire in 2010.

(2) No director otherwise serves as a director of an investment company subject to the 1940 Act.

(3) Messrs. Barry and Eliasek are each considered an "interested person" under the 1940 Act by virtue of serving as one o officers and having a relationship with Prospect Capital Management.

Information about Executive Officers who are not Directors

Name and Age	Position(s) Held with the Company	Term of Office and Length of Time Served	Principal Occupation(s) During Past Five Years
Brian H. Oswald, 49	Chief Financial Officer, Chief	November 2008 to present as Chief Financial	Joined Prospect Administration as Managing Director in June 2008.

Compliance Officer, Treasurer and Secretary	Officer and October 2008 to present as Chief Compliance Officer	Previously Managing Director in Structured Finance Group at GSC Group (2006 to 2008) and Chief Financial Officer at Capital Trust, Inc. (2003 to 2005)

Independent Directors

Graham D.S. Anderson. Mr. Anderson has served as General Partner of Euclid SR Partners from 1996 to presen Anderson currently serves as a member of the Board of Directors of Acurian, Inc. (a clinical trial recruitment comp FatWire Software Corp. (a web content management company), iJet Risk Management (an

operational risk management information company), Plateau Systems Limited (a human capital management sof
company) and SkinMedica Inc. (a dermatology and cosmeceuticals company).

Andrew C. Cooper. Mr. Cooper has 24 years of experience in growth company management, venture investing and inves
banking. He has a wide range of operational, marketing, technology, and debt and equity capital raising expertise. Mr. Coo
an entrepreneur, who over the last 11 years has founded, built, run and sold three companies. Prior to that, Mr. Cooper fo
on venture capital and investment banking for Morgan Stanley for 14 years. He is Co-Chief Executive Officer of Uniso
Management, Inc., a specialty finance company focusing on cell site easements, and Executive Director of Brand Asset D
a digital media marketing and distribution company. His current Board appointments include Unison Site Management,
Brand Asset Digital, LLC and Aquatic Energy, LLC.

Eugene S. Stark. Mr. Stark has served as Principal Financial Officer, Chief Compliance Officer and Vice Presi
Administration of General American Investors Company, Inc. from May 2005 to present. Prior to his role with Ge
American Investors Company, Inc., Mr. Stark served as the Chief Financial Officer of Prospect Capital Corporation
January 2005 to April 2005. From May 1987 to December 2004 Mr. Stark served as Senior Vice President (division leve
Vice President (corporate level) with Prudential Financial, Inc. in various financial management positions. Mr. Stark serve
member of the Board of Directors of Prospect Capital Funding LLC, a wholly-owned subsidiary of the Company, and s
the Board of Trustees and is a Member of the Finance Committee of Mount Saint Mary Academy.

Interested Directors

John F. Barry III. Mr. Barry is chairman and chief executive officer of the Company and is a control person of Prospect C
Management and a managing director of Prospect Administration. Mr. Barry is chairman of Prospect's investment comm
and has been an officer of Prospect since 1990. In addition to overseeing Prospect, Mr. Barry has served on the boa
directors of twelve private and public Prospect portfolio companies. Mr. Barry has served on the board of advisors of U
Inc., a publicly-traded energy company. Mr. Barry has served as chairman and chief executive officer of Bondnet Tr
Systems. From 1988 to 1989, Mr. Barry managed the investment bank of L.F. Rothschild & Company, focusing on p
equity and debt financings for energy and other companies. From 1983 to 1988, Mr. Barry was a senior investmen
merchant banker at Merrill Lynch & Co., where he was a founding member of the project finance group, executing more
$4 billion in energy and other financings. From 1979 to 1983, Mr. Barry was a corporate securities attorney at Davis P
Wardwell, where he advised energy companies and their commercial and investment bankers. From 1978 to 1979, Mr.
served as law clerk to Circuit Judge, formerly Chief Judge, J. Edward Lumbard of the U.S. Court of Appeals for the Se
Circuit in New York City. Mr. Barry is chairman of the board of directors of the Mathematics Foundation of Amer
non-profit foundation which enhances opportunities in mathematics education for students from diverse backgrounds. Mr.
received his JD cum laude from Harvard Law School, where he was an editor of the Harvard Law Review, and his Bache
Arts magna cum laude from Princeton University, where he was a University Scholar.

M. Grier Eliasek. Mr. Eliasek is president and chief operating officer of the Company and a managing director of Pro
Capital Management and Prospect Administration. At the Company, Mr. Eliasek is responsible for various administrativ
investment management functions and leads and supervises other Prospect professionals in origination and assessme
investments. Mr. Eliasek has served as a senior investment professional at Prospect since 1999. Prior to joining Prospec
Eliasek assisted the chief financial officer of Amazon.com in 1999 in corporate strategy, customer acquisition, and new pr
launches. From 1995 to 1998, Mr. Eliasek served as a consultant with Bain & Company, a global strategy consulting
where he managed engagements for companies in several different industries. At Bain, Mr. Eliasek analyzed new li

businesses, developed market strategies, revamped sales organizations and improved operational performance. Mr. El
received his MBA from Harvard Business School. Mr. Eliasek received his Bachelor of Science in Chemical Engineering
Highest Distinction from the University of Virginia, where he was a Jefferson Scholar and a Rodman Scholar.

Executive Officer

Brian H. Oswald. Mr. Oswald is chief financial officer, chief compliance officer, secretary and treasurer of the Compan began his career at KPMG Peat Marwick, where he held various positions over his ten-year tenure, finishing as a S Manager in the financial institutions group. During his time at KPMG, he served as the reviewing senior manager for se initial public offerings of financial institutions. After KPMG, Mr. Oswald served as the Executive Vice President and Pre of Gloversville Federal Savings and Loan Association, served as the Director of Financial Reporting and Subsidiary Accou for River Bank America and served as the Corporate Controller for Magic Solutions, Inc. In each of these positions, Mr. O instituted significant operational changes and was instrumental in raising additional equity for River Bank America. From to 2005, Mr. Oswald led Capital Trust, Inc., a self-managed finance and investment management REIT which speciali credit-sensitive structured financial products, as Chief Financial Officer. From 1997 to 2003, he served as Chief Accou Officer for Capital Trust. Prior to joining the Company, Mr. Oswald spent two years with the Structured Finance Divis GSC Group, serving as Managing Director of Finance for this asset management company. At GSC, Mr. Oswald manag finances for a REIT, two hedge funds and thirteen CDOs. Mr. Oswald joined the Administrator on June 16, 2008. Mr. O holds a B.A. degree in Accounting from Moravian College. He is a licensed Certified Public Accountant in the States o York and Pennsylvania, and is a Certified Management Accountant. Mr. Oswald also serves as a board member of Laboratories, Inc.

For information on the investment professionals of Prospect Capital Management, see "Business — The Investment Staffing."

Committees of the Board of Directors

Our Board of Directors has established an Audit Committee and a Nominating and Corporate Governance Committee. F fiscal year ended June 30, 2009, our Board of Directors held twenty-two Board of Director meetings, eleven Audit Com meetings, and five Nominating and Corporate Governance Committee meeting. All directors attended at least 75% aggregate number of meetings of the Board of Directors and of the respective committees on which they served. We re each director to make a diligent effort to attend all board and committee meetings, as well as each annual meeti stockholders.

The Audit Committee. The Audit Committee operates pursuant to a charter approved by the Board of Directors. The c sets forth the responsibilities of the Audit Committee, which include selecting or retaining each year an independent regi public accounting firm, or the independent accountants, to audit the accounts and records of the Company; reviewin discussing with management and the independent accountants the annual audited financial statements of the Com including disclosures made in management's discussion and analysis, and recommending to the Board of Directors wheth audited financial statements should be included in the Company's annual report on Form 10-K; reviewing and discussing management and the independent accountants the Company's quarterly financial statements prior to the filings of its qua reports on Form 10-Q; pre-approving the independent accountants' engagement to render audit and/or permissible non services; and evaluating the qualifications, performance and independence of the independent accountants. The Committee is presently composed of three persons: Messrs. Anderson, Cooper and Stark, each of whom is not an "inte person" as defined in the 1940 Act and is considered independent under the Marketplace Rules of the NASDAQ Stock M LLC. The Company's Board of Directors has determined that Mr. Stark is an "audit committee financial expert" as that t defined under Item 407 of Regulation S-K and Mr. Stark serves as the Chairman of the Audit Committee. The Audit Com may delegate its pre-approval responsibilities to one or more of its members. The member(s) to whom such responsibi delegated must report, for informational purposes only, any pre-approval decisions to the Audit Committee at its next sche

meeting. Messrs. Stark, Anderson and Cooper were added to the Audit Committee concurrent with their election to the Bo
Directors on September 4, 2008, September 15, 2008 and February 12, 2009, respectively.

The function of the Audit Committee is oversight. Our management is primarily responsible for maintaining appro
systems for accounting and financial reporting principles and policies and internal controls

and procedures that provide for compliance with accounting standards and applicable laws and regulations. The indepe
accountants are primarily responsible for planning and carrying out a proper audit of our annual financial stateme
accordance with generally accepted accounting standards. The independent accountants are accountable to the Boa
Directors and the Audit Committee, as representatives of our stockholders. The Board of Directors and the Audit Comn
have the ultimate authority and responsibility to select, evaluate and, where appropriate, replace our independent accou
(subject, if applicable, to stockholder ratification).

In fulfilling their responsibilities, it is recognized that members of the Audit Committee are not our full-time employe
management and are not, and do not represent themselves to be, accountants or auditors by profession. As such, it is n
duty or the responsibility of the Audit Committee or its members to conduct "field work" or other types of auditi
accounting reviews or procedures, to determine that the financial statements are complete and accurate and are in accor
with generally accepted accounting principles, or to set auditor independence standards. Each member of the Audit Comn
is entitled to rely on (a) the integrity of those persons within and outside us and management from which it rec
information; (b) the accuracy of the financial and other information provided to the Audit Committee absent actual know
to the contrary (which is required to be promptly reported to the Board of Directors); and (c) statements made by our of
and employees, our Investment Adviser or other third parties as to any information technology, internal audit and
non-audit services provided by the independent accountants to us.

The Nominating and Corporate Governance Committee. The Nominating and Corporate Governance Committee, o
Nominating and Governance Committee, is responsible for selecting qualified nominees to be elected to the Board of Dire
by stockholders; selecting qualified nominees to fill any vacancies on the Board of Directors or a committee thereof; devel
and recommending to the Board of Directors a set of corporate governance principles applicable to the Company; overs
the evaluation of the Board of Directors and management; and undertaking such other duties and responsibilities as may
time to time be delegated by the Board of Directors to the Nominating and Governance Committee. The Nominatin
Governance Committee is presently composed of three persons: Messrs. Anderson, Cooper and Stark, each of whom is n
"interested person" as defined in Section 2(a)(19) of the 1940 Act and Mr. Anderson serves as the Chairman of the Nomi
and Governance Committee. Messrs. Stark, Anderson and Cooper were added to the Nominating and Governance Comn
concurrent with their election to the Board of Directors on September 4, 2008, September 15, 2008 and February 12,
respectively.

The Nominating and Governance Committee will consider stockholder recommendations for possible nominees for elect
directors when such recommendations are submitted in accordance with the Company's bylaws and any applicable law, r
regulation regarding director nominations. Nominations should be sent to the Corporate Secretary, c/o Prospect C
Corporation, 10 East 40th Street, 44th Floor, New York, New York 10016. When submitting a nomination to the Compa
consideration, a stockholder must provide all information that would be required under applicable SEC rules to be disclo
connection with election of a director, including the following minimum information for each director nominee: full nam
and address; principal occupation during the past five years; current directorships on publicly held companies and inves
companies; number of shares of our common stock owned, if any; and, a written consent of the individual to stand for elec
nominated by the Board of Directors and to serve if elected by the stockholders. Criteria considered by the Nominatin
Governance Committee in evaluating the qualifications of individuals for election as members of the Board of Directors in
compliance with the independence and other applicable requirements of the Marketplace Rules of NASDAQ and the 194
and all other applicable laws, rules, regulations and listing standards, the criteria, policies and principles set forth
Nominating and Corporate Governance Committee Charter, and the ability to contribute to the effective management
Company, taking into account our needs and such factors as the individual's experience, perspective, skills, expertis
knowledge of the industries in which the Company operates, personal and professional integrity, character, business judg

time availability in light of other commitments, dedication and conflicts of interest. The Nominating and Gover
Committee also may consider such other factors as it may deem to be in our best interests and those of our stockholders
Board of Directors also believes it is appropriate for certain key members of our management to participate as members
Board of Directors.

Corporate Governance

Corporate Governance Guidelines. Upon the recommendation of the Nominating and Governance Committee, the Bo Directors has adopted Corporate Governance Guidelines on behalf of the Company. These Corporate Governance Guid address, among other things, the following key corporate governance topics: director responsibilities; the size, compositio membership criteria of the Board of Directors; composition and responsibilities of directors serving on committees of the of Directors; director access to officers, employees, and independent advisors; director orientation and continuing educ director compensation; and an annual performance evaluation of the Board of Directors.

Code of Conduct. We have adopted a code of conduct which applies to, among others, our senior officers, including our Executive Officer and Chief Financial Officer, as well as all of our employees. Our code of conduct is an exhibit to our A Report on Form 10-K filed with the SEC, and can be accessed via the Internet site of the SEC at http://www.sec.gov. We i to disclose amendments to or waivers from a required provision of the code of conduct on Form 8-K.

Code of Ethics. We, Prospect Capital Management and Prospect Administration have each adopted a code of ethics pursu Rule 17j-1 under the 1940 Act that establishes procedures for personal investments and restricts certain personal secu transactions. Personnel subject to each code may invest in securities for their personal investment accounts, including secu that may be purchased or held by us, so long as such investments are made in accordance with the code's requirements.

Internal Reporting and Whistle Blower Protection Policy. The Company's Audit Committee has established guideline procedures regarding the receipt, retention and treatment of complaints regarding accounting, internal accounting contr auditing matters, collectively, Accounting Matters, and the confidential, anonymous submission by our employees of con regarding questionable accounting or auditing matters. Persons with complaints or concerns regarding Accounting Matter submit their complaints to our Chief Compliance Officer, or CCO. Persons who are uncomfortable submitting complaints CCO, including complaints involving the CCO, may submit complaints directly to our Audit Committee Chairman. Comp may be submitted on an anonymous basis.

The CCO may be contacted at: Prospect Capital Corporation, Chief Compliance Officer, 10 East 40th Street, 44th Floor York, New York 10016.

The Audit Committee Chairman may be contacted at: Prospect Capital Corporation, Audit Committee Chairman, 10 Eas Street, 44th Floor, New York, New York 10016.

Independent Directors

The Board of Directors, in connection with the 1940 Act and the applicable Marketplace Rules of NASDAQ, has conside independence of members of the Board of Directors who are not employed by Prospect Capital Management and has conc that Messrs. Anderson, Cooper and Stark are not "interested persons" as defined by the 1940 Act and therefore qual independent directors under the standards promulgated by the Marketplace Rules of NASDAQ. In reaching this conclusi Board of Directors concluded that Messrs. Anderson, Cooper and Stark had no relationships with Prospect Capital Manag or any of its affiliates, other than their positions as directors of the Company and, if applicable, investments in us that are same terms as those of other stockholders.

Proxy Voting Policies And Procedures

We have delegated our proxy voting responsibility to Prospect Capital Management. The guidelines are reviewed period
by Prospect Capital Management and our non-interested directors, and, accordingly, are subject to change. See "Regul
Proxy Voting Policies and Procedures."

Compensation of Directors and Officers

The following table sets forth information regarding the compensation received by the directors and executive officers fro
Company for the fiscal year ended June 30, 2009. No compensation is paid to the interested directors by the Company.

Name and Position	Aggregate Compensation from the Company	Pension or Retirement Benefits Accrued as Part of the Company's Expenses(1)	Total Compensati Paid to Director/ Of
Interested Directors			
John F. Barry(2)	None	None	None
M. Grier Eliasek(2)	None	None	None
Independent Directors			
Graham D.S. Anderson(3)	$ 67,750	None	$ 67
Andrew C. Cooper(4)	$ 32,381	None	$ 32
Eugene S. Stark(5)	$ 70,500	None	$ 70
Executive Officers			
William E. Vastardis(6,7)	—	None	—
Brian H. Oswald(2)	None	None	None

---

(1) We do not have a bonus, profit sharing or retirement plan, and directors do not receive any pension or retire
benefits.

(2) We have not paid, and we do not intend to pay, any annual cash compensation to our executive officers for
services as executive officers. Messrs. Barry and Eliasek are compensated by Prospect Capital Management fro
income Prospect Capital Management receives under the management agreement between Prospect Ca
Management and us. Mr. Oswald is compensated by Prospect Administration from the income Pros
Administration receives under the Administration Agreement.

(3) Mr. Anderson joined our Board of Directors on September 15, 2008.

(4) Mr. Cooper joined our Board of Directors on February 12, 2009.

(5) Mr. Stark joined our Board of Directors on September 4, 2008.

(6) Mr. Vastardis is no longer employed by the Company, but served as Chief Compliance Officer from January 4,
through September 30, 2008, and served as Chief Financial Officer and Treasurer from April 30, 2005 thr
November 11, 2008. Mr. Vastardis served as Secretary from April 30, 2005 through June 6, 2008.

(7) The compensation of William E. Vastardis for his service as Chief Financial Officer and Treasurer of the Com
was paid by Vastardis Fund Services LLC, formerly our sub-administrator. Vastardis Fund Services was in turn

by the Company at a monthly minimum rate of $33,333.33 or annual fees on gross assets of 0.20% on the first million, 0.15% on the next $250 million, 0.10% on the next $250 million, 0.075% on the next $250 millio 0.05% over one billion. The compensation of William E. Vastardis for his service as Chief Compliance Offic the Company was paid by Vastardis Compliance Services LLC. Vastardis Compliance Services LLC was i paid by the Company at a monthly rate of $6,250. In addition, the Company paid Vastardis Compliance Se LLC for certain other services at the rate of $270 per hour. Both Vastardis Fund Services LLC and Vast Compliance Services LLC determined the compensation to be paid to Mr. Vastardis with respect to the Com based on a case-by-case evaluation of the time and resources that is required to fulfill his duties to the Compan the fiscal year ending June 30, 2009, the Company paid Vastardis Compliance Services LLC $25,000 for se rendered by Mr. Vastardis as Chief Compliance

Officer. For the fiscal year ending June 30, 2009, the Company paid Vastardis Fund Services LLC approxin $827,083 for services required to be provided by Prospect Administration, including, but not limited to, (a) cl bookkeeping and record keeping services, (b) conducting relations with custodians, depositories, transfer a and other third-party service providers and (c) furnishing reports to Prospect Administration and the Boa Directors of the Company of its performance of obligations. In addition, the fees paid to Vastardis Fund Se LLC cover the services rendered by Mr. Vastardis as our Chief Financial Officer and Treasurer.

Effective July 1, 2008, the independent directors received an annual fee of $90,000 plus reimbursement of any reaso out-of-pocket expenses incurred. The chairman of the Audit Committee received an additional annual cash retainer of $ and the chairman of the Nominating and Corporate Governance Committee received an additional annual cash retair $5,000. Effective September 15, 2008, the independent directors who do not serve on any committees of the board recei annual fee of $11,250.

Effective October 1, 2008, the independent directors who serve on a committee of the Board receive an annual fee of $8 plus reimbursement of any reasonable out-of-pocket expenses incurred and committee chairmen no longer receiv additional compensation.

Effective January 12, 2009, the independent directors who serve on both committees of the Board receive an annual $85,000 plus reimbursement of any reasonable out-of-pocket expenses incurred, the independent directors who serve o committee of the Board receive an annual fee of $60,000 plus reimbursement of any reasonable out-of-pocket expenses inc and the independent directors who do not serve on any committees of the board receive an annual fee of $11,25 compensation was paid to directors who are interested persons of the Company as defined in 1940 Act. In additio Company purchases directors' and officers' liability insurance on behalf of the directors and officers. Through Decemb 2009, each of the three independent directors has been paid $42,500 for the fiscal year ending June 30, 2010.

Management Services

Investment Advisory Agreement

We have entered into the Investment Advisory Agreement with Prospect Capital Management under which the Inves Adviser, subject to the overall supervision of our Board of Directors, manages the day-to-day operations of, and pro investment advisory services to, us. Under the terms of the Investment Advisory Agreement, our Investment Advis determines the composition of our portfolio, the nature and timing of the changes to our portfolio and the mann implementing such changes, (ii) identifies, evaluates and negotiates the structure of the investments we make (incl performing due diligence on our prospective portfolio companies); and (iii) closes and monitors investments we make.

Prospect Capital Management's services under the Investment Advisory Agreement are not exclusive, and it is free to fu similar services to other entities so long as its services to us are not impaired. For providing these services the Inves Adviser receives a fee from us, consisting of two components: a base management fee and an incentive fee. The management fee is calculated at an annual rate of 2% on our gross assets (including amounts borrowed). For services ren under the Investment Advisory Agreement, the base management fee is payable quarterly in arrears. The base manageme is calculated based on the average value of our gross assets at the end of the two most recently completed calendar quarte appropriately adjusted for any share issuances or repurchases during the current calendar quarter. Base management fees fo partial month or quarter are appropriately prorated.

The incentive fee has two parts. The first part, the income incentive fee, which is payable quarterly in arrears, will equal 20
the excess, if any, of our pre-incentive fee net investment income that exceeds a 1.75% quarterly (7% annualized) hurdle
subject to a "catch up" provision measured as of the end of each calendar

quarter. In the three months ended December 31, 2009, we paid an incentive fee of $4.23 million (see calculation below) this purpose, pre-incentive fee net investment income means interest income, dividend income and any other income (incl any other fees (other than fees for providing managerial assistance), such as commitment, origination, structuring, diligenc consulting fees and other fees that we receive from portfolio companies) accrued during the calendar quarter, minu operating expenses for the quarter (including the base management fee, expenses payable under the Administration Agre described below, and any interest expense and dividends paid on any issued and outstanding preferred stock, but excludin incentive fee). Pre-incentive fee net investment income includes, in the case of investments with a deferred interest feature as original issue discount, debt instruments with payment in kind interest and zero coupon securities), accrued income th have not yet received in cash. Pre-incentive fee net investment income does not include any realized capital gains, rea capital losses or unrealized capital appreciation or depreciation. Pre-incentive fee net investment income, expressed as a r return on the value of our net assets at the end of the immediately preceding calendar quarter, is compared to a "hurdle ra 1.75% per quarter (7% annualized).

We expect the incentive fees we pay to increase to the extent we earn greater interest and dividend income throug investments in portfolio companies and, to a lesser extent, realize capital gains upon the sale of warrants or other e investments in our portfolio companies and to decrease if our interest and dividend income and capital gains decrease "catch-up" provision requires us to pay 100% of our pre-incentive fee net investment income with respect to that portion o income, if any, that exceeds the hurdle rate but is less than 125% of the quarterly hurdle rate in any calendar quarter (8 annualized assuming an annualized hurdle rate of 7%). The catch-up provision is meant to provide Prospect Ca Management with 20% of our pre-incentive fee net investment income as if a hurdle rate did not apply when our pre-inc fee net investment income exceeds 125% of the quarterly hurdle rate in any calendar quarter (8.75% annualized assumi annualized hurdle rate of 7%). The income incentive fee will be computed and paid on income that may include interest accrued but not yet received in cash. If interest income is accrued but never paid, the Board of Directors would decide to off the accrual in the quarter when the accrual is determined to be uncollectible. The write off would cause a decrease in in income for the quarter equal to the amount of the prior accrual. The Investment Adviser is not under any obligation to reim us for any part of the incentive fee it received that was based on accrued income that we never receive as a result of a defa an entity on the obligation that resulted in the accrual of such income.

The net investment income used to calculate this part of the incentive fee is also included in the amount of the gross assets to calculate the 2% base management fee. We pay the Investment Adviser an income incentive fee with respect t pre-incentive fee net investment income in each calendar quarter as follows:

- no incentive fee in any calendar quarter in which our pre-incentive fee net investment income does not excee the hurdle rate;
- 100.00% of our pre-incentive fee net investment income with respect to that portion of such pre-incentive fee investment income, if any, that exceeds the hurdle rate but is less than 125.00% of the quarterly hurdle rate in any calendar quarter (8.75% annualized assuming a 7.00% annualized hurdle rate); and
- 20.00% of the amount of our pre-incentive fee net investment income, if any, that exceeds 125.00% of the quarterly hurdle rate in any calendar quarter (8.75% annualized assuming a 7.00% annualized hurdle rate).

These calculations are appropriately prorated for any period of less than three months and adjusted for any share issuan repurchases during the current quarter.

The second part of the incentive fee, the capital gains incentive fee, is determined and payable in arrears as of the end of
calendar year (or upon termination of the Investment Advisory Agreement, as of the termination date), and equals 20%
realized capital gains for the calendar year, if any, computed net of all realized capital losses and unrealized capital deprec
at the end of such year. In determining the capital gains incentive fee

payable to the Investment Adviser, we calculate the aggregate realized capital gains, aggregate realized capital losse aggregate unrealized capital depreciation, as applicable, with respect to each investment that has been in our portfolio. F purpose of this calculation, an "investment" is defined as the total of all rights and claims which may be asserted aga portfolio company arising out of our participation in the debt, equity, and other financial instruments issued by that com Aggregate realized capital gains, if any, equals the sum of the differences between the aggregate net sales price of investment and the aggregate cost basis of such investment when sold or otherwise disposed. Aggregate realized capital equal the sum of the amounts by which the aggregate net sales price of each investment is less than the aggregate cost ba such investment when sold or otherwise disposed. Aggregate unrealized capital depreciation equals the sum of the differe if negative, between the aggregate valuation of each investment and the aggregate cost basis of such investment as applicable calendar year-end. At the end of the applicable calendar year, the amount of capital gains that serves as the bas our calculation of the capital gains incentive fee involves netting aggregate realized capital gains against aggregate rea capital losses on a since-inception basis and then reducing this amount by the aggregate unrealized capital depreciation. number is positive, then the capital gains incentive fee payable is equal to 20% of such amount, less the aggregate amo any capital gains incentive fees paid since inception.

The following is a calculation of the most recently paid incentive fee paid in January 2010 (for the quarter ended Decemb 2009) (in thousands):

Prior Quarter Net Asset Value (adjusted for stock offerings during the quarter)	$ 637,507
Quarterly Hurdle Rate	1.75
Current Quarter Hurdle	$ 11,156
125% of the Quarterly Hurdle Rate	2.1875

125% of the Current Quarter Hurdle	$ 13,945
Current Quarter Pre Incentive Fee Net Investment Income	$ 21,156
Incentive Fee — "Catch-Up"	$ 2,789
Incentive Fee — 20% in excess of 125% of the Current Quarter Hurdle	$ 1,442
Total Current Quarter Incentive Fee	$ 4,231

The total base management fees earned by and paid to Prospect Capital Management during the twelve months ended Ju
2009, June 30, 2008 and June 30, 2007 were $11.9 million, $8.9 million and $5.4 million, respectively. The total
management fees earned by and paid to Prospect Capital Management for the six months ended December 31, 200
December 31, 2009 were $6.4 million and $5.7 million, respectively.

The income incentive fees were $14.8 million, $11.3 million and $5.8 million for the twelve months ended June 30, 2009
30, 2008 and June 30, 2007, respectively. No capital gains incentive fees were earned for the twelve months ended Ju
2009, June 30, 2008 and June 30, 2007. The total income incentive fees for the six months ended December 31, 200
December 31, 2008 were $7.3 million and $8.9 million, respectively.

The total investment advisory fees were $26.7 million, $20.2 million and $11.2 million for the twelve months ended Ju
2009, June 30, 2008 and June 30, 2007, respectively. The total investment advisory fees for the six months ended Decemb
2009 and December 31, 2008 were $13.7 million and $14.6 million, respectively.

Because of the structure of the incentive fee, it is possible that we may have to pay an incentive fee in a quarter where we
a loss. For example, if we receive pre-incentive fee net investment income in excess of the hurdle rate for a quarter, we wi
the applicable income incentive fee even if we have incurred negative total return in that quarter due to realized or unrea
losses on our investments.

Examples of Quarterly Incentive Fee Calculation

Example 1: Income Incentive Fee(*):

Alternative 1

Assumptions

Investment income (including interest, dividends, fees, etc.) = 1.25%

Hurdle rate(1) = 1.75%

Base management fee(2) = 0.50%

Other expenses (legal, accounting, custodian, transfer agent, etc.)(3) = 0.20%

(*) The hypothetical amount of pre-incentive fee net investment income shown is based on a percentage of tot
assets.

(1) Represents 7% annualized hurdle rate

(2) Represents 2% annualized base management fee.

(3) Excludes organizational and offering expenses.

Pre-incentive fee net investment income (investment income — (base management fee + other expenses)) = 0.55%

Pre-incentive net investment income does not exceed hurdle rate, therefore there is no income incentive fee.

Alternative 2

Assumptions

Investment income (including interest, dividends, fees, etc.) = 2.70%

Hurdle rate(1) = 1.75%

Base management fee(2) = 0.50%

Other expenses (legal, accounting, custodian, transfer agent, etc.)(3) = 0.20%

Pre-incentive fee net investment income (investment income — (base management fee + other expenses)) = 2%

Pre-incentive net investment income exceeds hurdle rate, therefore there is an income incentive fee payable by us t
Investment Adviser.

Income incentive Fee	= 100% × "Catch Up" + the greater of 0% AND (20% × (pre-incentive fee net investment income - 2.1875%)
	= (100% × (2% - 1.75%)) + 0%
	= 100% × 0.25% + 0%
	= 0.25%

Alternative 3

Assumptions

Investment income (including interest, dividends, fees, etc.) = 3%

Hurdle rate(1) = 1.75%

Base management fee(2) = 0.50%

Other expenses (legal, accounting, custodian, transfer agent, etc.)(3) = 0.20%

Pre-incentive fee net investment income (investment income — (base management fee + other expenses)) = 2.30%

Pre-incentive net investment income exceeds hurdle rate, therefore there is an income incentive fee payable by us t
Investment Adviser.

Income incentive Fee	= 100% × "Catch Up" + the greater of 0% AND (20% × (pre-incentive fee net investment income - 2.1875%)
	= (100% × (2.1875% - 1.75%)) + the greater of 0% AND (20% × (2.30% - 2.1875%))
	= (100% × 0.4375%) + (20% × 0.1125%)
	= 0.4375% + 0.0225%
	= 0.46%

Example 2: Capital Gains Incentive Fee:

Alternative 1

Assumptions

· Year 1: $20 million investment made

· Year 2: Fair market value, or FMV of investment determined to be $22 million

---

(1) Represents 7% annualized hurdle rate.

(2) Re presents 2% annualized base management fee.

(3) Excludes organizational and offering expenses.

· Year 3: FMV of investment determined to be $17 million

· Year 4: Investment sold for $21 million

The impact, if any, on the capital gains portion of the incentive fee would be:

· Year 1: No impact

· Year 2: No impact

·

Year 3: Decrease base amount on which the second part of the incentive fee is calculated by $3 million (unrealized capital depreciation)

- Year 4: Increase base amount on which the second part of the incentive fee is calculated by $4 million ($1 million of realized capital gain and $3 million reversal in unrealized capital depreciation)

Alternative 2

Assumptions

- Year 1: $20 million investment made
- Year 2: FMV of investment determined to be $17 million
- Year 3: FMV of investment determined to be $17 million
- Year 4: FMV of investment determined to be $21 million
- Year 5: FMV of investment determined to be $18 million
- Year 6: Investment sold for $15 million

The impact, if any, on the capital gains portion of the incentive fee would be:

- Year 1: No impact
- Year 2: Decrease base amount on which the second part of the incentive fee is calculated by $3 million (unrealized capital depreciation)
- Year 3: No impact
- Year 4: Increase base amount on which the second part of the incentive fee is calculated by $3 million (rever in unrealized capital depreciation)
- Year 5: Decrease base amount on which the second part of the incentive fee is calculated by $2 million (unrealized capital depreciation)
- Year 6: Decrease base amount on which the second part of the incentive fee is calculated by $3 million ($5 million of realized capital loss offset by a $2 million reversal in unrealized capital depreciation)

Alternative 3

Assumptions

- Year 1: $20 million investment made in company A, or Investment A, and $20 million investment made in company B, or Investment B
- Year 2: FMV of Investment A is determined to be $21 million, and Investment B is sold for $18 million
- Year 3: Investment A is sold for $23 million

The impact, if any, on the capital gains portion of the incentive fee would be:

- Year 1: No impact

- Year 2: Decrease base amount on which the second part of the incentive fee is calculated by $2 million (real capital loss on Investment B)
- Year 3: Increase base amount on which the second part of the incentive fee is calculated by $3 million (reali capital gain on Investment A)

Alternative 4

Assumptions

- Year 1: $20 million investment made in company A, or Investment A, and $20 million investment made in company B, or Investment B
- Year 2: FMV of Investment A is determined to be $21 million, and FMV of Investment B is determined to b $17 million
- Year 3: FMV of Investment A is determined to be $18 million, and FMV of Investment B is determined to b $18 million
- Year 4: FMV of Investment A is determined to be $19 million, and FMV of Investment B is determined to b $21 million
- Year 5: Investment A is sold for $17 million, and Investment B is sold for $23 million

The impact, if any, on the capital gains portion of the incentive fee would be:

- Year 1: No impact
- Year 2: Decrease base amount on which the second part of the incentive fee is calculated by $3 million (unrealized capital depreciation on Investment B)
- Year 3: Decrease base amount on which the second part of the incentive fee is calculated by $1 million ($2 million in unrealized capital depreciation on Investment A and $1 million recovery in unrealized capital depreciation on Investment B)
- Year 4: Increase base amount on which the second part of the incentive fee is calculated by $3 million ($1 million recovery in unrealized capital depreciation on Investment A and $2 million recovery in unrealized ca depreciation on Investment B)
- Year 5: Increase base amount on which the second part of the incentive fee is calculated by $1 million ($3 million realized capital gain on Investment B offset by $3 million realized capital loss on Investment A plus a million reversal in unrealized capital depreciation on Investment A from Year 4)

Payment of our expenses

All investment professionals of the Investment Adviser and its staff, when and to the extent engaged in providing inves advisory and management services, and the compensation and routine overhead expenses of such personnel allocable to services, will be provided and paid for by the Investment Adviser. We bear all other costs and expenses of our operation

transactions, including those relating to: organization and offering; calculation of our net asset value (including the co
expenses of any independent valuation firm); expenses incurred by Prospect Capital Management payable to third pa
including agents, consultants or other advisers (such as independent valuation firms, accountants and legal couns
monitoring our financial and legal affairs and in monitoring our investments and performing due diligence on our prosp
portfolio companies; interest payable on debt, if any, and dividends payable on preferred stock, if any, incurred to finan
investments;

offerings of our debt, our preferred shares, our common stock and other securities; investment advisory fees; fees paya
third parties, including agents, consultants or other advisors, relating to, or associated with, evaluating and making investr
transfer agent and custodial fees; registration fees; listing fees; taxes; independent directors' fees and expenses; co
preparing and filing reports or other documents with the SEC; the costs of any reports, proxy statements or other noti
stockholders, including printing costs; our allocable portion of the fidelity bond, directors and officers/errors and omis
liability insurance, and any other insurance premiums; direct costs and expenses of administration, including auditor and
costs; and all other expenses incurred by us, by our Investment Adviser or by Prospect Administration in connection
administering our business, such as our allocable portion of overhead under the Administration Agreement, including re
our allocable portion of the costs of our chief compliance officer and chief financial officer and his staff, including the in
legal staff.

Duration and termination

The Investment Advisory Agreement was originally approved by our Board of Directors on June 23, 2004 and was rec
re-approved by the Board of Directors on June 17, 2009 for an additional one-year term expiring June 24, 2010. U
terminated earlier as described below, it will remain in effect from year to year thereafter if approved annually by our Bo
Directors or by the affirmative vote of the holders of a majority of our outstanding voting securities, including, in either
approval by a majority of our directors who are not interested persons. The Investment Advisory Agreement will automat
terminate in the event of its assignment. The Investment Advisory Agreement may be terminated by either party without pe
upon not more than 60 days' written notice to the other. See "Risk factors — Risks Relating to Our Business — We are
upon Prospect Capital Management's key management personnel for our future success."

Administration Agreement

We have also entered into an Administration Agreement with Prospect Administration under which Prospect Administr
among other things, provides (or arranges for the provision of) administrative services and facilities for us. For providing
services, we reimburse Prospect Administration for our allocable portion of overhead incurred by Prospect Administrat
performing its obligations under the Administration Agreement, including rent and our allocable portion of the costs of our
compliance officer and chief financial officer and his staff, including the internal legal staff. Under this agreement, Pro
Administration furnishes us with office facilities, equipment and clerical, bookkeeping and record keeping services at
facilities. Prospect Administration also performs, or oversees the performance of, our required administrative services,
include, among other things, being responsible for the financial records that we are required to maintain and preparing rep
our stockholders and reports filed with the Securities and Exchange Commission, or the SEC. In addition, Pro
Administration assists us in determining and publishing our net asset value, overseeing the preparation and filing of o
returns and the printing and dissemination of reports to our stockholders, and generally oversees the payment of our exp
and the performance of administrative and professional services rendered to us by others. Under the Administration Agree
Prospect Administration also provides on our behalf managerial assistance to those portfolio companies to which w
required to provide such assistance. The Administration Agreement may be terminated by either party without penalty up
days' written notice to the other party. Prospect Administration is a wholly owned subsidiary of our Investment Adviser.

Prospect Administration previously engaged Vastardis Fund Services LLC ("Vastardis") to serve as our sub-administra
perform certain services required of Prospect Administration. On April 30, 2009 we gave a 60-day notice to Vastar
termination of our agreement for Vastardis to provide sub-administration services effective June 30, 2009. We entered
new consulting services agreement for the period from July 1, 2009 until the filing of our Form 10-K for the year ended Ju
2009. We paid Vastardis a total of $30,000 for services rendered in conjunction with preparation of Form 10-K under th

agreement. All administration services were assumed by Prospect Administration effective September 14, 2009.

We reimbursed Prospect Administration $2.9 million, $2.1 million and $0.5 million for the twelve months ended June 30, June 30, 2008 and June 30, 2007, respectively, for services it provided to the Company at cost.

Indemnification

The Investment Advisory Agreement provides that, absent willful misfeasance, bad faith or gross negligence in the perforr of its duties or by reason of the reckless disregard of its duties and obligations, Prospect Capital Management and its off managers, agents, employees, controlling persons, members and any other person or entity affiliated with it are entit indemnification from us for any damages, liabilities, costs and expenses (including reasonable attorneys' fees and am reasonably paid in settlement) arising from the rendering of Prospect Capital Management's services under the Inves Advisory Agreement or otherwise as our investment adviser.

The Administration Agreement provides that, absent willful misfeasance, bad faith or negligence in the performance duties or by reason of the reckless disregard of its duties and obligations, Prospect Administration and its officers, man partners, agents, employees, controlling persons, members and any other person or entity affiliated with it are entit indemnification from us for any damages, liabilities, costs and expenses (including reasonable attorneys' fees and am reasonably paid in settlement) arising from the rendering of Prospect Administration's services under the Administ Agreement or otherwise as our administrator.

Under the sub-administration agreement (which, as described above, was terminated as of June 30, 2009), Vastardis a officers, partners, agents, employees, controlling persons, members, and any other person or entity affiliated with Vastard not liable to the Administrator or to us for any action taken or omitted to be taken by Vastardis in connection wi performance of any of its duties or obligations or otherwise as sub-administrator for the Administrator on our behalf agreement also provides that, absent willful misfeasance, bad faith or negligence in the performance of Vastardis' duties reason of the reckless disregard of Vastardis' duties and obligations, Vastardis and its officers, partners, agents, emplo controlling persons, members, and any other person or entity affiliated with Vastardis are entitled to indemnification fro Administrator and us. All damages, liabilities, costs and expenses (including reasonable attorneys' fees and amounts reaso paid in settlement) incurred in or by reason of any pending, threatened or completed action, suit, investigation or proceeding (including an action or suit by or in the right of the Administrator or us or our security holders) arising out otherwise based upon the performance of any of Vastardis' duties or obligations under the agreement or otherw sub-administrator for the Administrator on our behalf.

Board of Directors approval of the Investment Advisory Agreement

On June 17, 2009, our Board of Directors voted unanimously to renew the Investment Advisory Agreement for the 12-r period ending June 24, 2010. In its consideration of the Investment Advisory Agreement, the Board of Directors focus information it had received relating to, among other things: (a) the nature, quality and extent of the advisory and other se to be provided to us by Prospect Capital Management; (b) comparative data with respect to advisory fees or expense ratio by other business development companies with similar investment objectives; (c) our projected operating expenses; (projected profitability of Prospect Capital Management and any existing and potential sources of indirect income to Pro Capital Management or Prospect Administration from their relationships with us and the profitability of those relationship information about the services to be performed and the personnel performing such services under the Investment Adv Agreement; (f) the organizational capability and financial condition of Prospect Capital Management and its affiliates ar the possibility of obtaining similar services from other third party service providers or through an internally managed stru In approving the renewal of the Investment Advisory Agreement, the Board of Directors, including all of the directors wh not "interested persons," considered the following:

.

Nature, Quality and Extent of Services. The Board of Directors considered the nature, extent and quality of th
investment selection process employed by Prospect Capital Management. The Board of Directors also conside
Prospect Capital Management's personnel and their prior experience in connection with the types of investmen
made by us. The Board of Directors concluded that the services to be provided under the Investment Advisory
Agreement are generally the same as those of comparable business development companies described in the
available market data.

- Investment Performance. The Board of Directors reviewed our investment performance as well as comparati data with respect to the investment performance of other externally managed business development compani The Board of Directors concluded that Prospect Capital Management was delivering results consistent with o investment objective and that our investment performance was satisfactory when compared to comparable business development companies.
- The reasonableness of the fees paid to Prospect Capital Management. The Board of Directors considered comparative data based on publicly available information on other business development companies with res to services rendered and the advisory fees (including the management fees and incentive fees) of other busine development companies as well as our projected operating expenses and expense ratio compared to other business development companies. The Board of Directors, on behalf of the Company, also considered the profitability of Prospect Capital Management. Based upon its review, the Board of Directors concluded that t fees to be paid under the Investment Advisory Agreement are reasonable compared to other business development companies.
- Economies of Scale. The Board of Directors considered information about the potential of Prospect Capital Management to realize economies of scale in managing our assets, and determined that at this time there wer not economies of scale to be realized by Prospect Capital Management.

Based on the information reviewed and the discussions detailed above, the Board of Directors (including all of the director are not "interested persons") concluded that the investment advisory fee rates and terms are fair and reasonable in relation services provided and approved the renewal of the Investment Advisory Agreement with Prospect Capital Management as in the best interests of the Company and its stockholders.

Portfolio Managers

The following individuals function as portfolio managers primarily responsible for the day-to-day management of our port Our portfolio managers are not responsible for day-to-day management of any other accounts. For a description of principal occupations for the past five years, see above.

Name	Position	Length of Se with Comp (Years)
John F. Barry	Chairman and Chief Executive Officer	5
M. Grier Eliasek	President and Chief Operating Officer	5

Mr. Eliasek receives no compensation from the Company. Mr. Eliasek receives a salary and bonus from Prospect C Management that takes into account his role as a senior officer of the Company and of Prospect Capital Manageme performance and the performance of each of Prospect Capital Management and the Company. Mr. Barry receiv compensation from the Company. Mr. Barry, as the sole member of Prospect Capital Management, receives a salary a bonus from Prospect Capital Management and is entitled to equity distributions after all other obligations of Prospect C Management are met.

The following table sets forth the dollar range of our common stock beneficially owned by each of the portfolio man described above as of June 30, 2009.

Name	Aggregate Dollar Range of Common Stock Beneficially Owned by Prospect Capital Management
John F. Barry	Over $100,000
M. Grier Eliasek	Over $100,000

Managerial Assistance

As a business development company, we offer, and must provide upon request, managerial assistance to certain of our por companies. This assistance could involve, among other things, monitoring the operations of our portfolio compa participating in board and management meetings, consulting with and advising officers of portfolio companies and prov other organizational and financial guidance. We billed $846,000, $1,027,000, and $505,000 of managerial assistance fees f years ended June 30, 2009, June 30, 2008, and June 30, 2007, respectively, of which $60,000 and $380,000 remains c consolidated statement of assets and liabilities as of June 30, 2009, and June 30, 2008, respectively. These fees are paid Administrator so we simultaneously accrue a payable to the Administrator for the same amounts, which remain c consolidated statements of assets and liabilities.

License Agreement

We entered into a license agreement with Prospect Capital Management, pursuant to which Prospect Capital Manage agreed to grant us a nonexclusive, royalty free license to use the name "Prospect Capital." Under this agreement, we have a to use the Prospect Capital name, for so long as Prospect Capital Management or one of its affiliates remains our inves adviser. Other than with respect to this limited license, we have no legal right to the Prospect Capital name. This li agreement will remain in effect for so long as the Investment Advisory Agreement with our Investment Adviser is in effect

CERTAIN RELATIONSHIPS AND TRANSACTIONS

We have entered into the Investment Advisory Agreement with Prospect Capital Management. Our Chairman of the Bo Directors is the sole member of and controls Prospect Capital Management. Our senior management may in the futur serve as principals of other investment managers affiliated with Prospect Capital Management that may in the future m investment funds with investment objectives similar to ours. In addition, our executive officers and directors and the prin of Prospect Capital Management may serve as officers, directors or principals of entities that operate in the same or relatec of business as we do or of investment funds managed by affiliates. Accordingly, we may not be given the opportun participate in certain investments made by investment funds managed by advisers affiliated with Prospect Capital Manage However, our Investment Adviser and other members of the affiliated present and predecessor companies of Prospect C Management intend to allocate investment opportunities in a fair and equitable manner consistent with our invest objectives and strategies so that we are not disadvantaged in relation to any other client. See "Risk Factors — Risks Rel Our Business — Potential conflicts of interest could impact our investment returns."

In addition, pursuant to the terms of the Administration Agreement, Prospect Administration provides, or arranges to pro the Company with the office facilities and administrative services necessary to conduct our day-to-day operations. Pro Capital Management is the sole member of and controls Prospect Administration.

We have no intention of investing in any portfolio company in which Prospect Capital Management or any affiliate cur has an investment.

CONTROL PERSONS AND PRINCIPAL STOCKHOLDERS

As of February 25, 2010, there were no persons that owned 25% or more of our outstanding voting securities, and we belie
person should be deemed to control us, as such term is defined in the 1940 Act.

The following table sets forth, as of February 25, 2010, certain ownership information with respect to our common sto
those persons who directly or indirectly own, control or hold with the power to vote, 5% or more

---

of our outstanding common stock and all officers and directors, as a group. Unless otherwise indicated, we believe th
beneficial owners set forth in the tables below have sole voting and investment power.

Name and Address	Type of Ownership	Shares Owned	Percentag Common S Outstandin
Prospect Capital Management LLC(2)	Record and beneficial	968,251	1.52%
All officers and directors as a group (6 persons)(3)	Record and beneficial	1,940,391	3.05%

---

(1) Does not reflect shares of common stock reserved for issuance upon any exercise of any underwriters' overallo option.
(2) John F. Barry is a control person of Prospect Capital Management.
(3) Represents shares of common stock held by Prospect Capital Management. Because John F. Barry controls Pro Capital Management, he may be deemed to be the beneficial owner of shares of our common stock held by Pro Capital Management. The address for all officers and directors is c/o Prospect Capital Corporation, 10 East 40th S 44th Floor, New York, NY 10016.

The following table sets forth the dollar range of our equity securities beneficially owned by each of our directors and of as of December 31, 2009. We are not part of a "family of investment companies" as that term is defined in the 1940 Act.

Name of Director or Officer	Dollar Range Equity Securities in t Company(1
Independent Directors	
Graham D.S. Anderson	$50,001 — $10
Andrew C. Cooper	none
Eugene S. Stark	$50,001 — $10
Interested Directors	
John F. Barry III(2)	Over $100,0
M. Grier Eliasek	Over $100,0
Officer	
Brian H. Oswald	$50,001 — $10

(1) Dollar ranges are as follows: none, $1-$10,000, $10,001-$50,000, $50,001-$100,000 or over $100,000.
(2) Represents an indirect beneficial ownership in shares of our common stock, that are beneficially owned direct Prospect Capital Management, by reason of Mr. Barry's position as a control person of Prospect Capital Managemen

PORTFOLIO COMPA

The following is a listing of our portfolio companies at December 31, 2009. Values are as of December 31, 2009.

The portfolio companies are presented in three categories: "companies more than 25% owned" are portfolio companies in Prospect directly or indirectly owns more than 25% of the outstanding voting securities of such portfolio company therefore, such portfolio company is presumed to be controlled by us under the 1940 Act; "companies owned 5% to 25% portfolio companies where Prospect directly or indirectly owns 5% to 25% of the outstanding voting securities of such por company and/or holds one or more seats on the portfolio company's Board of Directors and, therefore, such portfolio con is deemed to be an affiliated person with us under the 1940 Act; "companies less than 5% owned" are portfolio comp where Prospect directly or indirectly owns less than 5% of the outstanding voting securities of such portfolio compan where it has no other affiliations with such portfolio company. As of December 31, 2009, Prospect owned 100.00% of the diluted common equity of GSHI, 100.00% of the common equity of CCEHI, 49.00% of the fully diluted common equ Integrated, 79.83% of the fully diluted common equity of Iron Horse, 100.00% of the members unit of AWCNC, LLC, 100 of the common equity of Coalbed, Inc., 100.00% of the fully diluted equity of Freedom Marine Holdings Inc., 79.40% fully diluted equity of Nupla Corporation, 80.00% of the fully diluted common equity of NRG, 40.00% of the fully d equity of Sidump'r Trailer Company, Inc., 74.51% of the fully diluted equity of R-V, 78.11% of the fully diluted common of Ajax and 100.00% of the fully diluted common equity of Yatesville. Prospect makes available significant mana assistance to its portfolio companies. Prospect generally requests and may receive rights to observe the meetings of its por companies' Boards of Directors.

Name of Portfolio Company	Nature of its Principal Business (Location)	Title and Class of Securities Held	Collateral Held	Investment Structure	Equity Securities Held, at Fair Value	Loans Fair V
Companies more than 25% owned						
Ajax Rolled Ring and Machine	Manufacturing (South Carolina)	Senior secured debt, subordinated secured debt, preferred stock and common equity	First priority lien on substantially all assets	Common shares; Preferred shares; Senior secured note Tranche A, 10.50% due 4/01/2013; Subordinated secured note Tranche B, 11.50% plus 6.00% PIK due 4/01/2013; Subordinated secured note Tranche B, 15.00% due 10/30/2010	0.0	25.8
AWCNC, LLC	Machinery (North Carolina)	Members Units	N/A	Members units	0.0	0.0
C&J Cladding LLC	Metal services (Texas)	Warrants	N/A — loan repaid	Warrants, common shares, expiring 3/30/2014	3.1	0.0

Change Clean Energy Holdings, Inc	Biomass power (Maine)	Common equity	First priority lien on substantially all assets	Common shares	2.0	0.0
Coalbed, Inc. / Coalbed, LLC	Oil & Gas Production (Tennessee)	Senior secured debt and common equity	First priority lien on substantially all assets	Common shares; Senior secured note, 14.50%, in non-accrual status effective 10/21/2009 due 6/30/2010	0.0	3.7
Fischbein, LLC	Machinery (North Carolina)	Senior subordinated debt and membership interests	Second priority lien on all assets and stock	Membership interests; Senior subordinated debt, 12.00% plus 6.50% PIK due 5/01/2013	1.9	3.5
Freedom Marine Services LLC	Shipping vessels (Louisiana)	Subordinated secured debt and net profit interest	Second priority lien on substantially all assets	Net profit interest, 22.50%; Subordinated secured note, 16.00% PIK due 12/31/2011	0.0	6.2
Gas Solutions Holdings, Inc.	Gas gathering and processing (Texas)	Senior and junior secured debt and common equity	First priority lien on substantially all assets	Common shares; Senior secured note, 18.00% due 12/22/2018; Junior secured note, 18.00% due 12/23/2018	55.2	30.0
Integrated Contract Services, Inc.	Contracting (North Carolina)	Senior and junior secured debt, preferred stock and common equity	First priority lien on substantially all assets	Common shares; Preferred shares; Senior and junior secured notes, 7.00% plus 7.00% PIK plus 6.00% default interest, in non-accrual status effective 10/09/2007 past due; Senior demand note, 15.00% due 12/31/2009	0.0	5.3
Iron Horse Coiled Tubing, Inc.	Production services (Alberta, Canada)	Senior secured debt, bridge loan and common equity	First priority lien on substantially all assets	Common shares; Bridge loan, 15.00% plus 3.00% PIK, in non-accrual status effective 5/01/2009 due 12/31/2009; Senior secured note, 15.00%, in non-accrual status effective 5/01/2009 due 12/31/2009	0.0	12.3
NRG Manufacturing, Inc.	Manufacturing (Texas)	Senior secured debt and common equity	First priority lien on substantially all assets	Common shares; Senior secured note, 16.50% due 8/31/2011	13.6	13.1

Name of Portfolio Company	Nature of its Principal Business (Location)	Title and Class of Securities Held	Collateral Held	Investment Structure	Equity Securities Held, at Fair Value	Loans Fair Va
Nupla Corporation	Home & Office Furnishings, Housewares & Durable (California)	Revolving line of credit, senior secured debt, senior subordinated debt, preferred stock and common equity	First priority lien on substantially all assets	Common shares; Preferred shares; Revolving line of credit, 0.50%-7.25% plus 2.00% default interest due 9/04/2012; Senior secured Term Loan A, 8.00% plus 2.00% default interest due 9/04/2012; Senior subordinated debt, 10.00% plus 5.00% PIK, in non-accrual status effective 4/01/2009 due 3/04/2013	0.0	2.4
R-V Industries, Inc.	Manufacturing (Pennsylvania)	Warrants and common equity	N/A — loan repaid	Common shares; Warrants, common shares, expiring 6/30/2017	12.0	0.0
Sidump'r Trailer Company, Inc.	Automobile (Nebraska)	Revolving line of credit, senior secured debt, preferred stock and common equity	First priority lien on all assets and stock	Common shares; Preferred shares; Revolving line of credit, 0.50%-7.25%, in non-accrual status effective 11/01/2008 due 1/10/2011; Senior secured Term Loan A, 7.25%, in non-accrual status effective 11/01/2008 due 1/10/2011; Senior secured Term Loan B, 8.75%, in non-accrual status effective 11/01/2008 due 1/10/2011; Senior secured Term Loan C, 16.50% PIK, in non-accrual status effective 9/27/2008 due 7/10/2011; Senior secured Term Loan D 7.25%, in non-accrual status effective 11/01/2008 due 7/10/2011	0.0	0.9
Yatesville Coal Holdings, Inc.	Mining and coal production (Kentucky)	Senior and junior secured debt and common equity	First priority lien on substantially all assets	Common shares; Senior secured note, 15.77% due 12/31/2010, in non-accrual status effective 1/01/2009;	0.0	1.0

				Junior secured note, 15.77% due 12/31/2010, in non-accrual status effective 1/01/2009		
Companies 5% to 25% owned						
Appalachian Energy Holdings LLC	Construction services (West Virginia)	Senior secured debt, warrants and preferred units	First priority lien on substantially all assets	Preferred stock; Warrants, common shares, expiring 2/13/2016, 6/17/2018, 11/30/2018; Senior secured note Tranche A, 14.00% plus 3.00% PIK plus 3.00% default interest non-accrual status effective 11/01/2008 due 1/31/2011; Senior secured note Tranche B, 14.00% plus 3.00% PIK 3.00% default interest non-accrual status effective 11/01/2008, past due	0.0	1.2
Biotronic NeuroNetwork	Healthcare (Michigan)	Senior secured debt and preferred stock	First priority lien on substantially all assets	Preferred shares; Senior secured note, 11.50% plus 1.00% PIK due 2/21/2013	3.5	27.0
Boxercraft Incorporated	Textiles & Leather (Georgia)	Revolving line of credit, senior secured debt, preferred stock and common equity	First priority lien on substantially all assets	Common shares; Preferred shares; Revolving line of credit, 0.50% due 9/16/2013; Senior secured Term Loan A, 9.50%-10.50% due 9/16/2013; Senior secured Term Loan B, 10.00%-11.00% due 9/16/2013; Senior secured Term Loan C, 12.00% plus 6.50% PIK due 3/16/2014	0.0	12.4
KTPS Holdings LLC	Textiles & Leather (Colorado)	Revolving line of credit, senior secured debt and membership interests	First priority lien on all assets and stock	Membership interests; Revolving line of credit, 0.50% due 1/31/2012; Senior secured Term Loan A, 10.50%-11.25% due 1/31/2012; Senior secured Term Loan B, 12.00% due 1/31/2012; Senior secured	0.0	7.2

				Term Loan C 12.00% plus 6.00% PIK due 3/31/2012		
Miller Petroleum, Inc.	Oil and gas production (Tennessee)	Warrants	N/A — loan repaid	Warrants, expiring 5/04/2010 through 12/31/2014	0.9	0.0
Smart, LLC	Diversified / Conglomerate Service (New York)	Membership interests	N/A	Membership interests	0.0	0.0
Sports Helmets Holdings, LLC	Personal & Nondurable Consumer Products (New York)	Revolving line of credit, senior secured debt, senior subordinated debt and common equity	First priority lien on all assets and stock	Common shares; Revolving line of credit, 0.50% due 12/14/2013; Senior secured Term Loan A, 4.26%-6.00% due 12/14/2013; Senior secured Term Loan B, 4.76%-6.50% due 12/14/2013; Senior subordinated debt Series A, 12.00% plus 3.00% PIK due 6/14/2014; Senior subordinated debt Series B, 10.00% plus 5.00% PIK due 6/14/2014	0.4	13.9
Companies less than 5% owned						
ADAPCO, Inc.	Ecological (Florida)	Common equity	N/A	Common shares	0.3	0.0
Aircraft Fasteners International, LLC	Machinery (California)	Revolving line of credit, senior and junior secured debt and convertible preferred stock	First priority lien on all assets and stock	Convertible preferred shares; Revolving line of credit, 0.50% due 11/01/2012; Senior secured Term Loan, 3.92%-5.40% due 11/01/2012; Junior secured Term Loan, 12.00% plus 2.00% PIK due 5/01/2013	0.4	8.3
Allied Defense Group, Inc.	Aerospace & Defense (Virginia)	Common equity	N/A	Common shares	0.0	0.0
American Gilsonite Company	Specialty minerals (Utah)	Senior subordinated secured debt and membership	Second priority lien on substantially all assets	Membership interests; Senior subordinated secured note, 12.00% plus 3.00% PIK due 3/14/2013	2.7	15.1

interests

Name of Portfolio Company	Nature of its Principal Business (Location)	Title and Class of Securities Held	Collateral Held	Investment Structure	Equity Securities Held, at Fair Value	Loans
Arrowhead General Insurance Agency, Inc.	Insurance (California)	Junior secured debt	Second perfected priority lien on substantially all assets	Junior secured Term Loan, 10.25% plus 2.50% PIK due 2/08/2013	0.0	3.9
Borga, Inc.	Mining, Steel, Iron and Non-Precious Metal and Coal Production (California)	Revolving line of credit, senior secured debt and warrants	First priority lien on all assets and pledge of all stock	Warrants; Revolving line of credit, 0.50%-5.00% plus 3.00% default interest due 5/06/2010; Senior secured Term Loan B, 8.50% plus 3.00% default interest due 5/06/2010; Senior secured Term Loan C, 12.00% plus 4.00% PIK plus 3.00% default interest due 5/06/2010	0.0	2.7
Caleel & Hayden, LLC	Personal & Nondurable Consumer Products (Colorado)	Junior secured debt, senior subordinated debt, common equity and options	First priority lien on all assets and stock	Options; Common shares; Junior secured Term Loan B, 9.75%-10.00% due 11/10/2011; Senior subordinated debt, 12.00% plus 4.50% PIK due 11/10/2012	0.3	14.2
Castro Cheese Company, Inc.	Food products (Texas)	Junior secured debt	Second priority lien on substantially all assets	Junior secured note, 11.00% plus 2.00% PIK due 2/28/2013	0.0	7.6
Copernicus Group	Healthcare (North Carolina)	Revolving line of credit, senior secured debt, senior subordinated debt and preferred stock	First priority lien on substantially all assets	Preferred shares; Revolving line of credit, 0.50%-10.50% due 10/08/2013; Senior secured Term Loan A, 10.50%-11.50% due 10/08/2013; Senior subordinated debt, 12.00% plus 6.00% PIK-10.00% plus 10.00% PIK due 4/08/2014	0.1	17.2
Custom Direct, Inc.	Printing & Publishing	Senior and junior secured	First priority lien on	Senior secured Term Loan, 3.06% due	0.0	2.5

	(Maryland)	debt	substantially all assets	12/31/2013; Junior secured Term Loan 6.31% due 12/31/2014		
Deb Shops, Inc.	Retail (Pennsylvania)	Second lien debt	Second priority lien on substantially all assets	Second lien note, 1.00% plus 13.00% PIK due 10/23/2014	0.0	2.3
Diamondback Operating LP	Oil and gas production (Oklahoma)	Net profit interest	N/A — loan repaid.	Net profit interest, 15.00%	0.4	0.0
Dover Saddlery, Inc.	Retail (Massachusetts)	Common equity	N/A	Common shares	0.0	0.0
EXL Acquisition Corporation	Electronics (South Carolina)	Revolving line of credit, Senior secured debt and common equity	First priority lien on all assets and stock	Common shares; Revolving line of credit, 0.50% due 3/15/2012; Senior secured Term Loan A, 3.93%-5.50% due 3/15/2011; Senior secured Term Loan B, 4.18%-5.75% due 3/15/2012; Senior secured Term Loan C, 4.68%-6.25% due 3/15/2012; Senior secured Term Loan D, 12.00% plus 3.00% PIK due 3/15/2012	0.8	13.6
Fairchild Industrial Products, Co.	Electronics (North Carolina)	Preferred stock and common equity	N/A	Common shares; Preferred shares	0.6	0.0
H&M Oil & Gas LLC	Oil and gas production (Texas)	Senior secured debt and net profit interest	First priority lien on substantially all assets	Net profit interest, 8.00%; Senior secured note, 13.00% due 6/30/2010	1.0	46.1
Hudson Products Holdings, Inc.	Mining, Steel, Iron and Non-Precious Metals and Coal Production (Texas)	Senior secured debt	First priority lien on substantially all assets	Senior secured Term Loan, 8.00% due 8/24/2015	0.0	7.0
IEC Systems LP/Advanced Rig Services LLC ("ARS")	Oilfield fabrication (Texas)	Senior secured debt	First priority lien on substantially all assets	Senior secured notes 12.00% plus 3.00% PIK due 11/20/2012	0.0	32.3
					0.0	13.0

Impact Products, LLC	Machinery (Ohio)	Junior secured debt and senior subordinated debt	Second priority lien on all assets and stock	Junior secured Term Loan, 6.25%-8.25% due 9/09/2012; Senior subordinated debt, 10.00% plus 5.00% PIK due 9/09/2012		
Label Corp Holdings, Inc.	Printing & Publishing (Nebraska)	Senior secured debt	First priority lien on substantially all assets	Senior secured Term Loan, 8.50% due 8/08/2014	0.0	5.3
LHC Holdings Corp.	Healthcare (Florida)	Revolving line of credit, senior secured debt, senior subordinated debt and membership interests	First priority lien on all assets and stock	Membership interests; Revolving line of credit, 0.50% due 11/30/2012; Senior secured Term Loan A, 4.31%-5.75% due 11/30/2012; Senior subordinated debt, 12.00% plus 2.50% PIK due 5/31/2013	0.2	6.3
Mac & Massey Holdings, LLC	Food Products (Georgia)	Senior subordinated debt and common equity	Subordinated lien on substantially all assets	Common shares; Senior subordinated debt, 10.00% plus 5.75% PIK due 2/10/2013	0.2	6.9
Maverick Healthcare LLC	Healthcare (Arizona)	Second lien debt, preferred units and common units	Second priority lien on substantially all assets	Common units; Preferred units; Second lien debt, 12.50% plus 3.50% PIK due 4/30/2014	1.7	12.9
Northwestern Management Services, LLC	Healthcare (Florida)	Revolving line of credit, senior and junior secured debt and common equity	First priority lien on all assets and stock	Common shares; Revolving line of credit, 0.50% due 12/13/2012; Senior secured Term Loan A, 4.24%-5.75% due 12/13/2012; Senior secured Term Loan B, 4.74%-6.25% due 12/13/2012; Junior secured Term Loan, 12.00% plus 3.00% due 6/13/2013	0.4	7.1
Prince Mineral Company, Inc.	Metal Services and Minerals (New York)	Junior secured debt and senior subordinated debt	Second priority lien on substantially all assets	Junior secured Term Loan, 5.29%-7.00% due 12/21/2012; Senior subordinated debt, 13.00% plus 1.00% due 7/21/2013	0.0	9.1
Qualitest Pharmaceuticals, Inc.	Pharmaceuticals (Alabama)	Second lien debt	Second priority lien on substantially all	Second lien debt, 7.78% due 4/30/2015	0.0	12.0

assets

Name of Portfolio Company	Nature of its Principal Business (Location)	Title and Class of Securities Held	Collateral Held	Investment Structure	Equity Securities Held, at Fair Value	Loans
Regional Management Corp.	Financial services (South Carolina)	Second lien debt	Second priority lien on substantially all assets	Second lien debt, 13.00% plus 2.00% PIK due 6/29/2012	0.0	24.5
R-O-M Corporation	Manufacturing (Missouri)	Revolving line of credit, senior secured debt and senior subordinated debt	First priority lien on all assets and stock	Revolving line of credit, 0.50% due 2/08/2013; Senior secured Term Loan a, 3.00%-4.75% due 2/08/2013; Senior secured Term Loan B, 4.50%-6.25% due 5/08/2013; Senior subordinated debt, 12.00% plus 3.00% PIK due 8/08/2013	0.0	18.7
Shearer's Foods, Inc.	Food products (Ohio)	Second lien debt and membership interests	Second priority lien on substantially all assets	Membership interests; Second lien debt, 15.00% due 10/31/2013	4.5	18.2
Stryker Energy LLC	Oil and gas production (Ohio)	Subordinated secured revolving credit facility and overriding royalty interest	Second priority lien on substantially all assets	Overriding royalty interest; Subordinated secured revolving credit facility, 12.00% due 12/01/2011	2.8	28.3
TriZetto Group	Healthcare (California)	Subordinated unsecured debt	Unsecured	Subordinated unsecured note, 12.00% plus 1.50% PIK due 10/01/2016	0.0	15.8
Unitek	Technical services (Pennsylvania)	Second lien debt	Second priority lien on substantially all assets	Second lien debt, 13.08% due 12/31/2013	0.0	11.7
Wind River Resources Corp. and Wind River II Corp.	Oil and gas production (Utah)	Senior secured debt and net profit interest	First priority lien on substantially all assets	Net profit interest, 5.00%; Senior secured note, 13.00% plus 3.00% default interest, in non-accrual status effective 12/01/2008 due 7/31/2010	0.0	10.6

DETERMINATION OF NET ASSET VALUE

The net asset value per share of our outstanding shares of common stock will be determined quarterly by dividing the va total assets minus liabilities by the total number of shares outstanding.

In calculating the value of our total assets, we will value investments for which market quotations are readily available a market quotations. Short-term investments which mature in 60 days or less, such as U.S. Treasury bills, are valued at amo cost, which approximates market value. The amortized cost method involves recording a security at its cost (i.e., prin amount plus any premium and less any discount) on the date of purchase and thereafter amortizing/accreting that diffe between the principal amount due at maturity and cost assuming a constant yield to maturity as determined at the ti purchase. Short-term securities which mature in more than 60 days are valued at current market quotations by an indepe pricing service or at the mean between the bid and ask prices obtained from at least two brokers or dealers (if availab otherwise by a principal market maker or a primary market dealer). Investments in money market mutual funds are valu their net asset value as of the close of business on the day of valuation.

Most of the investments in our portfolio do not have market quotations which are readily available, meaning the investme not have actively traded markets. Debt and equity securities for which market quotations are not readily available are v with the assistance of an independent valuation service using a documented valuation policy and a valuation process t consistently applied under the direction of our Board of Directors. For a discussion of the risks inherent in determining the of securities for which readily available market values do not exist, see "Risk Factors — Risks Relating to Our Business our portfolio investments are recorded at fair value as determined in good faith by our Board of Directors and, as a result, is uncertainty as to the value of our portfolio investments."

The factors that may be taken into account in valuing such investments include, as relevant, the portfolio company's abi make payments, its estimated earnings and projected discounted cash flows, the nature and realizable value of any collater financial environment in which the portfolio company operates, comparisons to securities of similar publicly traded comp changes in interest rates for similar debt instruments and other relevant factors. Due to the inherent uncertainty of determ the fair value of investments that do not have readily available market quotations, the fair value of these investments may significantly from the values that would have been used had such market quotations existed for such investments, and any differences could be material.

As part of the fair valuation process, the independent valuation firm engaged by the Board of Directors performs a revi each debt and equity investment and provides a range of values for each investment, which, along with management's valu recommendations, is reviewed by the Audit Committee. Management and the independent valuation firm may adjust preliminary evaluations to reflect comments provided by the Audit Committee. The Audit Committee reviews the valuation report and management's valuation recommendations and makes a recommendation to the Board of Directors on its analysis of the methodologies employed and the various weights that should be accorded to each portion of the valu as well as factors that the independent valuation firm and management may not have included in their evaluation processe Board of Directors then evaluates the Audit Committee recommendations and undertakes a similar analysis to determine th value of each investment in the portfolio in good faith.

Determination of fair values involves subjective judgments and estimates not susceptible to substantiation by auc
procedures. Accordingly, under current accounting standards, the notes to our financial statements will refer to the uncer
with respect to the possible effect of such valuations, and any change in such valuations, on our financial statements.

SALES OF COMMON STOCK BELOW NET ASSET VALUE

At our 2008 annual meeting of stockholders held on February 12, 2009 and our 2009 annual meeting of stockholders he December 11, 2009, our stockholders approved our ability to sell an unlimited number of shares of our common stock a level of discount from net asset value (NAV) per share during the twelve-month period following such approval. In order t shares pursuant to this authorization a majority of our directors who have no financial interest in the sale and a majority o independent directors must (a) find that the sale is in our best interests and in the best interests of our stockholders, and consultation with any underwriter or underwriters of the offering, make a good faith determination as of a time o immediately prior to the first solicitation by us or on our behalf of firm commitments to purchase such shares, or immed prior to the issuance of such shares, that the price at which such shares are to be sold is not less than a price which cl approximates the market value of such shares, less any distributing commission or discount. Any offering of common below NAV per share will be designed to raise capital for investment in accordance with our investment objective.

In making a determination that an offering below NAV per share is in our and our stockholders' best interests, our Bo Directors would consider a variety of factors, including:

- The effect that an offering below NAV per share would have on our stockholders, including the potential dilu they would experience as a result of the offering;
- The amount per share by which the offering price per share and the net proceeds per share are less than the m recently determined NAV per share;
- The relationship of recent market prices of par common stock to NAV per share and the potential impact of t offering on the market price per share of our common stock;
- Whether the estimated offering price would closely approximate the market value of our shares;
- The potential market impact of being able to raise capital during the current financial market difficulties;
- The nature of any new investors anticipated to acquire shares in the offering;
- The anticipated rate of return on and quality, type and availability of investments; and
- The leverage available to us.

Our Board of Directors would also consider the fact that sales of common stock at a discount will benefit our Advisor Advisor will earn additional investment management fees on the proceeds of such offerings, as it would from the offering o other securities of the Company or from the offering of common stock at premium to NAV per share.

We will not sell shares under a prospectus supplement to the registration statement or current post-effective amendment th of which this prospectus forms a part (the "current registration statement") if the cumulative dilution to our NAV per share offerings under the current registration statement exceeds 15%. This limit would be measured separately for each off pursuant to the current amendment by calculating the percentage dilution or accretion to aggregate NAV from that offerin

then summing the percentage from each offering. For example, if our most recently determined NAV at the time of th
offering is $10.06 and we have 64 million shares outstanding, sale of 16 million shares at net proceeds to us of $5.03 per
(a 50% discount) would produce dilution of 10.00%. If we subsequently determined that our NAV per share increased to $
on the then 80 million shares outstanding and then made an additional offering, we could, for example, sell approximately

additional 8.885 million shares at net proceeds to us of $5.50 per share, which would produce dilution of 5.00%, befo
would reach the aggregate 15% limit. If we file a new post-effective amendment, the threshold would reset.

Sales by us of our common stock at a discount from NAV pose potential risks for our existing stockholders whether or no
participate in the offering, as well as for new investors who participate in the offering.

The following three headings and accompanying tables will explain and provide hypothetical examples on the impact
offering at a price less than NAV per share on three different set of investors:

- existing shareholders who do not purchase any shares in the offering;
- existing shareholders who purchase a relatively small amount of shares in the offering or a relatively large amount of shares in the offering; and
- new investors who become shareholders by purchasing shares in the offering.

Impact On Existing Stockholders Who Do Not Participate in the Offering

Our existing stockholders who do not participate in an offering below NAV per share or who do not buy additional shares
secondary market at the same or lower price we obtain in the offering (after expenses and commissions) face the gr
potential risks. These stockholders will experience an immediate decrease (often called dilution) in the NAV of the share
hold and their NAV per share. These stockholders will also experience a disproportionately greater decrease in
participation in our earnings and assets and their voting power than the increase we will experience in our assets, pot
earning power and voting interests due to the offering. These shareholders may also experience a decline in the market pr
their shares, which often reflects to some degree announced or potential increases and decreases in NAV per share
decrease could be more pronounced as the size of the offering and level of discounts increases.

The following chart illustrates the level of NAV dilution that would be experienced by a nonparticipating stockholder in
different hypothetical offerings of different sizes and levels of discount from NAV per share. It is not possible to predi
level of market price decline that may occur.

The examples assume that the issuer has 64,000,000 common shares outstanding, $700,000,000 in total assets and $56,16
in total liabilities. The current NAV and NAV per share are thus $643,840,000 and $10.06. The chart illustrates the di
effect on Stockholder A of (1) an offering of 3,200,000 shares (5% of the outstanding shares) at $9.56 per share after of
expenses and commission (a 5% discount from NAV), (2) an offering of 6,400,000 shares (10% of the outstanding shar
$9.05 per share after offering expenses and commissions (a 10% discount from NAV) and (3) an offering of 12,800,000 s
(20% of the outstanding shares) at $8.05 per share after offering expenses and commissions (a 20% discount from NAV
prospectus supplement pursuant to which any discounted offering is made will include a chart based on the actual num
shares in such offering and the actual discount to the most recently determined NAV, as applicable.

	Prior to Sale Below	Example 1 5% Offering at 5% Discount Following	%	Example 2 10% Offering at 10% Discount Following	%	Example 3 20% Offering at 20% Discount Following	%

	NAV	Sale	Change	Sale	Change	Sale	Chang
Offering Price							
Price per Share to Public		$ 10.06	—	$ 9.53	—	$ 8.47	—
Net Proceeds per Share to Issuer		$ 9.56	—	$ 9.05	—	$ 8.05	—
Decrease to NAV							
Total Shares Outstanding	64,000,000	67,200,000	5.00 %	70,400,000	10.00 %	76,800,000	20.0
NAV per Share	$ 10.06	$ 10.04	(0.24)%	$ 9.97	(0.91)%	$ 9.72	(3.33
Dilution to Nonparticipating Stockholder							
Shares Held by Stockholder A	64,000	64,000	0.00 %	64,000	0.00 %	64,000	0.00

Percentage Held by Stockholder A	0.10 %	0.10 %	(4.76)%	0.09 %	(9.09)%	0.08 %	(16.67
Total NAV Held by Stockholder A	$ 643,840	$ 642,307	(0.24)%	$ 637,987	(0.91)%	$ 622,379	(3.33
Total Investment by Stockholder A (Assumed to be $10.06 per Share)	$ 643,840	$ 643,840		$ 643,840		$ 643,840	
Total Dilution to Stockholder A (Total NAV Less Total Investment)		$ (1,553)		$ (5,853)		$ (21,461)	
NAV per Share Held by Stockholder A		$ 10.04		$ 9.97		$ 9.72	
Investment per Share Held by Stockholder A (Assumed to be $10.06 per Share on Shares Held Prior to Sale)	$ 10.06	$ 10.06		$ 10.06		$ 10.06	
Dilution per Share Held by Stockholder A (NAV per Share Less Investment per Share)		$ (0.02)		$ (0.09)		$ (0.34)	
Percentage Dilution to Stockholder A (Dilution per Share Divided by Investment per Share)			(0.24)%		(0.91)%		(3.33

Impact On Existing Stockholders Who Do Participate in the Offering

Our existing stockholders who participate in an offering below NAV per share or who buy additional shares in the seco market at the same or lower price as we obtain in the offering (after expenses and commissions) will experience the same of NAV dilution as the nonparticipating stockholders, albeit at a lower level, to the extent they purchase less than the percentage of the discounted offering as their interest in our shares immediately prior to the offering. The level of NAV di will decrease as the number of shares such stockholders purchase increases. Existing stockholders who buy more than percentage will experience NAV dilution but will, in contrast to existing stockholders who purchase less than proportionate share of the offering, experience an increase (often called accretion) in NAV per share over their investme share and will also experience a disproportionately greater increase in their participation in our earnings and assets and voting power than our increase in assets, potential earning power and voting interests due to the offering. The level of acc will increase as the excess number of shares such stockholder purchases increases. Even a stockholder who overpartic will, however, be subject to the risk that we may make additional discounted offerings in which such stockholder doe participate, in which case such a stockholder will experience NAV dilution as described above in such subsequent offe These shareholders may also experience a decline in the market price of their shares, which often reflects to some d announced or potential increases and decreases in NAV per share. This decrease could be more pronounced as the size offering and level of discounts increases.

The following chart illustrates the level of dilution and accretion in the hypothetical 20% discount offering from the prior (Example 3) for a stockholder that acquires shares equal to (1) 50% of its proportionate share of the offering (i.e., 6,400 s which is 0.05% of an offering of 12,800,000 shares) rather than its 0.10% proportionate share and (2) 150% of such perce (i.e. 19,200 shares, which is 0.15% of an offering of 12,800,000 shares rather than its 0.10% proportionate share) prospectus supplement pursuant to which any discounted offering is made will include a chart for these examples based o actual number of shares in such offering and the actual discount from the most recently determined NAV per sha applicable. It is not possible to predict the level of market price decline that may occur.

	Prior to Sale Below NAV	50% Participation Following Sale	50% Participation % Change	150% Participation Following Sale	150% Participation % Change
Offering Price					
Price per Share to Public		$ 8.47		$ 8.47	
Net Proceeds per Share to Issuer		$ 8.05		$ 8.05	
Decrease/Increase to NAV					
Total Shares Outstanding	64,000,000	76,800,000	20.00 %	76,800,000	20.00
NAV per Share	$ 10.06	$ 9.72	(3.33)%	$ 9.72	(3.33
Dilution/Accretion to Participating Stockholder					
Shares Held by Stockholder A	64,000	70,400	10.00 %	83,200	30.00
Percentage Held by Stockholder A	0.10 %	0.09 %	(8.33)%	0.11 %	8.33
Total NAV Held by Stockholder A	$ 643,840	$ 684,617	6.33 %	$ 809,092	25.67
Total Investment by Stockholder A (Assumed to be $10.06 per Share on Shares held Prior to Sale)		$ 698,058		$ 806,494	
Total Dilution/Accretion to Stockholder A (Total NAV Less Total Investment)		$ (13,441)		$ 2,598	
NAV per Share Held by Stockholder A		$ 9.72		$ 9.72	
Investment per Share Held by Stockholder A (Assumed to Be $10.06 on Shares Held Prior to Sale)	$ 10.06	$ 9.91	(1.44)%	$ 9.69	(3.64

Dilution/Accretion per Share Held by Stockholder A (NAV per Share Less Investment per Share)	$ (0.19)	$ 0.03
Percentage Dilution/Accretion to Stockholder A (Dilution/Accretion per Share Divided by Investment per Share)	(1.93)%	0.32

Impact On New Investors

Investors who are not currently stockholders and who participate in an offering below NAV but whose investment per sh greater than the resulting NAV per share due to selling compensation and expenses paid by the issuer will experien immediate decrease, albeit small, in the NAV of their shares and their NAV per share compared to the price they pay for shares. Investors who are not currently stockholders and who participate in an offering below NAV per share and v investment per share is also less than the resulting NAV per share due to selling compensation and expenses paid by the being significantly less than the discount per share will experience an immediate increase in the NAV of their shares and NAV per share compared to the price they pay for their shares. These investors will experience a disproportionately g participation in our earnings and assets and their voting power than our increase in assets, potential earning power and v interests. These investors will, however, be subject to the risk that we may make additional discounted offerings in which new stockholder does not participate, in which case such new stockholder will experience dilution as described above in subsequent offerings. These investors may also experience a decline in the market price of their shares, which often refle some degree announced or potential increases and decreases in NAV per share. This decrease could be more pronounced size of the offering and level of discounts increases.

The following chart illustrates the level of dilution or accretion for new investors that would be experienced by a new inv in the same hypothetical 5%, 10% and 20% discounted offerings as described in the first chart above. The illustration is new investor who purchases the same percentage (0.10%) of the shares in the offering as Stockholder A in the prior exa held immediately prior to the offering. The prospectus supplement pursuant to which any discounted offering is mad include a chart for these examples based on the actual number of shares in such offering and the actual discount from the recently determined NAV per share, as applicable. It is not possible to predict the level of market price decline that may oc

	Prior to Sale Below NAV	Example 1 5% Offering at 5% Discount Following Sale	% Change	Example 2 10% Offering at 10% Discount Following Sale	% Change	Example 3 20% Offering at 20% Discount Following Sale	% Chang
Offering Price							
Price per Share to Public		$ 10.06		$ 9.53		$ 8.47	
Net Proceeds per Share to Issuer		$ 9.56		$ 9.05		$ 8.05	
Decrease/Increase to NAV							
Total Shares Outstanding	64,000,000	67,200,000	5.00 %	70,400,000	10.00 %	76,800,000	20.0
NAV per Share	$ 10.06	$ 10.04	(0.24)%	$ 9.97	(0.91)%	$ 9.72	(3.3
Dilution/Accretion to New Investor A							
Shares Held by Investor A	0	3,200		6,400		12,800	
Percentage Held by Investor A	0.00 %	0.00 %		0.01 %		0.02 %	
	$ 0	$ 32,115		$ 63,799		$ 124,476	

Total NAV Held by Investor A				
Total Investment by Investor A (At Price to Public)		$ 32,192	$ 60,995	$ 108,436
Total Dilution/Accretion to Investor A (Total NAV Less Total Investment)		$ (77)	$ 2,804	$ 16,040
NAV per Share Held by Investor A		$ 10.04	$ 9.97	$ 9.72
Investment per Share Held by Investor A	$ 0	$ 10.06	$ 9.53	$ 8.47
Dilution/Accretion per Share Held by Investor A (NAV per Share Less Investment per Share)		$ (0.02)	$ 0.44	$ 1.25
Percentage Dilution/Accretion to Investor A (Dilution/Accretion per Share Divided by Investment per Share)		(0.24)%	4.60%	14.79

DIVIDEND REINVESTMENT PLAN

We have adopted a dividend reinvestment plan that provides for reinvestment of our distributions on behalf of our stockho
unless a stockholder elects to receive cash as provided below. As a result, when our Board of Directors authorizes, ar
declare, a cash dividend, then our stockholders who have not "opted out" of our dividend reinvestment plan will have thei
dividends automatically reinvested in additional shares of our common stock, rather than receiving the cash dividends.

No action is required on the part of a registered stockholder to have their cash dividend reinvested in shares of our co
stock. A registered stockholder may elect to receive an entire dividend in cash by notifying the plan administrator an
transfer agent and registrar, in writing so that such notice is received by the plan administrator no later than the record da
dividends to stockholders. The plan administrator sets up an account for shares acquired through the plan for each stockh
who has not elected to receive dividends in cash and hold such shares in non-certificated form. Upon request by a stockh
participating in the plan, the plan administrator will, instead of crediting shares to the participant's account, issue a certi
registered in the participant's name for the number of whole shares of our common stock and a check for any fractional
Such request by a stockholder must be received three days prior to the dividend payable date in order for that dividend
paid in cash. If such request is received less than three days prior to the dividend payable date, then the dividends are reinv
and shares are repurchased for the stockholder's account; however, future dividends are paid out in cash on all balances. '
stockholders whose shares are held by a broker or other financial intermediary may receive dividends in cash by notifying
broker or other financial intermediary of their election.

We primarily use newly issued shares to implement the plan, whether our shares are trading at a premium or at a discount
asset value. However, we reserve the right to purchase shares in the open market in connection with our implementation
plan. The number of shares to be issued to a stockholder is determined by dividing the total dollar amount of the div
payable to such stockholder by the market price per share of our common stock at the close of regular trading on The NAS
Global Select Market on the valuation date for such dividend. If we use newly-issued shares to implement the pla
valuation date will not be earlier than the last day that stockholders have the right to elect to receive cash in lieu of sl
Market price per share on that date will be the closing price for such shares on The NASDAQ Global Select Market or
sale is reported for such day, at the average of their reported bid and asked prices. The number of shares of our common st
be outstanding after giving effect to payment of the dividend cannot be established until the value per share at which addi
shares will be issued has been determined and elections of our stockholders have been tabulated. Stockholders who do no
to receive dividends in shares of common stock may experience accretion to the net asset value of their shares if our shar
trading at a premium at the time we issue new shares under the plan and dilution if our shares are trading at a discoun
level of accretion or discount would depend on various factors, including the proportion of our stockholders who particip
the plan, the level of premium or discount at which our shares are trading and the amount of the dividend payabl
stockholder.

There are no brokerage charges or other charges to stockholders who participate in the plan. The plan administrator's fees
the plan are paid by us. If a participant elects by written notice to the plan administrator to have the plan administrator se
or all of the shares held by the plan administrator in the participant's account and remit the proceeds to the participant, th
administrator is authorized to deduct a $15 transaction fee plus a $0.10 per share brokerage commissions from the proceeds

Stockholders who receive dividends in the form of stock are subject to the same U.S. Federal, state and local tax consequ
as are stockholders who elect to receive their dividends in cash. A stockholder's basis for determining gain or loss upon th
of stock received in a dividend from us will be equal to the total dollar amount of the dividend payable to the stockholde
stock received in a dividend will have a new holding period for tax purposes commencing on the day following the d
which the shares are credited to the U.S. stockholder's account.

Participants may terminate their accounts under the plan by notifying the plan administrator via its webs www.amstock.com or by filling out the transaction request form located at the bottom of their statement and sending it plan administrator at American Stock Transfer & Trust Company, P.O. Box 922, Wall Street Station, New York 10269-0560 or by calling the plan administrator's Interactive Voice Response System at (888) 888-0313.

The plan may be terminated by us upon notice in writing mailed to each participant at least 30 days prior to any payable da the payment of any dividend by us. All correspondence concerning the plan should be directed to the plan administrator by at American Stock Transfer & Trust Company, 59 Maiden Lane, New York, NY 10007 or by telephone at (718) 921-8200.

Stockholders who purchased their shares through or hold their shares in the name of a broker or financial institution s consult with a representative of their broker or financial institution with respect to their participation in our div reinvestment plan. Such holders of our stock may not be identified as our registered stockholders with the plan adminis and may not automatically have their cash dividend reinvested in shares of our common stock by the administrator.

MATERIAL U.S. FEDERAL INCOME TAX CONSIDERATIONS

The following discussion is a general summary of the material U.S. Federal income tax considerations applicable to us and investment in our shares. This summary does not purport to be a complete description of the income tax considera applicable to us or our investors on such an investment. For example, we have not described tax consequences that we as to be generally known by investors or certain considerations that may be relevant to certain types of holders subject to s treatment under U.S. Federal income tax laws, including stockholders subject to the alternative minimum tax, tax-ex organizations, insurance companies, dealers in securities, pension plans and trusts, financial institutions, U.S. stockholde defined below) whose functional currency is not the U.S. dollar, persons who mark-to-market our shares and persons who our shares as part of a "straddle," "hedge" or "conversion" transaction. This summary assumes that investors hold our co stock as capital assets (within the meaning of the Code). The discussion is based upon the Code, Treasury regulation administrative and judicial interpretations, each as of the date of this prospectus and all of which are subject to change, po retroactively, which could affect the continuing validity of this discussion. We have not sought and will not seek any from the Internal Revenue Service, or the IRS, regarding this offering. This summary does not discuss any aspects of U.S. or gift tax or foreign, state or local tax. It does not discuss the special treatment under U.S. Federal income tax laws that result if we invested in tax-exempt securities or certain other investment assets.

A "U.S. stockholder" is a beneficial owner of shares of our common stock that is for U.S. Federal income tax purposes:

- a citizen or individual resident of the United States;
- a corporation, or other entity treated as a corporation for U.S. Federal income tax purposes, created or organi in or under the laws of the United States or any state thereof or the District of Columbia;
- an estate, the income of which is subject to U.S. Federal income taxation regardless of its source; or
- a trust if (1) a U.S. court is able to exercise primary supervision over the administration of such trust and one more U.S. persons have the authority to control all substantial decisions of the trust or (2) it has a valid electi

in place to be treated as a U.S. person.

A "Non-U.S. stockholder" is a beneficial owner of shares of our common stock that is not a partnership and is not a
stockholder.

If a partnership (including an entity treated as a partnership for U.S. Federal income tax purposes) holds shares of our co stock, the tax treatment of a partner in the partnership will generally depend upon the status of the partner and the activit the partnership. A prospective stockholder that is a partner of a partnership holding shares of our common stock should c its tax advisors with respect to the purchase, ownership and disposition of shares of our common stock.

Tax matters are very complicated and the tax consequences to an investor of an investment in our shares will depend facts of his, her or its particular situation. We encourage investors to consult their own tax advisors regarding the sp consequences of such an investment, including tax reporting requirements, the applicability of U.S. Federal, state, loca foreign tax laws, eligibility for the benefits of any applicable tax treaty and the effect of any possible changes in the tax law

Election To Be Taxed As A RIC

As a business development company, we have qualified and elected to be treated as a RIC under Subchapter M of the Co a RIC, we generally are not subject to corporate-level U.S. Federal income taxes on any ordinary income or capital gai we distribute to our stockholders as dividends. To qualify as a RIC, we must, among other things, meet ce source-of-income and asset diversification requirements (as described below). In addition, to obtain RIC tax treatment, we distribute to our stockholders, for each taxable year, at least 90% of our "investment company taxable income," wh generally our ordinary income plus the excess of realized net short-term capital gains over realized net long-term capital l or the Annual Distribution Requirement.

Taxation As A RIC

Provided that we qualify as a RIC and satisfy the Annual Distribution Requirement, we will not be subject to U.S. Fe income tax on the portion of our investment company taxable income and net capital gain (which we define as net long capital gains in excess of net short-term capital losses) we timely distribute to stockholders. We will be subject to U.S. F income tax at the regular corporate rates on any income or capital gain not distributed (or deemed distributed) t stockholders.

We will be subject to a 4% non-deductible U.S. Federal excise tax on certain undistributed income of RICs unless we dist in a timely manner an amount at least equal to the sum of (1) 98% of our ordinary income for each calendar year, (2) 98% capital gain net income for the one-year period ending October 31 in that calendar year and (3) any income realized, b distributed, in preceding years.

In December 2008, our Board of Directors elected to retain excess profits generated in the quarter ended September 30, and pay a 4% excise tax on such retained earnings. We paid $533,000 for the excise tax with the filing of our tax retu March 2009.

In order to qualify as a RIC for U.S. Federal income tax purposes, we must, among other things:

·

qualify to be treated as a business development company or be registered as a management investment comp
under the 1940 Act at all times during each taxable year;

- derive in each taxable year at least 90% of our gross income from dividends, interest, payments with respect
certain securities loans, gains from the sale or other disposition of stock or other securities or currencies or ot
income derived with respect to our business of investing in such stock, securities or currencies and net incom
derived from an interest in a "qualified publicly traded partnership" (as defined in the Code) or the 90% Inco
Test; and

- diversify our holdings so that at the end of each quarter of the taxable year:

- at least 50% of the value of our assets consists of cash, cash equivalents, U.S. Government securities, securiti
of other RICs, and other securities if such other securities of any one issuer do not represent more than 5% of
value of our assets or more than 10% of the outstanding voting securities of the issuer (which for these purpo
includes the equity securities of a "qualified publicly traded partnership"); and
- no more than 25% of the value of our assets is invested in the securities, other than U.S. Government securiti
or securities of other RICs, (i) of one issuer (ii) of two or more issuers that are controlled, as determined unde
applicable tax rules, by us and that are engaged in the same or similar or related trades or businesses or (iii) o
one or more "qualified publicly traded partnerships," or the diversification tests.

To the extent that we invest in entities treated as partnerships for U.S. Federal income tax purposes (other than a "qua
publicly traded partnership"), we generally must include the items of gross income derived by the partnerships for purpo
the 90% Income Test, and the income that is derived from a partnership (other than a "qualified publicly traded partners
will be treated as qualifying income for purposes of the 90% Income Test only to the extent that such income is attributa
items of income of the partnership which would be qualifying income if realized by us directly. In addition, we generally
take into account our proportionate share of the assets held by partnerships (other than a "qualified publicly traded partner
in which we are a partner for purposes of the diversification tests.

In order to meet the 90% Income Test, we may establish one or more special purpose corporations to hold assets from whi
do not anticipate earning dividend, interest or other qualifying income under the 90% Income Test. Any such special pu
corporation would generally be subject to U.S. Federal income tax, and could result in a reduced after-tax yield on the port
our assets held there.

We may be required to recognize taxable income in circumstances in which we do not receive cash. For example, if we
debt obligations that are treated under applicable tax rules as having original issue discount (such as debt instruments
payment-in-kind interest or, in certain cases, increasing interest rates or issued with warrants), we must include in income
year a portion of the original issue discount that accrues over the life of the obligation, regardless of whether cash represe
such income is received by us in the same taxable year. Because any original issue discount accrued will be included i
investment company taxable income for the year of accrual, we may be required to make a distribution to our stockhold
order to satisfy the Annual Distribution Requirement, even though we will not have received any corresponding cash amou

Gain or loss realized by us from warrants acquired by us as well as any loss attributable to the lapse of such warrants gen
will be treated as capital gain or loss. Such gain or loss generally will be long-term or short-term, depending on how lon
held a particular warrant.

Although we do not presently expect to do so, we are authorized to borrow funds and to sell assets in order to sa
distribution requirements. However, under the 1940 Act, we are not permitted to make distributions to our stockholders
our debt obligations and other senior securities are outstanding unless certain "asset coverage" tests are met. See "Regul
Senior Securities." Moreover, our ability to dispose of assets to meet our distribution requirements may be limited by (
illiquid nature of our portfolio and/or (2) other requirements relating to our status as a RIC, including the diversification te
we dispose of assets in order to meet the Annual Distribution Requirement or to avoid the excise tax, we may make
dispositions at times that, from an investment standpoint, are not advantageous.

If we fail to satisfy the Annual Distribution Requirement or otherwise fail to qualify as a RIC in any taxable year, we w
subject to tax in that year on all of our taxable income, regardless of whether we make any distributions to our stockholde
that case, all of such income will be subject to corporate-level U.S. Federal

income tax, reducing the amount available to be distributed to our stockholders. See "Failure To Obtain RIC Tax Treatmen

As a regulated investment company, we are not allowed to carry forward or carry back a net operating loss for purpo computing our investment company taxable income in other taxable years. Certain of our investment practices may be subj special and complex U.S. Federal income tax provisions that may, among other things, (i) disallow, suspend or otherwise the allowance of certain losses or deductions, (ii) convert lower taxed long-term capital gain and qualified dividend incom higher taxed short-term capital gain or ordinary income, (iii) convert an ordinary loss or a deduction into a capital los deductibility of which is more limited), (iv) cause us to recognize income or gain without a corresponding receipt of cas adversely affect the time as to when a purchase or sale of stock or securities is deemed to occur, (vi) adversely alt characterization of certain complex financial transactions, and (vii) produce income that will not be qualifying incon purposes of the 90% Income Test. We will monitor our transactions and may make certain tax elections in order to mitiga effect of these provisions.

As described above, to the extent that we invest in equity securities of entities that are treated as partnerships for U.S. Fe income tax purposes, the effect of such investments for purposes of the 90% Income Test and the diversification test depend on whether or not the partnership is a "qualified publicly traded partnership" (as defined in the Code). If the partne is a "qualified publicly traded partnership," the net income derived from such investments will be qualifying incon purposes of the 90% Income Test and will be "securities" for purposes of the diversification tests. If the partnership, howe not treated as a "qualified publicly traded partnership," then the consequences of an investment in the partnership will de upon the amount and type of income and assets of the partnership allocable to us. The income derived from such invest may not be qualifying income for purposes of the 90% Income Test and, therefore, could adversely affect our qualificatio RIC. We intend to monitor our investments in equity securities of entities that are treated as partnerships for U.S. Fe income tax purposes to prevent our disqualification as a RIC.

We may invest in preferred securities or other securities the U.S. Federal income tax treatment of which may not be cl may be subject to recharacterization by the IRS. To the extent the tax treatment of such securities or the income from securities differs from the expected tax treatment, it could affect the timing or character of income recognized, requiring purchase or sell securities, or otherwise change our portfolio, in order to comply with the tax rules applicable to RICs und Code.

Taxation Of U.S. Stockholders

Distributions by us generally are taxable to U.S. stockholders as ordinary income or capital gains. Distributions o "investment company taxable income" (which is, generally, our ordinary income plus realized net short-term capital ga excess of realized net long-term capital losses) will be taxable as ordinary income to U.S. stockholders to the extent o current or accumulated earnings and profits, whether paid in cash or reinvested in additional common stock. For taxable beginning on or before December 31, 2010, to the extent such distributions paid by us to noncorporate stockholders (incl individuals) are attributable to dividends from U.S. corporations and certain qualified foreign corporations, such distribu generally will be eligible for taxation at rates applicable to long term capital gains (currently a maximum tax rate of provided that we properly designate such distribution as derived from "qualified dividend income" and certain holding p and other requirements are satisfied. In this regard, it is not anticipated that a significant portion of distributions paid by u be attributable to qualified dividends and, therefore, generally will not qualify for the long term capital gains. Distributio our net capital gains (which is generally our realized net long-term capital gains in excess of realized net short-term c losses) properly designated by us as "capital gain dividends" will be taxable to a U.S. stockholder as long-term capital (currently at a maximum rate of 15% in the case of individuals, trusts or estates), regardless of the U.S. stockholder's ho period for his, her or its common stock and regardless of whether paid in cash or reinvested in additional common s Distributions in excess of our current and accumulated earnings and profits first will reduce a U.S. stockholder's adjust basis in such stockholder's common stock and, after the adjusted basis is reduced to zero, will constitute capital gains to U.S. stockholder.

Although we currently intend to distribute any long-term capital gains at least annually, we may in the future decide to some or all of our long-term capital gains, but designate the retained amount as a "deemed distribution." In that case, a other consequences, we will pay tax on the retained amount, each U.S. stockholder will be required to include his, her proportionate share of the deemed distribution in income as if it had been actually distributed to the U.S. stockholder, ar U.S. stockholder will be entitled to claim a credit equal to his, her or its allocable share of the tax paid thereon by us amount of the deemed distribution net of such tax will be added to the U.S. stockholder's tax basis for his, her or its cor stock. Since we expect to pay tax on any retained capital gains at our regular corporate tax rate, and since that rate is in e of the maximum rate currently payable by individuals on long-term capital gains, the amount of tax that individual stockho will be treated as having paid and for which they will receive a credit will exceed the tax they owe on the retained net c gain. Such excess generally may be claimed as a credit against the U.S. stockholder's other U.S. Federal income tax oblig or may be refunded to the extent it exceeds a stockholder's liability for U.S. Federal income tax. A stockholder that subject to U.S. Federal income tax or otherwise required to file a U.S. Federal income tax return would be required to file a Federal income tax return on the appropriate form in order to claim a refund for the taxes we paid. In order to utilize the de distribution approach, we must provide written notice to our stockholders prior to the expiration of 60 days after the close relevant taxable year. We cannot treat any of our investment company taxable income as a "deemed distribution."

For purposes of determining (1) whether the Annual Distribution Requirement is satisfied for any year and (2) the amo capital gain dividends paid for that year, we may, under certain circumstances, elect to treat a dividend that is paid durin following taxable year as if it had been paid during the taxable year in question. If we make such an election, the stockholder will still be treated as receiving the dividend in the taxable year in which the distribution is made. Howeve dividend declared by us in October, November or December of any calendar year, payable to stockholders of record specified date in any such month and actually paid during January of the following year, will be treated as if it had received by our U.S. stockholders on December 31 of the year in which the dividend was declared.

If an investor purchases shares of our common stock shortly before the record date of a distribution, the price of the share include the value of the distribution and the investor will be subject to tax on the distribution even though it represents a of his, her or its investment.

A U.S. stockholder generally will recognize taxable gain or loss if the stockholder sells or otherwise disposes of his, her shares of our common stock. Any gain arising from such sale or disposition generally will be treated as long-term capital g loss if the stockholder has held his, her or its shares for more than one year. Otherwise, it would be classified as short capital gain or loss. However, any capital loss arising from the sale or disposition of shares of our common stock held f months or less will be treated as long-term capital loss to the extent of the amount of capital gain dividends receiv undistributed capital gain deemed received, with respect to such shares. In addition, all or a portion of any loss recognized a disposition of shares of our common stock may be disallowed if other substantially identical shares are purchased (wh through reinvestment of distributions or otherwise) within 30 days before or after the disposition. The ability to othe deduct capital losses may be subject to other limitations under the code.

In general, individual U.S. stockholders currently are subject to a maximum U.S. Federal income tax rate of 15% on the capital gain, or the excess of realized net long-term capital gain over realized net short-term capital loss for a taxable including a long-term capital gain derived from an investment in our shares. Such rate is lower than the maximum ra ordinary income currently payable by individuals. Corporate U.S. stockholders currently are subject to U.S. Federal incor on net capital gain at the maximum 35% rate also applied to ordinary income. Noncorporate stockholders with net capital for a year (which we define as capital losses in excess of capital gains) generally may deduct up to $3,000 of such losses a

their ordinary income each year; any net capital losses of a noncorporate stockholder in excess of $3,000 generally m
carried forward and used in subsequent years as provided in the Code. Corporate stockholders generally may not deduct ar
capital losses for a year, but may carry back such losses for three years or carry forward such losses for five years.

We will send to each of our U.S. stockholders, as promptly as possible after the end of each calendar year, a notice detaili a per share and per distribution basis, the amounts includible in such U.S. stockholder's taxable income for such year as ord income and as long-term capital gain. In addition, the U.S. Federal tax status of each year's distributions generally w reported to the IRS (including the amount of dividends, if any, eligible for the 15% maximum rate). Distributions may a subject to additional state, local and foreign taxes depending on a U.S. stockholder's particular situation. Dividends distri by us generally will not be eligible for the dividends-received deduction or the preferential rate applicable to quali dividends.

We may be required to withhold U.S. Federal income tax, or backup withholding, currently at a rate of 28% (until Janu 2011 when a higher rate of 31% will apply absent Congressional action) from all taxable distributions to any noncorporat stockholder (1) who fails to furnish us with a correct taxpayer identification number or a certificate that such stockhol exempt from backup withholding, or (2) with respect to whom the IRS notifies us that such stockholder has failed to pro report certain interest and dividend income to the IRS and to respond to notices to that effect. An individual's tax identification number is his or her social security number. Backup withholding is not an additional tax, and any an withheld may be refunded or credited against the U.S. stockholder's U.S. Federal income tax liability, provided that p information is timely provided to the IRS.

Taxation Of Non-U.S. Stockholders

Whether an investment in the shares is appropriate for a Non-U.S. stockholder will depend upon that person's part circumstances. An investment in the shares by a Non-U.S. stockholder may have adverse tax consequences. Non stockholders should consult their tax advisers before investing in our common stock.

Distributions of our "investment company taxable income" to Non-U.S. stockholders that are not "effectively connected" U.S. trade or business carried on by the Non-U.S. stockholder, will generally be subject to withholding of U.S. Federal in tax at a rate of 30% (or lower rate provided by an applicable treaty) to the extent of our current and accumulated earning profits. However, effective for taxable years beginning before January 1, 2010, we generally will not be required to wit any amounts with respect to distributions of (i) U.S.-source interest income that would not have been subject to withhold U.S. Federal income tax if they had been earned directly by a Non-U.S. stockholder, and (ii) net short-term capital ga excess of net long-term capital losses that would not have been subject to withholding of U.S. Federal income tax if the been earned directly by a Non-U.S. stockholder, in each case only to the extent that such distributions are properly desig by us as "interest-related dividends" or "short-term capital gain dividends," as the case may be, and certain other require are met.

Actual or deemed distributions of our net capital gains to a Non-U.S. stockholder, and gains realized by a Non-U.S. stockh upon the sale of our common stock, that are not effectively connected with a U.S. trade or business carried on by the Nor stockholder, will generally not be subject to U.S. Federal withholding tax and generally will not be subject to U.S. Fe income tax unless the Non-U.S. stockholder is a nonresident alien individual and is physically present in the United Stat more than 182 days during the taxable year and meets certain other requirements. However, withholding of U.S. Federal in tax at a rate of 30% on capital gains of nonresident alien individuals who are physically present in the United States for than the 182 day period only applies in exceptional cases because any individual present in the United States for more tha days during the taxable year is generally treated as a resident for U.S. income tax purposes; in that case, he or she wou subject to U.S. income tax on his or her worldwide income at the graduated rates applicable to U.S. citizens, rather than the

U.S. Federal withholding tax.

If we distribute our net capital gains in the form of deemed rather than actual distributions (which we may do in the futu
Non-U.S. stockholder will be entitled to a U.S. Federal income tax credit or tax refund equal to the stockholder's allocable
of the tax we pay on the capital gains deemed to have been distributed. In order to obtain the refund, the Non-U.S. stockh
must obtain a U.S. taxpayer identification number and file a U.S.

Federal income tax return even if the Non-U.S. stockholder would not otherwise be required to obtain a U.S. tax identification number or file a U.S. Federal income tax return. Accordingly, investment in the shares may not be appropria a Non-U.S. stockholder.

Distributions of our "investment company taxable income" and net capital gains (including deemed distributions) to Nor stockholders, and gains realized by Non-U.S. stockholders upon the sale of our common stock that is "effectively conne with a U.S. trade or business carried on by the Non-U.S. stockholder (or if an income tax treaty applies, attributabl "permanent establishment" in the United States), will be subject to U.S. Federal income tax at the graduated rates applica U.S. citizens, residents and domestic corporations. Corporate Non-U.S. stockholders may also be subject to an additional b profits tax at a rate of 30% imposed by the Code (or lower rate provided by an applicable treaty). In the case of a non-corp Non-U.S. stockholder, we may be required to withhold U.S. Federal income tax from distributions that are otherwise ex from withholding tax (or taxable at a reduced rate) unless the Non-U.S. stockholder certifies his or her foreign status penalties of perjury or otherwise establishes an exemption.

The tax consequences to a Non-U.S. stockholder entitled to claim the benefits of an applicable tax treaty may differ from described herein. Non-U.S. stockholders are advised to consult their own tax advisers with respect to the particul consequences to them of an investment in our shares.

A Non-U.S. stockholder who is a nonresident alien individual may be subject to information reporting and backup withho of U.S. Federal income tax on dividends unless the Non-U.S. stockholder provides us or the dividend paying agent with a Form W-8BEN (or an acceptable substitute form) or otherwise meets documentary evidence requirements for establishing is a Non-U.S. stockholder or otherwise establishes an exemption from backup withholding.

Non-U.S. persons should consult their own tax advisors with respect to the U.S. Federal income tax and withholding tax state, local and foreign tax consequences of an investment in the shares.

Failure To Obtain RIC Tax Treatment

If we were unable to obtain tax treatment as a RIC, we would be subject to tax on all of our taxable income at regular cor rates. We would not be able to deduct distributions to stockholders, nor would they be required to be made. Distributions generally be taxable to our stockholders as ordinary dividend income (currently eligible for the 15% maximum rate) extent of our current and accumulated earnings and profits. Subject to certain limitations under the Code, corporate distrib would be eligible for the dividends-received deduction.

Distributions in excess of our current and accumulated earnings and profits would be treated first as a return of capital extent of the stockholder's tax basis, and any remaining distributions would be treated as a capital gain.

The discussion set forth herein does not constitute tax advice, and potential investors should consult their own tax adv concerning the tax considerations relevant to their particular situation.

DESCRIPTION OF OUR CAPITAL STOCK

The following description is based on relevant portions of the Maryland General Corporation Law and on our charte
bylaws. This summary is not necessarily complete, and we refer you to the Maryland General Corporation Law and our c
and bylaws for a more detailed description of the provisions summarized below.

Capital Stock

Our authorized capital stock consists of 100,000,000 shares of stock, par value $0.001 per share, all of which is ini classified as common stock. Our common stock is traded on The NASDAQ Global Select Market under the symbol "PS There are no outstanding options or warrants to purchase our stock. No stock has been authorized for issuance under any c compensation plans. Under Maryland law, our stockholders generally are not personally liable for our debts or obligations.

Under our charter, our Board of Directors is authorized to classify and reclassify any unissued shares of stock into other c or series of stock, and to authorize the issuance of such shares, without obtaining stockholder approval. As permitted b Maryland General Corporation Law, our charter provides that the Board of Directors, without any action by our stockho may amend the charter from time to time to increase or decrease the aggregate number of shares of stock or the numb shares of stock of any class or series that we have authority to issue.

The below table sets forth each class of our outstanding securities as of February 25, 2010:

(1) Title of Class	(2) Amount Authorized	(3) Amount Held by the Company or for its Account	(4) Amoun Outstand Exclusiv Amoun Showr Under(
Common Stock	100,000,000	0	63,586,7

Common Stock

All shares of our common stock have equal rights as to earnings, assets, dividends and voting and, when they are issued, w duly authorized, validly issued, fully paid and nonassessable. Distributions may be paid to the holders of our common sto as and when authorized by our Board of Directors and declared by us out of funds legally available therefor. Shares c common stock have no preemptive, conversion or redemption rights and are freely transferable, except where their trans restricted by U.S. Federal and state securities laws or by contract. In the event of a liquidation, dissolution or winding up each share of our common stock would be entitled to share ratably in all of our assets that are legally available for distrib after we pay all debts and other liabilities and subject to any preferential rights of holders of our preferred stock, if any pre stock is outstanding at such time. Each share of our common stock is entitled to one vote on all matters submitted to a v stockholders, including the election of directors. Except as provided with respect to any other class or series of stoc holders of our common stock will possess exclusive voting power. There is no cumulative voting in the election of dire which means that prior to the issuance of preferred stock holders of a majority of the outstanding shares of common stoc elect all of our directors, and holders of less than a majority of such shares will be unable to elect any director.

Preferred Stock

Our charter authorizes our Board of Directors to classify and reclassify any unissued shares of stock into other classes or of stock, including preferred stock. Prior to issuance of shares of each class or series, the Board of Directors is requir Maryland law and by our charter to set the terms, preferences, conversion or other rights, voting powers, restrictions, limit as to dividends or other distributions, qualifications and terms or conditions of redemption for each class or series. Thu

Board of Directors could authorize the issuance of shares of preferred stock with terms and conditions which could hav
effect of delaying, deferring or preventing a transaction or a change in control that might involve a premium price for hold
our common stock or otherwise be in their best interest. You should note, however, that any issuance of preferred stock
comply with the requirements of the 1940 Act. The 1940 Act requires, among other things, that (1) immediately after iss
and before any dividend or other distribution (other than in shares of stock) is made with respect to our common stoc
before any purchase of common stock is made, such preferred stock together with all other senior securities

---

must not exceed an amount equal to 50% of our total assets after deducting the amount of such dividend, distributi
purchase price, as the case may be, and (2) the holders of shares of preferred stock, if any are issued, must be entitled as a
to elect two directors at all times and to elect a majority of the directors if dividends on such preferred stock become in a
by two years or more until all arrears are cured. Certain matters under the 1940 Act require the separate vote of the hold
any issued and outstanding preferred stock. For example, holders of preferred stock would vote separately from the hold
common stock on a proposal to operate other than as an investment company. We believe that the availability for issuar
preferred stock will provide us with increased flexibility in structuring future financings and acquisitions.

Limitation On Liability Of Directors And Officers; Indemnification And Advance Of Expenses

Maryland law permits a Maryland corporation to include in its charter a provision limiting the liability of its director
officers to the corporation and its stockholders for money damages except for liability resulting from (a) actual receipt
improper benefit or profit in money, property or services or (b) active and deliberate dishonesty established by a final judg
as being material to the cause of action. Our charter contains such a provision which eliminates directors' and officers' lia
to the maximum extent permitted by Maryland law, subject to the requirements of the 1940 Act.

Our charter authorizes us, to the maximum extent permitted by Maryland law and subject to the requirements of the 1940
to obligate ourselves to indemnify any present or former director or officer or any individual who, while serving as a direc
officer and at our request, serves or has served another corporation, real estate investment trust, partnership, joint venture,
employee benefit plan or other enterprise as a director, officer, partner or trustee, from and against any claim or liabil
which that person may become subject or which that person may incur by reason of his or her service in any such capacit
to pay or reimburse their reasonable expenses in advance of final disposition of a proceeding. Our bylaws obligate us,
maximum extent permitted by Maryland law and subject to the requirements of the 1940 Act, to indemnify any prese
former director or officer or any individual who, while serving as a director or officer and at our request, serves or has s
another corporation, real estate investment trust, partnership, joint venture, trust, employee benefit plan or other enterpris
director, officer, partner or trustee and who is made, or threatened to be made, a party to the proceeding by reason of his
service in any such capacity from and against any claim or liability to which that person may become subject or whic
person may incur by reason of his or her service in any such capacity and to pay or reimburse their reasonable expen
advance of final disposition of a proceeding. The charter and bylaws also permit us to indemnify and advance expenses t
person who served a predecessor of us in any of the capacities described above and any of our employees or agents o
employees or agents of our predecessor. In accordance with the 1940 Act, we will not indemnify any person for any liabi
which such person would be subject by reason of such person's willful misfeasance, bad faith, gross negligence or rec
disregard of the duties involved in the conduct of his or her office.

Maryland law requires a corporation (unless its charter provides otherwise, which our charter does not) to indemnify a di
or officer who has been successful, on the merits or otherwise, in the defense of any proceeding to which he or she is ma
threatened to be made, a party by reason of his or her service in that capacity. Maryland law permits a corporation to inde
its present and former directors and officers, among others, against judgments, penalties, fines, settlements and reaso
expenses actually incurred by them in connection with any proceeding to which they may be made, or threatened to be m
party by reason of their service in those or other capacities unless it is established that (a) the act or omission of the direc
officer was material to the matter giving rise to the proceeding and (1) was committed in bad faith or (2) was the result of
and deliberate dishonesty, (b) the director or officer actually received an improper personal benefit in money, prope
services or (c) in the case of any criminal proceeding, the director or officer had reasonable cause to believe that the
omission was unlawful. However, under Maryland law, a Maryland corporation may not indemnify for an adverse judgmer
suit by or in the right of the corporation or for a judgment of liability on the basis that a personal benefit was impro

received, unless in either case a court orders indemnification, and then only for expenses. In addition, Maryland law per corporation to advance reasonable expenses to a director or officer upon the corporation's receipt of (a) a written affirmati the director or officer of his or her good faith belief that he or she has met the standard of conduct necessary for indemnifi by the corporation and (b) a written undertaking by him or her or on his or her behalf to repay the amount paid or reimbursed by the corporation if it is ultimately determine the standard of conduct was not met.

Our insurance policy does not currently provide coverage for claims, liabilities and expenses that may arise out of activitie a present or former director or officer of us has performed for another entity at our request. There is no assurance tha entities will in fact carry such insurance. However, we note that we do not expect to request our present or former direct officers to serve another entity as a director, officer, partner or trustee unless we can obtain insurance providing covera such persons for any claims, liabilities or expenses that may arise out of their activities while serving in such capacities.

Provisions Of The Maryland General Corporation Law And Our Charter And Bylaws

Anti-takeover Effect

The Maryland General Corporation Law and our charter and bylaws contain provisions that could make it more difficul potential acquiror to acquire us by means of a tender offer, proxy contest or otherwise. These provisions are expec discourage certain coercive takeover practices and inadequate takeover bids and to encourage persons seeking to acquire c of us to negotiate first with our Board of Directors. These provisions could have the effect of depriving stockholders opportunity to sell their shares at a premium over prevailing market prices by discouraging a third party from seeking to control of us. We believe that the benefits of these provisions outweigh the potential disadvantages of discouraging any acquisition proposals because, among other things, the negotiation of such proposals may improve their terms.

Control Share Acquisitions

The Maryland General Corporation Law under the Control Share Act provides that control shares of a Maryland corpo acquired in a control share acquisition have no voting rights except to the extent approved by a vote of two-thirds of the entitled to be cast on the matter. Shares owned by the acquiror, by officers or by directors who are employees of the corpo are excluded from shares entitled to vote on the matter. Control shares are voting shares of stock which, if aggregated w other shares of stock owned by the acquiror or in respect of which the acquiror is able to exercise or direct the exercise of power (except solely by virtue of a revocable proxy), would entitle the acquiror to exercise voting power in electing dir within one of the following ranges of voting power:

- one-tenth or more but less than one-third,
- one-third or more but less than a majority, or
- a majority or more of all voting power.

The requisite stockholder approval must be obtained each time an acquiror crosses one of the thresholds of voting pow forth above. Control shares do not include shares the acquiring person is then entitled to vote as a result of having previ obtained stockholder approval. A control share acquisition means the acquisition of control shares, subject to certain excep

A person who has made or proposes to make a control share acquisition may compel the Board of Directors of the corpo to call a special meeting of stockholders to be held within 50 days of demand to consider the voting rights of the shares right to compel the calling of a special meeting is subject to the satisfaction of certain conditions, including an undertak

pay the expenses of the meeting. If no request for a meeting is made, the corporation may itself present the question a
stockholders meeting.

If voting rights are not approved at the meeting or if the acquiring person does not deliver an acquiring person statem
required by the statute, then the corporation may repurchase for fair value any or all of the control shares, except tho
which voting rights have previously been approved. The right of the corporation to repurchase control shares is subj
certain conditions and limitations, including, as provided in our bylaws, compliance with the 1940 Act. Fair value is detern
without regard to the absence of voting rights for the control shares, as of the date of the last control share acquisition b
acquiror or of any meeting of stockholders at which the voting rights of the shares are considered and not approved. If v
rights for control shares are approved at a stockholders meeting and the acquiror becomes entitled to vote a majority
shares entitled to vote, all other stockholders may exercise appraisal rights. The fair value of the shares as determine
purposes of appraisal rights may not be less than the highest price per share paid by the acquiror in the control share acquis

The Control Share Act does not apply (a) to shares acquired in a merger, consolidation or share exchange if the corporatio
party to the transaction or (b) to acquisitions approved or exempted by the charter or bylaws of the corporation.

Our bylaws contain a provision exempting from the Control Share Act any and all acquisitions by any person of our sha
stock. There can be no assurance that such provision will not be amended or eliminated at any time in the future. Howeve
will notify the Division of Investment Management at the SEC prior to amending our bylaws to be subject to the Control
Act and will make such amendment only if the Board of Directors determines that it would be in our best interests.

Business Combinations

Under Maryland law, "business combinations" between a Maryland corporation and an interested stockholder or an affili
an interested stockholder are prohibited for five years after the most recent date on which the interested stockholder becon
interested stockholder. These business combinations include a merger, consolidation, share exchange or, in circumst
specified in the statute, an asset transfer or issuance or reclassification of equity securities. An interested stockholder is de
as:

- any person who beneficially owns 10% or more of the voting power of the corporation's shares; or
- an affiliate or associate of the corporation who, at any time within the two-year period prior to the date in question, was the beneficial owner of 10% or more of the voting power of the then outstanding voting stock o the corporation.

A person is not an interested stockholder under this statute if the Board of Directors approved in advance the transacti
which he otherwise would have become an interested stockholder. However, in approving a transaction, the Board of Dir
may provide that its approval is subject to compliance, at or after the time of approval, with any terms and condi
determined by the Board of Directors.

After the five-year prohibition, any business combination between the Maryland corporation and an interested stockh
generally must be recommended by the Board of Directors of the corporation and approved by the affirmative vote of at lea

- 80% of the votes entitled to be cast by holders of outstanding shares of voting stock of the corporation; and
-

two-thirds of the votes entitled to be cast by holders of voting stock of the corporation other than shares held
the interested stockholder with whom or with whose affiliate the business combination is to be effected or he
by an affiliate or associate of the interested stockholder.

These super-majority vote requirements do not apply if the corporation's common stockholders receive a minimum pri
defined under Maryland law, for their shares in the form of cash or other consideration in the same form as previously pa
the interested stockholder for its shares.

The statute permits various exemptions from its provisions, including business combinations that are exempted by the Bo
Directors before the time that the interested stockholder becomes an interested stockholder. Our Board of Directors has ad
a resolution that any business combination between us and any other person is exempted from the provisions of the Bus
Combination Act, provided that the business combination is first approved by the Board of Directors, including a majority
directors who are not interested persons as defined in the 1940 Act. This resolution, however, may be altered or repea
whole or in part at any time. If this resolution is repealed, or the Board of Directors does not otherwise approve a bus
combination, the statute may discourage others from trying to acquire control of us and increase the difficulty of consumn
any offer.

Conflict with 1940 Act

Our bylaws provide that, if and to the extent that any provision of the Maryland General Corporation Law, including the C
Share Act (if we amend our bylaws to be subject to such Act) and the Business Combination Act, or any provision o
charter or bylaws conflicts with any provision of the 1940 Act, the applicable provision of the 1940 Act will control.

Classified Board of Directors

Our Board of Directors is divided into three classes of directors serving staggered three-year terms. The current terms
first, second and third classes will expire in 2011, 2012 and 2010 respectively, and in each case, until their successors are
elected and qualify. Each year one class of directors will be elected to the Board of Directors by the stockholders. A clas
board may render a change in control of us or removal of our incumbent management more difficult. We believe, howeve
the longer time required to elect a majority of a classified Board of Directors will help to ensure the continuity and stabi
our management and policies.

Election of Directors

Our charter and bylaws provide that the affirmative vote of the holders of a majority of the outstanding shares of stock en
to vote in the election of directors will be required to elect a director. Under the charter, our Board of Directors may amen
bylaws to alter the vote required to elect directors.

Number of Directors; Vacancies; Removal

Our charter provides that the number of directors will be set only by the Board of Directors in accordance with our bylaws
bylaws provide that a majority of our entire Board of Directors may at any time increase or decrease the number of dire
However, unless our bylaws are amended, the number of directors may never be less than three nor more than eight. Our c
provides that, at such time as we have three independent directors and our common stock is registered under the Exchang
of 1934, as amended, or the Exchange Act, we elect to be subject to the provision of Subtitle 8 of Title 3 of the Mar
General Corporation Law regarding the filling of vacancies on the Board of Directors. Accordingly, at such time, except a

be provided by the Board of Directors in setting the terms of any class or series of preferred stock, any and all vacancies o
Board of Directors may be filled only by the affirmative vote of a majority of the remaining directors in office, even
remaining directors do not constitute a quorum, and any director elected to fill a vacancy will serve for the remainder of th
term of the directorship in which the vacancy occurred and until a successor is elected and qualifies, subject to any appli
requirements of the 1940 Act.

Our charter provides that a director may be removed only for cause, as defined in our charter, and then only by the affirm
vote of at least two-thirds of the votes entitled to be cast in the election of directors.

Action by Stockholders

The Maryland General Corporation Law provides that stockholder action can be taken only at an annual or special meet
stockholders or (unless the charter provides for stockholder action by less than unanimous written consent, which our c
does not) by unanimous written consent in lieu of a meeting. These provisions, combined with the requirements of our b
regarding the calling of a stockholder-requested special meeting of stockholders discussed below, may have the eff
delaying consideration of a stockholder proposal until the next annual meeting.

Advance Notice Provisions for Stockholder Nominations and Stockholder Proposals

Our bylaws provide that with respect to an annual meeting of stockholders, nominations of persons for election to the Bo
Directors and the proposal of business to be considered by stockholders may be made only (1) pursuant to our notice
meeting, (2) by the Board of Directors or (3) by a stockholder who is entitled to vote at the meeting and who has complie
the advance notice procedures of the bylaws. With respect to special meetings of stockholders, only the business specified
notice of the meeting may be brought before the meeting. Nominations of persons for election to the Board of Director
special meeting may be made only (1) pursuant to our notice of the meeting, (2) by the Board of Directors or (3) provide
the Board of Directors has determined that directors will be elected at the meeting, by a stockholder who is entitled to v
the meeting and who has complied with the advance notice provisions of the bylaws.

The purpose of requiring stockholders to give us advance notice of nominations and other business is to afford our Bo
Directors a meaningful opportunity to consider the qualifications of the proposed nominees and the advisability of any
proposed business and, to the extent deemed necessary or desirable by our Board of Directors, to inform stockholders and
recommendations about such qualifications or business, as well as to provide a more orderly procedure for conducting me
of stockholders. Although our bylaws do not give our Board of Directors any power to disapprove stockholder nominatio
the election of directors or proposals recommending certain action, they may have the effect of precluding a contest f
election of directors or the consideration of stockholder proposals if proper procedures are not followed and of discourag
deterring a third party from conducting a solicitation of proxies to elect its own slate of directors or to approve its own pro
without regard to whether consideration of such nominees or proposals might be harmful or beneficial to us an
stockholders.

Calling of Special Meetings of Stockholders

Our bylaws provide that special meetings of stockholders may be called by our Board of Directors and certain of our off
Additionally, our bylaws provide that, subject to the satisfaction of certain procedural and informational requirements b
stockholders requesting the meeting, a special meeting of stockholders will be called by the secretary of the corporation
the written request of stockholders entitled to cast not less than a majority of all the votes entitled to be cast at such meeting

Approval of Extraordinary Corporate Action; Amendment of Charter and Bylaws

Under Maryland law, a Maryland corporation generally cannot dissolve, amend its charter, merge, sell all or substantially its assets, engage in a share exchange or engage in similar transactions outside the ordinary course of business, unless app by the affirmative vote of stockholders entitled to cast at least two-thirds of the votes entitled to be cast on the matter. How a Maryland corporation may provide in its charter for approval of these matters by a lesser percentage, but not less t majority of all of the votes entitled to be cast on the matter. Our charter generally provides for approval of charter amend and extraordinary transactions by the stockholders entitled to cast at least a majority of the votes entitled to be cast o matter.

Our charter also provides that certain charter amendments and any proposal for our conversion, whether by merger or othe from a closed-end company to an open-end company or any proposal for our liquidation or dissolution requires the appro the stockholders entitled to cast at least 80 percent of the votes entitled to be cast on such matter. However, if such amen or proposal is approved by at least two-thirds of our continuing directors (in addition to approval by our Board of Dire such amendment or proposal may be approved by a majority of the votes entitled to be cast on such a matter. The "conti directors" are defined in our charter as our current directors as well as those directors whose nomination for election b stockholders or whose election by the directors to fill vacancies is approved by a majority of the continuing directors then Board of Directors.

Our charter and bylaws provide that the Board of Directors will have the exclusive power to make, alter, amend or repea provision of our bylaws.

No Appraisal Rights

Except with respect to appraisal rights arising in connection with the Control Share Act discussed above, as permitted Maryland General Corporation Law, our charter provides that stockholders will not be entitled to exercise appraisal rights.

DESCRIPTION OF OUR PREFERRED STOCK

In addition to shares of common stock, our charter authorizes the issuance of preferred stock. If we offer preferred stock this prospectus, we will issue an appropriate prospectus supplement. We may issue preferred stock from time to time in more series, without stockholder approval. Our Board of Directors is authorized to fix for any series of preferred sto number of shares of such series and the designation, relative powers, preferences and rights, and the qualifications, limit or restrictions of such series; except that, such an issuance must adhere to the requirements of the 1940 Act, Maryland la any other limitations imposed by law.

The 1940 Act requires, among other things, that (1) immediately after issuance and before any distribution is made with r to common stock, the liquidation preference of the preferred stock, together with all other senior securities, must not exce amount equal to 50% of our total assets (taking into account such distribution) and (2) the holders of shares of preferred st any are issued, must be entitled as a class to elect two directors at all times and to elect a majority of the directors if divi on the preferred stock are in arrears by two years or more.

For any series of preferred stock that we may issue, our Board of Directors will determine and the prospectus suppl relating to such series will describe:

- the designation and number of shares of such series;
- the rate and time at which, and the preferences and conditions under which, any dividends will be paid on sh of such series, the cumulative nature of such dividends and whether such dividends have any participating feature;

- any provisions relating to convertibility or exchangeability of the shares of such series;
- the rights and preferences, if any, of holders of shares of such series upon our liquidation, dissolution or winc
  up of our affairs;
- the voting powers of the holders of shares of such series;
- any provisions relating to the redemption of the shares of such series;

- any limitations on our ability to pay dividends or make distributions on, or acquire or redeem, other securitie while shares of such series are outstanding;
- any conditions or restrictions on our ability to issue additional shares of such series or other securities;
- if applicable, a discussion of certain U.S. Federal income tax considerations; and
- any other relative power, preferences and participating, optional or special rights of shares of such series, and qualifications, limitations or restrictions thereof.

All shares of preferred stock that we may issue will be identical and of equal rank except as to the particular terms there may be fixed by our Board of Directors, and all shares of each series of preferred stock will be identical and of equa except as to the dates from which cumulative dividends thereon will be cumulative.

DESCRIPTION OF OUR DEBT SECURITIES

We may issue debt securities in one or more series which, if publicly offered, will be under an indenture to be entere between us and a trustee. The specific terms of each series of debt securities we publicly offer will be described in the part prospectus supplement relating to that series. For a complete description of the terms of a particular series of debt securitie should read both this prospectus and the prospectus supplement relating to that particular series.

The prospectus supplement, which will accompany this prospectus, will describe the particular series of debt securities offered by including:

- the designation or title of the series of debt securities;
- the total principal amount of the series of debt securities;
- the percentage of the principal amount at which the series of debt securities will be offered;
- the date or dates on which principal will be payable;
- the rate or rates (which may be either fixed or variable) and/or the method of determining such rate or rates o interest, if any;
- the date or dates from which any interest will accrue, or the method of determining such date or dates, and th date or dates on which any interest will be payable;
- the terms for redemption, extension or early repayment, if any;
- the currencies in which the series of debt securities are issued and payable;
- the provision for any sinking fund;
- any restrictive covenants;
- any events of default;

- whether the series of debt securities are issuable in certificated form;
- any provisions for defeasance or covenant defeasance;

- any special U.S. Federal income tax implications, including, if applicable, U.S. Federal income tax considerations relating to original issue discount;
- any provisions for convertibility or exchangeability of the debt securities into or for any other securities;
- whether the debt securities are subject to subordination and the terms of such subordination;
- the listing, if any, on a securities exchange;
- the name and address of the trustee; and
- any other terms.

The debt securities may be secured or unsecured obligations. Under the provisions of the 1940 Act, we are permittec business development company, to issue debt only in amounts such that our asset coverage, as defined in the 1940 Act, equ least 200% after each issuance of debt. Unless the prospectus supplement states otherwise, principal (and premium, if any interest, if any, will be paid by us in immediately available funds.

DESCRIPTION OF OUR WARRANTS

We may issue warrants to purchase shares of our common stock, preferred stock or debt securities from time to time. warrants may be issued independently or together with one of our Securities and may be attached or separate from securities. We will issue each series of warrants under a separate warrant agreement to be entered into between us and a w agent. The warrant agent will act solely as our agent and will not assume any obligation or relationship of agency for o holders or beneficial owners of warrants.

A prospectus supplement will describe the particular terms of any series of warrants we may issue, including the following

- the title of such warrants;
- the aggregate number of such warrants;
- the price or prices at which such warrants will be issued;
- the currency or currencies, including composite currencies, in which the price of such warrants may be payab
- the number of shares of common stock, preferred stock or debt securities issuable upon exercise of such warrants;
- the price at which and the currency or currencies, including composite currencies, in which the shares of common stock, preferred stock or debt securities purchasable upon exercise of such warrants may be purchas
- the date on which the right to exercise such warrants will commence and the date on which such right will ex
- whether such warrants will be issued in registered form or bearer form;
- if applicable, the minimum or maximum amount of such warrants which may be exercised at any one time;

- if applicable, the number of such warrants issued with each share of common stock, preferred stock or debt securities;
- if applicable, the date on and after which such warrants and the related shares of common stock, preferred sto or debt securities will be separately transferable;
- information with respect to book-entry procedures, if any;
- if applicable, a discussion of certain U.S. Federal income tax considerations; and
- any other terms of such warrants, including terms, procedures and limitations relating to the exchange and exercise of such warrants.

We and the warrant agent may amend or supplement the warrant agreement for a series of warrants without the consent holders of the warrants issued thereunder to effect changes that are not inconsistent with the provisions of the warrants an do not materially and adversely affect the interests of the holders of the warrants.

Under the 1940 Act, we may generally only offer warrants provided that (1) the warrants expire by their terms within ten (2) the exercise or conversion price is not less than the current market value at the date of issuance; (3) our stockho authorize the proposal to issue such warrants, and our Board of Directors approves such issuance on the basis that the iss is in our best interests and the best interest of our stockholders; and (4) if the warrants are accompanied by other securitie warrants are not separately transferable unless no class of such warrants and the securities accompanying them has publicly distributed. The 1940 Act also provides that the amount of our voting securities that would result from the exerc all outstanding warrants at the time of issuance may not exceed 25% of our outstanding voting securities.

REGULATION

We are a closed-end, non-diversified investment company that has filed an election to be treated as a business develop company under the 1940 Act and has elected to be treated as a RIC under Subchapter M of the Code. The 1940 Act co prohibitions and restrictions relating to transactions between business development companies and their affiliates (includin investment advisers or sub-advisers), principal underwriters and affiliates of those affiliates or underwriters and requires majority of the directors be persons other than "interested persons," as that term is defined in the 1940 Act. In addition, the Act provides that we may not change the nature of our business so as to cease to be, or to withdraw our election as, a bu development company unless approved by a majority of our outstanding voting securities.

We may invest up to 100% of our assets in securities acquired directly from issuers in privately negotiated transactions. respect to such securities, we may, for the purpose of public resale, be deemed an "underwriter" as that term is defined Securities Act. Our intention is to not write (sell) or buy put or call options to manage risks associated with the publicly-t securities of our portfolio companies, except that we may enter into hedging transactions to manage the risks associate interest rate and other market fluctuations. However, in connection with an investment or acquisition financing of a por company, we may purchase or otherwise receive warrants to purchase the common stock of the portfolio company. Simila connection with an acquisition, we may acquire rights to require the issuers of acquired securities or their affilia repurchase them under certain circumstances. We also do not intend to acquire securities issued by any investment com that exceed the limits imposed by the 1940 Act. Under these limits, except with respect to money market funds we gen cannot acquire more than 3% of the voting stock of any registered investment company, invest more than 5% of the value o total assets in the securities of one investment company or invest more than 10% of the value of our total assets in the secu of more than one investment company. With regard to that portion of our portfolio invested in securities issued by inves companies, it should be noted that such investments subject our stockholders indirectly to additional expenses. None of policies are fundamental and may be changed without stockholder approval.

Qualifying Assets

Under the 1940 Act, a business development company may not acquire any asset other than assets of the type listed in Se 55(a) of the 1940 Act, which are referred to as qualifying assets, unless, at the time the acquisition is made, qualifying represent at least 70% of the company's total assets. The principal categories of qualifying assets relevant to our business a following:

(1) Securities purchased in transactions not involving any public offering from the issuer of such securities, which i (subject to certain limited exceptions) is an eligible portfolio company, or from any person who is, or has been durin preceding 13 months, an affiliated person of an eligible portfolio company, or from any other person, subject to such ru may be prescribed by the SEC. An "eligible portfolio company" is defined in the 1940 Act and rules adopted pursuant ther any issuer which:

(a) is organized under the laws of, and has its principal place of business in, the United States;

(b) is not an investment company (other than a small business investment company wholly owned by the busin development company) or a company that would be an investment company but for exclusions under the 19 Act for certain financial companies such as banks, brokers, commercial finance companies, mortgage companies and insurance companies; and

(c) satisfies any of the following:

1. does not have any class of securities with respect to which a broker or dealer may extend margin credit
2. is controlled by a business development company or a group of companies including a business development company and the business development company has an affiliated person who is a directo the eligible portfolio company;
3. is a small and solvent company having total assets of not more than $4 million and capital and surplus o not less than $2 million;
4. does not have any class of securities listed on a national securities exchange; or
5. has a class of securities listed on a national securities exchange, but has an aggregate market value of outstanding voting and non-voting common equity of less than $250 million.

(2) Securities in companies that were eligible portfolio companies when we made our initial investment if certain requirements are satisfied.

(3) Securities of any eligible portfolio company which we control.

(4) Securities purchased in a private transaction from a U.S. issuer that is not an investment company or from an affi person of the issuer, or in transactions incident thereto, if the issuer is in bankruptcy and subject to reorganization or issuer, immediately prior to the purchase of its securities was unable to meet its obligations as they came due without ma assistance other than conventional lending or financing agreements.

(5) Securities of an eligible portfolio company purchased from any person in a private transaction if there is no ready mark
such securities and we already own 60% of the outstanding equity of the eligible portfolio company.

(6) Securities received in exchange for or distributed on or with respect to securities described in (1) through (4) abo
pursuant to the exercise of warrants or rights relating to such securities.

---

(7) Cash, cash equivalents, U.S. government securities or high-quality debt securities maturing in one year or less from th
of investment.

In addition, a business development company must have been organized and have its principal place of business in the U
States and must be operated for the purpose of making investments in the types of securities described in (1), (2), (3)
above.

Managerial Assistance to Portfolio Companies

In order to count portfolio securities as qualifying assets for the purpose of the 70% test, the business development co
must either control the issuer of the securities or must offer to make available to the issuer of the securities (other than sma
solvent companies described above) significant managerial assistance; except that, where the business development co
purchases such securities in conjunction with one or more other persons acting together, one of the other persons in the
may make available such managerial assistance. Making available significant managerial assistance means, among other t
any arrangement whereby the business development company, through its directors, officers or employees, offers to pr
and, if accepted, does so provide, significant guidance and counsel concerning the management, operations or bu
objectives and policies of a portfolio company.

Temporary Investments

Pending investment in other types of "qualifying assets," as described above, our investments may consist of cash
equivalents, including money market funds, U.S. government securities or high quality debt securities maturing in one y
less from the time of investment, which we refer to, collectively, as temporary investments, so that 70% of our asse
qualifying assets. Typically, we will invest in money market funds, U.S. treasury bills or in repurchase agreements that ar
collateralized by cash or securities issued by the U.S. government or its agencies. A repurchase agreement involves the pu
by an investor, such as us, of a specified security and the simultaneous agreement by the seller to repurchase it at an a
upon future date and at a price which is greater than the purchase price by an amount that reflects an agreed-upon interes
There is no percentage restriction on the proportion of our assets that may be invested in such repurchase agreements. Ho
if more than 25% of our total assets constitute repurchase agreements from a single counterparty, we would not me
diversification tests in order to qualify as a RIC for U.S. Federal income tax purposes. Thus, we do not intend to ente
repurchase agreements with a single counterparty in excess of this limit. Our Investment Adviser will monit
creditworthiness of the counterparties with which we enter into repurchase agreement transactions.

Senior Securities

We are permitted, under specified conditions, to issue multiple classes of indebtedness and one class of stock senior
common stock if our asset coverage, as defined in the 1940 Act, is at least equal to 200% immediately after each such iss
In addition, while any preferred stock or public debt securities remain outstanding, we must make provisions to prohib
distribution to our stockholders or the repurchase of such securities or shares unless we meet the applicable asset coverage
after giving effect to such distribution or repurchase. We may also borrow amounts up to 5% of the value of our total ass
temporary or emergency purposes without regard to asset coverage. For a discussion of the risks associated with levera
"Risk Factors."

Code of Ethics

We, Prospect Capital Management and Prospect Administration have each adopted a code of ethics pursuant to Rule
under the 1940 Act that establishes procedures for personal investments and restricts certain personal securities transac
Personnel subject to each code may invest in securities for their personal investment accounts, including securities that m
purchased or held by us, so long as such investments are made in accordance with the code's requirements. For informati
how to obtain a copy of each code of ethics, see "Available Information."

Investment Concentration

Our investment objective is to generate both current income and long-term capital appreciation through debt and e investments. While we are diversifying the portfolio, many of our existing investments are in the energy and energy r industries.

Compliance Policies and Procedures

We and our Investment Adviser have adopted and implemented written policies and procedures reasonably designed to pr violation of the U.S. Federal securities laws, and are required to review these compliance policies and procedures annual their adequacy and the effectiveness of their implementation, and to designate a Chief Compliance Officer to be responsib administering the policies and procedures. Brian H. Oswald serves as our Chief Compliance Officer.

Proxy Voting Policies and Procedures

We have delegated our proxy voting responsibility to Prospect Capital Management. The Proxy Voting Policies and Proce of Prospect Capital Management are set forth below. The guidelines are reviewed periodically by Prospect Capital Manage and our independent directors, and, accordingly, are subject to change.

Introduction. As an investment adviser registered under the Advisers Act, Prospect Capital Management has a fiduciary d act solely in the best interests of its clients. As part of this duty, Prospect Capital Management recognizes that it must vote securities in a timely manner free of conflicts of interest and in the best interests of its clients.

These policies and procedures for voting proxies for Prospect Capital Management's Investment Advisory clients are int to comply with Section 206 of, and Rule 206(4)-6 under, the Advisers Act.

Proxy policies. These policies are designed to be responsive to the wide range of subjects that may be the subject of a vote. These policies are not exhaustive due to the variety of proxy voting issues that Prospect Capital Management m required to consider. In general, Prospect Capital Management will vote proxies in accordance with these guidelines unle Prospect Capital Management has determined to consider the matter on a case-by-case basis (as is stated in these guidel (2) the subject matter of the vote is not covered by these guidelines, (3) a material conflict of interest is present, or (4) Pro Capital Management might find it necessary to vote contrary to its general guidelines to maximize stockholder value and v its clients' best interests. In such cases, a decision on how to vote will be made by the Proxy Voting Committee (as desc below). In reviewing proxy issues, Prospect Capital Management will apply the following general policies:

Elections of directors. In general, Prospect Capital Management will vote in favor of the management-proposed sl directors. If there is a proxy fight for seats on the Board of Directors or Prospect Capital Management determines that the other compelling reasons for withholding votes for directors, the Proxy Voting Committee will determine the appropriat on the matter. Prospect Capital Management believes that directors have a duty to respond to stockholder actions that received significant stockholder support. Prospect Capital Management may withhold votes for directors that fail to act c issues such as failure to implement proposals to declassify boards, failure to implement a majority vote requirement, fail submit a rights plan to a stockholder vote and failure to act on tender offers where a majority of stockholders have tendere

shares. Finally, Prospect Capital Management may withhold votes for directors of non-U.S. issuers where there is insuff
information about the nominees disclosed in the proxy statement.

Appointment of auditors. Prospect Capital Management believes that the Company remains in the best position to choo
auditors and will generally support management's recommendation.

Changes in capital structure. Changes in a company's charter, articles of incorporation or by-laws may be required by st
U.S. Federal regulation. In general, Prospect Capital Management will cast its votes in accordance with the Comp
management on such proposal. However, the Proxy Voting Committee will review and analyze on a case-by-case basi
proposals regarding changes in corporate structure that are not required by state or U.S. Federal regulation.

Corporate restructurings, mergers and acquisitions. Prospect Capital Management believes proxy votes dealing with corp
reorganizations are an extension of the investment decision. Accordingly, the Proxy Voting Committee will analyze
proposals on a case-by-case basis.

Proposals affecting the rights of stockholders. Prospect Capital Management will generally vote in favor of proposals tha
stockholders a greater voice in the affairs of the Company and oppose any measure that seeks to limit those rights. How
when analyzing such proposals, Prospect Capital Management will weigh the financial impact of the proposal again
impairment of the rights of stockholders.

Corporate governance. Prospect Capital Management recognizes the importance of good corporate governance in ensurin
management and the Board of Directors fulfill their obligations to the stockholders. Prospect Capital Management f
proposals promoting transparency and accountability within a company.

Anti-takeover measures. The Proxy Voting Committee will evaluate, on a case-by-case basis, proposals regarding anti-tak
measures to determine the measure's likely effect on stockholder value dilution.

Stock splits. Prospect Capital Management will generally vote with the management of the Company on stock split matter

Limited liability of directors. Prospect Capital Management will generally vote with management on matters that would
the limited liability of directors.

Social and corporate responsibility. The Proxy Voting Committee may review and analyze on a case-by-case basis prop
relating to social, political and environmental issues to determine whether they will have a financial impact on stockh
value. Prospect Capital Management may abstain from voting on social proposals that do not have a readily determi
financial impact on stockholder value.

Proxy voting procedures. Prospect Capital Management will generally vote proxies in accordance with these guidelin
circumstances in which (1) Prospect Capital Management has determined to consider the matter on a case-by-case basis
stated in these guidelines), (2) the subject matter of the vote is not covered by these guidelines, (3) a material conflict of in
is present, or (4) Prospect Capital Management might find it necessary to vote contrary to its general guidelines to max
stockholder value and vote in its clients' best interests, the Proxy Voting Committee will vote the proxy.

Proxy voting committee. Prospect Capital Management has formed a proxy voting committee to establish general p
policies and consider specific proxy voting matters as necessary. In addition, members of the committee may conta

management of the Company and interested stockholder groups as necessary to discuss proxy issues. Members of the comm
will include relevant senior personnel. The committee may also evaluate proxies where we face a potential conflict of in
(as discussed below). Finally, the committee monitors adherence to guidelines, and reviews the policies contained i
statement from time to time.

Conflicts of interest. Prospect Capital Management recognizes that there may be a potential conflict of interest when it v proxy solicited by an issuer that is its advisory client or a client or customer of one of our affiliates or with whom it has ar business or personal relationship that may affect how it votes on the issuer's proxy. Prospect Capital Management believe adherence to these policies and procedures ensures that proxies are voted with only its clients' best interests in mind. To e that its votes are not the product of a conflict of interests, Prospect Capital Management requires that: (i) anyone involved decision making process (including members of the Proxy Voting Committee) disclose to the chairman of the Proxy V Committee any potential conflict that he or she is aware of and any contact that he or she has had with any interested regarding a proxy vote; and (ii) employees involved in the decision making process or vote administration are prohibited revealing how Prospect Capital Management intends to vote on a proposal in order to reduce any attempted influence interested parties.

Proxy voting. Each account's custodian will forward all relevant proxy materials to Prospect Capital Management, electronically or in physical form to the address of record that Prospect Capital Management has provided to the custodian.

Proxy recordkeeping. Prospect Capital Management must retain the following documents pertaining to proxy voting:

- copies of its proxy voting polices and procedures;
- copies of all proxy statements;
- records of all votes cast by Prospect Capital Management;
- copies of all documents created by Prospect Capital Management that were material to making a decision hov vote proxies or that memorializes the basis for that decision; and
- copies of all written client requests for information with regard to how Prospect Capital Management voted proxies on behalf of the client as well as any written responses provided.

All of the above-referenced records will be maintained and preserved for a period of not less than five years from the end fiscal year during which the last entry was made. The first two years of records must be maintained at our office.

Proxy voting records. Clients may obtain information about how Prospect Capital Management voted proxies on their beh making a written request for proxy voting information to: Compliance Officer, Prospect Capital Management LLC, 10 Eas Street, 44th Floor, New York, NY 10016.

Sarbanes-Oxley Act of 2002

The Sarbanes-Oxley Act of 2002 imposes a variety of regulatory requirements on publicly-held companies. In addition Chief Executive and Chief Financial Officers' required certifications as to the accuracy of our financial reporting, we ar required to disclose the effectiveness of our disclosure controls and procedures as well as report on our assessment c internal controls over financial reporting, the latter of which must be audited by our independent registered public accou firm.

The Sarbanes-Oxley Act also requires us to continually review our policies and procedures to ensure that we rem
compliance with all rules promulgated under the Act.

CUSTODIAN, TRANSFER AND DIVIDEND PAYING AGENT AND REGISTRAR

Our Securities are held under a custody agreement by U.S. Bank National Association. The address of the custodian is: North Rivercenter Drive, MK-WI-5302, Milwaukee, WI 53212, Attention: Mutual Fund Custody Account Administ facsimile: (866) 350-1430. American Stock Transfer & Trust Company acts as our transfer agent, dividend paying ager registrar. The principal business address of American Stock Transfer & Trust Company is 59 Maiden Lane, New Yorl 10007, telephone number: (718) 921-8200.

BROKERAGE ALLOCATION AND OTHER PRACTICES

Since we generally acquire and dispose of our investments in privately negotiated transactions, we infrequently use brok the normal course of our business. The aggregate amount of brokerage commissions paid by us during the three most r fiscal years is $101,746. Subject to policies established by our Board of Directors, Prospect Capital Management is prin responsible for the execution of the publicly-traded securities portion of our portfolio transactions and the allocati brokerage commissions.

Prospect Capital Management does not expect to execute transactions through any particular broker or dealer, but se obtain the best net results for the Company, taking into account such factors as price (including the applicable brok commission or dealer spread), size of order, difficulty of execution, and operational facilities of the firm and the firm's ris skill in positioning blocks of securities. While Prospect Capital Management generally seeks reasonably competitive execution costs, the Company will not necessarily pay the lowest spread or commission available. Subject to applicable requirements, Prospect Capital Management may select a broker based partly upon brokerage or research services provide and the Company and any other clients. In return for such services, we may pay a higher commission than other brokers v charge if Prospect Capital Management determines in good faith that such commission is reasonable in relation to the se provided.

PLAN OF DISTRIBUTION

We may sell the Securities pursuant to this prospectus and a prospectus supplement in any of four ways (or in any combina (a) through underwriters or dealers; (b) directly to a limited number of purchasers or to a single purchaser, including ex stockholders in a rights offering; (c) through agents; or (d) directly to our stockholders and others through the issuar transferable or non-transferable rights to our stockholders. In the case of a rights offering, the applicable prospectus supple will set forth the number of shares of our common stock issuable upon the exercise of each right and the other terms of rights offering. We will not sell shares of common stock in a rights offering to our stockholder at a price below NAV per under this prospectus. Any underwriter or agent involved in the offer and sale of the Securities will also be named applicable prospectus supplement. The Securities may be sold "at-the-market" to or through a market maker or into an ex trading market for the securities, on an exchange or otherwise. The prospectus supplement will set forth the terms o offering of such securities, including:

·

- the name or names of any underwriters or agents and the amounts of Securities underwritten or placed by eac them;
- the offering price of the Securities and the proceeds to us and any discounts, commissions or concessions allo or reallowed or paid to underwriters or agents; and
- any securities exchanges on which the Securities may be listed.

In addition, pursuant to the terms of certain applicable registration rights agreements entered into by us or that we may into in the future, certain of our stockholders may resell shares of our common stock under this prospectus and as descril any related prospectus supplement.

We may use Securities to acquire investments in companies, the terms of which will be further disclosed in a prosp
supplement if such stock is issued in an offering hereunder.

Any offering price and any discounts or concessions allowed or reallowed or paid to underwriters or agents may be ch
from time to time.

We may sell our common stock, or warrants, options or rights to acquire our common stock, at a price below the curre
asset value of our common stock in certain circumstances, including if (i)(1) the holders of a majority of our shares (or, i
at least 67% of a quorum consisting of a majority of our shares) and a similar majority of the holders of our shares who a
affiliated persons of us approve the sale of our common stock at a price that is less than the current net asset value, and
majority of our Directors who have no financial interest in the transaction and a majority of our independent Directo
determine that such sale is in our and our stockholders' best interests and (b) in consultation with any underwri
underwriters of the offering, make a good faith determination as of a time either immediately prior to the first solicitation
or on our behalf of firm commitments to purchase such shares, or immediately prior to the issuance of such shares, that the
at which such shares are to be sold is not less than a price which closely approximates the market value of such shares, les
distributing commission or discount or if (ii) a majority of the number of the beneficial holders of our common stock entit
vote at the annual meeting, without regard to whether a majority of such shares are voted in favor of the proposal, appro
sale of our common stock at a price that is less than the current net asset value per share. As stated above, we will not us
prospectus to sell our common stock to our shareholders in a rights offering at a price below current net asset value.

If underwriters are used in the sale of any Securities, Securities acquired by the underwriters for their own account m
resold from time to time in one or more transactions, including negotiated transactions, at a fixed public offering price
varying prices determined at the time of sale. The Securities may be either offered to the public through underwriting synd
represented by managing underwriters, or directly by underwriters. Generally, any obligations by the underwriters to pu
the Securities will be subject to certain conditions precedent.

The maximum commission or discount to be received by any FINRA member or independent broker-dealer will not excee
In connection with any rights offering to our stockholders, we may also enter into a standby underwriting arrangement wi
or more underwriters pursuant to which the underwriter(s) will purchase our common stock remaining unsubscribed for aft
rights offering.

We may sell the Securities through agents from time to time. The prospectus supplement will name any agent involved
offer or sale of the Securities and any commissions we pay to them. Generally, any agent will be acting on a best efforts
for the period of its appointment.

Agents, dealers and underwriters may be entitled to indemnification by us against certain civil liabilities, including liab
under the Securities Act or to contribution with respect to payments which the agents or underwriters may be required to
in respect thereof. Agents, dealers and underwriters may be customers of, engage in transactions with, or perform services
in the ordinary course of business.

We may enter into derivative transactions with third parties, or sell Securities outside of this prospectus to third part privately negotiated transactions. If the applicable prospectus supplement indicates, in connection with those derivative third parties may sell Securities covered by this prospectus and the applicable prospectus supplement, including in shor transactions. If so, the third party may use Securities pledged by us or borrowed from us or others to settle those sales or to out any related open borrowings of stock, and may use securities received from us in settlement of those derivatives to clo any related open borrowings of stock. The third party in such sale transactions will be an underwriter and, if not identif this prospectus, will be identified in the applicable prospectus supplement (or a post-effective amendment). We or one c affiliates may loan or pledge Securities to a financial institution or other third party that in turn may sell the securities usir prospectus. Such

financial institution or third party may transfer its short position to investors in our Securities or in connection v
simultaneous offering of other Securities offered by this prospectus or otherwise.

In order to comply with the securities laws of certain states, if applicable, the Securities offered hereby will be sold ir
jurisdictions only through registered or licensed brokers or dealers. In addition, in certain states, the Securities may not b
unless they have been registered or qualified for sale in the applicable state or an exemption from the registrati
qualification requirements is available and is complied with.

LEGAL MATTERS

Certain legal matters regarding the securities offered by this prospectus will be passed upon for the Company by Skadden,
Slate, Meagher & Flom LLP, New York, NY, and Venable LLP as special Maryland counsel.

INDEPENDENT REGISTERED ACCOUNTING FIRM

BDO Seidman, LLP is the independent registered public accounting firm of the Company.

AVAILABLE INFORMATION

We have filed with the SEC a registration statement on Form N-2, together with all amendments and related exhibits, und
Securities Act, with respect to our Securities offered by this prospectus. The registration statement contains addit
information about us and the Securities being registered by this prospectus. We file with or submit to the SEC annual, qua
and current periodic reports, proxy statements and other information meeting the informational requirements of the Excl
Act. This information and the information specifically regarding how we voted proxies relating to portfolio securities f
period ended June 30, 2009, are available free of charge by contacting us at 10 East 40th Street, 44th floor, New York
10016 or by telephone at toll-free (888) 748-0702. You may inspect and copy these reports, proxy statements and
information, as well as the registration statement and related exhibits and schedules, at the Public Reference Room of the
at 100 F Street NE, Washington, D.C. 20549. You may obtain information on the operation of the Public Reference Roo
calling the SEC at (202) 551-8090 or by calling 1-800-SEC-0330. The SEC maintains an Internet site that contains re
proxy and information statements and other information filed electronically by us with the SEC which are available o
SEC's Internet site at http://www.sec.gov. Copies of these reports, proxy and information statements and other information
be obtained, after paying a duplicating fee, by electronic request at the following E-mail address: publicinfo@sec.gov,
writing the SEC's Public Reference Section, Washington, D.C. 20549-0102.

INDEX TO FINANCIAL STATEMENTS

PROSPECT CAPITAL CORPORATION

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF ASSETS AND LIABILITIES
December 31, 2009 and June 30, 2009

	December 31, 2009 (Unaudited)	June 30, 2009 (Audited)
Assets (Note 10)		
Investments at fair value (cost of $633,636 and $531,424, respectively, Note 3)		
Control investments (cost of $165,867 and $187,105, respectively)	$ 191,898	$ 206,332
Affiliate investments (cost of $68,052 and $33,544, respectively)	66,479	32,254
Non-control/Non-affiliate investments (cost of $399,717 and $310,775, respectively)	389,758	308,582
Total investments at fair value	648,135	547,168
Investments in money market funds	23,418	98,735
Cash	3,844	9,942
Receivables for:		
Interest, net	5,723	3,562
Dividends	2	28
Other	359	571
Prepaid expenses	175	68
Due from Prospect Administration (Note 8)	998	—
Deferred financing costs, net	5,891	6,951
Other assets	535	—
Total Assets	$ 689,080	$ 667,025
Liabilities		
Credit facility payable (Note 10)	10,000	124,800
Dividend payable	25,894	—
Due to Prospect Administration (Note 8)	—	842
Due to Prospect Capital Management (Note 8)	7,412	5,871
Accrued expenses	8,039	2,381
Other liabilities	258	535
Total Liabilities	51,603	134,429
Net Assets	$ 637,477	$ 532,596
Components of Net Assets		
Common stock, par value $0.001 per share (100,000,000 and 100,000,000 common shares authorized, respectively; 63,349,746 and 42,943,084 issued and outstanding, respectively)	$ 63	$ 43
Paid-in capital in excess of par	741,520	545,707
Under/(over) distributed net investment income	(14,326)	24,152
Accumulated realized losses on investments	(104,279)	(53,050)
Unrealized appreciation on investments	14,499	15,744
Net Assets	$ 637,477	$ 532,596
Net Asset Value Per Share	$ 10.06	$ 12.40

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF OPERATIONS
For The Three and Six Months Ended December 31, 2009 and 2008

	For The Three Months Ended December 31,		For The Six Months End December 31,	
	2009	2008	2009	2008
Investment Income				
Interest Income				
Control investments (Net of foreign withholding tax of ($52), $62, ($19), and $109, respectively)	$ 5,052	$ 5,075	$ 9,643	$ 11,797
Affiliate investments (Net of foreign withholding tax of $0, $0, $0, and $0, respectively)	1,539	1,075	2,388	1,635
Non-control/non-affiliate investments	11,948	11,091	21,343	21,365
Total interest income	18,539	17,241	33,374	34,797
Dividend income				
Control investments	4,160	4,584	10,360	9,168
Money market funds	10	81	28	220
Total dividend income	4,170	4,665	10,388	9,388
Other income: (Note 5)				
Control/affiliate investments	75	87	75	831
Gain on Patriot acquisition (Note 2)	5,714	—	5,714	—
Non-control/non-affiliate investments	385	220	849	12,996
Total other income	6,174	307	6,638	13,827
Total Investment Income	28,883	22,213	50,400	58,012
Operating Expenses				
Investment advisory fees:				
Base management fee (Note 8)	3,176	2,940	6,385	5,763
Income incentive fee (Note 8)	4,231	2,990	7,311	8,865
Total investment advisory fees	7,407	5,930	13,696	14,628
Interest and credit facility expenses	1,995	1,965	3,369	3,483
Sub-administration fees (Including former Chief Financial Officer and Chief Compliance Officer)	—	217	—	467
Legal fees	390	184	390	483
Valuation services	153	110	273	422
Audit, compliance and tax related fees	239	306	501	629
Allocation of overhead from Prospect Administration (Note 8)	840	588	1,680	1,176
Insurance expense	63	63	126	124
Directors' fees	64	62	128	143
Other general and administrative expenses	807	295	994	462

Tax expense	—	533	—	533
Total Operating Expenses	11,958	10,253	21,157	22,550
Net Investment Income	16,925	11,960	29,243	35,462
Net realized (loss) gain on investments	(51,229)	16	(51,229)	1,661
Net change in unrealized appreciation/depreciation on investments	17,451	(5,452)	(1,245)	(16,601
Net (Decrease) Increase in Net Assets Resulting from Operations	$ (16,853)	$ 6,524	$ (23,231)	$ 20,522
Net (decrease) increase in net assets resulting from operations per share: (Note 7)	$ (0.29)	$ 0.22	$ (0.43)	$ 0.69
Dividends/distributions declared per share:	$ 0.41	$ 0.40	$ 0.82	$ 0.80

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS
For The Six Months Ended December 31, 2009 and 2008

	For The Six Months Ende	
	December 31, 2009	December 2008
(Decrease) Increase in Net Assets from Operations:		
Net investment income	$ 29,243	$ 35,462
Net realized (loss) gain on investments	(51,229)	1,661
Net change in unrealized depreciation on investments	(1,245)	(16,601
Net (Decrease) Increase in Net Assets Resulting from Operations	(23,231)	20,522
Dividends/Distributions to Shareholders:	(67,721)	(23,848
Capital Share Transactions:		
Net proceeds from capital shares sold	98,833	—
Less: Offering costs of public share offerings	(1,158)	—
Fair value of equity issued in conjunction with Patriot acquisition	92,800	—
Reinvestment of dividends/distributions	5,358	1,506
Net Increase in Net Assets Resulting from Capital Share Transactions	195,833	1,506
Total Increase in Net Assets:	104,881	(1,820
Net assets at beginning of period	532,596	429,623
Net Assets at End of Period	$ 637,477	$ 427,803
Capital Share Activity:		
Shares sold	11,431,797	—
Shares issued for Patriot acquisition	8,444,068	—
Shares issued through reinvestment of dividends/distributions	530,797	117,549
Net increase in capital share activity	20,406,662	117,549
Shares outstanding at beginning of period	42,943,084	29,520,3
Shares Outstanding at End of Period	63,349,746	29,637,9

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS
For The Six Months Ended December 31, 2009 and 2008

	For The Six Months Ende	
	December 31,	
	2009	2008
Cash Flows from Operating Activities:		
Net (decrease) increase in net assets resulting from operations	$ (23,231)	$ 20,522
Net realized loss (gain) on investments	51,229	(1,661
Net change in unrealized depreciation on investments	1,245	16,601
Accretion of original issue discount on investments	(6,670)	(2,128
Amortization of deferred financing costs	2,106	360
Gain on settlement of net profits interest	—	(12,576
Gain on Patriot acquisition	(5,714)	—
Change in operating assets and liabilities:		
Payments for purchases of investments	(7,321)	(70,513
Payment-in-kind interest	(2,059)	(931
Proceeds from sale of investments and collection of investment principal	69,735	13,077
Purchases of cash equivalents	(199,997)	(19,999
Sales of cash equivalents	199,997	19,999
Net decrease investments in money market funds	75,317	10,394
Decrease (increase) in interest receivable	163	(336
Decrease in dividends receivable	26	4,229
Decrease in loan principal receivable	—	71
Increase in receivable for managerial assistance	—	(25
Increase in receivable for potential deal expenses	—	(86
Decrease (increase) in other receivables	212	(17
Increase in prepaid expenses	(72)	(505
Decrease in due from Prospect Administration	502	—
Increase in other assets	(535)	—
Decrease in due to Prospect Administration	(842)	(12
Increase (decrease) in due to Prospect Capital Management	1,541	(317
(Decrease) increase in accrued expenses	(227)	997
Decrease in other liabilities	(277)	(270
Net Cash Provided By (Used In) Operating Activities:	155,128	(23,126
Cash Flows from Investing Activities:		
Acquisition of Patriot, net of cash acquired (Note 2)	(106,586)	—
Net Cash Used In Investing Activities:	(106,586)	—
Cash Flows from Financing Activities:		
Borrowings under credit facility	60,000	54,500
Payments under credit facility	(174,800)	(7,000
Financing costs paid and deferred	(1,046)	(270
Net proceeds from issuance of common stock	98,833	—

Offering costs from issuance of common stock	(1,158	)	—
Dividends/distributions paid	(36,469	)	(22,221
Net Cash Provided By Financing Activities:	54,640		25,009
Total (Decrease) Increase in Cash	(6,098	)	1,883
Cash balance at beginning of period	9,942		555
Cash Balance at End of Period	$ 3,844		$ 2,438
Cash Paid For Interest	$ 496		$ 2,862
Non-Cash Financing Activity:			
Fair value of shares issued in connection with Patriot acquisition	$ 92,800		$ —
Fair value of shares issued in connection with dividend reinvestment plan	$ 5,358		$ 2,901

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS
December 31, 2009 and June 30, 2009
(in thousands, except share data)

			December 31, 2009			
Portfolio Company	Locale / Industry	Investments(1)	Principal Value	Cost	Fair Value(2)	% of Net Assets
LEVEL 3 INVESTMENTS:						
Control Investments (25.00% or greater of voting control)						
Ajax Rolled Ring & Machine, Inc.	South Carolina / Manufacturing	Senior Secured Note – Tranche A (10.50%, due 4/01/2013)(3), (4)	$ 21,266	$ 21,266	$ 21,266	3.3
		Subordinated Secured Note – Tranche B (11.50% plus 6.00% PIK, due 4/01/2013)(3), (4)	12,038	12,038	4,536	0.7
		Subordinated Secured Note – Tranche B (15.00%, due 10/30/2010)	500	500	—	0.0
		Convertible Preferred Stock – Series A (6,143 shares)		6,057	—	0.0
		Unrestricted Common Stock (6 shares)		—	—	0.0
				39,861	25,802	4.0
AWCNC, LLC(20)	North Carolina / Machinery	Members Units – Class A (1,800,000 units)		—	—	0.0
		Members Units – Class B-1 (1 unit)		—	—	0.0
		Members Units – Class B-2 (7,999,999 units)		—	—	0.0
				—	—	0.0
C&J Cladding LLC	Texas / Metal Services and	Warrants (400 warrants, expiring 3/30/2014)		580	3,095	0.5

	Minerals					
				580	3,095	0.5
Change Clean Energy Holdings, Inc. ("CCEHI")(5)	Maine / Biomass Power	Common Stock (1,000 shares)		2,825	1,976	0.3
				2,825	1,976	0.3
Coalbed, Inc. / Coalbed, LLC(6)	Tennessee / Oil & Gas Production	Senior Secured Note (14.50%, in non-accrual status effective 10/21/2009, due 6/30/2010)	10,441	10,441	3,686	0.6
		Common Stock (1,000 shares)		—	—	0.0
				10,441	3,686	0.6
Fischbein, LLC	North Carolina / Machinery	Senior Subordinated Debt (12.00% plus 6.50% PIK, due 5/01/2013)	3,707	3,508	3,515	0.5
		Membership Interest – Class A (2,800,000 units)		1,877	1,876	0.3
				5,385	5,391	0.8
Freedom Marine Services LLC	Louisiana / Shipping Vessels	Subordinated Secured Note (16.00% PIK, due 12/31/2011)(3)	7,960	7,899	6,181	1.0
		Net Profits Interest (22.50% payable on Equity distributions)(3), (7)		—	—	0.0
				7,899	6,181	1.0
Gas Solutions Holdings, Inc.(8)	Texas / Gas Gathering and Processing	Senior Secured Note (18.00%, due 12/22/2018)(3)	25,000	25,000	25,000	3.9
		Junior Secured Note (18.00%, due 12/23/2018)(3)	5,000	5,000	5,000	0.8
		Common Stock (100 shares)(3)		5,003	55,187	8.7
				35,003	85,187	13.4
Integrated Contract Services, Inc.(9)	North Carolina / Contracting	Senior Demand Note (15.00%, due 12/31/2009)(10)	1,170	1,170	1,170	0.2
		Senior Secured Note (7.00% plus 7.00% PIK plus 6.00% default interest, in non-accrual status effective 10/09/2007, past due)	800	800	928	0.1

Junior Secured Note (7.00% plus 7.00% PIK plus 6.00% default interest, in non-accrual status effective 10/09/2007, past due)	14,003	14,003	3,177	0.5
Preferred Stock – Series A (10 shares)		—	—	0.0
Common Stock (49 shares)		679	—	0.0
		16,652	5,275	0.8

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS — (CONTINUED)
December 31, 2009 and June 30, 2009
(in thousands, except share data)

			December 31, 2009			
Portfolio Company	Locale / Industry	Investments(1)	Principal Value	Cost	Fair Value(2)	% N As
LEVEL 3 INVESTMENTS:						
Control Investments (25.00% or greater of voting control)						
Iron Horse Coiled Tubing, Inc.	Alberta, Canada / Production Services	Bridge Loan (15.00% plus 3.00% PIK, in non-accrual status effective 5/01/2009, due 12/31/2009)	$ 11,418	$ 11,199	$ 10,440	1.6
		Senior Secured Note (15.00%, in non-accrual status effective 5/01/2009, due 12/31/2009)	9,250	9,250	1,878	0.3
		Common Stock (1,781 shares)		268	—	0.0
				20,717	12,318	1.9
NRG Manufacturing, Inc.	Texas / Manufacturing	Senior Secured Note (16.50%, due 8/31/2011)(3), (4)	13,080	13,080	13,080	2.1
		Common Stock (800 shares)		2,317	13,610	2.1
				15,397	26,690	4.2
Nupla Corporation	California / Home & Office Furnishings, Housewares & Durable	Revolving Line of Credit (0.50% – 7.25% plus 2.00% default interest, due 9/04/2012)(4)	1,093	933	929	0.2
		Senior Secured Term Loan A (8.00% plus 2.00% default interest, due 9/04/2012)(4)	5,139	1,503	1,503	0.2
		Senior Subordinated Debt (10.00% plus	3,204	—	—	0.0

		5.00% PIK, in non-accrual status effective 4/01/2009, due 3/04/2013)				
		Preferred Stock – Class A (475 shares)		—	—	0.0
		Preferred Stock – Class B (1,045 shares)		—	—	0.0
		Common Stock (1,140,584 shares)		—	—	0.0
				2,436	2,432	0.4
R-V Industries, Inc.	Pennsylvania / Manufacturing	Warrants (200,000 warrants, expiring 6/30/2017)		1,682	3,211	0.5
		Common Stock (545,107 shares)		5,086	8,751	1.4
				6,768	11,962	1.9
Sidump'r Trailer Company, Inc.	Nebraska / Automobile	Revolving Line of Credit (0.50% – 7.25%, in non-accrual status effective 11/01/2008, due 1/10/2011)(4)	950	404	404	0.0
		Senior Secured Term Loan A (7.25%, in non-accrual status effective 11/01/2008, due 1/10/2011)(4)	2,048	464	464	0.1
		Senior Secured Term Loan B (8.75%, in-non-accrual status effective 11/01/2008, due 1/10/2011)(4)	2,321	—	—	0.0
		Senior Secured Term Loan C (16.50% PIK, in non-accrual status effective 9/27/2008, due 7/10/2011)	2,841	—	—	0.0
		Senior Secured Term Loan D (7.25%, in non-accrual status effective 11/01/2008, due 7/10/2011)(4)	1,700	—	—	0.0
		Preferred Stock (49,635 shares)		—	—	0.0
		Common Stock (64,050 shares)		—	—	0.0
				868	868	0.1
	Kentucky /		10,000	1,035	1,035	0.2

Yatesville Coal Holdings, Inc.(11)	Mining, Steel,	Senior Secured Note (15.77%, in non-accrual status effective 1/01/2009, due 12/31/2010)(4)				
	Iron and Non-Precious Metals	Junior Secured Note (15.77%, in non-accrual status effective 1/01/2009, due 12/31/2010)(4)	41,836	—	—	0.0
	and Coal Production	Common Stock (1,000 shares)		—	—	0.0
				1,035	1,035	0.2
		Total Control Investments		165,867	191,898	30.1

See notes to consolidated financial statements.

F-6

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS — (CONTINUED)
December 31, 2009 and June 30, 2009
(in thousands, except share data)

			December 31, 2009			
Portfolio Company	Locale / Industry	Investments(1)	Principal Value	Cost	Fair Value(2)	% of Net Asset
LEVEL 3 INVESTMENTS:						
Affiliate Investments (5.00% to 24.99% voting control)						
Appalachian Energy Holdings LLC(12)	West Virginia / Construction Services	Senior Secured Debt – Tranche A (14.00% plus 3.00% PIK plus 3.00% default interest, in non-accrual status effective 11/01/2008, due 1/31/2011)	$ 2,066	$ 1,897	$ 1,165	0.2
		Senior Secured Debt – Tranche B (14.00% plus 3.00% PIK plus 3.00% default interest, in non-accrual status effective 11/01/2008, past due)	2,120	1,960	—	0.0
		Preferred Stock – Series A (200 units)		82	—	0.0
		Preferred Stock – Series B (241 units)		241	—	0.0
		Preferred Stock – Series C (500 units)		500	—	0.0
		Warrants (6,065 warrants, expiring 2/13/2016)		176	—	0.0
		Warrants (6,025 warrants, expiring 6/17/2018)		172	—	0.0
		Warrants (25,000 warrants, expiring		—	—	0.0

		11/30/2018)				
				5,028	1,165	0.2
Biotronic NeuroNetwork(17)	Michigan / Healthcare	Senior Secured Note (11.50% plus 1.00% PIK, due 2/21/2013)(3), (4)	26,227	26,227	27,014	4.2
		Preferred Stock (9,925 shares)(13)		2,300	3,497	0.6
				28,527	30,511	4.8
Boxercraft Incorporated	Georgia / Textiles & Leather	Revolving Line of Credit (0.50%, due 9/16/2013)		—	—	0.0
		Senior Secured Term Loan A (9.50% – 10.50%, due 9/16/2013)(4)	4,049	3,412	3,140	0.5
		Senior Secured Term Loan B (10.00% – 11.00%, due 9/16/2013)(4)	4,835	3,750	3,788	0.5
		Senior Secured Term Loan C (12.00% plus 6.50% PIK, due 3/16/2014)	7,003	5,468	5,467	0.9
		Preferred Stock (1,000,000 shares)		—	—	0.0
		Common Stock (10,000 shares)		—	—	0.0
				12,630	12,395	1.9
KTPS Holdings, LLC	Colorado / Textiles & Leather	Revolving Line of Credit (0.50%, due 1/31/2012)		—	—	0.0
		Senior Secured Term Loan A (10.50% – 11.25%, due 1/31/2012)(4)	3,530	3,142	2,840	0.4
		Senior Secured Term Loan B (12.00%, due 1/31/2012)	445	372	372	0.1
		Senior Secured Term Loan C (12.00% plus 6.00% PIK, due 3/31/2012)	4,725	4,027	3,959	0.6
		Membership Interest – Class A (730 units)		—	—	0.0
		Membership Interest – Common (199,795 units)		—	—	0.0
				7,541	7,171	1.1

Miller Petroleum, Inc.	Tennessee / Oil & Gas Production	Warrants, Common Stock (2,117,689 warrants, expiring 5/04/2010 to 12/31/2014)(14)	150	937	0.2
			150	937	0.2
Smart, LLC(15)	New York / Diversified / Conglomerate Service	Membership Interest – Class B (1,218 units)	—	—	0.0
		Membership Interest – Class D (1 unit)	—	—	0.0
			—	—	0.0

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS — (CONTINUED)
December 31, 2009 and June 30, 2009
(in thousands, except share data)

(in thousands, except share data)

				December 31, 2009		
Portfolio Company	Locale / Industry	Investments(1)	Principal Value	Cost	Fair Value(2)	% of Net Asset
LEVEL 3 INVESTMENTS:						
Affiliate Investments (5.00% to 24.99% voting control)						
Sport Helmets Holdings, LLC(15)	New York / Personal & Nondurable Consumer Products	Revolving Line of Credit (0.50%, due 12/14/2013)	$	$ —	$ —	0.0
		Senior Secured Term Loan A (4.26% – 6.00%, due 12/14/2013)(4)	3,975	2,302	2,329	0.3
		Senior Secured Term Loan B (4.76% – 6.50%, due 12/14/2013)(4)	7,425	4,963	5,072	0.8
		Senior Subordinated Debt – Series A (12.00% plus 3.00% PIK, due 6/14/2014)	7,215	5,655	5,646	0.9
		Senior Subordinated Debt – Series B (10.00% plus 5.00% PIK, due 6/14/2014)	1,324	898	895	0.1
		Common Stock (20,000 shares)		358	358	0.1
				14,176	14,300	2.2
		Total Affiliate Investments		68,052	66,479	10.4
Non-control/Non-affiliate Investments (less than 5.00% of voting control)						
ADAPCO, Inc.	Florida / Ecological	Common Stock (5,000 shares)		141	295	0.0

				141	295	0.0
		Revolving Line of Credit (0.50%, due 11/01/2012)		—	—	0.0
Aircraft Fasteners International, LLC	California / Machinery	Senior Secured Term Loan (3.92% – 5.40%, due 11/01/2012)(4)	5,188	3,653	3,675	0.6
		Junior Secured Term Loan (12.00% plus 2.00% PIK, due 5/01/2013)	5,433	4,555	4,613	0.7
		Convertible Preferred Stock (32,500 units)		396	396	0.1
				8,604	8,684	1.4
American Gilsonite Company	Utah / Specialty Minerals	Senior Subordinated Note (12.00% plus 3.00% PIK, due 3/14/2013)(3)	14,783	14,783	15,078	2.4
		Membership Interest Units in AGC/PEP, LLC (99.9999%)(16)		1,031	2,728	0.4
				15,814	17,806	2.8
Arrowhead General Insurance Agency, Inc.(17)	California / Insurance	Junior Secured Term Loan (10.25% plus 2.50% PIK, due 2/8/2013)	5,085	3,873	3,871	0.6
				3,873	3,871	0.6
Borga, Inc.	California / Mining, Steel, Iron and Non-Precious Metals and Coal Production	Revolving Line of Credit (0.50% – 5.00% plus 3.00% default interest, due 5/06/2010)(4)	800	701	680	0.1
		Senior Secured Term Loan B (8.50% plus 3.00% default interest, due 5/6/2010)(4)	1,612	1,411	1,375	0.2
		Senior Secured Term Loan C (12.00% plus 4.00% PIK plus 3.00% default interest, due 5/06/2010)	8,453	651	622	0.1
		Warrants (33,750 warrants)		—	—	0.0

	2,763	2,677	0.4

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS — (CONTINUED)
December 31, 2009 and June 30, 2009
(in thousands, except share data)

			December 31, 2009			
Portfolio Company	Locale / Industry	Investments(1)	Principal Value	Cost	Fair Value(2)	% of Net Assets
LEVEL 3 INVESTMENTS:						
Non-control/Non-affiliate Investments (less than 5.00% of voting control)						
Caleel + Hayden, LLC (15)	Colorado / Personal & Nondurable Consumer Products	Junior Secured Term Loan B (9.75% – 10.00%, due 11/10/2011)(4)	$ 8,425	$ 8,399	$ 8,416	1.3
		Senior Subordinated Debt (12.00% plus 4.50% PIK, due 11/10/2012)	6,250	5,779	5,778	0.9
		Common Stock (7,500 shares)		351	351	0.1
		Options in Mineral Fusion Natural Brands, LLC (11,662 options)		—	—	0.0
				14,529	14,545	2.3
Castro Cheese Company, Inc.	Texas / Food Products	Junior Secured Note (11.00% plus 2.00% PIK, due 2/28/2013)(3)	7,615	7,505	7,655	1.2
				7,505	7,655	1.2
Copernicus Group	North Carolina / Healthcare	Revolving Line of Credit (0.50% – 10.50%, due 10/08/2013)(4)	150	3	—	0.0
		Senior Secured Term Loan A (10.50% – 11.50%, due 10/08/2013)(4)	6,250	5,272	5,205	0.8
		Senior Subordinated Debt (12.00% plus 6.00% PIK – 10.00% plus 10.00% PIK, due 4/08/2014)	12,741	10,661	11,948	1.9
		Preferred Stock – Series A (1,000,000 shares)		67	—	0.0
		Preferred Stock – Series C (212,121 shares)		212	140	0.0

				16,215	17,293	2.7
Custom Direct, Inc. (17)	Maryland / Printing & Publishing	Senior Secured Term Loan (3.06%, due 12/31/2013)(4)	1,651	1,204	1,219	0.2
		Junior Secured Term Loan (6.31%, due 12/31/2014)(4)	2,000	1,243	1,278	0.2
				2,447	2,497	0.4
Deb Shops, Inc.(17)	Pennsylvania / Retail	Second Lien Debt (1.00% plus 13.00% PIK, in non-accrual status effective 2/24/2009, due 10/23/2014)	16,378	14,607	2,318	0.4
				14,607	2,318	0.4
Diamondback Operating, LP	Oklahoma / Oil & Gas Production	Net Profits Interest (15.00% payable on Equity distributions)(7)		—	404	0.1
				—	404	0.1
EXL Acquisition Corp.	South Carolina / Electronics	Revolving Line of Credit (0.50%, due 3/15/2012)		—	—	0.0
		Senior Secured Term Loan A (3.93% – 5.50%, due 3/15/2011)(4)	1,790	1,494	1,473	0.2
		Senior Secured Term Loan B (4.18% – 5.75%, due 3/15/2012)(4)	4,053	3,680	3,714	0.6
		Senior Secured Term Loan C (4.68% – 6.25%, due 3/15/2012)(4)	2,500	2,294	2,316	0.4
		Senior Secured Term Loan D (12.00% plus 3.00% PIK, due 3/15/2012)	5,967	6,039	6,085	0.9
		Common Stock – Class A (2,475 shares)		509	509	0.1
		Common Stock – Class B (25 shares)		306	306	0.1
				14,322	14,403	2.3
Fairchild Industrial Products, Co.(2)	North Carolina / Electronics	Preferred Stock – Class A (378 shares)		377	380	0.1
		Common Stock – Class B (28 shares)		211	211	0.0
				588	591	0.1

			December 31, 2009			
Portfolio Company	Locale / Industry	Investments(1)	Principal Value	Cost	Fair Value(2)	% o Net Asse
H&M Oil & Gas, LLC	Texas / Oil & Gas Production	Senior Secured Note (13.00%, due 6/30/2010)	$ 49,661	$ 49,661	$ 46,081	7.2
		Net Profits Interest (8.00% payable on Equity distributions)(7)		—	1,047	0.2
				49,661	47,128	7.4

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS — (CONTINUED)
December 31, 2009 and June 30, 2009
(in thousands, except share data)

			December 31, 2009			
Portfolio Company	Locale / Industry	Investments(1)	Principal Value	Cost	Fair Value(2)	% of Net Assets
LEVEL 3 INVESTMENTS:						
Non-control/Non-affiliate Investments (less than 5.00% of voting control)						
Hudson Products Holdings, Inc.(17)	Texas / Mining, Steel, Iron and Non-Precious Metals and Coal Production	Senior Secured Term Loan (8.00%, due 8/24/2015)(4)	$ 7,406	$ 6,729	$ 6,993	1.1
				6,729	6,993	1.1
IEC Systems LP ("IEC") /Advanced Rig Services LLC ("ARS")	Texas / Oilfield Fabrication	IEC Senior Secured Note (12.00% plus 3.00% PIK, due 11/20/2012)(3), (4)	20,209	20,209	20,209	3.2
		ARS Senior Secured Note (12.00% plus 3.00% PIK, due 11/20/2012)(3), (4)	12,128	12,128	12,128	1.9
				32,337	32,337	5.1
Impact Products, LLC	Ohio / Machinery	Junior Secured Term Loan (6.25% – 8.25%, due 9/09/2012)(4)	8,835	7,704	7,753	1.2
		Senior Subordinated Debt (10.00% plus 5.00%, due 9/09/2012)	5,548	5,259	5,260	0.8
				12,963	13,013	2.0
Label Corp Holdings, Inc.	Nebraska / Printing & Publishing	Senior Secured Term Loan (8.50%, due 8/08/2014)(4)	5,823	5,193	5,306	0.8
				5,193	5,306	0.8
LHC Holdings Corp.(17)	Florida / Healthcare	Revolving Line of Credit (0.50%, due 11/30/2012)		—	—	0.0
			2,918	2,114	2,177	0.3

		Senior Secured Term Loan A (4.31% – 5.75%, due 11/30/2012)(4)				
		Senior Subordinated Debt (12.00% plus 2.50% PIK, due 5/31/2013)	4,565	4,157	4,156	0.7
		Membership Interest (125 units)		216	216	0.0
				6,487	6,549	1.0
Mac & Massey Holdings, LLC	Georgia / Food Products	Senior Subordinated Debt (10.00% plus 5.75% PIK, due 2/10/2013)	8,426	6,960	6,940	1.1
		Common Stock (250 shares)		169	170	0.0
				7,129	7,110	1.1
Maverick Healthcare, LLC	Arizona / Healthcare	Second Lien Debt (12.50% plus 3.50% PIK, due 4/30/2014)(3)	12,894	12,894	12,894	2.0
		Preferred Units (1,250,000 units)		1,252	1,693	0.3
		Common Units (1,250,000 units)		—	—	0.0
				14,146	14,587	2.3
Northwestern Management Services, LLC	Florida / Healthcare	Revolving Line of Credit (0.50%, due 12/13/2012)		—	—	0.0
		Senior Secured Term Loan A (4.24% – 5.75%, due 12/13/2012)(4)	5,050	4,050	3,936	0.6
		Senior Secured Term Loan B (4.74% – 6.25%, due 12/13/2012)(4)	1,228	864	865	0.1
		Junior Secured Term Loan (12.00% plus 3.00%, due 6/13/2013)	2,927	2,372	2,370	0.4
		Common Stock (50 shares)		371	371	0.1
				7,657	7,542	1.2

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS — (CONTINUED)
December 31, 2009 and June 30, 2009
(in thousands, except share data)

			December 31, 2009			
Portfolio Company	Locale / Industry	Investments(1)	Principal Value	Cost	Fair Value(2)	% of Net Asset
LEVEL 3 INVESTMENTS:						
Non-control/Non-affiliate Investments (less than 5.00% of voting control)						
Prince Mineral Company, Inc.	New York / Metal Services and Minerals	Junior Secured Term Loan (5.29% – 7.00%, due 12/21/2012)(4)	$ 11,175	$ 7,633	$ 7,816	1.2
		Senior Subordinated Debt (13.00% plus 1.00%, due 7/21/2013)	12,168	1,279	1,269	0.2
				8,912	9,085	1.4
Qualitest Pharmaceuticals, Inc.(17)	Alabama / Pharmaceuticals	Second Lien Debt (7.78%, due 4/30/2015)(3), (4)	12,000	11,952	12,000	1.9
				11,952	12,000	1.9
Regional Management Corp.	South Carolina / Financial Services	Second Lien Debt (13.00% plus 2.00% PIK, due 6/29/2012)(3)	25,685	25,685	24,511	3.8
				25,685	24,511	3.8
R-O-M Corporation	Missouri / Manufacturing	Revolving Line of Credit (0.50%, due 2/08/2013)		—	—	0.0
		Senior Secured Term Loan A (3.00% – 4.75%, due 2/08/2013)(4)	5,440	4,600	4,456	0.7
		Senior Secured Term Loan B (4.50% – 6.25%, due 5/08/2013)(4)	8,294	7,035	7,263	1.1
			7,282	6,929	6,939	1.1

		Senior Subordinated Debt (12.00% plus 3.00% due 8/08/2013)				
				18,564	18,658	2.9
		Second Lien Debt (15.00%, due 10/31/2013)(3)	18,000	18,000	18,180	2.8
Shearer's Foods, Inc.	Ohio / Food Products	Membership Interest Units in Mistral Chip Holdings, LLC (2,000 units)(18)		2,000	4,467	0.7
				20,000	22,647	3.5
Stryker Energy, LLC	Ohio / Oil & Gas Production	Subordinated Secured Revolving Credit Facility (12.00%, due 12/01/2011)(3), (4)	29,500	29,217	28,360	4.5
		Overriding Royalty Interests(19)		—	2,762	0.4
				29,217	31,122	4.9
TriZetto Group(17)	California / Healthcare	Subordinated Unsecured Note (12.00% plus 1.50% PIK, due 10/01/2016)(3)	15,319	15,185	15,771	2.5
				15,181	15,771	2.5
Unitek(17)	Pennsylvania / Technical Services	Second Lien Debt (13.08%, due 12/31/2013)(3), (4)	11,500	11,373	11,615	1.8
				11,373	11,615	1.8
Wind River Resources Corp. and Wind River II Corp.	Utah / Oil & Gas Production	Senior Secured Note (13.00% plus 3.00% default interest, in non-accrual status effective 12/01/2008, due 7/31/2010)(4)	15,000	15,000	10,627	1.7
		Net Profits Interest (5.00% payable on Equity distributions)(7)		—	—	0.0
				15,000	10,627	1.7

Total Non-Control/Non-Affiliate Investments (Level 3 Investments)	399,598	389,640	61.1
Total Level 3 Portfolio Investments	633,517	648,017	101.

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS — (CONTINUED)
December 31, 2009 and June 30, 2009
(in thousands, except share data)

				December 31, 2009		
Portfolio Company	Locale / Industry	Investments(1)	Principal Value	Cost	Fair Value(2)	% of Net Assets
LEVEL 1 INVESTMENTS:						
Non-control/Non-affiliate Investments (less than 5.00% of voting control)						
Allied Defense Group, Inc.	Virginia / Aerospace & Defense	Common Stock (10,000 shares)		$ 56	$ 48	0.0
				56	48	0.0
Dover Saddlery, Inc.	Massachusetts / Retail	Common Stock (30,974 shares)		63	70	0.0
				63	70	0.0
	Total Non-Control/Non-Affiliate Investments (Level 1 Investments)			119	118	101.6
		Total Portfolio Investments		633,636	648,135	101.6
LEVEL 2 INVESTMENTS:						
Money Market Funds						
Fidelity Institutional Money Market Funds — Government Portfolio (Class I)				16,070	16,070	2.5
Fidelity Institutional Money Market Funds — Government Portfolio (Class I)(3)				3,347	3,347	0.5
Victory Government Money Market Funds				4,001	4,001	0.7
	Total Money Market Funds (Level 2 Investments)			23,418	23,418	3.7
		Total Investments		657,054	671,553	105.3

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS
December 31, 2009 and June 30, 2009
(in thousands, except share data)

			June 30, 2009			
Portfolio Company	Locale / Industry	Investments(1)	Principal Value	Cost	Fair Value(2)	% of Net Assets
LEVEL 3 INVESTMENTS:						
Control Investments (25.00% or greater of voting control)						
Ajax Rolled Ring & Machine, Inc.	South Carolina / Manufacturing	Senior Secured Note – Tranche A (10.50%, due 4/01/2013)(3), (4)	$ 21,487	$ 21,487	$ 21,487	4.0
		Subordinated Secured Note – Tranche B (11.50% plus 6.00% PIK, due 4/01/2013)(3), (4)	11,675	11,675	10,151	1.9
		Convertible Preferred Stock – Series A (6,143 shares)		6,057	—	0.0
		Unrestricted Common Stock (6 shares)		—	—	0.0
				39,219	31,638	5.9
C&J Cladding LLC	Texas / Metal Services and Minerals	Senior Secured Note (14.00%, due 3/30/2012)(3), (4)	3,150	2,722	3,308	0.6
		Warrants (400 warrants, expiring 3/30/2014)		580	3,825	0.7
				3,302	7,133	1.3
Change Clean Energy Holdings, Inc.	Maine / Biomass Power	Common Stock (1,000 shares)		2,530	2,530	0.5
				2,530	2,530	0.5
Gas Solutions Holdings, Inc.(8)	Texas / Gas Gathering and Processing	Senior Secured Note (18.00%, due 12/22/2018)(3)	25,000	25,000	25,000	4.7
		Junior Secured Note (18.00%, due 12/23/2018)(3)	5,000	5,000	5,000	0.9
				5,003	55,187	10.4

		Common Stock (100 shares)(3)				
				35,003	85,187	16.0
Integrated Contract Services, Inc.(9)	North Carolina / Contracting	Senior Demand Note (15.00%, due 6/30/2009)(10)	1,170	1,170	1,170	0.2
		Senior Secured Note (7.00% plus 7.00% PIK plus 6.00% default interest, in non-accrual status effective 10/09/2007, past due)	800	800	800	0.1
		Junior Secured Note (7.00% plus 7.00% PIK plus 6.00% default interest, in non-accrual status effective 10/09/2007, past due)	14,003	14,003	3,030	0.6
		Preferred Stock – Series A (10 shares)		—	—	0.0
		Common Stock (49 shares)		679	—	0.0
				16,652	5,000	0.9
Iron Horse Coiled Tubing, Inc.	Alberta, Canada / Production Services	Bridge Loan (15.00% plus 3.00% PIK, due 12/31/2009)	9,826	9,826	9,602	1.8
		Senior Secured Note (15.00%, due 12/31/2009)	9,250	9,250	3,004	0.6
		Common Stock (1,781 shares)		268	—	0.0
				19,344	12,606	2.4
NRG Manufacturing, Inc.	Texas / Manufacturing	Senior Secured Note (16.50%, due 8/31/2011)(3), (4)	13,080	13,080	13,080	2.5
		Common Stock (800 shares)		2,317	19,294	3.6
				15,397	32,374	6.1
R-V Industries, Inc.	Pennsylvania / Manufacturing	Warrants (200,000 warrants, expiring 6/30/2017)		1,682	4,500	0.8
		Common Stock (545,107 shares)		5,086	12,267	2.3
				6.768	16,767	3.1
Yatesville Coal Holdings, Inc.(11)	Kentucky / Mining, Steel,	Senior Secured Note (15.72%, in non-accrual	10,000	10,000	10,000	1.9

	status effective 1/01/2009, due 12/31/2010)(4)				
Iron and Non-Precious Metals	Junior Secured Note (15.72%, in non-accrual status effective 1/01/2009, due 12/31/2010)(4)	38,463	38,463	3,097	0.6
and Coal Production	Common Stock (1,000 shares)		427	—	0.0
			48,890	13,097	2.5
	Total Control Investments		187,105	206,332	38.7

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS — (CONTINUED)
December 31, 2009 and June 30, 2009
(in thousands, except share data)

			June 30, 2009			
Portfolio Company	Locale / Industry	Investments(1)	Principal Value	Cost	Fair Value(2)	% of N Asset
LEVEL 3 INVESTMENTS:						
Affiliate Investments (5.00% to 24.99% voting control)						
Appalachian Energy Holdings LLC(12)	West Virginia / Construction Services	Senior Secured Debt – Tranche A (14.00% plus 3.00% PIK plus 3.00% default interest, in non-accrual status effective 11/01/2008, due 1/31/2011)	$ 1,997	$ 1,891	$ 2,052	0.4
		Senior Secured Debt – Tranche B (14.00% plus 3.00% PIK plus 3.00% default interest, in non-accrual status effective 11/01/2008, past due)	2,050	1,955	356	0.1
		Preferred Stock – Series A (200 units)		82	—	0.0
		Preferred Stock – Series B (241 units)		241	—	0.0
		Preferred Stock – Series C (500 units)		500	—	0.0
		Warrants (6,065 warrants, expiring 2/13/2016)		176	—	0.0
		Warrants (6,025 warrants, expiring 6/17/2018)		172	—	0.0
		Warrants (25,000 warrants, expiring 11/30/2018)		—	—	0.0
				5,017	2,408	0.5
Biotronic NeuroNetwork(17)	Michigan / Healthcare	Senior Secured Note (11.50% plus 1.00% PIK, due 2/21/2013)(3), (4)	26,227	26,227	27,007	5.1

		Preferred Stock (9,925 shares)(13)		2,300	2,839	0.5
				28,527	29,846	5.6
		Total Affiliate Investments		33,544	32,254	6.1
Non-control/Non-affiliate Investments (less than 5.00% of voting control)						
American Gilsonite Company	Utah / Specialty Minerals	Senior Subordinated Note (12.00% plus 3.00% PIK, due 3/14/2013)(3)	14,783	14,783	15,073	2.8
		Membership Interest Units in AGC/PEP, LLC (99.9999%)(16)		1,031	3,851	0.7
				15,814	18,924	3.5
Castro Cheese Company, Inc.	Texas / Food Products	Junior Secured Note (11.00% plus 2.00% PIK, due 2/28/2013)(3)	7,538	7,413	7,637	1.4
				7,413	7,637	1.4
Conquest Cherokee, LLC(6)	Tennessee / Oil & Gas Production	Senior Secured Note (13.00% plus 4.00% default interest, in non-accrual status effective 4/01/2009, past due)(4)	10,200	10,191	6,855	1.3
		Overriding Royalty Interests(19)		—	565	0.1
				10,191	7,420	1.4
Deb Shops, Inc.(17)	Pennsylvania / Retail	Second Lien Debt (8.67%, due 10/23/2014)	15,000	14,623	6,272	1.2
				14,623	6,272	1.2
Diamondback Operating, LP	Oklahoma / Oil & Gas Production	Net Profits Interest (15.00% payable on Equity distributions) (7)		—	458	0.1
				—	458	0.1
Freedom Marine Services LLC	Louisiana / Shipping Vessels	Subordinated Secured Note (12.00% plus 4.00% PIK, due 12/31/2011)(3)	7,234	7,160	7,152	1.4
		Net Profits Interest (22.50% payable on Equity distributions)(3), (7)		—	229	0.0
				7,160	7,381	1.4

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS — (CONTINUED)
December 31, 2009 and June 30, 2009
(in thousands, except share data)

				June 30, 2009		
Portfolio Company	Locale / Industry	Investments(1)	Principal Value	Cost	Fair Value(2)	% of Net Assets
LEVEL 3 INVESTMENTS:						
Non-control/Non-affiliate Investments (less than 5.00% of voting control)						
H&M Oil & Gas, LLC(3)	Texas / Oil & Gas Production	Senior Secured Note (13.00%, due 6/30/2010)(3)	$ 49,688	$ 49,688	$ 49,697	9.3
		Net Profits Interest (8.00% payable on Equity distributions)(3), (7)		—	1,682	0.3
				49,688	51,379	9.6
IEC Systems LP ("IEC") /Advanced Rig Services LLC ("ARS")	Texas / Oilfield Fabrication	IEC Senior Secured Note (12.00% plus 3.00% PIK, due 11/20/2012)(3), (4)	21,411	21,411	21,839	4.1
		ARS Senior Secured Note (12.00% plus 3.00% PIK, due 11/20/2012)(3), (4)	12,836	12,836	13,092	2.5
				34,247	34,931	6.6
Maverick Healthcare, LLC	Arizona / Healthcare	Second Lien Debt (12.00% plus 1.50% PIK, due 4/30/2014)(3)	12,691	12,691	12,816	2.4
		Preferred Units (1,250,000 units)		1,252	1,300	0.2
		Common Units (1,250,000 units)		—	—	0.0
				13,943	14,116	2.6
Miller Petroleum, Inc.	Tennessee / Oil & Gas Production	Warrants, Common Stock (1,935,523 warrants, expiring 5/04/2010 to 6/30/2014)(14)		150	241	0.1
				150	241	0.1
Peerless Manufacturing	Texas / Manufacturing	Subordinated Secured Note (11.50% plus 3.50%	20,000	20,000	20,400	3.8

		PIK, due 4/29/2013)(3)				
				20,000	20,400	3.8
Qualitest Pharmaceuticals, Inc.(17)	Alabama / Pharmaceuticals	Second Lien Debt (8.10%, due 4/30/2015)(3), (4)	12,000	11,949	11,452	2.2
				11,949	11,452	2.2
Regional Management Corp.	South Carolina / Financial Services	Second Lien Debt (12.00% plus 2.00% PIK, due 6/29/2012)(3)	25,424	25,424	23,073	4.3
				25,424	23,073	4.3
Resco Products, Inc.	Pennsylvania / Manufacturing	Second Lien Debt (8.67%, due 6/22/2014)(3), (4)	9,750	9,594	9,750	1.8
				9,594	9,750	1.8
Shearer's Foods, Inc.	Ohio / Food Products	Second Lien Debt (14.00%, due 10/31/2013)(3)	18,000	18,000	18,360	3.5
		Membership Interest Units in Mistral Chip Holdings, LLC (2,000 units)(18)		2,000	3,419	0.6
				20,000	21,779	4.1
Stryker Energy, LLC	Ohio / Oil & Gas Production	Subordinated Secured Revolving Credit Facility (12.00%, due 12/01/2011)(3), (4)	29,500	29,154	29,554	5.5
		Overriding Royalty Interests(19)		—	2,918	0.6
				29,154	32,472	6.1
TriZetto Group(17)	California / Healthcare	Subordinated Unsecured Note (12.00% plus 1.50% PIK, due 10/01/2016)(3)	15,205	15,065	16,331	3.1
				15,065	16,331	3.1
Unitek(17)	Pennsylvania / Technical Services	Second Lien Debt (13.08%, due 12/31/2013)(3), (4)	11,500	11,360	11,730	2.2
				11,360	11,730	2.2

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS — (CONTINUED)
December 31, 2009 and June 30, 2009
(in thousands, except share data)

Portfolio Company	Locale / Industry	Investments(1)	Principal Value	June 30, 2009 Cost	Fair Value(2)	% of Net Assets
LEVEL 3 INVESTMENTS:						
Non-control/Non-affiliate Investments (less than 5.00% of voting control)						
Wind River Resources Corp. and Wind River II Gas Corp.	Utah / Oil & Gas Production	Senior Secured Note (13.00% plus 3.00% default interest, in non-accrual status effective 12/01/2008, due 7/31/2010)(4)	$ 15,000	$ 15,000	$ 12,644	2.4
		Net Profits Interest (5.00% payable on Equity distributions)(7)		—	192	0.0
				15,000	12,836	2.4
		Total Non-Control/Non-Affiliate Investments		310,775	308,582	57.9
		Total Level 3 Portfolio Investments		531,424	547,168	102.7
LEVEL 2 INVESTMENTS:						
Money Market Funds						
Fidelity Institutional Money Market Funds — Government Portfolio (Class I)				94,753	94,753	17.8
Fidelity Institutional Money Market Funds — Government Portfolio (Class I)(3)				3,982	3,982	0.7
		Total Money Market Funds (Level 2 Investments)		98,735	98,735	18.5
		Total Investments		630,159	645,903	121.2

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS — (CONTINUED)
December 31, 2009 and June 30, 2009
(in thousands, except share data)

Endnote Explanations for the Consolidated Schedule of Investments as of December 31, 2009 and June 30, 2009

(1) The securities in which Prospect Capital Corporation ("we", "us" or "our") has invested were acquired in transactions that were exempt from registration under the Securities Act of 1933, as amended, or the "Securit Act." These securities may be resold only in transactions that are exempt from registration under the Securiti Act.

(2) Fair value is determined by or under the direction of our Board of Directors. As of December 31, 2009, two o our portfolio investments, Allied Defense Group, Inc. and Dover Saddlery, Inc., were publically traded and classified as Level 1 within the valuation hierarchy established by Accounting Standards Codification 820, F Value Measurements and Disclosures ("ASC 820"). As of December 31, 2009 and June 30, 2009, the fair val of our remaining portfolio investments was determined using significant unobservable inputs. ASC 820 class such inputs used to measure fair value as Level 3 within the valuation hierarchy. Our investments in money market funds are classified as Level 2. See Note 3 and Note 4 within the accompanying consolidated financia statements for further discussion.

(3) Security, or portion thereof, is held as collateral for the revolving credit facility (see Note 10). The market va of these investments at December 31, 2009 and June 30, 2009 were $339,012 and $434,069, respectively; the represent 50.5% and 67.2% of total investments at fair value, respectively.

(4) Floating rate loan. Stated interest rate was in effect at December 31, 2009 and June 30, 2009.

(5) There are several entities involved in the Biomass investment. We own 100 shares of common stock in Worcester Energy Holdings, Inc. ("WEHI"), representing 100% of the issued and outstanding common stock WEHI, in turn, owns 51 membership certificates in Biochips LLC ("Biochips"), which represents a 51% ownership stake.

We own 282 shares of common stock in Worcester Energy Co., Inc. ("WECO"), which represents 51% of the issued and outstanding common stock. We own directly 1,665 shares of common stock in Change Clean Ene Inc. ("CCEI"), f/k/a Worcester Energy Partners, Inc., which represents 51% of the issued and outstanding common stock and the remaining 49% is owned by WECO. CCEI owns 100 shares of common stock in Precision Logging and Landclearing, Inc. ("Precision"), which represents 100% of the issued and outstanding common stock.

During the quarter ended March 31, 2009, we created two new entities in anticipation of the foreclosure proceedings against the co-borrowers (WECO, CCEI and Biochips) Change Clean Energy Holdings, Inc. ("CCEHI") and DownEast Power Company, LLC ("DEPC"). We own 1,000 shares of CCEHI, representing 100% of the issued and outstanding stock, which in turn, owns a 100% of the membership interests in DEPC

On March 11, 2009, we foreclosed on the assets formerly held by CCEI and Biochips with a successful credi of $6,000 to acquire the assets. The assets were subsequently assigned to DEPC. WECO, CCEI and Biochips joint borrowers on the term note issued to Prospect Capital. Effective July 1, 2008, this loan was placed on non-accrual status.

Biochips, WECO, CCEI, Precision and WEHI currently have no material operations and no significant assets of June 30, 2009, our Board of Directors assessed a fair value of $0 for all of these equity positions and the lo position. We determined that the impairment of both CCEI and CCEHI as of June 30, 2009 was other than temporary and recorded a realized loss for the amount that the amortized cost exceeds the fair value at June 3 2009. Our Board of Directors set the value of the remaining CCEHI investment at $1,976 and $2,530 as of December 31, 2009 and June 30, 2009, respectively.

(6) During the three months ended December 31, 2009, we created two new entities, Coalbed Inc. and Coalbed L to foreclose on the outstanding senior secured loan and assigned rights and interests of Conquest Cherokee, L ("Conquest"), as a result of the deterioration of Conquest's financial performance and inability to service deb payments. We own 1,000 shares of common stock in Coalbed Inc., representing 100% of the issued and outstanding common stock. Coalbed Inc., in turn owns 100% of the membership interest in Coalbed LLC.

On October 21, 2009, Coalbed LLC foreclosed on the loan formerly made to Conquest. As of December 31, 2009, our Board of Directors assessed a fair value of $3,686 for the equity and the loan position in Coalbed L

(7) In addition to the stated returns, the net profits interest held will be realized upon sale of the borrower or a sa of the interests.

(8) Gas Solutions Holdings, Inc. is a wholly-owned investment of us.

(9) Entity was formed as a result of the debt restructuring of ESA Environmental Specialist, Inc. In early 2009, foreclosed on the two loans on non-accrual status and purchased the underlying personal and real property. V own 1,000 shares of common stock in The Healing Staff ("THS"), f/k/a Lisamarie Fallon, Inc. representing 100% ownership. We own 1,500 shares of Vets Securing America, Inc. ("VSA"), representing 100% owners VSA is a holding company for the real property of Integrated Contract Services, Inc. ("ICS") purchased duri the foreclosure process.

(10) Loan is with THS an affiliate of ICS.

(11) On June 30, 2008, we consolidated our holdings in four coal companies into Yatesville Coal Holdings, Inc. ("Yatesville"), and consolidated the operations under one management team. As part of the transaction, the d that we held of C&A Construction, Inc. ("C&A"), Genesis Coal Corp. ("Genesis"), North Fork Collieries LL ("North Fork") and Unity Virginia Holdings LLC ("Unity") were exchanged for newly issued debt from Yatesville, and our ownership interests in C&A, E&L Construction, Inc. ("E&L"), Whymore Coal Company Inc. ("Whymore"), Genesis and North Fork were exchanged for 100% of the equity of Yatesville. This reorganization allows for a better utilization of the assets in the consolidated group. Genesis Coal Corp. ("Genesis"), was not part of the transaction.

At December 31, 2009 and at June 30, 2009, Yatesville owned 100% of the membership interest of North Fo In addition, Yatesville held a $9,325 and $8,062, respectively, note receivable from North Fork as of those t respective dates.

At December 31, 2009 and at June 30, 2009, Yatesville owned 90% and 87%, respectively, of the common stock of Genesis and held a note receivable of $20,897 and $20,802, respectively, as of those two respective dates.

Yatesville held a note receivable of $4,261 from Unity at December 31, 2009 and at June 30, 2009.

There are several entities involved in Yatesville's investment in Whymore at June 30, 2009. As of June 30, 2009, Yatesville owned 10,000 shares of common stock or 100% of the equity and held a $14,973 senior secured debt receivable from C&A, which owns the equipment. Yatesville owned 10,000 shares of common stock or 100% of the equity of E&L, which leases the equipment from C&A, employs the workers, is listed the operator with the Commonwealth of Kentucky, mines the coal, receives revenues and pays all operating expenses. Yatesville owned 4,900 shares of common stock or 49% of the equity of Whymore, which applies and holds permits on behalf of E&L. Yatesville also owned 4,285 Series A convertible preferred shares in ea of C&A, E&L and Whymore. Whymore and E&L are guarantors under the C&A credit agreement with Yatesville.

In August 2009, Yatesville sold its 49% ownership interest in the common shares of Whymore to the 51% holder of the Whymore common shares ("Whymore Purchaser"). All reclamation liability was transferred to Whymore Purchaser. In September 2009, Yatesville completed an auction for all of its equipment.

Yatesville currently has no material operations. As of December 31, 2009, our Board of Directors determine that the impairment of Yatesville was other than temporary and we recorded a realized loss for the amount th the amortized cost exceeds the fair value. Our Board of Directors set the value of the remaining Yatesville investment at $1,035 as of December 31, 2009.

(12) There are several entities involved in the Appalachian Energy Holdings LLC ("AEH") investment. We own warrants, the exercise of which will permit us to purchase 37,090 Class A common units of AEH at a nomin cost and in near-immediate fashion. We own 200 units of Series A preferred equity, 241 units of Series B preferred equity, and 500 units of Series C preferred equity of AEH. The senior secured notes are with C&S Operating LLC and East Cumberland L.L.C., both operating companies owned by AEH.

(13) On a fully diluted basis represents, 11.677% of voting common shares.

(14) Total common shares outstanding of 19,310,956 as of December 9, 2009 from Miller Petroleum, Inc.'s Quar Report on Form 10-Q filed on December 21, 2009 as applicable to our December 31, 2009 reporting date. T common shares outstanding of 15,811,856 as of March 11, 2009 from Miller's Quarterly Report on Form 10 filed on March 16, 2009.

(15) A portion of the positions listed were issued by an affiliate of the portfolio company.

(16) We own 99.9999% of AGC/PEP, LLC. AGC/PEP, LLC owns 2,038 out of a total of 83,639 shares (includin 4,932 vested an unvested management options) of American Gilsonite Holding Company which owns 100% American Gilsonite Company.

(17) Syndicated investment which had been originated by another financial institution and broadly distributed.

(18) Mistral Chip Holdings, LLC owns 44,800 shares out of 50,650 total shares outstanding of Chip Holdings, In
the parent company of Shearer's Foods, Inc., before adjusting for management options.

(19) The overriding royalty interests held receive payments at the stated rates based upon operations of the borro

(20) On December 31, 2009, we sold our investment in Aylward Enterprises, LLC. AWCNC, LLC is the remaini
holding company with zero assets and our remaining outstanding debt has no value of December 31, 2009

.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2009
(Unaudited)
(In thousands, except share and per share data)

Note 1. Organization

References herein to "we", "us" or "our" refer to Prospect Capital Corporation ("Prospect") and its subsidiary unless the co specifically requires otherwise.

We were formerly known as Prospect Energy Corporation, a Maryland corporation. We were organized on April 13, 200 were funded in an initial public offering ("IPO"), completed on July 27, 2004. We are a closed-end investment company th filed an election to be treated as a Business Development Company ("BDC"), under the Investment Company Act of 194 "1940 Act"). As a BDC, we have qualified and have elected to be treated as a regulated investment company ("RIC"), Subchapter M of the Internal Revenue Code. We invest primarily in senior and subordinated debt and equity of compan need of capital for acquisitions, divestitures, growth, development, project financings, recapitalizations, and other purposes

On May 15, 2007, we formed a wholly-owned subsidiary, Prospect Capital Funding, LLC, a Delaware limited lia company, for the purpose of holding certain of our loan investments in the portfolio which are used as collateral for our facility.

Note 2. Patriot Acquisition

On December 2, 2009, we acquired the outstanding shares of Patriot Capital Funding, Inc. ("Patriot") common stoc $201,083. Under the terms of the merger agreement, Patriot common shareholders received 0.363992 shares of our co stock for each share of Patriot common stock, resulting in 8,444,068 shares of common stock being issued by us. In conn with the transaction, we repaid all the outstanding borrowings of Patriot, in compliance with the merger agreement.

On December 2, 2009, Patriot made a final dividend payment equal to its undistributed net ordinary income and capital ga $0.38 per share. In accordance with a recent IRS revenue procedure, the dividend was paid 10% in cash and 90% in issued shares of Patriot's common stock. The exchange ratio was adjusted to give effect to the final income distribution.

The merger has been accounted for as an acquisition of Patriot by Prospect in accordance with acquisition method of accou as detailed in ASC 805, Business Combinations ("ASC 805"). The fair value of the consideration paid was allocated assets acquired and liabilities assumed based on their fair values as of the date of acquisition. As described in more de ASC 805, goodwill, if any, would have been recognized as of the acquisition date, if the consideration transferred exceed fair value of identifiable net assets acquired. As of the acquisition date, the fair value of the identifiable net assets ac exceeded the fair value of the consideration transferred, and we recognized the excess as a gain. A gain of $5,714 was rec by Prospect in the quarter ended December 31, 2009 related to the acquisition of Patriot. The acquisition of Patrio negotiated in July 2009 with the purchase agreement being signed on August 3, 2009. Between July 2009 and Decem 2009, our valuation of certain of the investments acquired from Patriot increased due to market improvement, which resul the recognition of the gain at closing.

Preliminary Purchase Price Allocation

The purchase price has been allocated to the assets acquired and the liabilities assumed based on their estimated fair valu
summarized in the following table:

Cash (to repay Patriot debt)	$ 107,313
Cash (to fund purchase of restricted stock from former Patriot employees)	970
Common stock issued (1)	92,800
Total purchase price	201,083
Assets acquired:	
Investments (2)	207,126
Cash and cash equivalents	1,697
Other assets	3,859
Assets acquired	212,682
Other liabilities assumed	(5,885
Net assets acquired	206,797
Preliminary gain on Patriot acquisition (3)	$ 5,714

(1) The value of the shares of common stock exchanged with the Patriot common shareholders was based upon the closing of our common stock on December 2, 2009, the price immediately prior to the closing of the transaction.

(2) The fair value of Patriot's investments were determined by the Board of Directors in conjunction with an independent valuation agent. This valuation resulted in a purchase price which was $98,150 below the amortized cost of such investments. For those assets which are performing, Prospect will record the accretion to par value in interest income o the remaining term of the investment.

(3) The preliminary gain has been determined based upon the estimated value of certain liabilities which are not yet settled Any changes to such accruals will be recoded in future periods as an adjustment to such gain. We do not believe such adjustments will be material.

Preliminary Condensed Statement of Net Assets Acquired

The following condensed statement of net assets acquired reflects the preliminary values assigned to Patriot's net assets as acquisition date, December 2, 2009.

Investment securities	$ 207,126
Cash and cash equivalents	1,697
Other assets	3,859
Total assets	212,682
Other liabilities	(5,885
Preliminary fair value of net assets acquired	$ 206,797

The following unaudited pro forma condensed combined financial information does not purport to be indicative of a financial position or results of our operations had the Patriot acquisition actually been consummated at the beginning of period presented. Certain one-time charges have been eliminated. The pro forma adjustments reflecting the allocation

purchase price of Patriot and the gain of $5,714 recognized on the Patriot Acquisition have been eliminated from all pe
presented. Management expects to realize net operating synergies from this transaction. The pro forma condensed com
financial information does not reflect the potential impact of these synergies and does not reflect any impact of addi
accretion which would have been recognized on the transaction, except for that which was recorded after the transactio
consummated on December 2, 2009.

	Three months ended December 31,		Six months ended December 31,	
	2009	2008	2009	2008
Total Investment Income	$ 30,730	$ 32,384	$ 60,298	$ 78,412
Net Investment Income	18,098	16,392	31,812	44,953
Net Increase (Decrease) in Net Assets Resulting from Operations	(15,901)	(11,944)	(26,766)	239
Net Increase (Decrease) in Net Assets Resulting from Operations per share	(0.25)	(0.23)	(0.44)	0.00

Note 3. Significant Accounting Policies

The following are significant accounting policies consistently applied by us:

Basis of Presentation

The accompanying interim financial statements, which are not audited, have been prepared in accordance with accou principles generally accepted in the United States of America ("GAAP") for interim financial information and pursuant requirements for reporting on Form 10-Q and Article 6 and 10 of Regulation S-X, as appropriate.

Use of Estimates

The preparation of GAAP financial statements requires us to make estimates and assumptions that affect the reported am of assets and liabilities at the date of the financial statements and the reported amounts of income and expenses durin reported period. Changes in the economic environment, financial markets, creditworthiness of our portfolio companies an other parameters used in determining these estimates could cause actual results to differ, and these differences cou material.

Basis of Consolidation

Under the 1940 Act rules, the regulations pursuant to Article 6 of Regulation S-X and the American Institute of Certified Accountants' Audit and Accounting Guide for Investment Companies, we are precluded from consolidating any entity than another investment company or an operating company which provides substantially all of its services and benefits Our financial statements include our accounts and the accounts of Prospect Capital Funding, LLC, our only wholly-ov closely-managed subsidiary that is also an investment company. All intercompany balances and transactions have eliminated in consolidation.

Investment Classification

We are a non-diversified company within the meaning of the 1940 Act. We classify our investments by level of contro defined in the 1940 Act, control investments are those where there is the ability or power to exercise a controlling infl

over the management or policies of a company. Control is generally deemed to exist when a company or individual posses
has the right to acquire within 60 days or less, a beneficial ownership of 25% or more of the voting securities of an inv
company. Affiliated investments and affiliated companies are defined by a lesser degree of influence and are deemed to
through the possession outright or via the right to acquire within 60 days or less, beneficial ownership of 5% or more
outstanding voting securities of another person.

Investments are recognized when we assume an obligation to acquire a financial instrument and assume the risks for ga losses related to that instrument. Investments are derecognized when we assume an obligation to sell a financial instrume forego the risks for gains or losses related to that instrument. Specifically, we record all security transactions on a trad basis. Investments in other, non-security financial instruments are recorded on the basis of subscription date or redemption as applicable. Amounts for investments recognized or derecognized but not yet settled are reported as receivabl investments sold and payables for investments purchased, respectively, in the Consolidated Statements of Assets and Liabi

Investment Risks

The Company's investments are subject to a variety of risks. Those risks include the following:

Market Risk

Market risk represents the potential loss that can be caused by a change in the fair value of the financial instrument.

Credit Risk

Credit risk represents the risk that the Partnership would incur if the counterparties failed to perform pursuant to the te their agreements with the Partnership.

Liquidity Risk

Liquidity risk represents the possibility that the Partnership may not be able to rapidly adjust the size of its positions in ti high volatility and financial stress at a reasonable price.

Interest Rate Risk

Interest rate risk represents a change in interest rates, which could result in an adverse change in the fair value interest-bearing financial instrument.

Prepayment Risk

Most of the Company's debt investments allow for prepayment of principal without penalty. Downward changes in interes may cause prepayments to occur at a faster than expected rate, thereby effectively shortening the maturity of the securit making the security less likely to be an income producing instrument.

Investment Valuation

Our Board of Directors has established procedures for the valuation of our investment portfolio. These procedures are de below. Investments for which market quotations are readily available are valued at such market quotations.

For most of our investments, market quotations are not available. With respect to investments for which market quotatio
not readily available or when such market quotations are deemed not to represent fair value, our Board of Directo
approved a multi-step valuation process each quarter, as described below:

(1) Each portfolio company or investment is reviewed by our investment professionals with the independent valuation fir

(2) the independent valuation firm engaged by our Board of Directors conducts independent appraisals and makes thei independent assessment;

(3) the audit committee of our Board of Directors reviews and discusses the preliminary valuation of our Inves Adviser and that of the independent valuation firm; and

(4) the Board of Directors discusses valuations and determines the fair value of each investment in our portfolio in gooc based on the input of our Investment Adviser, the respective independent valuation firm and the audit committee.

Investments are valued utilizing a market approach, an income approach, or both approaches, as appropriate. The m approach uses prices and other relevant information generated by market transactions involving identical or comparable or liabilities (including a business). The income approach uses valuation techniques to convert future amounts (for exa cash flows or earnings) to a single present value amount (discounted) calculated based on an appropriate discount rate measurement is based on the net present value indicated by current market expectations about those future amour following these approaches, the types of factors that we may take into account in fair value pricing our investments inclu relevant: available current market data, including relevant and applicable market trading and transaction compara applicable market yields and multiples, security covenants, call protection provisions, information rights, the natur realizable value of any collateral, the portfolio company's ability to make payments, its earnings and discounted cash flow markets in which the portfolio company does business, comparisons of financial ratios of peer companies that are public, comparables, the principal market and enterprise values, among other factors.

In September 2006, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Codification ("A 820, Fair Value Measurements and Disclosures ("ASC 820"). ASC 820 defines fair value, establishes a framewor measuring fair value in GAAP, and expands disclosures about fair value measurements. We adopted ASC 820 on a prosp basis beginning in the quarter ended September 30, 2008.

ASC 820 classifies the inputs used to measure these fair values into the following hierarchy:

Level 1: Quoted prices in active markets for identical assets or liabilities, accessible by us at the measurement date.

Level 2: Quoted prices for similar assets or liabilities in active markets, or quoted prices for identical or similar ass liabilities in markets that are not active, or other observable inputs other than quoted prices.

Level 3: Unobservable inputs for the asset or liability.

In all cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has determined based on the lowest level of input that is significant to the fair value measurement. Our assessment c significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors spec each investment. The changes to GAAP from the application of ASC 820 relate to the definition of fair value, framewo measuring fair value, and the expanded disclosures about fair value measurements. ASC 820 applies to fair value measure

already required or permitted by other standards. In accordance with ASC 820, the fair value of our investments is defin
the price that we would receive upon selling an investment in an orderly transaction to an independent buyer in the princi
most advantageous market in which that investment is transacted.

In April 2009, the FASB issued ASC Subtopic 820-10-65, Determining Fair Value When the Volume and Level of Activi
the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly" ("ASC 820-10")
update provides further clarification for ASC 820 in markets that are not active and provides additional guidanc
determining when the volume of trading level of activity for an asset or liability has

significantly decreased and for identifying circumstances that indicate a transaction is not orderly. ASC 820-10-65 is effe
for interim and annual reporting periods ending after June 15, 2009. The adoption of ASC 820-10-65 for the three an
months ended December 31, 2009, did not have any effect on our net asset value, financial position or results of operatio
there was no change to the fair value measurement principles set forth in ASC 820.

Valuation of Other Financial Assets and Financial Liabilities

In February 2007, FASB issued ASC Subtopic 820-10-05-1, The Fair Value Option for Financial Assets and Fina
Liabilities ("ASC 820-10-05-1"). ASC 820-10-05-1 permits an entity to elect fair value as the initial and subse
measurement attribute for many of assets and liabilities for which the fair value option has been elected and similar asse
liabilities measured using another measurement attribute. We adopted this statement on July 1, 2008 and have elected
value other assets and liabilities at fair value as would be permitted by ASC 820-10-05-1.

Revenue Recognition

Realized gains or losses on the sale of investments are calculated using the specific identification method.

Interest income, adjusted for amortization of premium and accretion of discount, is recorded on an accrual basis. Origin
closing and/or commitment fees associated with investments in portfolio companies are accreted into interest income ov
respective terms of the applicable loans. Accretion of such purchase discounts or premiums is calculated by the effective in
method as of the purchase date and adjusted only for material amendments or prepayments. Upon the prepayment of a lo
debt security, any prepayment penalties and unamortized loan origination, closing and commitment fees are recorded as in
income. The purchase discount for portfolio investments acquired from Patriot was determined based on the difference be
par value and fair market value as of December 2, 2009, and will continue to accrete until maturity or repayment o
respective loans.

Dividend income is recorded on the ex-dividend date.

Structuring fees and similar fees are recognized as income as earned, usually when paid. Structuring fees, excess deal dep
net profits interests and overriding royalty interests are included in other income.

Loans are placed on non-accrual status when principal or interest payments are past due 90 days or more or when th
reasonable doubt that principal or interest will be collected. Accrued interest is generally reversed when a loan is plac
non-accrual status. Interest payments received on non-accrual loans may be recognized as income or applied to prin
depending upon management's judgment. Non-accrual loans are restored to accrual status when past due principal and inte
paid and in management's judgment, are likely to remain current.

Federal and State Income Taxes

We have elected to be treated as a regulated investment company and intend to continue to comply with the requirements
Internal Revenue Code of 1986 (the "Code"), applicable to regulated investment companies. We are required to distrib

least 90% of our investment company taxable income and intend to distribute (or retain through a deemed distribution) all o
investment company taxable income and net capital gain to stockholders; therefore, we have made no provision for in
taxes. The character of income and gains that we will distribute is determined in accordance with income tax regulation
may differ from GAAP. Book and tax basis differences relating to stockholder dividends and distributions and other perm
book and tax differences are reclassified to paid-in capital.

If we do not distribute (or are not deemed to have distributed) at least 98% of our annual taxable income in the calendar y
is earned, we will generally be required to pay an excise tax equal to 4% of the amount by which 98% of our annual ta
income exceeds the distributions from such taxable income for the year. To the extent that we determine that our esti
current year annual taxable income will be in excess of estimated current year dividend distributions from such taxable in
we accrue excise taxes, if any, on estimated excess taxable income as taxable income is earned using an annual effective e
tax rate. The annual effective excise tax rate is determined by dividing the estimated annual excise tax by the estimated a
taxable income.

We adopted FASB ASC 740, Income Taxes ("ASC 740"). ASC 740 provides guidance for how uncertain tax positions s
be recognized, measured, presented, and disclosed in the financial statements. ASC 740 requires the evaluation of tax pos
taken or expected to be taken in the course of preparing our tax returns to determine whether the tax positio
"more-likely-than-not" of being sustained by the applicable tax authority. Tax positions not deemed to me
more-likely-than-not threshold are recorded as a tax benefit or expense in the current year. Adoption of ASC 740 was appl
all open tax years as of July 1, 2007. The adoption of ASC 740 did not have an effect on our net asset value, financial con
or results of operations as there was no liability for unrecognized tax benefits and no change to our beginning net asset valu
of December 31, 2009 and for the three and six months then ended, we did not have a liability for any unrecognize
benefits. Management's determinations regarding ASC 740 may be subject to review and adjustment at a later date based
factors including, but not limited to, an on-going analysis of tax laws, regulations and interpretations thereof.

Dividends and Distributions

Dividends and distributions to common stockholders are recorded on the ex-dividend date. The amount, if any, to be pai
dividend or distribution is approved by our Board of Directors each quarter and is generally based upon our manage
estimate of our earnings for the quarter. Net realized capital gains, if any, are distributed at least annually.

Financing Costs

We record origination expenses related to our credit facility as deferred financing costs. These expenses are deferre
amortized as part of interest expense using the effective interest method over the stated life of the facility.

We record registration expenses related to shelf filings as prepaid assets. These expenses consist principally of Securitie
Exchange Commission ("SEC") registration fees, legal fees and accounting fees incurred. These prepaid assets will be ch
to capital upon the receipt of an equity offering proceeds or charged to expense if no offering completed.

Guarantees and Indemnification Agreements

We follow FASB ASC 460, Guarantees ("ASC 460"). ASC 460 elaborates on the disclosure requirements of a guarantor
interim and annual financial statements about its obligations under certain guarantees that it has issued. It also requ
guarantor to recognize, at the inception of a guarantee, for those guarantees that are covered by ASC 460, the fair value
obligation undertaken in issuing certain guarantees. ASC 460 did not have a material effect on the financial statements. Re
Note 4, Note 8 and Note 11 for further discussion of guarantees and indemnification agreements.

Per Share Information

Net increase or decrease in net assets resulting from operations per common share are calculated using the weighted av
number of common shares outstanding for the period presented. Diluted net increase or decrease in net assets resulting
operations per share are not presented as there are no potentially dilutive securities outstanding.

Subsequent Events

In May 2009, the FASB issued ASC 855, Subsequent Events ("ASC 855"). ASC 855 establishes general standar accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued available to be issued. The standard, which includes a new required disclosure of the date through which an entity has eval subsequent events, is effective for interim or annual periods ending after June 15, 2009. We evaluated all events or transa that occurred after December 31, 2009 up through February 26, 2010, the date we issued the accompanying fina statements. During this period, we did not have any material recognizable subsequent events other than those disclosed financial statements.

Recent Accounting Pronouncements

In June 2009, the FASB issued ASC 105, Generally Accepted Accounting Principles ("ASC 105"), which establishes the Codification which supersedes all existing accounting standard documents and will become the single source of authori non-governmental U.S. GAAP. All other accounting literature not included in the Codification will be consi non-authoritative. The Codification did not change GAAP but reorganizes the literature. ASC 105 is effective for interi annual periods ending after September 15, 2009. We have conformed our financial statements and related Notes to th Codification for the quarter ended December 31, 2009.

In June 2009, the FASB issued ASC 860, Accounting for Transfers of Financial Assets — an amendment to FAS 14 860"). ASC 860 improves the relevance, representational faithfulness, and comparability of the information that a rep entity provides in its financial statements about a transfer of financial assets: the effects of a transfer on its financial pos financial performance, and cash flows: and a transferor's continuing involvement, if any, in transferred financial assets. 860 is effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafte management does not believe that the adoption of the amended guidance in ASC 860 will have a significant effect o financial statements.

In June 2009, the FASB issued ASC 810, Amendments to FASB Interpretation No. 46(R) ("ASC 810"). ASC 810 is inten (1) address the effects on certain provisions of FASB Interpretation No. 46 (revised December 2003), Consolidation of Va Interest Entities, as a result of the elimination of the qualifying special-purpose entity concept in ASC 860, and (2) const concerns about the application of certain key provisions of Interpretation 46(R), including those in which the accountin disclosures under the Interpretation do not always provided timely and useful information about an enterprise's involveme variable interest entity. ASC 810 is effective as of the beginning of our first annual reporting period that begins after Nov 15, 2009. Our management does not believe that the adoption of the amended guidance in ASC 860 will have a signi effect on our financial statements.

In August 2009, the FASB issued Accounting Standards Update ("ASU") 2009-05, Measuring Liabilities at Fair Val amend FASB Accounting Standards Codification ASC 820, Fair Value Measurements and Disclosures ("ASC 820"), to c how entities should estimate the fair value of liabilities. ASC 820, as amended, includes clarifying guidance for circumst in which a quoted price in an active market is not available, the effect of the existence of liability transfer restrictions, a effect of quoted prices for the identical liability, including when the identical liability is traded as an asset. We adopted 2009-05 effective October 1, 2009. The amended guidance in ASC 820 does not have a significant effect on our fin statements for the quarter ended December 31, 2009.

In September 2009, the FASB issued ASU 2009-12, Measuring Fair Value of Certain Investments ("ASU 2009-12") update provides further amendments to ASC 820 to offer investors a practical expedient for measuring the fair val investments in certain entities that calculate net asset value per share. Specifically, measurement using net asset value per is reasonable for investments within the scope of ASU 2009-12. We adopted ASU 2009-12

effective October 1, 2009. The amended guidance in ASC 820 does not have a significant effect on our financial statemen
the quarter ended December 31, 2009.

In January 2010, the FASB issued Accounting Standards Update 2010-06, Fair Value Measurements and Disclosures (
820): Improving Disclosures about Fair Value Measurements ("ASC 2010-06"). ASU 2010-06 amends ASC 820-1
clarifies and provides additional disclosure requirements related to recurring and non-recurring fair value measuremen
employers' disclosures about postretirement benefit plan assets. ASU 2010-06 is effective for interim and annual rep
periods beginning after December 15, 2009. Our management does not believe that the adoption of the amended guida
ASC 820-10 will have a significant effect on our financial statements.

Note 4. Portfolio Investments

At December 31, 2009, we had invested in 55 long-term portfolio investments, which had an amortized cost of $633,636 a
fair value of $648,135. At June 30, 2009, we had invested in 30 long-term portfolio investments, which had an amortized c
$531,424 and a fair value of $547,168.

As of December 31, 2009, we own controlling interests in Ajax Rolled Ring & Machine ("Ajax"), AWCNC, LLC.
Cladding, LLC ("C&J"), Change Clean Energy Holdings, Inc. ("CCEHI"), Coalbed, Inc./Coalbed, LLC (formerly Co
Cherokee, LLC) ("Coalbed"), Fischbein, LLC ("Fischbein"), Freedom Marine Services LLC ("Freedom Marine")
Solutions Holdings, Inc. ("GSHI"), Integrated Contract Services, Inc. ("ICS"), Iron Horse Coiled Tubing, Inc. ("Iron Ho
NRG Manufacturing, Inc. ("NRG"), Nupla Corporation ("Nupla"), R-V Industries, Inc. ("R-V"), Sidump'r Trailer Com
Inc. ("Sidump'r") and Yatesville Coal Holdings, Inc. ("Yatesville"). We also own an affiliated interest in Appalachian E
Holdings, LLC ("AEH"), Biotronic NeuroNetwork ("Biotronic"), Boxercraft Incorporated ("Boxercraft"), KTPS Holdings
("KTPS"), Miller Petroleum, Inc. ("Miller"), Smart, LLC ("Smart") and Sport Helmets Holdings, LLC ("Sport Helmets").

The fair values of our portfolio investments as of December 31, 2009 disaggregated into the three levels of the AS
valuation hierarchy are as follows:

	Quoted Prices in Active Markets for Identical Securities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Investments at fair value				
Control investments	$ —	$ —	$ 191,898	$ 191,89
Affiliate investments	—	—	66,479	66,479
Non-control/non-affiliate investments	118	—	389,640	389,75
	118	—	648,017	648,13
Investments in money market funds	—	23,418	—	23,418
Total assets reported at fair value	$ 118	$ 23,418	$ 648,017	$ 671,55

The aggregate values of Level 3 portfolio investments changed during the six months ended December 31, 2009 as follows

	Fair Value Measurements Using Unobservable Inputs (Leve			
	Control Investments	Affiliate Investments	Non-Control/ Non-Affiliate Investments	Total
Fair value as of June 30, 2009	$ 206,332	$ 32,254	$ 308,582	$ 547,16
Total realized losses	(51,229)	—	—	(51,229

Change in unrealized appreciation (depreciation)	7,390	(283)	(7,209)	(102
Assets acquired in the Patriot acquisition	10,534	36,400	160,073	207,007
Purchases of portfolio investments	5,854	—	1,467	7,321
Payment-in-kind interest	725	193	1,141	2,059
Accretion of original issue discount	3,343	281	3,046	6,670
Dispositions of portfolio investments	(8,733)	(2,516)	(59,628)	(70,877
Transfers within Level 3	17,682	150	(17,832)	—
Transfers in (out) of Level 3	—	—	—	—
Fair value as of December 31, 2009	$ 191,898	$ 66,479	$ 389,640	$ 648,017

(1) Relates to assets held at December 31, 2009.

As of December 31, 2009, the valuation methodology for Ajax changed from a discounted cash flow analysis to an ente and equity valuation. The independent valuation agent proposed this adjustment due to our controlling equity interest in As a result, and combined with declining financial results, the fair market value of Ajax decreased from $31,638 to $25,8 of June 30, 2009 and December 31, 2009, respectively. There were no other material changes to our valuation methodology

At December 31, 2009, nine loan investments were on non-accrual status: AEH, Coalbed, Deb Shops, ICS, Iron Horse, N Sidump'r, Wind River Resources Corp. and Wind River II Corp. ("Wind River"), and Yatesville. At June 30, 2009, five investments were on non-accrual status: AEH, Coalbed, ICS, Wind River and Yatesville. The loan principal of these amounted to $146,376 and $92,513 as of December 31, 2009 and June 30, 2009, respectively. The fair values of investments represent approximately 5.7% and 7.3% of our net assets as of December 31, 2009 and June 30, 2009, respect For the three months ended December 31, 2009 and December 31, 2008, the income foregone as a result of not accruing in on non-accrual debt investments amounted to $8,052 and $2,528, respectively. For the six months ended December 31, and December 31, 2008, the income foregone as a result of not accruing interest on non-accrual debt investments amoun $12,510 and $4,983, respectively. At December 31, 2009, we held one asset on which payment of interest was past-due than 90 days for which we continue to accrue interest, H&M Oil and Gas, LLC. The principal balance of this loan is $4 and the accrued interest receivable is $2,744 at December 31, 2009. We expect full repayment of principal and interest o loan.

During the three months ended December 31, 2009, we discontinued operations at Yatesville. As of December 31, consistent with the decision to discontinue operations, we determined that the impairment of Yatesville other-than-temporary and recorded a realized loss of $51,228 for the amount that the amortized cost exceeded the fair n value. As of December 31, 2009 and June 30, 2009, Yatesville is valued at $1,035 and $13,097, respectively.

GSHI has indemnified us against any legal action arising from its investment in Gas Solutions, LP. We have inc approximately $2,093 from the inception of the investment in GSHI through December 31, 2009 for fees associated with a action, and GSHI has reimbursed us for the entire amount. Of the $2,093 reimbursement, $41 and $182 was reflect dividend income: control investments in the Consolidated Statements of Operations for the three and six months e December 31, 2008, respectively. There were no such legal fees incurred or reimbursed for the three and six months e December 31, 2009. Additionally, certain other expenses incurred by us which are attributable to GSHI have been reimb by GSHI and are reflected as dividend income: control investments in the Consolidated Statements of Operations. For the months ended December 31, 2009 and December 31, 2008, such reimbursements totaled as $800 and $1,895, respectivel the six months ended December 31, 2009 and December 31, 2008, such reimbursements totaled as $2,031and $3 respectively.

The original cost basis of debt placements and equity securities acquired (including purchases of portfolio investm
follow-on investments and payment-in-kind interest) totaled to approximately $210,438 and $13,564

during the three months ended December 31, 2009 and December 31, 2008, respectively. These placements and acquis
totaled to approximately $216,506 and $84,020 during the six months ended December 31, 2009 and December 31,
respectively. The $210,438 and $216,506 for the three and six months ended December 31, 2009, respectively, in
$207,126 of portfolio investments acquired from Patriot. Debt repayments and sales of equity securities with a cost ba
approximately $45,494 and $2,112 were received during the three months ended December 31, 2009 and December 31,
respectively. These repayments and sales amounted to $69,735 and $11,416 during the six months ended December 31,
and December 31, 2008, respectively.

Note 5. Other Investment Income

Other investment income consists of the gain on our acquisition of Patriot, structuring and amendment fees, overriding ro
interests, settlement of net profit interests, deal deposits, administrative agent fee, and other miscellaneous and sundry
receipts. Income from such sources for the three and six months ended December 31, 2009 and December 31, 2008 w
follows:

Income Source	For The Three Months Ended December 31, 2009	2008	For The Six Months End December 31, 2009	2008
Gain on Patriot acquisition	$ 5,714	$ —	$ 5,714	$ —
Structuring and amendment fees	398	87	803	774
Overriding royalty interests	44	173	88	331
Settlement of net profits interests	10	—	10	12,576
Miscellaneous	8	47	23	146
Other Investment Income	$ 6,174	$ 307	$ 6,638	$ 13,827

Note 6. Equity Offerings and Related Expenses

We issued 11,437,797 shares of our common stock in public and private offerings during the six months ended December,
We did not issue any common stock during the six months ended December 31, 2008. The proceeds raised, the related
underwriting fees, the offering expenses and the prices at which these shares were issued are as follows:

Issuances of Common Stock	Number of Shares Issued	Offering Price	Gross Proceeds Raised	Underwriting Fees	Offerin Expens
July 7, 2009	5,175,000	$ 9.000	$ 46,575	$ 2,329	$ 200
August 20, 2009 (1)	3,449,686	$ 8.500	$ 29,322	—	$ 117
September 24, 2009 (1)	2,807,111	$ 9.000	$ 25,264	—	$ 840

(1) Concurrent with the sale of these shares, we entered into a registration rights agreement in which we granted the purch
certain registration rights with respect to the shares. We have filed with the SEC a post-effective amendment
registration statement on Form N-2 which has been declared effective by the SEC.

Our shareholders' equity accounts at December 31, 2009 and June 30, 2009 reflect cumulative shares issued as of
respective dates. Our common stock has been issued through public offerings, a registered direct offering, private offering
exercise of over-allotment options on the part of the underwriters, our dividend reinvestment plan and business combina
When our common stock is issued, the related offering expenses have been charged against paid-in capital in excess of pa
underwriting fees and offering expenses were borne by us.

On December 2, 2009, we issued 8,444,068 shares of common stock to acquire Patriot. This transaction is described in f
detail in Note 2.

On July 20, 2009 and October 19, 2009, we issued shares of our common stock in connection with the dividend reinves
plan of 297,274 and 233,523, respectively.

On October 9, 2008, our Board of Directors approved a share repurchase plan under which we may repurchase up to $20,0
our common stock at prices below our net asset value as reported in our financial statements published for the year ended
30, 2008. We have not made any purchases of our common stock during the period from October 9, 2008 to December 31,
pursuant to this plan.

Note 7. Net Decrease (Increase) in Net Assets per Common Share

The following information sets forth the computation of net (decrease) increase in net assets resulting from operation
common share for the three and six months ended December 31, 2009 and December 31, 2008, respectively.

	For The Three Months Ended December 31,		For The Six Months Ende December 31,	
	2009	2008	2009	2008
Net (decrease) increase in net assets resulting from operations	$ (16,853)	$ 6,524	$ (23,231)	$ 20,522
Weighted average common shares outstanding	57,613,489	29,618,762	53,709,197	29,569,5
Net (decrease) increase in net assets resulting from operations per common share	$ (0.29)	$ 0.22	$ (0.43)	$ 0.69

Note 8. Related Party Agreements and Transactions

Investment Advisory Agreement

We have entered into an investment advisory and management agreement with Prospect Capital Management (the "Inves
Advisory Agreement") under which the Investment Adviser, subject to the overall supervision of our Board of Dire
manages the day-to-day operations of, and provides investment advisory services to us. Under the terms of the Inves
Advisory Agreement, our Investment Adviser: (i) determines the composition of our portfolio, the nature and timing
changes to our portfolio and the manner of implementing such changes, (ii) identifies, evaluates and negotiates the struct
the investments we make (including performing due diligence on our prospective portfolio companies); and (iii) close
monitors investments we make.

Prospect Capital Management's services under the Investment Advisory Agreement are not exclusive, and it is free to fu
similar services to other entities so long as its services to us are not impaired. For providing these services the Inves
Adviser receives a fee from us, consisting of two components: a base management fee and an incentive fee. The
management fee is calculated at an annual rate of 2.00% on our gross assets (including amounts borrowed). For ser

currently rendered under the Investment Advisory Agreement, the base management fee is payable quarterly in arrears base management fee is calculated based on the average value of our gross assets at the end of the two most recently comp calendar quarters and appropriately adjusted for any share issuances or repurchases during the current calendar quarter.

The total base management fees incurred to the favor of the Investment Adviser for the three months ended December 31, and December 31, 2008 were $3,176, and $2,940, respectively. The fees incurred for the six months ended December 31, and December 31, 2008 were $6,385, and $5,763, respectively.

The incentive fee has two parts. The first part, the income incentive fee, is calculated and payable quarterly in arrears bas
our pre-incentive fee net investment income for the immediately preceding calendar quarter. For this purpose, pre-incenti
net investment income means interest income, dividend income and any other income (including any other fees (other tha
for providing managerial assistance), such as commitment, origination, structuring, diligence and consulting fees and othe
that we receive from portfolio companies) accrued during the calendar quarter, minus our operating expenses for the q
(including the base management fee, expenses payable under the Administration Agreement described below, and any in
expense and dividends paid on any issued and outstanding preferred stock, but excluding the incentive fee). Pre-incenti
net investment income includes, in the case of investments with a deferred interest feature (such as original issue discount
instruments with payment in kind interest and zero coupon securities), accrued income that we have not yet received in
Pre-incentive fee net investment income does not include any realized capital gains, realized capital losses or unrealized c
appreciation or depreciation. Pre-incentive fee net investment income, expressed as a rate of return on the value of our net
at the end of the immediately preceding calendar quarter, is compared to a "hurdle rate" of 1.75% per quarter (7
annualized).

The net investment income used to calculate this part of the incentive fee is also included in the amount of the gross assets
to calculate the 2.00% base management fee. We pay the Investment Adviser an income incentive fee with respect t
pre-incentive fee net investment income in each calendar quarter as follows:

- no incentive fee in any calendar quarter in which our pre-incentive fee net investment income does not excee the hurdle rate;
- 100.00% of our pre-incentive fee net investment income with respect to that portion of such pre-incentive fee investment income, if any, that exceeds the hurdle rate but is less than 125.00% of the quarterly hurdle rate in any calendar quarter (8.75% annualized assuming a 7.00% annualized hurdle rate); and
- 20.00% of the amount of our pre-incentive fee net investment income, if any, that exceeds 125.00% of the quarterly hurdle rate in any calendar quarter (8.75% annualized assuming a 7.00% annualized hurdle rate).

These calculations are appropriately prorated for any period of less than three months and adjusted for any share issuan
repurchases during the current quarter.

The second part of the incentive fee, the capital gains incentive fee, is determined and payable in arrears as of the end o
calendar year (or upon termination of the Investment Advisory Agreement, as of the termination date), and equals 20.0
our realized capital gains for the calendar year, if any, computed net of all realized capital losses and unrealized c
depreciation at the end of such year. In determining the capital gains incentive fee payable to the Investment Advise
calculate the aggregate realized capital gains, aggregate realized capital losses and aggregate unrealized capital depreciati
applicable, with respect to each investment that has been in its portfolio. For the purpose of this calculation, an "investme
defined as the total of all rights and claims which maybe asserted against a portfolio company arising from our participat
the debt, equity, and other financial instruments issued by that company. Aggregate realized capital gains, if any, equals th
of the differences between the aggregate net sales price of each investment and the aggregate cost basis of such inves
when sold or otherwise disposed. Aggregate realized capital losses equal the sum of the amounts by which the aggrega
sales price of each investment is less than the aggregate cost basis of such investment when sold or otherwise disp
Aggregate unrealized capital depreciation equals the sum of the differences, if negative, between the aggregate valuation o
investment and the aggregate cost basis of such investment as of the applicable calendar year-end . At the end of the appl
calendar year, the amount of capital gains that serves as the basis for our calculation of the capital gains incentive fee inv

netting aggregate realized capital gains against aggregate realized capital losses on a since-inception basis and then reducin
amount by the aggregate unrealized capital depreciation. If this number is positive, then the capital gains incentive fee pa
is equal to 20.00% of such amount, less the aggregate amount of any capital gains incentive fees paid since inception.

For the three months ended December 31, 2009 and December 31, 2008, income incentive fees of $4,231 and $2
respectively, were incurred. For the six months ended December 31, 2009 and December 31, 2008, income incentive fe
$7,311 and $8,865, respectively, were incurred. No capital gains incentive fees were incurred for the three or six months e
December 31, 2009 and December 31, 2008.

Administration Agreement

We have also entered into an Administration Agreement with Prospect Administration, LLC ("Prospect Administration")
which Prospect Administration, among other things, provides (or arranges for the provision of) administrative service
facilities for us. For providing these services, we reimburse Prospect Administration for our allocable portion of ove
incurred by Prospect Administration in performing its obligations under the Administration Agreement, including rent an
allocable portion of the costs of our chief compliance officer and chief financial officer and their respective staffs. For the
months ended December 31, 2009 and 2008, the reimbursement was approximately $840 and $588, respectively. For t
months ended December 31, 2009 and 2008, the reimbursement was approximately $1,680 and $1,176, respectively. Unde
agreement, Prospect Administration furnishes us with office facilities, equipment and clerical, bookkeeping and record ke
services at such facilities. Prospect Administration also performs, or oversees the performance of, our required administ
services, which include, among other things, being responsible for the financial records that we are required to maintai
preparing reports to our stockholders and reports filed with the SEC. In addition, Prospect Administration assists
determining and publishing our net asset value, overseeing the preparation and filing of our tax returns and the printin
dissemination of reports to our stockholders, and generally oversees the payment of our expenses and the performan
administrative and professional services rendered to us by others. Under the Administration Agreement, Pro
Administration also provides on our behalf managerial assistance to those portfolio companies to which we are requi
provide such assistance. The Administration Agreement may be terminated by either party without penalty upon 60
written notice to the other party. Prospect Administration is a wholly owned subsidiary of our Investment Adviser.

The Administration Agreement provides that, absent willful misfeasance, bad faith or negligence in the performance
duties or by reason of the reckless disregard of its duties and obligations, Prospect Administration and its officers, man
partners, agents, employees, controlling persons, members and any other person or entity affiliated with it are entit
indemnification from us for any damages, liabilities, costs and expenses (including reasonable attorneys' fees and am
reasonably paid in settlement) arising from the rendering of Prospect Administration's services under the Administr
Agreement or otherwise as administrator for us.

Prospect Administration, pursuant to the approval of our Board of Directors, engaged Vastardis Fund Services
("Vastardis") to serve as our sub-administrator to perform certain services required of Prospect Administration. Und
sub-administration agreement, Vastardis provided us with office facilities, equipment, clerical, bookkeeping and record ke
services at such facilities. Vastardis also conducted relations with custodians, depositories, transfer agents, dividend disbu
agents, other stockholder servicing agents, accountants, attorneys, underwriters, brokers and dealers, corporate fiduci
insurers, banks and such other persons in any such other capacity deemed to be necessary or desirable. Vastardis pro
reports to the Administrator and the Directors of its performance of obligations and furnished advice and recommendation
respect to such other aspects of our business and affairs as it shall determine to be desirable. Under the sub-administ
agreement, Vastardis also provided the service of William E. Vastardis as our Chief Financial Officer ("CFO"
compensated Vastardis for providing us these services by the payment of an asset-based fee with a $400 annual mini
payable monthly. Our service agreement was amended on September 28, 2008 so that Mr. Vastardis no longer served a
CFO effective as of November 11, 2008. At that time, Brian H. Oswald, a managing director at Prospect Administr

assumed the role of CFO.

We terminated our agreement with Vastardis to provide sub-administration services effective June 30, 2009. We entered new consulting services agreement for the period from July 1, 2009 until the filing of our Form 10-K for the year ended Ju 2009. We paid Vastardis a total of $30 for services rendered in conjunction with

---

preparation of Form 10-K under the new agreement. All services previously provided by Vastardis were assumed by Pro
Administration beginning on July 1, 2009 for the fiscal year ending June 30, 2010 and thereafter.

Managerial Assistance

As a business development company, we offer, and must provide upon request, managerial assistance to certain of our por
companies. This assistance could involve, among other things, monitoring the operations of our portfolio compa
participating in board and management meetings, consulting with and advising officers of portfolio companies and prov
other organizational and financial guidance. We billed $260 and $215 of managerial assistance fees for the three months e
December 31, 2009 and June 30, 2009, respectively, of which $135 and $60 remains on the consolidated statement of asse
liabilities as of December 31, 2009, and June 30, 2009, respectively. We billed $461 and $431 of managerial assistance fe
the six months ended December 31, 2009 and June 30, 2009, respectively. These fees are paid to the Administrator
received. We simultaneously accrue a payable to the Administrator for the same amounts, which remain on the consoli
statements of assets and liabilities.

Note 9. Financial Highlights

	For The Three Months Ended December 31, 2009	For The Three Months Ended December 31, 2008	For The Six Months Ended December 31, 2009	For The Six Months Ended December 3 2008
Per Share Data(1):				
Net asset value at beginning of period	$ 11.11	$ 14.63	$ 12.40	$ 14.55
Net investment income	0.29	0.40	0.54	1.20
Net realized gain (loss)	(0.89)	—	(0.95)	0.06
Net unrealized appreciation (depreciation)	0.30	(0.18)	(0.02)	(0.56
Net decrease in net assets as a result of public offerings and DRIP issuance	(0.01)	—	(0.79)	—
Net increase in net assets as a result of shares issued for Patriot acquisition	0.08	—	0.14	—
Dividends declared and paid	(0.82)	(0.42)	(1.26)	(0.82
Net asset value at end of period	$ 10.06	$ 14.43	$ 10.06	$ 14.43
Per share market value at end of period	$ 11.81	$ 11.97	$ 11.81	$ 11.97
Total return based on market value(2)	14.09 %	(3.41 %)	37.87 %	(3.17
Total return based on net asset value(2)	(6.32 %)	1.96 %	(12.87 %)	5.74
Shares outstanding at end of period	63,349,746	29,637,928	63,349,746	29,637,928
Average weighted shares outstanding for period	57,613,489	29,618,762	53,709,197	29,569,57
Ratio / Supplemental Data:				
Net assets at end of period (in thousands)	$ 637,477	$ 427,803	$ 637,477	$ 427,803
Annualized ratio of operating expenses to average net assets	7.65 %	9.34 %	7.24 %	10.14
Annualized ratio of net operating income to average net assets	10.91 %	11.33 %	9.77 %	16.86

Note 9: Financial Highlights (continued)

	Year Ended June 30, 2009	Year Ended June 30, 2008	Year Ended June 30, 2007	Year Ended June 30, 2006	Year Ended June 30, 2005
Per Share Data(1):					
Net asset value at beginning of period	$ 14.55	$ 15.04	$ 15.31	$ 14.59	$ (0.01
Costs related to the initial public offering	—	—	—	0.01	(0.21
Costs related to the secondary public offering	—	(0.07)	(0.06)	—	—
Net investment income	1.87	1.91	1.47	1.21	0.34
Realized (loss) gain	(1.24)	(0.69)	0.12	0.04	—
	0.48	(0.05)	(0.52)	0.58	0.90

Net unrealized appreciation (depreciation)														
Net (decrease) increase in net assets as a result of public offering		(2.11	)		—			0.26			—			13.95
Dividends declared and paid		(1.15	)		(1.59	)		(1.54	)		(1.12	)		(0.38
Net asset value at end of period	$	12.40		$	14.55			15.04			15.31			14.59
Per share market value at end of period	$	9.20		$	13.18		$	17.47		$	16.99		$	12.60
Total return based on market value(2)		(22.04	%)		(15.90	%)		12.65	%		44.90	%		(13.46
Total return based on net asset value(2)		(4.81	%)		7.84	%		7.62	%		12.76	%		7.40
Shares outstanding at end of period		42,943,084			29,520,379			19,949,065			7,069,873			7,055,10
Average weighted shares outstanding for period		31,559,905			23,626,642			15,724,095			7,056,846			7,055,10

Ratio / Supplemental Data:									
Net assets at end of period	$ 532,596		$ 429,623		$ 300,048		$ 108,270		$ 102,967
Annualized ratio of operating expenses to average net assets	9.03	%	9.62	%	7.36	%	8.19	%	5.52
Annualized ratio of net investment income to average net assets	13.14	%	12.66	%	9.71	%	7.90	%	8.50

(1) Financial highlights are based on weighted average shares.

(2) Total return based on market value is based on the change in market price per share between the opening and ending m prices per share in each period and assumes that dividends are reinvested in accordance with our dividend reinvestment Total return based on net asset value is based upon the change in net asset value per share between the opening and e net asset values per share in each period and assumes that dividends are reinvested in accordance with our div reinvestment plan.

Note 10. Revolving Credit Agreements

On June 6, 2007, we closed on a $200,000 three-year revolving credit facility (as amended on December 31, 2007) Rabobank Nederland ("Rabobank") as administrative agent and sole lead arranger (the "Rabobank Facility"). Until Nove 14, 2008, interest on the Rabobank Facility was charged at LIBOR plus 175 basis points; thereafter, under the term commitment letter with Rabobank to arrange and structure a new rated credit facility, we agreed to an immediate increase current borrowing rate on the Rabobank Facility to LIBOR plus 250 basis points. Additionally, Rabobank charged a fee o unused portion of the facility. This fee is assessed at the rate of 37.5 basis points per annum of the amount of that u portion.

On June 25, 2009, we completed a first closing on an expanded $250,000 revolving credit facility (the "Syndicated Faci The new Syndicated Facility, which had $195,000 and $175,000 total commitments as of December 31, 2009 and Jun 2009, respectively, includes an accordion feature which allows the Syndicated Facility to accept up to an aggregate to $250,000 of commitments for which we continue to solicit additional commitments from other lenders for the addit $55,000 as of December 31, 2009. The revolving period extends through June 24, 2010. If not renewed or extended b participant banks, a one year amortization period would commence whereby we may not borrow additional funds. Thereaft ten years, all principal, interest and fee payments received in conjunction with collateral pledged to the Syndicated Facility a monthly servicing fee payable to us, are required to be used to repay outstanding borrowings under the Syndicated Fa Any remaining outstanding borrowings would be due and payable on the commitment termination date, which is currently 24, 2011.

The Syndicated Facility contains restrictions pertaining to the geographic and industry concentrations of funded l maximum size of funded loans, interest rate payment frequency of funded loans, maturity dates of funded loans and min equity requirements. The Syndicated Facility also contains certain requirements relating to portfolio performance, incl required minimum portfolio yield and limitations on delinquencies and charge-offs, violation of which could result in the termination of the Syndicated Facility. The Syndicated Facility also requires the maintenance of a minimum liqu requirement. At December 31, 2009 and June 30, 2009, we were in compliance with the applicable covenants.

Interest on borrowings under the credit facility is one-month LIBOR plus 400 basis points, subject to a minimum Libor fl
200 basis points. Additionally, the banks charge a fee on the unused portion of the credit facility equal to 100 basis points.
December 31, 2009 and June 30, 2009, we had $10,000 and $124,800 outstanding under our credit facility, respectively.
December 31, 2009 and June 30, 2009, $62,914 and $946 was available to us for additional borrowing under our credit fa
respectively. As we make additional investments which are eligible to be pledged under the credit facility, we will ge
additional availability to the extent such investments are eligible to be placed into the borrowing base. At December 31,
and June 30, 2009, the investments used as collateral for the Syndicated Facility had an aggregate market value of $339,01
$434,069, which represents 53.2% and 81.5% of net assets, respectively.

In connection with the origination and amendment of the Syndicated Facility, we incurred approximately $9,472 of fees w
are being amortized over the term of the facility.

Note 11. Commitments and Off-Balance Sheet Risks

From time to time, we provide guarantees for portfolio companies for payments to counterparties, usually as an alternat
investing additional capital. We provide indemnifications to Prospect Administration in accordance with our respe
agreements with that service provider. These indemnifications are described in further detail in Note 8. As of Decemb
2009, no other material contingency agreements exist.

Note 12. Litigation

From time to time, we may become involved in various investigations, claims and legal proceedings that arise in the ord
course of our business. These matters may relate to intellectual property, employment, tax, regulation, contract or other m
The resolution of these matters as they arise will be subject to various uncertainties and, even if such claims are without
could result in the expenditure of significant financial and managerial resources.

On December 6, 2004, Dallas Gas Partners, L.P. ("DGP") served us with a complaint filed November 30, 2004 in the
District for the Southern District of Texas, Galveston Division. DGP alleges that DGP was defrauded and that we breache
fiduciary duty to DGP and tortiously interfered with DGP's contract to purchase Gas Solutions, Ltd. (a subsidiary o
portfolio company, GSHI) in connection with our alleged agreement in September 2004 to loan DGP funds with which
intended to buy Gas Solutions, Ltd. for approximately $26,000. The complaint sought relief not limited to $100,00
November 30, 2005, U.S. Magistrate Judge John R. Froeschner of the U.S. District Court for the Southern District of T
Galveston Division, issued a recommendation that the court grant our Motion for Summary Judgment dismissing all clai
DGP. On February 21, 2006, U.S. District Judge Samuel Kent of the U.S. District Court for the Southern District of T
Galveston Division issued an order granting our Motion for Summary Judgment dismissing all claims by DGP, against u
May 16, 2007, the Court also granted us summary judgment on DGP's liability to us on our counterclaim for DGP's breac
release and covenant not to sue. On January 4, 2008, the Court, Judge Melinda Harmon presiding, granted our motion to di
all DGP's claims asserted against certain of our officers and affiliates. On August 20, 2008, Judge Harmon entered a
Judgment dismissing all of DGP's claims. DGP appealed to the U.S. Court of Appeals for the Fifth Circuit, which affirme
Final Judgment on June 24, 2009. DGP then moved for rehearing on July 8, 2009, which the Fifth Circuit denied on Aug
2009. Our damage claims against DGP remain pending.

In May 2006, based in part on unfavorable due diligence and the absence of investment committee approval, we declin
extend a loan for $10,000 to a potential borrower ("plaintiff"). Plaintiff was subsequently sued by its own attorney in a
Texas court for plaintiff's failure to pay fees owed to its attorney. In December 2006, plaintiff filed a cross-action against u
certain affiliates (the "defendants") in the same local Texas court, alleging, among other things, tortuous interference
contract and fraud. We petitioned the United States District Court for the Southern District of New York (the "District C
to compel arbitration and to enjoin the Texas action. In February 2007, our motions were granted. Plaintiff appeale
decision. On July 24, 2008, the Second Circuit Court of Appeals affirmed the judgment of the District Court. The arbit
commenced in July 2007 and concluded in late November 2007. Post-hearing briefings were completed in February 200
April 14, 2008, the arbitrator rendered an award in our favor, rejecting all of plaintiff's claims. On April 18, 2008, we f

petition before the District Court to confirm the award. On October 8, 2008, the District Court granted the Company's petit
confirm the award, confirmed the awards and subsequently entered judgment thereon in favor of the Company in the amo
$2,288. After filing a defective notice of appeal to the United States Court of Appeals for the Second Circuit on Novem
2008, plaintiff's counsel resubmitted a new notice of appeal on January 9, 2009. The plaintiff subsequently requested th
Company agree to stipulate to the withdrawal of plaintiff's appeal to the Second Circuit. Such a stipulation was filed wi
Second Circuit on or about April 14, 2009. Based on this

stipulation, the Second Circuit issued a mandate terminating the appeal, which was transmitted to the District Court on Ap 2009. Post-judgment discovery against plaintiff is continuing and we have filed a motion for sanctions against plai counsel. Argument for the motion for sanctions was held on November 19, 2009 and a decision from the court is pending.

Note 13. Selected Quarterly Financial Data (Unaudited)

	Investment Income		Net Investment Income		Net Realized and Unrealized Gains (Losses)		Net Increase (Decrease) in Net Assets fro Operations	
Quarter Ended	Total	Per Share(1)	Total	Per Share(1)	Total	Per Share(1)	Total	Pe Share
September 30, 2006	$ 6,432	$ 0.65	$ 3,274	$ 0.33	$ 690	$ 0.07	$ 3,964	$ 0.40
December 31, 2006	8,171	0.60	4,493	0.33	(1,553)	(0.11)	2,940	0.22
March 31, 2007	12,069	0.61	7,015	0.36	(2,039)	(0.10)	4,976	0.26
June 30, 2007	14,009	0.70	8,349	0.42	(3,501)	(0.18)	4,848	0.24
September 30, 2007	15,391	0.77	7,865	0.39	685	0.04	8,550	0.43
December 31, 2007	18,563	0.80	10,660	0.46	(14,346)	(0.62)	(3,686)	(0.1
March 31, 2008	22,000	0.92	12,919	0.54	(14,178)	(0.59)	(1,259)	(0.0
June 30, 2008	23,448	0.85	13,669	0.50	10,317	0.38	23,986	0.88
September 30, 2008(2)	35,799	1.21	23,502	0.80	(9,504)	(0.33)	13,998	0.47
December 31, 2008	22,213	0.75	11,960	0.40	(5,436)	(0.18)	6,524	0.22
March 31, 2009	20,669	0.69	11,720	0.39	3,611	0.12	15,331	0.51
June 30, 2009	21,800	0.59	11,981	0.32	(12,730)	(0.34)	(749)	(0.0
September 30, 2009	21,517	0.43	12,318	0.25	(18,696)	(0.38)	(6,378)	(0.1
December 31, 2009	28,883	0.50	16,925	0.29	(33,778)	(0.59)	(16,853)	(0.2

(1) Per share amounts are calculated using weighted average shares during period.

(2) Additional income for this quarter was driven by other investment income from the settlement of net profits interests o Systems LP and Advanced Rig Services LLC.

Note 14. Subsequent Events

On January 25, 2010, we issued 236,985 shares of our common stock in connection with the dividend reinvestment plan.

On January 4, 2010, we completed a closing for an additional $15,000 commitment to the Syndicated Facility, increasing commitments to $210,000.

Merger Discussions with Allied Capital Corporation

On January 14, 2010, Prospect Capital delivered a proposal letter to the Allied Capital Board (the "First Prospect Capital M
Offer Letter") containing an offer to acquire each outstanding Allied Capital Corporation ("Allied Capital") Share in exc
for 0.385 of a share of Prospect Capital Common Stock (the "First Prospect Capital Merger Offer").

On January 19, 2010, Allied Capital filed a Form 8-K stating that the Allied Capital Board determined that the First Pro
Capital Merger Offer did not constitute a "Superior Proposal" as such term is defined in the Ares Capital Merger Agreemen

On January 20, 2010, Prospect Capital issued a press release containing a copy of a letter it subsequently sent to the A
Capital Board in connection with the First Prospect Capital Merger Offer.

On January 26, 2010, Prospect Capital announced that it delivered another letter to the Allied Capital Board, raising its of
acquire Allied Capital (the "Second Prospect Capital Merger Offer Letter").

On February 3, 2010, Allied Capital informed us and filed a Form 8-K stating that the Allied Capital Board determined th
Second Prospect Capital Merger Offer did not constitute a "Superior Proposal" as such term is defined in the Ares C
Merger Agreement.

On February 9, 2010, Prospect Capital announced that it delivered another letter to the Allied Capital Board, raising its of
acquire Allied Capital (the "Third Prospect Capital Merger Offer Letter").

On February 11, 2010, Allied Capital informed us and filed a Form 8-K stating that the Allied Capital Board determined th
Third Prospect Capital Merger Offer did not constitute a "Superior Proposal" as such term is defined in the Ares Capital M
Agreement. Prospect Capital has filed proxy material to solicit Allied Shareholders to vote against Allied's proposed m
with Ares Capital Corporation.

Report of Independent Registered Public Accounting Firm

Board of Directors and Stockholders
Prospect Capital Corporation
New York, New York

We have audited the accompanying consolidated statements of assets and liabilities of Prospect Capital Corporation, incl
the schedule of investments, as of June 30, 2009 and 2008, and the related consolidated statements of operations, changes
assets, and cash flows for each of the three years in the period ended June 30, 2009, and the financial highlights for each
periods presented. These financial statements and financial highlights are the responsibility of the Company's managemen
responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United S
Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the fina
statements and financial highlights are free of material misstatement. An audit also includes examining, on a test basis, evi
supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and signi
estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our
provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements and financial highlights referred to above present fairly, in all ma
respects, the financial position of Prospect Capital Corporation at June 30, 2009 and 2008, and the results of its operation
its cash flows for each of the three years in the period ended June 30, 2009, and the financial highlights for each of the p
presented in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United St
Prospect Capital Corporation's internal control over financial reporting as of June 30, 2009, based on criteria establish
Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Com
(COSO) and our report dated September 11, 2009 expressed an unqualified opinion thereon.

/s/ BDO Seidman, LLP

New York, New York
September 11, 2009

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF ASSETS AND LIABILITIES

	June 30, 2009	June 30, 2008
	(In thousands, except sha and per share data)	
ASSETS (NOTE 10)		
Investments at fair value (net cost of $531,424 and $496,805, respectively, Note 3)		
Control investments (net cost of $187,105 and $203,661, respectively)	$206,332	$ 205,827
Affiliate investments (net cost of $33,544 and $5,609, respectively)	32,254	6,043
Non-control/Non-affiliate investments (net cost of $310,775 and $287,535,respectively)	308,582	285,660
Total investments at fair value	547,168	497,530
Investments in money market funds	98,735	33,000
Cash	9,942	555
Receivables for:		
Interest, net	3,562	4,094
Dividends	28	4,248
Loan principal	—	71
Other	571	567
Prepaid expenses	68	273
Deferred financing costs	6,951	1,440
Total Assets	667,025	541,778
LIABILITIES		
Credit facility payable (Note 10)	124,800	91,167
Dividends payable	—	11,845
Due to Prospect Administration (Note 7)	842	695
Due to Prospect Capital Management (Note 7)	5,871	5,946
Accrued expenses	2,381	1,104
Other liabilities	535	1,398
Total Liabilities	134,429	112,155
Net Assets	$532,596	$ 429,623
Components of Net Assets		
Common stock, par value $0.001 per share (100,000,000 and 100,000,000 common shares authorized, respectively; 42,943,084 and 29,520,379 issued and outstanding, respectively) (Note 5)	$43	$ 30
Paid-in capital in excess of par	545,707	441,332
Undistributed net investment income	24,152	1,508
Accumulated realized losses on investments	(53,050)	(13,972
Unrealized appreciation on investments	15,744	725
Net Assets	$532,596	$ 429,623
Net Asset Value Per Share	$12.40	$ 14.55

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except share and per share data)

	Year Ended		
	June 30, 2009	June 30, 2008	June 3 2007
	(In thousands, except share and per shar data)		
Investment Income			
Interest income:			
Control investments (Net of foreign withholding tax of $166, $230, and $178, respectively)	$19,281	$21,709	$13,500
Affiliate investments (Net of foreign withholding tax of $ — , $70, and $237, respectively)	3,039	1,858	3,489
Non-control/Non-affiliate investments	40,606	35,466	13,095
Total interest income	62,926	59,033	30,084
Dividend income			
Control investments	22,468	11,327	3,400
Money market funds	325	706	2,753
Total dividend income	22,793	12,033	6,153
Other income: (Note 4)			
Control/affiliate investments	1,249	1,123	230
Non-control/Non-affiliate investments	13,513	7,213	4,214
Total other income	14,762	8,336	4,444
Total Investment Income	100,481	79,402	40,681
Operating Expenses			
Investment advisory fees:			
Base management fee (Note 7)	11,915	8,921	5,445
Income incentive fee (Note 7)	14,790	11,278	5,781
Total investment advisory fees	26,705	20,199	11,226
Interest and credit facility expenses	6,161	6,318	1,903
Sub-administration fees (including former Chief Financial Officer and Chief Compliance Officer)	846	859	567
Legal fees	947	2,503	1,365
Valuation services	705	577	395
Audit, compliance and tax related fees	1,015	470	599
Allocation of overhead from Prospect Administration (Note 7)	2,856	2,139	532
Insurance expense	246	256	291
Directors' fees	269	253	230
Other general and administrative expenses	1,035	715	442

Excise taxes	533	—	—
Total Operating Expenses	41,318	34,289	17,550
Net Investment Income	59,163	45,113	23,131
Net realized (loss) gain on investments	(39,078)	(16,222)	1,949
Net change in unrealized appreciation (depreciation) on investments	15,019	(1,300)	(8,352
Net Increase in Net Assets Resulting from Operations	$35,104	$27,591	$16,728
Net increase in net assets resulting from operations per share: (Note 6 and Note 8)	$1.11	$1.17	$1.06
Weighted average shares of common stock outstanding:	31,559,905	23,626,642	15,724

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS
(In thousands, except share data)

	Year Ended		
	June 30, 2009	June 30, 2008	June 3 200
	(In thousands, except share data)		
Increase in Net Assets from Operations:			
Net investment income	$59,163	$45,113	$23,131
Net realized (loss) gain on investments	(39,078)	(16,222)	1,949
Net change in unrealized appreciation (depreciation) on investments	15,019	(1,300)	(8,352
Net Increase in Net Assets Resulting from Operations	35,104	27,591	16,728
Dividends to Shareholders	(36,519)	(39,513)	(27,54
Capital Share Transactions:			
Net proceeds from capital shares sold	100,304	140,249	197,55
Less: Offering costs of public share offerings	(1,023)	(1,505)	(874
Reinvestment of dividends	5,107	2,753	5,908
Net Increase in Net Assets Resulting from Capital ShareTransactions	104,388	141,497	202,59
Total Increase in Net Assets:	102,973	129,575	191,77
Net assets at beginning of year	429,623	300,048	108,27
Net Assets at End of Year	$532,596	$429,623	$300,04
Capital Share Activity:			
Shares sold	12,942,500	9,400,000	12,526
Shares issued through reinvestment of dividends	480,205	171,314	352,54
Net increase in capital share activity	13,422,705	9,571,314	12,879
Shares outstanding at beginning of year	29,520,379	19,949,065	7,069,8
Shares Outstanding at End of Year	42,943,084	29,520,379	19,949

See notes to consolidated financial statements.

F-44

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands, except share data)

	Year Ended		
	June 30, 2009	June 30, 2008	June 3 2007
	(In thousands, except share data)		
Cash Flows from Operating Activities:			
Net increase in net assets resulting from operations	$35,104	$27,591	$16,728
Net realized loss (gain) on investments	39,078	16,239	(1,947
Net change in unrealized (appreciation) depreciation on investments	(15,019)	1,300	8,352
Accretion of original issue discount on investments	(2,399)	(2,095)	(1,808
Amortization of deferred financing costs	759	727	1,264
Change in Operating Assets and Liabilities:			
Payments for purchases of investments	(98,305)	(311,947)	(167,2
Proceeds from sale of investments and collection of investment principal	27,007	127,212	38,407
Purchases of cash equivalents	(39,999)	(274,949)	(259,8
Sales of cash equivalents	39,999	274,932	259,88
Net (increase) decrease investments in money market funds	(65,735)	8,760	(40,15
Decrease (increase) in interest receivable, net	532	(1,955)	(500
Decrease (increase) in dividends receivable	4,220	(3,985)	(250
Decrease (increase) in loan principal receivable	71	(71)	385
Decrease in receivable for securities sold	—	—	369
Decrease in receivable for structuring fees	—	1,625	—
Decrease in due from Prospect Administration	—	—	28
Decrease in due from Prospect Capital Management	—	—	5
Increase in other receivables	(4)	(296)	(1,896
Decrease (increase) in prepaid expenses	205	198	(394
(Decrease) increase in payables for securities purchased	—	(70,000)	32
Increase in due to Prospect Administration	147	365	330
(Decrease) increase in due to Prospect Capital Management	(75)	1,438	3,763
Increase (decrease) in accrued expenses	1,277	(208)	469
(Decrease) increase in other liabilities	(863)	1,094	182
Net Cash Used In Operating Activities:	(74,000)	(204,025)	(143,8
Cash Flows from Financing Activities:			
Borrowings under credit facility	100,157	238,492	—
Payments under credit facility	(66,524)	(147,325)	(28,50
Financing costs paid and deferred	(6,270)	(416)	(2,660
Net proceeds from issuance of common stock	100,304	140,249	197,55
Offering costs from issuance of common stock	(1,023)	(1,505)	(874
Dividends paid	(43,257)	(24,915)	(21,63
Net Cash Provided By Financing Activities:	83,387	204,580	143,89
Total Increase in Cash	9,387	555	—
Cash balance at beginning of year	555	—	—
Cash Balance at End of Year	$9,942	$555	$—

Cash Paid For Interest	$5,014	$4,942	$639
Non-Cash Financing Activity:			
Amount of shares issued in connection with dividend reinvestment plan	$5,107	$2,753	$5,908

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY

CONSOLIDATED SCHEDULES OF INVESTMENTS

June 30, 2009 and June 30, 2008

		June 30, 2009			
Portfolio Investments(1)	Locale/Industry	Par Value/ Shares/ Ownership %	Cost	Fair Value(2)	% of N Assets
		(In thousands, except share data)			
Control Investments (25.00% or greater of voting control)					
Ajax Rolled Ring & Machine	South Carolina/ Manufacturing				
Unrestricted common shares (7 total unrestricted common shares issued and outstanding and 681.85 restricted common shares issued and outstanding)		6	$—	$—	0.0
Series A convertible preferred shares (7,192.6 total preferred shares issued and outstanding)		6,142.6	6,057	—	0.0
Subordinated secured note — Tranche B,11.50% plus 6.00% PIK, 4/01/2013(3),(4)		$11,675	11,675	10,151	1.9
Senior secured note — Tranche A, 10.50%, 4/01/2013(3),(5)		$21,487	21,487	21,487	4.0
Total			39,219	31,638	5.9
C&J Cladding LLC	Texas/Metal Services				
Warrant, common units, expiring 3/30/2014 (1,000 total company units outstanding)		400	580	3,825	0.7
Senior secured note, 14.00%, 3/30/2012(3),(6)		$3,150	2,722	3,308	0.6
Total			3,302	7,133	1.3
Change Clean Energy Holdings, Inc. ("CCEHI")(7)	Maine/Biomass Power				
CCEHI common shares (1,000 total common shares issued and outstanding)		1,000	2,530	2,530	0.5
Gas Solutions Holdings, Inc.(3),(8)	Texas/Gas Gathering and Processing				
Common shares (100 total common shares outstanding)		100	5,003	55,187	10.4
Junior secured note, 18.00%, 12/23/2018		$5,000	5,000	5,000	0.9

Senior secured note, 18.00%, 12/22/2018		$25,000	25,000	25,000	4.7
Total			35,003	85,187	16.0
Integrated Contract Services, Inc.(9)	North Carolina/ Contracting				
Common stock (100 total common shares outstanding)		49	$679	$—	0.0
Series A preferred shares (10 total Series A preferred shares outstanding)		10	—	—	0.0
Junior secured note, stated rate 7.00% plus 7.00% PIK plus 6.00% default interest, in non-accrual status effective 10/09/2007, past due		$14,003	14,003	3,030	0.6
Senior secured note, stated rate 7.00% plus 7.00% PIK plus 6.00% default interest, in non-accrual status effective 10/09/2007, past due		$800	800	800	0.1
Senior demand note, 15.00%, 6/30/2009(10)		$1,170	1,170	1,170	0.2
Total			16,652	5,000	0.9
Iron Horse Coiled Tubing, Inc.	Alberta, Canada/ Production Services				
Common shares (2,231 total class A common shares outstanding)		1,781	268	—	0.0
Senior secured note, 15.00%, 12/31/2009		$9,250	9,250	3,004	0.6
Bridge loan, 15.00% plus 3.00% PIK, 12/31/2009		$9,826	9,826	9,602	1.8
Total			19,344	12,606	2.4
NRG Manufacturing, Inc.	Texas/ Manufacturing				
Common shares (1,000 total common shares issued and outstanding)		800	2,317	19,294	3.6
Senior secured note, 16.50%, 8/31/2011(3),(11)		$13,080	13,080	13,080	2.5
Total			15,397	32,374	6.1
R-V Industries, Inc.	Pennsylvania/ Manufacturing				
Common shares (750,000 total common shares issued and outstanding)		545,107	5,086	12,267	2.3
Warrants, common shares, expiring 6/30/2017 (200,000 total common shares outstanding)		200,000	1,682	4,500	0.8
Total			6,768	16,767	3.1
Yatesville Coal Holdings, Inc.(12)	Kentucky/ Mining and Coal Production				
Common stock (1,000 total common shares outstanding)		1,000	$427	$—	0.0
Junior secured note, 15.72%, in non-accrual status effective 1/01/2009, matures 12/31/2010		$38,463	38,463	3,097	0.6
		$10,000	10,000	10,000	1.9

Senior secured note, 15.72%, in non-accrual status effective 1/01/2009, matures 12/31/2010					
Total			48,890	13,097	2.5
Total Control Investments			187,105	206,332	38.7
Affiliate Investments (5.00% to 24.99% of voting control)					
Appalachian Energy Holdings LLC(13)	West Virginia/ Construction Services				
Warrants — Class A common units, expiring 2/13/2016 (86,843 total fully-diluted class A common units outstanding)		6,065	176	—	0.0
Warrants — Class A common units, expiring 6/17/2018 (86,843 total fully-diluted class A common units outstanding)		6,025	172	—	0.0
Warrants — Class A common units, expiring 11/30/2018 (86,843 total fully-diluted class A common units outstanding)		25,000	—	—	0.0
Series A preferred equity (1,075 total series A preferred equity units outstanding)		200	82	—	0.0
Series B preferred equity (794 total series B preferred equity units outstanding)		241	241	—	0.0
Series C preferred equity (500 total series C preferred equity units outstanding)		500	500	—	0.0
Senior Secured Debt Tranche B, 14.00% plus 3.00% PIK plus 3.00% default interest, non-accrual status effective 11/01/2008, past due		$2,050	1,955	356	0.1

Senior Secured Debt Tranche A, 14.00% plus 3.00% PIK plus 3.00% default interest, non-accrual status effective 11/01/2008, matures 1/31/2011		$1,997		1,891	2,052	0.4
Total				5,017	2,408	0.5
Biotronic Neuro Network	Michigan/ Healthcare					
Preferred shares (85,000 total preferred shares outstanding)(14)		9,925.455		$2,300	$2,839	0.5
Senior secured note, 11.50% plus 1.00% PIK, 2/21/2013(3),(15)		$26,227		26,227	27,007	5.1
Total				28,527	29,846	5.6
Total Affiliate Investments				33,544	32,254	6.1
Non-control/Non-affiliate Investments (less than 5.00% of voting control)						
American Gilsonite Company	Utah/Specialty Minerals					
Membership interest units in AGC PEP, LLC(16)		99.9999	%	1,031	3,851	0.7
Senior subordinated note, 12.00% plus 3.00% PIK, 3/14/2013(3)		$14,783		14,783	15,073	2.8
Total				15,814	18,924	3.5
Castro Cheese Company, Inc.(3)	Texas/Food Products					
Junior secured note, 11.00% plus 2.00% PIK, 2/28/2013		$7,538		7,413	7,637	1.4
Conquest Cherokee, LLC(17)	Tennessee/Oil and Gas Production					
Overriding Royalty Interests		—		—	565	0.1
Senior secured note, 13.00%, in non-accrual status effective 4/01/2009 plus 4.00% default interest, past due(18)		$10,200		10,191	6,855	1.3
Total				10,191	7,420	1.4
Deb Shops, Inc.(19)	Pennsylvania/ Retail					
Second lien debt, 8.67%, 10/23/2014		$15,000		$14,623	$6,272	1.2
Diamondback Operating, LP	Oklahoma/Oil and Gas Production					
Net profits interest, 15.00% payable on equity distributions(20)		—		—	458	0.1
Freedom Marine Services LLC(3),(21)	Louisiana/ Shipping Vessels					
Net profits interest, 22.50% payable on equity distributions		—		—	229	0.0
Subordinated secured note, 12.00% plus 4.00% PIK, 12/31/2011(22)		$7,234		7,160	7,152	1.4
Total				7,160	7,381	1.4
H&M Oil & Gas, LLC(3),(21)	Texas/Oil and Gas Production					

Net profits interest, 8.00% payable on equity distributions		—	—	1,682	0.3
Senior secured note, 13.00%, 6/30/2010(23)		$49,688	49,688	49,697	9.3
Total			49,688	51,379	9.6
IEC Systems LP ("IEC") /Advanced Rig Services LLC ("ARS")(3),(24)	Texas/Oilfield Fabrication				
IEC senior secured note, 12.00% plus 3.00% PIK, 11/20/2012		$21,411	21,411	21,839	4.1
ARS senior secured note, 12.00% plus 3.00% PIK, 11/20/2012		$12,836	12,836	13,092	2.5
Total			34,247	34,931	6.6
Maverick Healthcare, LLC	Arizona/ Healthcare				
Common units (79,000,000 total class A common units outstanding)		1,250,000	—	—	0.0
Preferred units (79,000,000 total preferred units outstanding)		1,250,000	1,252	1,300	0.2
Second lien debt, 12.00% plus 1.50% PIK, 4/30/2014(3)		$12,691	12,691	12,816	2.4
Total			13,943	14,116	2.6
Miller Petroleum, Inc.(25)	Tennessee/Oil and Gas Production				
Warrants, common shares, expiring 5/04/2010 to 6/30/2014 (15,811,856 total common shares outstanding)		1,935,523	$150	$241	0.1
Peerless Manufacturing Co.(3)	Texas/ Manufacturing				
Subordinated secured note, 11.50% plus 3.50%PIK, 4/29/2013		$20,000	20,000	20,400	3.8
Qualitest Pharmaceuticals, Inc.(3),(26)	Alabama/ Pharmaceuticals				
Second lien debt, 8.10%, 4/30/2015		$12,000	11,949	11,452	2.2
Regional Management Corp.(3)	South Carolina/ Financial Services				
Second lien debt, 12.00% plus 2.00% PIK, 6/29/2012		$25,424	25,424	23,073	4.3
Resco Products, Inc.(3),(27)	Pennsylvania/ Manufacturing				
Second lien debt, 8.67%, 6/22/2014		$9,750	9,594	9,750	1.8
Shearer's Foods, Inc.	Ohio/Food Products				
Membership interest units in Mistral Chip Holdings, LLC (45,300 total membership units outstanding)(28)		2,000	2,000	3,419	0.6
Second lien debt, 14.00%, 10/31/2013(3)		$18,000	18,000	18,360	3.5
Total			20,000	21,779	4.1
Stryker Energy, LLC(29)	Ohio/Oil and Gas Production				
Overriding Royalty Interests		—	—	2,918	0.6
Subordinated secured revolving credit facility, 12.00%, 12/01/2011(3),(30)		$29,500	29,154	29,554	5.5
Total			29,154	32,472	6.1

TriZetto Group(3)	California/ Healthcare				
Subordinated unsecured note, 12.00% plus 1.50% PIK, 10/01/2016		$15,205	$15,065	$16,331	3.1
Unitek(3),(31)	Pennsylvania/ Technical Services				
Second lien debt, 13.08%, 12/31/2013		$11,500	11,360	11,730	2.2
Wind River Resources Corp. and Wind River II Corp.(21)	Utah/Oil and Gas Production				
Net profits interest, 5.00% payable on equity distributions		—	—	192	0.0

Senior secured note, stated rate 13.00% plus 3.00% default interest, in non-accrual status effective 12/01/2008, matures 7/31/2010(32)		$15,000	15,000	12,644	2.4
Total			15,000	12,836	2.4
Total Non-control/Non-affiliate Investments			310,775	308,582	57.9
Total Portfolio Investments			531,424	547,168	102.7
Money Market Funds					
Fidelity Institutional Money Market Funds -Government Portfolio (Class I)		94,752,972	94,753	94,753	17.8
Fidelity Institutional Money Market Funds -Government Portfolio (Class I)(3)		3,982,278	3,982	3,982	0.7
Total Money Market Funds			98,735	98,735	18.5
Total Investments			$630,159	$645,903	121.2
Control Investments (25.00% or greater of voting control)					
Ajax Rolled Ring & Machine	South Carolina/ Manufacturing				
Unrestricted common shares (7 total unrestricted common shares issued and outstanding and 803.18 restricted common shares issued and outstanding)		6	$—	$—	0.0
Series A convertible preferred shares (7,222.6 total preferred shares issued and outstanding)		6,142.6	6,293	6,293	1.5
Subordinated secured note — Tranche B,11.50% plus 6.00% PIK, 4/01/2013(3),(4)		$11,500	11,500	11,500	2.6
Senior secured note — Tranche A, 10.50%, 4/01/2013(3),(5)		$21,890	21,890	21,890	5.1
Total			39,683	39,683	9.2
C&J Cladding LLC(3)	Texas/Metal Services				
Warrant, common units, expiring 3/30/2014 (600 total company units outstanding)		400	580	2,222	0.5
Senior secured note, 14.00%, 3/30/2012(6)		$4,800	4,085	4,607	1.1
Total			4,665	6,829	1.6
Gas Solutions Holdings, Inc.(8)	Texas/Gas Gathering and Processing				
Common shares (100 total common shares outstanding)		100	5,221	41,542	9.7
Subordinated secured note, 18.00%, 12/22/2009(3)		$20,000	20,000	20,000	4.7
Total			25,221	61,542	14.4
Integrated Contract Services, Inc.(9)	North Carolina/ Contracting				
		49	491	—	0.0

Common stock (100 total common shares outstanding)					
Series A preferred shares (10 total Series A preferred shares outstanding)		10	—	—	0.0
Junior secured note, 14.00%, 9/30/2010		$14,003	14,003	3,030	0.7
Senior secured note, 14.00%, 9/30/2010		$800	800	800	0.2
Senior demand note, 15.00%, 6/30/2009(10)		$1,170	1,170	1,170	0.3
Total			16,464	5,000	1.2
Iron Horse Coiled Tubing, Inc.	Alberta, Canada/ Production Services				
Common shares (1,093 total common shares outstanding)		643	$268	$49	0.0
Warrants for common shares(33)		1,138	—	—	0.0
Senior secured note, 15.00%, 4/19/2009		$9,250	9,094	9,073	2.1
Bridge loan, 15.00% plus 3.00% PIK, 12/11/2008			2,103	2,060	0.5
Total			11,465	11,182	2.6
NRG Manufacturing, Inc.	Texas/ Manufacturing				
Common shares (1,000 total common shares issued and outstanding)		800	2,317	8,656	2.0
Senior secured note, 16.50%, 8/31/2011(3),(11)		$13,080	13,080	13,080	3.0
Total			15,397	21,736	5.0
R-V Industries, Inc.	Pennsylvania/ Manufacturing				
Common shares (800,000 total common shares outstanding)		545,107	5,031	8,064	1.9
Warrants, common shares, expiring 6/30/2017		200,000	1,682	2,959	0.7
Senior secured note, 15.00%, 6/30/2017(3)		$7,526	5,912	7,526	1.8
Total			12,625	18,549	4.4
Worcester Energy Partners, Inc.(7)	Maine/ Biomass Power				
Equity ownership		—	457	1	0.0
Senior secured note, 12.50%, 12/31/2012		$37,388	37,264	15,579	3.6
Total			37,721	15,580	3.6
Yatesville Coal Holdings, Inc.(12)	Kentucky/ Mining and Coal Production				
Common stock (1,000 total common shares outstanding)		1,000	284	—	0.0
Junior secured note, 12.50%, 12/31/2010		$30,136	30,136	15,726	3.7
Senior secured note, 12.50%, 12/31/2010		$10,000	10,000	10,000	2.3
Total			40,420	25,726	6.0
Total Control Investments			203,661	205,827	48.0
Affiliate Investments (5.00% to 24.99% of voting control)					

Appalachian Energy Holdings LLC(3),(13)	West Virginia/ Construction Services				
Warrants — Class A common units, expiring 2/13/2016 (49,753 total class A common units outstanding)		12,090	$348	$794	0.2
Series A preferred equity (16,125 total series A preferred equity units outstanding)		3,000	72	162	0.0
Series B preferred equity (794 total series B preferred equity units outstanding)		241	241	—	0.0
Senior Secured Debt Tranche A, 14.00% plus 3.00% PIK, 1/31/2011		$3,003	3,003	3,003	0.7
Senior Secured Debt Tranche B, 14.00% plus 3.00% PIK, 05/01/2009		$1,945	1,945	2,084	0.5
Total			5,609	6,043	1.4
Total Affiliate Investments			5,609	6,043	1.4
Non-control/Non-affiliate Investments (less than 5.00% of voting control)					
American Gilsonite Company	Utah/Specialty Minerals				
Membership interest units in AGC/PEP, LLC(16)		99.9999 %	1,000	1,000	0.2

Senior subordinated note, 12.00% plus 3.00%, 3/14/2013(3)		$14,632	14,632	14,632	3.4
Total			15,632	15,632	3.6
Conquest Cherokee, LLC(3), (17),(18)	Tennessee/Oil and Gas Production				
Senior secured note, 13.00%, 5/05/2009		$10,200	10,125	9,923	2.3
Deb Shops, Inc.(3),(19)	Pennsylvania/ Retail				
Second lien debt, 10.69%, 10/23/2014		$15,000	14,577	13,428	3.1
Deep Down, Inc.(3)	Texas/ Production Services				
Warrant, common shares, expiring 8/06/2012(174,732,501 total common shares outstanding)		4,960,585	—	2,856	0.7
Diamondback Operating, LP(3),(21)	Oklahoma/ Oil and Gas Production				
Senior secured note, 12.00% plus 2.00% PIK, 8/28/2011		$9,200	$9,200	$9,108	2.1
Freedom Marine Services LLC(3), (21),(22)	Louisiana/ Shipping Vessels				
Subordinated secured note, 12.00% plus 4.00% PIK, 12/31/2011		$6,948	6,850	6,805	1.6
H&M Oil & Gas, LLC(3), (21),(23)	Texas/Oil and Gas Production				
Senior secured note, 13.00%, 6/30/2010		$50,500	50,500	50,500	11.8
IEC Systems LP ("IEC")/Advanced Rig Services LLC ("ARS")(3),(24)	Texas/Oilfield Fabrication				
IEC senior secured note, 12.00% plus 3.00% PIK, 11/20/2012		$19,028	19,028	19,028	4.4
ARS senior secured note, 12.00% plus 3.00% PIK, 11/20/2012		$5,825	5,825	5,825	1.4
Total			24,853	24,853	5.8
Maverick Healthcare, LLC(3)	Arizona/ Healthcare				
Common units (78,100,000 total common units outstanding)		1,250,000	1,252	1,252	0.3
Preferred units (78,100,000 total preferred units outstanding)		1,250,000	—	—	0.0
Senior secured note, 12.00% plus 1.50% PIK, 10/13/2014		$12,500	12,500	12,500	2.4
Total			13,752	13,752	3.2
Miller Petroleum, Inc.	Tennessee/ Oil and Gas Production				
Warrants, common shares, expiring 5/04/2010 to3/31/2013 (14,566,856 total		1,571,191	150	111	0.0

common shares outstanding)					
Peerless Manufacturing Co.(3)	Texas/ Manufacturing				
Subordinated secured note, 11.50% plus 3.50% PIK, 4/30/2013		$20,000	20,000	20,000	4.7
Qualitest Pharmaceuticals, Inc.(3),(26)	Alabama/ Pharmaceuticals				
Second lien debt, 12.45%, 4/30/2015		$12,000	11,944	11,523	2.7
Regional Management Corp.(3)	South Carolina/ Financial Services				
Subordinated secured note, 12.00% plus 2.00% PIK, 6/29/2012		$25,000	$25,000	$23,699	5.5
Resco Products, Inc.(3),(27)	Pennsylvania/ Manufacturing				
Second lien debt, 11.06%, 6/24/2014		$9,750	9,574	9,574	2.2
Shearer's Foods, Inc.	Ohio/Food Products				
Mistral Chip Holdings, LLC membership unit (45,300 total membership units outstanding)(28)		2,000	2,000	2,000	0.5
Second lien debt, 14.00%, 10/31/2013(3)		$18,000	18,000	17,351	4.0
Total			20,000	19,351	4.5
Stryker Energy, LLC(3), (29),(30)	Ohio/Oil and Gas Production				
Subordinated revolving credit facility, 12.00%, 11/30/2011		$29,500	29,041	28,518	6.6
Unitek(3),(31)	Pennsylvania/ Technical Services				
Second lien debt, 12.75%, 12/27/2012		$11,500	11,337	11,337	2.6
Wind River Resources Corp. and Wind River II Corp.(3), (21),(32)	Utah/Oil and Gas Production				
Senior secured note, 13.00%, 7/31/2009		$15,000	15,000	14,690	3.4
Total Non-control/Non-affiliate Investments			287,535	285,660	66.4
Total Portfolio Investments			496,805	497,530	115.8
Money Market Funds					
Fidelity Institutional Money Market Funds -Government Portfolio (Class I)		25,954,531	25,954	25,954	6.0
First American Funds, Inc. — Prime Obligations Fund (Class A)(3)		7,045,610	7,046	7,046	1.6
Total Money Market Funds			33,000	33,000	7.6
Total Investments			$529,805	$530,530	123.4

Endnote Explanations for the Consolidated Schedules of Investments as of June 30, 2009 and June 30, 2008

(1) The securities in which Prospect Capital Corporation ("we", "us" or "our") has invested were acquire transactions that were exempt from registration under the Securities Act of 1933, as amended, or the "Secur Act." These securities may be resold only in transactions that are exempt from registration under the Secur Act.

(2) Fair value is determined by or under the direction of our Board of Directors (see Note 2).

(3) Security, or portion thereof, is held as collateral for the credit facility with Rabobank Nederland (see Note The market values of these investments at June 30, 2009 and June 30, 2008 were $434,069 and $376, respectively; they represent 67.2% and 71.0% of total investments at fair value, respectively.

(4) Interest rate is the greater of 11.5% or 3-month LIBOR plus 8.5%; rate reflected is as of the reporting date - 30, 2009 or June 30, 2008, as applicable.

(5) Interest rate is the greater of 10.5% or 3-month LIBOR plus 7.5%; rate reflected is as of the reporting date - 30, 2009 or June 30, 2008, as applicable.

(6) Interest rate is the greater of 14.0% or 12-Month LIBOR plus 7.5%; rate reflected is as of the reporting date - 30, 2009 or June 30, 2008, as applicable.

(7) There are several entities involved in the Biomass investment. We own 100 shares of common stoc Worcester Energy Holdings, Inc. ("WEHI"), representing 100% of the issued and outstanding common st WEHI, in turn, owns 51 membership certificates in Biochips LLC ("Biochips"), which represents a ownership stake.

We own 282 shares of common stock in Worcester Energy Co., Inc. ("WECO"), which represents 51% o issued and outstanding common stock. We own directly 1,665 shares of common stock in Change Clean En Inc. ("CCEI"), f/k/a Worcester Energy Partners, Inc., which represents 51% of the issued and outstan common stock and the remaining 49% is owned by WECO. CCEI owns 100 shares of common stoc Precision Logging and Landclearing, Inc. ("Precision"), which represents 100% of the issued and outstan common stock.

During the quarter ended March 31, 2009, we created two new entities in anticipation of the foreclo proceedings against the co-borrowers (WECO, CCEI and Biochips) Change Clean Energy Holdings, ("CCEHI") and DownEast Power Company, LLC ("DEPC"). We own 1,000 shares of CCEHI, represen 100% of the issued and outstanding stock, which in turn, owns a 100% of the membership interests in DEPC

On March 11, 2009, we foreclosed on the assets formerly held by CCEI and Biochips with a successful credi of $6,000 to acquire the assets. The assets were subsequently assigned to DEPC.

WECO, CCEI and Biochips are joint borrowers on the term note issued to Prospect Capital. Effective Ju 2008, this loan was placed on non-accrual status.

Biochips, WECO, CCEI, Precision and WEHI currently have no material operations and no significant asset of June 30, 2009, our Board of Directors assessed a fair value of $0 for all of these equity positions and the position. We have determined that the impairment of both CCEI and CCEHI as of June 30, 2009 is other temporary and have recorded a realized loss for the amount that the amortized cost exceeds the fair value at 30, 2009. Our Board of Directors set the value of the remaining CCEHI investment at $2,530 at June 30, 200

(8) Gas Solutions Holdings, Inc. is a wholly-owned investment of us.

(9) Entity was formed as a result of the debt restructuring of ESA Environmental Specialist, Inc. In early 2009 foreclosed on the two loans on non-accrual status and purchased the underlying personal and real property own 1,000 shares of common stock in The Healing Staff ("THS"), f/k/a Lisamarie Fallon, Inc. representing 1 ownership. We own 1,500 shares of Vets Securing America, Inc. ("VSA"), representing 100% ownership. is a holding company for the real property of Integrated Contract Services, Inc. ("ICS") purchased during foreclosure process.

(10) Loan is with THS an affiliate of ICS.

(11) Interest rate is the greater of 16.5% or 12-Month LIBOR plus 11.0%; rate reflected is as of the reporting June 30, 2009 or June 30, 2008, as applicable.

(12) On June 30, 2008, we consolidated our holdings in four coal companies into Yatesville Coal Holdings, ("Yatesville"), and consolidated the operations under one management team. In the transaction, the debt tha held of C&A Construction, Inc. ("C&A"), Genesis Coal Corp. ("Genesis"), North Fork Collieries LLC ("N Fork") and Unity Virginia Holdings LLC ("Unity") were exchanged for newly issued debt from Yatesville our ownership interests in C&A, E&L Construction, Inc. ("E&L"), Whymore Coal Company Inc. ("Whymo Genesis and North Fork were exchanged for 100% of the equity of Yatesville. This reorganization allows better utilization of the assets in the consolidated group.

At June 30, 2009 and at June 30, 2008, Yatesville owned 100% of the membership interest of North For addition, Yatesville held a $8,062 and $5,721, respectively, note receivable from North Fork as of those respective dates.

At June 30, 2009 and at June 30, 2008, Yatesville owned 87% and 75%, respectively, of the common stoc Genesis and held a note receivable of $20,802 and $17,692, respectively, as of those two respective dates.

Yatesville held a note receivable of $4,261 and $3,902, respectively, from Unity at June 30, 2009 and at Jun 2008.

There are several entities involved in Yatesville's investment in Whymore at June 30, 2009 and at June 30, 2 As of those two respective dates, Yatesville owned 10,000 shares of common stock or 100% of the equity held a $14,973 and $12,822, respectively, senior secured debt receivable from C&A, which owns the equipr Yatesville owned 10,000 shares of common stock or 100% of the equity of E&L, which leases the equipr from C&A, employs the workers, is listed as the operator with the Commonwealth of Kentucky, mines the receives revenues and pays all operating expenses. Yatesville owns 4,900 shares of common stock or 49% o equity of Whymore, which applies for and holds permits on behalf of E&L. Yatesville also owned 4,285 Seri convertible preferred shares in each of C&A, E&L and Whymore. Additionally, Yatesville retains an optio purchase the remaining 51% of Whymore. Whymore and E&L are guarantors under the C&A credit agree with Yatesville.

(13) There are several entities involved in the Appalachian Energy Holdings LLC ("AEH") investment. We warrants, the exercise of which will permit us to purchase 15,215 units of Class A common units of AEH nominal cost and in near-immediate fashion. We own 200 units of Series A preferred equity, 241 units of S B preferred equity, and 62.5 units of Series C preferred equity of AEH. The senior secured notes are with Operating LLC and East Cumberland L.L.C., both operating companies owned by AEH.

(14) On a fully diluted basis represents, 11.677% of voting common shares.

(15) Interest rate is the greater of 11.5% or 6-month LIBOR plus 7.0%; rate reflected is as of the reporting date 30, 2009 or June 30, 2008, as applicable.

(16) We own 99.9999% of AGC/PEP, LLC. AGC/PEP, LLC owns 2,038 out of a total of 65,232 shares of Ame Gilsonite Holding Company which owns 100% of American Gilsonite Company.

(17) In addition to the stated returns, we also hold overriding royalty interests on which we receive payment b upon operations of the borrower and net profits interest of 10.00% on equity distributions which will be rea upon sale of the borrower or a sale of the interests.

(18) Interest rate is the greater of 13.0% or 12-Month LIBOR plus 7.5% not to exceed 14.50%; rate reflected is the reporting date — June 30, 2009 or June 30, 2008, as applicable.

(19) Interest rate is 3-Month LIBOR plus 8.0%; rate reflected is as of the reporting date — June 30, 2009 or J 2008, as applicable.

(20) In January 2009, our loan was repaid in full and we retained a 15.0% net profits interest payable on e distributions.

(21) In addition to the stated returns, we also hold net profits interest which will be realized upon sale of the borr or a sale of the interests.

(22) Interest rate is the greater of 12.0% or 3-Month LIBOR plus 6.11%; rate reflected is as of the reporting date 30, 2009 or June 30, 2008, as applicable.

(23) Interest rate is the greater of 13.0% or 12-Month LIBOR plus 7.5%; rate reflected is as of the reporting date 30, 2009 or June 30, 2008, as applicable.

(24) Interest rate is the greater of 12.0% or 12-month LIBOR plus 6.0%; rate reflected is as of the reporting date 30, 2009 or June 30, 2008, as applicable.

(25) Total common shares outstanding of 15,811,856 as of March 11, 2009 from Miller Petroleum, Inc.'s Quar Report on Form 10-Q filed on March 16, 2009.

(26) Interest rate is 3-Month LIBOR plus 7.5%; rate reflected is as of the reporting date — June 30, 2009 or J 2008, as applicable.

(27) Interest rate is 3-Month LIBOR plus 8.0%; rate reflected is as of the reporting date — June 30, 2009 or Ju
2008, as applicable.

(28) Mistral Chip Holdings, LLC owns 45,300 shares out of 50,500 total shares outstanding of Chip Holdings,
the parent company of Shearer's Foods, Inc.

(29) In addition to the stated returns, we also hold overriding royalty interests on which we receive payment b
upon operations of the borrower.

(30) Interest rate is the greater of 12.0% or 12-Month LIBOR plus 7.0%; rate reflected is as of the reporting date
30, 2009 or June 30, 2008, as applicable.

(31) As of June 30, 2009 and June 30, 2008, interest rate is the greater of 13.08% and 12.75%, respectivel
3-Month LIBOR plus 7.25%; rate reflected is as of the reporting date — June 30, 2009 or June 30, 2
applicable.

(32) Interest rate is the greater of 13.0% or 12-month LIBOR plus 7.5% not to exceed 14.0%; rate reflected is
the reporting date — June 30, 2009 or June 30, 2008, as applicable.

(33) The number of these warrants which are exercisable is contingent upon the length of time that passes befor
bridge loan is repaid, 224 shares on August 11, 2008, 340 additional shares on October 11, 2008 and
additional shares on December 11, 2008.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2009
(In thousands, except share and per share data)

Note 1. Organization

References herein to "we", "us" or "our" refer to Prospect Capital Corporation and its subsidiary unless the context specif
requires otherwise.

We were formerly known as Prospect Energy Corporation, a Maryland corporation. We were organized on April 13, 200
were funded in an initial public offering ("IPO"), completed on July 27, 2004. We are a closed-end investment company th
filed an election to be treated as a Business Development Company ("BDC"), under the Investment Company Act of 194
"1940 Act"). As a BDC, we have qualified and have elected to be treated as a regulated investment company ("RIC"),
Subchapter M of the Internal Revenue Code. We invest primarily in senior and subordinated debt and equity of compan
need of capital for acquisitions, divestitures, growth, development, project financings, recapitalizations, and other purposes

On May 15, 2007, we formed a wholly-owned subsidiary, Prospect Capital Funding, LLC, a Delaware limited lia
company, for the purpose of holding certain of our loan investments in the portfolio which are used as collateral for our
facility.

Note 2. Significant Accounting Policies

The following are significant accounting policies consistently applied by us:

Basis of Presentation

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted
United States of America ("GAAP") and pursuant to the requirements for reporting on Form 10-K and Regulation S-X
financial results of our portfolio investments are not consolidated in the financial statements.

Use of Estimates

The preparation of GAAP financial statements requires us to make estimates and assumptions that affect the reported am
of assets and liabilities at the date of the financial statements and the reported amounts of income and expenses durin
reported period. Changes in the economic environment, financial markets, creditworthiness of our portfolio companies an
other parameters used in determining these estimates could cause actual results to differ, and these differences cou
material.

Basis of Consolidation

Under the 1940 Act rules, the regulations pursuant to Article 6 of Regulation S-X and the American Institute of Certified I
Accountants' Audit and Accounting Guide for Investment Companies, we are precluded from consolidating any entity
than another investment company or an operating company which provides substantially all of its services and benefits
Our financial statements include our accounts and the accounts of Prospect Capital Funding, LLC, our only wholly-ov
closely-managed subsidiary that is also an investment company. All intercompany balances and transactions have
eliminated in consolidation.

Investment Classification

We are a non-diversified company within the meaning of the 1940 Act. We classify our investments by level of contro
defined in the 1940 Act, control investments are those where there is the ability or power to exercise a controlling infl
over the management or policies of a company. Control is generally deemed to exist when a company or individual posses
has the right to acquire within 60 days or less, a beneficial ownership of 25% or more of the voting securities of an inv
company. Affiliated investments and affiliated companies are defined by a lesser degree of influence and are deemed to
through the possession outright or via the right to acquire within 60 days or less, beneficial ownership of 5% or more
outstanding voting securities of another person.

Investments are recognized when we assume an obligation to acquire a financial instrument and assume the risks for ga
losses related to that instrument. Investments are derecognized when we assume an obligation to sell a financial instrumen
forego the risks for gains or losses related to that instrument. Specifically, we record all security transactions on a trad
basis. Investments in other, non-security financial instruments are recorded on the basis of subscription date or redemption
as applicable. Amounts for investments recognized or derecognized but not yet settled are reported as receivable
investments sold and payables for investments purchased, respectively, in the Consolidated Statements of Assets and Liabi

Investment Valuation

Our Board of Directors has established procedures for the valuation of our investment portfolio. These procedures are de
below.

Investments for which market quotations are readily available are valued at such market quotations.

For most of our investments, market quotations are not available. With respect to investments for which market quotatio
not readily available or when such market quotations are deemed not to represent fair value, our Board of Director
approved a multi-step valuation process each quarter, as described below:

(1) Each portfolio company or investment is reviewed by our investment professionals with the independent valuation
engaged by our Board of Directors;

(2) the independent valuation firm conducts independent appraisals and makes their own independent assessment;

(3) the audit committee of our Board of Directors reviews and discusses the preliminary valuation of our Investment Ad
and that of the independent valuation firm; and

(4) the Board of Directors discusses valuations and determines the fair value of each investment in our portfolio in good
based on the input of our Investment Adviser, the respective independent valuation firm and the audit committee.

Investments are valued utilizing a market approach, an income approach, or both approaches, as appropriate. The m
approach uses prices and other relevant information generated by market transactions involving identical or comparable
or liabilities (including a business). The income approach uses valuation techniques to convert future amounts (for exa
cash flows or earnings) to a single present value amount (discounted) calculated based on an appropriate discount rate
measurement is based on the net present value indicated by current market expectations about those future amoun
following these approaches, the types of

factors that we may take into account in fair value pricing our investments include, as relevant: available current market
including relevant and applicable market trading and transaction comparables, applicable market yields and multiples, se
covenants, call protection provisions, information rights, the nature and realizable value of any collateral, the por
company's ability to make payments, its earnings and discounted cash flows, the markets in which the portfolio company
business, comparisons of financial ratios of peer companies that are public, M&A comparables, the principal marke
enterprise values, among other factors.

In September 2006, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Stan
No. 157, "Fair Value Measurements" ("FAS 157"). FAS 157 defines fair value, establishes a framework for measurin
value in GAAP and expands disclosures about fair value measurements. This statement is effective for financial state
issued for fiscal years beginning after November 15, 2007 and interim periods within those years. We have adopte
statement on a prospective basis beginning in the quarter ended September 30, 2008. Adoption of this statement did not h
material impact on our financial statements for the year ended June 30, 2009.

FAS 157 classifies the inputs used to measure these fair values into the following hierarchy:

Level 1: Quoted prices in active markets for identical assets or liabilities, accessible by us at the measurement date.

Level 2: Quoted prices for similar assets or liabilities in active markets, or quoted prices for identical or similar ass
liabilities in markets that are not active, or other observable inputs other than quoted prices.

Level 3: Unobservable inputs for the asset or liability.

In all cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has
determined based on the lowest level of input that is significant to the fair value measurement. Our assessment o
significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors spec
each investment. The changes to GAAP from the application of FAS 157 relate to the definition of fair value, framewo
measuring fair value, and the expanded disclosures about fair value measurements. FAS 157 applies to fair value measure
already required or permitted by other standards. In accordance with FAS 157, the fair value of our investments is defined
price that we would receive upon selling an investment in an orderly transaction to an independent buyer in the princi
most advantageous market in which that investment is transacted.

In April 2009, FASB issued Staff Position No. 157-4, "Determining Fair Value When the Volume and Level of Activity f
Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly" ("FSP FAS 157-4")
FAS 157-4 provides further clarification for the application of FAS 157 in markets that are not active and provides addi
guidance for determining when the volume of trading level of activity for an asset or liability has significantly decreased a
identifying circumstances that indicate a transaction is not orderly. FSP FAS 157-4 is effective for interim and annual rep
periods ending after June 15, 2009. The adoption of FSP FAS 157-4 for the year ended June 30, 2009, did not have any
on our net asset value, financial position or results of operations as there was no change to the fair value measurement prin
set forth in FAS 157.

Valuation of Other Financial Assets and Financial Liabilities

In February 2007, FASB issued Statement of Financial Accounting Standards No. 159, "The Fair Value Option for Fina
Assets and Financial Liabilities — including an amendment of FASB Statement No. 115"

("FAS 159"). FAS 159 permits an entity to elect fair value as the initial and subsequent measurement attribute for ma
assets and liabilities for which the fair value option has been elected and similar assets and liabilities measured using an
measurement attribute. This statement is effective for financial statements issued for fiscal years beginning after Novemb
2007, and interim periods within those years. We have adopted this statement on July 1, 2008 and have elected not to
some assets and liabilities at fair value as would be permitted by FAS 159.

Revenue Recognition

Realized gains or losses on the sale of investments are calculated using the specific identification method.

Interest income, adjusted for amortization of premium and accretion of discount, is recorded on an accrual basis. Origin
closing and/or commitment fees associated with investments in portfolio companies are accreted into interest income ov
respective terms of the applicable loans. Upon the prepayment of a loan or debt security, any prepayment penaltie
unamortized loan origination, closing and commitment fees are recorded as interest income.

Loans are placed on non-accrual status when principal or interest payments are past due 90 days or more or when th
reasonable doubt that principal or interest will be collected. Unpaid accrued interest is generally reversed when a loan is p
on non-accrual status. Interest payments received on non-accrual loans may be recognized as income or applied to prin
depending upon management's judgment. Non-accrual loans are restored to accrual status when past due principal and inte
paid and in management's judgment, are likely to remain current.

Dividend income is recorded on the ex-dividend date.

Structuring fees and similar fees are recognized as income as earned, usually when paid. Structuring fees, excess deal dep
net profits interests and overriding royalty interests are included in other income.

Federal and State Income Taxes

We have elected to be treated as a regulated investment company and intend to continue to comply with the requirements
Internal Revenue Code of 1986 (the "Code"), applicable to regulated investment companies. We are required to distrib
least 90% of our investment company taxable income and intend to distribute (or retain through a deemed distribution) all o
investment company taxable income and net capital gain to stockholders; therefore, we have made no provision for in
taxes. The character of income and gains that we will distribute is determined in accordance with income tax regulation
may differ from GAAP. Book and tax basis differences relating to stockholder dividends and distributions and other perm
book and tax differences are reclassified to paid-in capital.

If we do not distribute (or are not deemed to have distributed) at least 98% of our annual taxable income in the calenda
earned, we will generally be required to pay an excise tax equal to 4% of the amount by which 98% of our annual ta
income exceeds the distributions from such taxable income for the year. To the extent that we determine that our esti
current year annual taxable income will be in excess of estimated current year dividend distributions from such taxable inc
we accrue excise taxes, if any, on estimated excess taxable income as taxable income is earned using an annual effective e

tax rate. The annual effective excise tax rate is determined by dividing the estimated annual excise tax by the estimated a taxable income. During the quarter ended December 31, 2008, we elected to retain a portion of our annual taxable incom paid $533 for the excise tax with the filing of the return in March 2009.

We adopted FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" ("FIN 48"). FIN 48 provides gui for how uncertain tax positions should be recognized, measured, presented, and disclosed in the financial statements. F requires the evaluation of tax positions taken or expected to be taken in the course of preparing our tax returns to dete whether the tax positions are "more-likely-than-not" of being sustained by the applicable tax authority. Tax positio deemed to meet the more-likely-than-not threshold are recorded as a tax benefit or expense in the current year. Adoption o 48 was applied to all open tax years as of July 1, 2007. The adoption of FIN 48 did not have an effect on our net asset financial condition or results of operations as there was no liability for unrecognized tax benefits and no change t beginning net asset value. As of June 30, 2009 and for the twelve months then ended, we did not have a liability fo unrecognized tax benefits. Management's determinations regarding FIN 48 may be subject to review and adjustment at a date based upon factors including, but not limited to, an on-going analysis of tax laws, regulations and interpretations there

Dividends and Distributions

Dividends and distributions to common stockholders are recorded on the ex-dividend date. The amount, if any, to be pai dividend is approved by our Board of Directors each quarter and is generally based upon our management's estimate o earnings for the quarter. Net realized capital gains, if any, are distributed at least annually.

Financing Costs

We record origination expenses related to our credit facility as deferred financing costs. These expenses are deferre amortized as part of interest expense using a method that appropriates the effective interest method.

We record registration expenses related to shelf filings as prepaid assets. These expenses consist principally of Securitie Exchange Commission ("SEC") registration, legal and accounting fees incurred through June 30, 2009 that are related shelf filings that will be charged to capital upon the receipt of the capital or charged to expense if not completed.

Guarantees and Indemnification Agreements

We follow FASB Interpretation Number 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Incl Indirect Guarantees of Indebtedness of Others" ("FIN 45"). FIN 45 elaborates on the disclosure requirements of a guaran its interim and annual financial statements about its obligations under certain guarantees that it has issued. It also requ guarantor to recognize, at the inception of a guarantee, for those guarantees that are covered by FIN 45, the fair value obligation undertaken in issuing certain guarantees. FIN 45 did not have a material effect on the financial statements. Re Note 3, Note 7 and Note 10 for further discussion of guarantees and indemnification agreements.

Per Share Information

Net increase in net assets resulting from operations per common share are calculated using the weighted average numb common shares outstanding for the period presented. Diluted net increase in net assets resulting from operations per sha not presented as there are no potentially dilutive securities outstanding.

Reclassifications

Certain reclassifications have been made in the presentation of prior consolidated financial statements to conform
presentation as of and for the twelve months ended June 30, 2009.

Recent Accounting Pronouncements

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141(R) , "Business Combinat ("FAS 141(R)"). FAS 141(R) establishes accounting principles and disclosure requirements for all transactions in wl company obtains control over another business. The standard is effective for fiscal years beginning after December 15, Our management does not believe that the adoption of FAS 141(R) will have a material impact on our financial statements

In March 2008, the FASB issued Statement of Financial Accounting Standards No. 161, "Disclosures about Deriv Instruments and Hedging Activities — an amendment of FASB Statement No. 133" ("FAS 161"). FAS 161 is intended to financial reporting for derivative instruments by requiring enhanced disclosure that enables investors to understand hov why the entity uses derivatives, how derivatives are accounted for, and how derivatives affect an entity's results of opera financial position, and cash flows. FAS 161 becomes effective for fiscal years beginning after November 15, 2008; therefo applicable for our fiscal year beginning July 1, 2009. Our management does not believe that the adoption of FAS 161 wil a material impact on our financial statements.

In March 2008, the FASB issued Statement of Financial Accounting Standards No. 162, "The Hierarchy of Generally Acc Accounting Principles" ("FAS 162"). FAS 162 identifies the sources of accounting principles and the framework for sel the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in confo with GAAP. This statement is effective 60 days following the SEC's approval of the Public Company Accounting Ove Board amendments to AU Section 411, The Meaning of Present Fairly in Conformity With Generally Accepted Accou Principles. Our management does not believe that the adoption of FAS 162 will have a material impact on our fina statements.

In May 2009, the FASB issued Statement of Financial Accounting Standards No. 165, "Subsequent Events" ("FAS 165") 165 establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but b financial statements are issued or are available to be issued. The standard, which includes a new required disclosure of th through which an entity has evaluated subsequent events, is effective for interim or annual periods ending after June 15, We evaluated all events or transactions that occurred after June 30, 2009 up through September 11, 2009, the date we i these financial statements. Management has also evaluated all events or transactions from September 12, 2009 thr November 6, 2009, and has updated Note 12 for any additional transactions which have occurred, which are unaudited. D these periods, we did not have any material recognizable subsequent events other than those disclosed in Note 12.

In June 2009, the FASB issued Statement of Financial Accounting Standards No. 168, "The FASB Accounting Stan Codification and the Hierarchy of Generally Accepted Accounting Principles — a replacement of FASB Statement N ("FAS 168"). FAS 168 provides for the FASB Accounting Standards Codification (the "Codification") to become the s official source of authoritative, nongovernmental GAAP. The Codification did not change GAAP but reorganizes the liter FAS 168 is effective for interim and annual periods ending after September 15, 2009. Our management does not believe th adoption of FAS 168 will have a material impact on our financial statements.

Note 3. Portfolio Investments

At June 30, 2009, we had invested in 30 long-term portfolio investments, which had an amortized cost of $531,424 and value of $547,168 and at June 30, 2008, we had invested in 29 long-term portfolio investments (including a net profits in in Charlevoix Energy Trading LLC), which had an amortized cost of $496,805 and a fair value of $497,530.

As of June 30, 2009, we own controlling interests in Ajax Rolled Ring & Machine ("Ajax"), C&J Cladding, LLC ("C Change Clean Energy Holdings, Inc. ("CCEHI"), Gas Solutions Holdings, Inc. ("GSHI"), Integrated

Contract Services, Inc. ("ICS"), Iron Horse Coiled Tubing, Inc. ("Iron Horse"), NRG Manufacturing, Inc. ("NRG") Industries, Inc. ("R-V"), and Yatesville Coal Holdings, Inc. ("Yatesville"). We also own an affiliated interest in Appala Energy Holdings, LLC ("AEH") and Biotronic NeuroNetwork ("Biotronic").

The fair values of our portfolio investments as of June 30, 2009 disaggregated into the three levels of the FAS 157 valu hierarchy are as follows:

	Quoted Prices in Active Markets for Identical Securities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Tota
Investments at fair value				
Control investments	$—	$—	$ 206,332	$206,33
Affiliate investments	—	—	32,254	32,254
Non-control/Non-affiliate investments	—	—	308,582	308,58
	—	—	547,168	547,16
Investments in money market funds	—	98,735	—	98,735
Total assets reported at fair value	$—	$98,735	$ 547,168	$645,90

The aggregate values of Level 3 portfolio investments changed during the twelve months ended June 30, 2009 as follows:

Change in Portfolio Valuations using Significant Unobservable Inputs (Level 3)	
Fair value at June 30, 2008	$497,53
Total gains (losses) reported in the Consolidated Statement of Operations:	
Included in net investment income	
Interest income — accretion of original issue discount on investments	2,399
Included in realized (loss) gain on investments	(39,078
Included in net change in unrealized appreciation (depreciation) on investments	15,019
Payments for purchases of investments, payment-in-kind interest, and net profits interests	98,305
Proceeds from sale of investments and collection of investment principal	(27,007
Fair value at June 30, 2009	$547,16
The amount of net unrealized gain included in the results of operations attributable to Level 3 assets still held at June 30, 2009 and reported within the caption Net change in unrealized appreciation/depreciation in the Consolidated Statement of Operations:	$19,397

At June 30, 2009, we determined that one of our investments, Change Clean Energy Inc. ("CCEI"), was other than tempo impaired and recorded a realized loss representing the amount by which the amortized cost exceeded the fair value. At Ju 2009, five loan investments were on non-accrual status: AEH, Conquest Cherokee, LLC ("Conquest"), ICS, Wind Resources Corp. and Wind River II Corp. ("Wind River"), and Yatesville. At June 30, 2008, the loans extended to ICS w non-accrual status. The loan principal of these loans amounted to $92,513 and $14,803 as of June 30, 2009, and June 30, respectively. The fair values of these investments represent approximately 7.3% and 0.9% of our net assets as of June 30, and June 30, 2008, respectively. For the years ended June 30, 2009, June 30, 2008 and June 30, 2007, the income foregon result of not accruing interest on non-accrual debt investments amounted to $18,746, $3,449 and $1,270, respectively.

GSHI has indemnified us against any legal action arising from its investment in Gas Solutions, LP. We have inc
approximately $2,093 from the inception of the investment in GSHI through June 30, 2009 for fees associated with a
action, and GSHI has reimbursed us for the entire amount. The $2,093 reimbursement is reflected as dividend income: c
investments in the Consolidated Statements of Operations with $179, $118 and $178 reflected for the year ended June 30,
June 30, 2008 and June 30, 2007, respectively, and the remainder

reflected in prior periods. Additionally, certain other expenses incurred by us which are attributable to GSHI have reimbursed by GSHI and are reflected as dividend income: control investments in the Consolidated Statements of Opera For the years ended June 30, 2009, June 30, 2008 and June 30, 2007, such reimbursements totaled as $4,422, $4,58 $2,578, respectively.

The original cost basis of debt placements and equity securities acquired, including follow-on investments for existing por companies, totaled $98,305, $311,947 and $167,255 during the year ended June 30, 2009, June 30, 2008 and June 30, respectively. Debt repayments and sales of equity securities with a cost basis of approximately $66,084, $143,434 and $3 were received during the year ended June 30, 2009, June 30, 2008 and June 30, 2007, respectively.

Note 4. Other Investment Income

Other investment income consists of structuring fees, overriding royalty interests, prepayment penalty on net profits inte settlement of net profits interests, deal deposits, administrative agent fee, and other miscellaneous and sundry cash rec Income from such sources was $14,762, $8,336 and $4,444 for the years ended June 30, 2009, June 30, 2008 and June 30, respectively.

	For the Year Ended June 30,		
Income Source	2009	2008	2007
Structuring fees	$1,274	$4,751	$2,574
Overriding royalty interests	550	1,819	196
Prepayment penalty on net profits interests	—	1,659	986
Settlement of net profits interests	12,651	—	—
Deal deposit	62	49	688
Administrative agent fee	55	48	—
Miscellaneous	170	10	—
Other Investment Income	$14,762	$8,336	$4,444

Note 5. Equity Offerings and Related Expenses

During the year ended June 30, 2009, we issued 12,942,500 shares of our common stock through public offerings, a regi direct offering, and through the exercise of over-allotment options on the part of the underwriters. Offering expenses charged against paid-in capital in excess of par. All underwriting fees and offering expenses were borne by us. The pro raised, the related underwriting fees, the offering expenses, and the prices at which common stocks were issued since ince are detailed in the following table:

Issuances of Common Stock	Number of Shares Issued	Gross Proceeds Raised	Underwriting Fees	Offering Expenses	Offering Price
May 26, 2009 over-allotment	1,012,500	$8,353	$418	$—	$8.250
May 26, 2009	6,750,000	55,687	2,784	300	8.250
April 27, 2009 over-allotment	480,000	3,720	177	—	7.750
April 27, 2009	3,200,000	24,800	1,177	210	7.750
March 19, 2009	1,500,000	12,300	—	513	8.200
June 2, 2008	3,250,000	48,425	2,406	254	14.900
March 31, 2008	1,150,000	17,768	759	350	15.450

March 28, 2008	1,300,000	19,786	—	350	15.220
November 13, 2007 over-allotment	200,000	3,268	163	—	16.340
October 17, 2007	3,500,000	57,190	2,860	551	16.340
January 11, 2007 over-allotment	810,000	14,026	688	—	17.315
December 13, 2006	6,000,000	106,200	5,100	279	17.700
August 28, 2006 over-allotment	745,650	11,408	566	—	15.300
August 10, 2006	4,971,000	76,056	3,778	595	15.300
August 27, 2004 over-allotment	55,000	825	58	2	15.000
July 27, 2004	7,000,000	105,000	7,350	1,385	15.000

(1) We declared a dividend of $0.385 per share between offering and over — allotment dates.

Our shareholders' equity accounts at June 30, 2009 and June 30, 2008 reflect cumulative shares issued as of those resp
dates. Our common stock has been issued through public offerings, a registered direct offering, the exercise of over-allo
options on the part of the underwriters and our dividend reinvestment plan. When our common stock is issued, the re
offering expenses have been charged against paid-in capital in excess of par. All underwriting fees and offering expenses
borne by us.

On October 9, 2008, our Board of Directors approved a share repurchase plan under which we may repurchase up to $20,0
our common stock at prices below our net asset value as reported in our financial statements published for the year ended
30, 2008. We have not made any purchases of our common stock during the period from October 9, 2008 to June 30,
pursuant to this plan.

Note 6. Net Increase in Net Assets per Common Share

The following information sets forth the computation of net increase in net assets resulting from operations per common
for the years ended June 30, 2009, 2008 and 2007, respectively.

	For the Year Ended June 30,		
	2009	2008	2007
Net increase in net assets resulting from operations	$35,104	$27,591	$16,728
Weighted average common shares outstanding	31,559,905	23,626,642	15,724
Net increase in net assets resulting from operations per common share	$1.11	$1.17	$1.06

Note 7. Related Party Agreements and Transactions

Investment Advisory Agreement

We have entered into an investment advisory and management agreement with Prospect Capital Management (the "Inves
Advisory Agreement") under which the Investment Adviser, subject to the overall supervision of our Board of Dire
manages the day-to-day operations of, and provides investment advisory services to, us. Under the terms of the Inves
Advisory Agreement, our Investment Adviser: (i) determines the composition of our portfolio, the nature and timing
changes to our portfolio and the manner of implementing such changes, (ii) identifies, evaluates and negotiates the struct
the investments we make (including performing due diligence on our prospective portfolio companies); and (iii) close
monitors investments we make.

Prospect Capital Management's services under the Investment Advisory Agreement are not exclusive, and it is free to fu
similar services to other entities so long as its services to us are not impaired. For providing these services the Inves
Adviser receives a fee from us, consisting of two components: a base management fee and an incentive fee. The
management fee is calculated at an annual rate of 2.00% on our gross assets (including amounts borrowed). For ser
currently rendered under the Investment Advisory Agreement, the base management fee is payable quarterly in arrears
base management fee is calculated based on the average value of our gross assets at the end of the two most recently comp
calendar quarters and appropriately adjusted for any share issuances or repurchases during the current calendar quarter.

The Investment Adviser had previously voluntarily agreed to waive 0.5% of the base management fee if in the futu
average amount of our gross assets for each of the two most recently completed calendar quarters at that time, appropr

adjusted for any share issuances, repurchases or other transactions during such quarters, exceeds $750,000, for that port
the average amount of our gross assets that exceeds $750,000. The voluntary

---

agreement by the Investment Adviser for such waiver for each fiscal quarter after December 31, 2007 has been terminat
the Investment Adviser.

The total base management fees earned by and paid to Prospect Capital Management for the years ended June 30, 2009
30, 2008 and June 30, 2007 were $11,915, $8,921 and $5,445, respectively.

The incentive fee has two parts. The first part, the income incentive fee, is calculated and payable quarterly in arrears bas
our pre-incentive fee net investment income for the immediately preceding calendar quarter. For this purpose, pre-incenti
net investment income means interest income, dividend income and any other income (including any other fees (other tha
for providing managerial assistance), such as commitment, origination, structuring, diligence and consulting fees and othe
that we receive from portfolio companies) accrued during the calendar quarter, minus our operating expenses for the q
(including the base management fee, expenses payable under the Administration Agreement described below, and any in
expense and dividends paid on any issued and outstanding preferred stock, but excluding the incentive fee). Pre-incenti
net investment income includes, in the case of investments with a deferred interest feature (such as original issue discount
instruments with payment in kind interest and zero coupon securities), accrued income that we have not yet received in
Pre-incentive fee net investment income does not include any realized capital gains, realized capital losses or unrealized c
appreciation or depreciation. Pre-incentive fee net investment income, expressed as a rate of return on the value of our net
at the end of the immediately preceding calendar quarter, is compared to a "hurdle rate" of 1.75% per quarter (7
annualized).

Previously, our Investment Adviser had voluntarily agreed that for each fiscal quarter from January 1, 2005 to March 31,
the quarterly hurdle rate was to be equal to the greater of (a) 1.75% and (b) a percentage equal to the sum of 25.0% of the
average of the "quoted treasury rate" for each month in the immediately preceding two quarters plus 0.50%. "Quoted tre
rate" means the yield to maturity (calculated on a semi-annual bond equivalent basis) at the time of computation for Five
U.S. Treasury notes with a constant maturity (as compiled and published in the most recent Federal Reserve Statistical R
H). These calculations were to be appropriately prorated for any period of less than three months and adjusted for any
issuances or repurchases during the current quarter. The voluntary agreement by the Investment Adviser that the hurdle r
fluctuating for each fiscal quarter after January 1, 2005 (as discussed above) was terminated by the Investment Adviser as
June 30, 2007 quarter. The investment adviser had also voluntarily agreed that, in the event it is paid an incentive fee at a
when our common stock is trading at a price below $15 per share for the immediately preceding 30 days (as adjusted for
splits, recapitalizations and other transactions), it will cause the amount of such incentive fee payment to be held in an e
account by an independent third party, subject to applicable regulations. The Investment Adviser had further agreed tha
amount may not be drawn upon by the Investment Adviser or any affiliate or any other third party until such time as the pr
our common stock achieves an average 30 day closing price of at least $15 per share. The Investment Adviser als
voluntarily agreed to cause 30% of any incentive fee that it is paid and that is not otherwise held in escrow to be inves
shares of our common stock through an independent trustee. Any sales of such stock were to comply with any applicab
month holding period under Section 16(b) of the Securities Act and all other restrictions contained in any law or regulati
the fullest extent applicable to any such sale. These two voluntary agreements by the Investment Adviser have been termi
by the Investment Adviser for all incentive fees after December 31, 2007.

The net investment income used to calculate this part of the incentive fee is also included in the amount of the gross assets
to calculate the 2.00% base management fee. We pay the Investment Adviser an income incentive fee with respect t
pre-incentive fee net investment income in each calendar quarter as follows:

- no incentive fee in any calendar quarter in which our pre-incentive fee net investment income does not exceed the hurdle rate;
- 100.00% of our pre-incentive fee net investment income with respect to that portion of such pre-incentive fee net investment income, if any, that exceeds the hurdle rate but is less than 125.00% of the

---

quarterly hurdle rate in any calendar quarter (8.75% annualized assuming a 7.00% annualized hurdle rate); ar

- 20.00% of the amount of our pre-incentive fee net investment income, if any, that exceeds 125.00% of the quarterly hurdle rate in any calendar quarter (8.75% annualized assuming a 7.00% annualized hurdle rate).

These calculations are appropriately prorated for any period of less than three months and adjusted for any share issuanc repurchases during the current quarter.

The second part of the incentive fee, the capital gains incentive fee, is determined and payable in arrears as of the end of calendar year (or upon termination of the Investment Advisory Agreement, as of the termination date), and equals 20.00 our realized capital gains for the calendar year, if any, computed net of all realized capital losses and unrealized c depreciation at the end of such year. In determining the capital gains incentive fee payable to the Investment Advise calculate the aggregate realized capital gains, aggregate realized capital losses and aggregate unrealized capital depreciati applicable, with respect to each investment that has been in its portfolio. For the purpose of this calculation, an "investme defined as the total of all rights and claims which maybe asserted against a portfolio company arising from our participat the debt, equity, and other financial instruments issued by that company. Aggregate realized capital gains, if any, equals th of the differences between the aggregate net sales price of each investment and the aggregate cost basis of such inves when sold or otherwise disposed. Aggregate realized capital losses equal the sum of the amounts by which the aggrega sales price of each investment is less than the aggregate cost basis of such investment when sold or otherwise disp Aggregate unrealized capital depreciation equals the sum of the differences, if negative, between the aggregate valuation of investment and the aggregate cost basis of such investment as of the applicable calendar year-end . At the end of the appl calendar year, the amount of capital gains that serves as the basis for our calculation of the capital gains incentive fee inv netting aggregate realized capital gains against aggregate realized capital losses on a since-inception basis and then reducin amount by the aggregate unrealized capital depreciation. If this number is positive, then the capital gains incentive fee pa is equal to 20.00% of such amount, less the aggregate amount of any capital gains incentive fees paid since inception.

Income incentive fees totaling $14,790, $11,278 and $5,781 were earned for the years ended June 30, 2009, June 30, 200 June 30, 2007, respectively. No capital gains incentive fees were earned for years ended June 30, 2009, June 30, 2008 and 30, 2007.

Administration Agreement

We have also entered into an Administration Agreement with Prospect Administration, LLC ("Prospect Administration") which Prospect Administration, among other things, provides (or arranges for the provision of) administrative service facilities for us. For providing these services, we reimburse Prospect Administration for our allocable portion of ove incurred by Prospect Administration in performing its obligations under the Administration Agreement, including rent ar allocable portion of the costs of our chief compliance officer and chief financial officer and their respective staffs. For the ended June 30, 2009, 2008 and 2007, the reimbursement was approximately $2,856, $2,139 and $532, respectively. Unde agreement, Prospect Administration furnishes us with office facilities, equipment and clerical, bookkeeping and record ke services at such facilities. Prospect Administration also performs, or oversees the performance of, our required administ services, which include, among other things, being responsible for the financial records that we are required to maintai preparing reports to our stockholders and reports filed with the SEC. In addition, Prospect Administration assists determining and publishing our net asset value, overseeing the preparation and filing of our tax returns and the printin dissemination of reports to our stockholders, and generally oversees the payment of our expenses and the performan

administrative and professional services rendered to us by others. Under the Administration Agreement, Pro
Administration also provides on our behalf managerial assistance to those portfolio companies to which we are requi
provide such assistance. The Administration Agreement may be terminated by either party without penalty upon 60
written notice to the other party. Prospect Administration is a wholly owned subsidiary of our Investment Adviser.

The Administration Agreement provides that, absent willful misfeasance, bad faith or negligence in the performance duties or by reason of the reckless disregard of its duties and obligations, Prospect Administration and its officers, man partners, agents, employees, controlling persons, members and any other person or entity affiliated with it are entit indemnification from us for any damages, liabilities, costs and expenses (including reasonable attorneys' fees and am reasonably paid in settlement) arising from the rendering of Prospect Administration's services under the Administr Agreement or otherwise as administrator for us.

Prospect Administration previously engaged Vastardis Fund Services LLC ("Vastardis") to serve as our sub-administra perform certain services required of Prospect Administration. On April 30, 2009 we gave a 60-day notice to Vastar termination of our agreement to provide sub-administration services effective June 30, 2009. We entered into a new cons services agreement for the period from July 1, 2009 until the filing of our Form 10-K for the year ended June 30, 2009. W Vastardis a total of $30 for services rendered in conjunction with preparation of Form 10-K under the new agreemen administration services were assumed by Prospect Administration effective September 14, 2009.

Managerial Assistance

As a business development company, we offer, and must provide upon request, managerial assistance to certain of our por companies. This assistance could involve, among other things, monitoring the operations of our portfolio compa participating in board and management meetings, consulting with and advising officers of portfolio companies and prov other organizational and financial guidance. We billed $846, $1,027, and $505 of managerial assistance fees for the years June 30, 2009, June 30, 2008, and June 30, 2007, respectively, of which $60 and $380 remains on the consolidated statem assets and liabilities as of June 30, 2009, and June 30, 2008, respectively. These fees are paid to the Administrator simultaneously accrue a payable to the Administrator for the same amounts, which remain on the consolidated stateme assets and liabilities.

Note 8. Financial Highlights

	Year Ended				
	June 30, 2009	June 30, 2008	June 30, 2007	June 30, 2006	June 30 2005
Per Share Data(1):					
Net asset value at beginning of period	$14.55	$15.04	$15.31	$14.59	$(0.01
Costs related to the initial public offering	—	—	—	0.01	(0.21
Costs related to the secondary public offering	—	(0.07)	(0.06)	—	—
Net investment income	1.87	1.91	1.47	1.21	0.34
Realized (loss) gain	(1.24)	(0.69)	0.12	0.04	—
Net unrealized appreciation (depreciation)	0.48	(0.05)	(0.52)	0.58	0.90
Net (decrease) increase in net assets as a result of public offering	(2.11)	—	0.26	—	13.95
Dividends declared and paid	(1.15)	(1.59)	(1.54)	(1.12)	(0.38
Net asset value at end of period	$12.40	$14.55	$15.04	$15.31	$14.59
Per share market value at end of period	$9.20	$13.18	$17.47	$16.99	$12.60
Total return based on market value(2)	(22.04)%	(15.90)%	12.65%	44.90%	(13.46
Total return based on net asset value(2)	(4.81)%	7.84%	7.62%	12.76%	7.40

Shares outstanding at end of period	42,943,084		29,520,379		19,949,065		7,069,873		7,055,10	
Average weighted shares outstanding for period	31,559,905		23,626,642		15,724,095		7,056,846		7,055,10	
Ratio /Supplemental Data:										
Net assets at end of period (in thousands)	$532,596		$429,623		$300,048		$108,270		$102,967	
Annualized ratio of operating expenses to average net assets	9.03	%	9.62	%	7.36	%	8.19	%	5.52	
Annualized ratio of net investment income to average net assets	13.14	%	12.66	%	9.71	%	7.90	%	8.50	

(1) Financial highlights are based on weighted average shares.

(2) Total return based on market value is based on the change in market price per share between the opening and ending m
prices per share in each period and assumes that dividends are reinvested in accordance with our dividend reinvestment
Total return based on net asset value is based upon the change in net asset value per share between the opening and e
net asset values per share in each period and assumes that dividends are reinvested in accordance with our div
reinvestment plan.

Note 9. Litigation

From time to time, we may become involved in various investigations, claims and legal proceedings that arise in the ord
course of our business. These matters may relate to intellectual property, employment, tax, regulation, contract or other ma
The resolution of these matters as they arise will be subject to various uncertainties and, even if such claims are without
could result in the expenditure of significant financial and managerial resources.

On December 6, 2004, Dallas Gas Partners, L.P. ("DGP") served us with a complaint filed November 30, 2004 in the
District for the Southern District of Texas, Galveston Division. DGP alleges that DGP was defrauded and that we breache
fiduciary duty to DGP and tortiously interfered with DGP's contract to purchase Gas Solutions, Ltd. (a subsidiary o
portfolio company, GSHI) in connection with our alleged agreement in September 2004 to loan DGP funds with which
intended to buy Gas Solutions, Ltd. for approximately $26,000. The complaint sought relief not limited to $100,00
November 30, 2005, U.S. Magistrate Judge John R. Froeschner of the U.S. District Court for the Southern District of T
Galveston Division, issued a recommendation that the court grant our Motion for Summary Judgment dismissing all clai
DGP. On February 21, 2006, U.S. District Judge Samuel Kent of the U.S. District Court for the Southern District of T
Galveston Division issued an order granting our Motion for Summary Judgment dismissing all claims by DGP, against u
May 16, 2007, the Court also granted us summary judgment on DGP's liability to us on our counterclaim for DGP's breac
release and covenant not to sue. On January 4, 2008, the Court, Judge Melinda Harmon presiding, granted our motion to di
all DGP's claims asserted against certain of our officers and affiliates. On August 20, 2008, Judge Harmon entered a
Judgment dismissing all of DGP's claims. DGP appealed to the U.S. Court of Appeals for the Fifth Circuit, which affirme
Final Judgment on June 24, 2009. DGP has moved for rehearing. Our damage claims against DGP remain pending.

In May 2006, based in part on unfavorable due diligence and the absence of investment committee approval, we declin
extend a loan for $10,000 to a potential borrower ("plaintiff"). Plaintiff was subsequently sued by its own attorney in a
Texas court for plaintiff's failure to pay fees owed to its attorney. In December 2006, plaintiff filed a cross-action against u
certain affiliates (the "defendants") in the same local Texas court, alleging, among other things, tortuous interference
contract and fraud. We petitioned the United States District Court for the Southern District of New York (the "District C
to compel arbitration and to enjoin the Texas action. In February 2007, our motions were granted. Plaintiff appeale
decision. On July 24, 2008, the Second Circuit Court of Appeals affirmed the judgment of the District Court. The arbit
commenced in July 2007 and concluded in late November 2007. Post-hearing briefings were completed in February 200
April 14, 2008, the arbitrator rendered an award in our favor, rejecting all of plaintiff's claims. On April 18, 2008, we f
petition before the District Court to confirm the award. On October 8, 2008, the District Court granted the Company's petit
confirm the award, confirmed the awards and subsequently entered judgment thereon in favor of the Company in the amo
$2,288. After filing a defective notice of appeal to the United States Court of Appeals for the Second Circuit on Novem
2008, plaintiff's counsel resubmitted a new notice of appeal on January 9, 2009. The plaintiff subsequently requested th
Company agree to stipulate to the withdrawal of plaintiff's appeal to the Second Circuit. Such a stipulation was filed wi
Second Circuit on or about April 14, 2009. Based on this stipulation, the Second Circuit issued a mandate terminatin
appeal, which was transmitted to the District Court on April 23, 2009. Post-judgment discovery against plaintiff is conti

and we have filed a motion for sanctions against plaintiff's counsel which is scheduled for argument on October 5, 2009.

Note 10. Revolving Credit Agreements

On June 6, 2007, we closed on a $200,000 three-year revolving credit facility (as amended on December 31, 2007) Rabobank Nederland ("Rabobank") as administrative agent and sole lead arranger (the "Rabobank Facility"). Until Nove 14, 2008, interest on the Rabobank Facility was charged at LIBOR plus 175 basis points; thereafter, under the term commitment letter with Rabobank to arrange and structure a new rated credit facility, we agreed to an immediate increase current borrowing rate on the Rabobank Facility to LIBOR plus 250 basis points. Additionally, Rabobank charged a fee unused portion of the facility. This fee is assessed at the rate of 37.5 basis points per annum of the amount of that u portion.

On June 25, 2009, we completed a first closing on an expanded $250,000 revolving credit facility (the "Syndicated Faci The new Syndicated Facility, which had $175,000 total commitments as of June 30, 2009, includes an accordion feature allows the Syndicated Facility to accept up to an aggregate total of $250,000 of commitments for which we continue to s additional commitments from other lenders for the additional $75,000. The revolving period extends through June 24, with an additional one year amortization period thereafter whereby all principal, interest and fee payments receiv conjunction with collateral pledged to the Syndicated Facility, less a monthly servicing fee payable to us, are required to be to repay outstanding borrowings under the Syndicated Facility. Any remaining outstanding borrowings would be du payable on the commitment termination date, which is currently June 24, 2011.

The Syndicated Facility contains restrictions pertaining to the geographic and industry concentrations of funded maximum size of funded loans, interest rate payment frequency of funded loans, maturity dates of funded loans and min equity requirements. The Syndicated Facility also contains certain requirements relating to portfolio performance, incl required minimum portfolio yield and limitations on delinquencies and charge-offs, violation of which could result in the termination of the Syndicated Facility. The Syndicated Facility also requires the maintenance of a minimum liq requirement. At June 30, 2009, we were in compliance with the applicable covenants.

Interest on borrowings under the credit facility is one-month LIBOR plus 400 basis points, subject to a minimum Libor fl 200 basis points. Additionally, the banks charge a fee on the unused portion of the credit facility equal to 100 basis points. June 30, 2009, we had $124,800 outstanding under our credit facility. As of June 30, 2009, $946 was available to borrowing under our credit facility. As we make additional investments which are eligible to be pledged under the facility, we will generate additional availability to the extent such investments are eligible to be placed into the borrowing At June 30, 2009, the investments used as collateral for the Syndicated Facility had an aggregate market value of $434 which represents 81.5% of net assets.

In connection with the origination and amendment of the Syndicated Facility, we incurred approximately $6.3 million o which are being amortized over the term of the facility.

Note 11. Selected Quarterly Financial Data (Unaudited)

Quarter Ended	Investment Income Total	Investment Income Per	Net Investment Income Total	Net Investment Income Per	Net Realized and Unrealized Gains (Losses) Total	Net Realized and Unrealized Gains (Losses) Per	Net Increase (Decrease) in Net Assets fro Operations Total	Net Increase (Decrease) in Net Assets fro Operations Pe

		Share(1)		Share(1)		Share(1)		Share
September 30, 2006	$6,432	$0.65	$3,274	$0.33	$690	$0.07	$3,964	$0.40
December 31, 2006	8,171	0.60	4,493	0.33	(1,553)	(0.11)	2,940	0.22
March 31, 2007	12,069	0.61	7,015	0.36	(2,039)	(0.10)	4,976	0.26
June 30, 2007	14,009	0.70	8,349	0.42	(3,501)	(0.18)	4,848	0.24
September 30, 2007	15,391	0.77	7,865	0.39	685	0.04	8,550	0.43
December 31, 2007	18,563	0.80	10,660	0.46	(14,346)	(0.62)	(3,686)	(0.1
March 31, 2008	22,000	0.92	12,919	0.54	(14,178)	(0.59)	(1,259)	(0.0
June 30, 2008	23,448	0.85	13,669	0.50	10,317	0.38	23,986	0.88
September 30, 2008(2)	35,799	1.21	23,502	0.80	(9,504)	(0.33)	13,998	0.47
December 31, 2008	22,213	0.75	11,960	0.40	(5,436)	(0.18)	6,524	0.22
March 31, 2009	20,669	0.69	11,720	0.39	3,611	0.12	15,331	0.51
June 30, 2009	21,800	0.59	11,981	0.32	(12,730)	(0.34)	(749)	(0.0

---

(1) Per share amounts are calculated using weighted average shares during period.

(2) Additional income for this quarter was driven by other investment income from the settlement of net profits interests o
Systems LP and Advanced Rig Services LLC. See Note 4.

Note 12. Subsequent Events

On July 6, 2009, and July 8, 2009, we paid down $50,500 and $74,300 of our revolving credit facility, respectively, red our outstanding borrowing to zero.

On July 7, 2009, we closed a public offering of 5,175,000 shares of our common stock (including the exercise of over-allo options of our underwriters). The net proceeds to us were approximately $44,046 after deducting estimated offering expens

On July 20, 2009, we purchased 297,274 shares of our common stock in connection with the dividend reinvestment plan.

On August 3, 2009, we announced that we had entered into a definitive agreement to acquire Patriot Capital Funding (NASDAQ: PCAP) ("Patriot") for approximately $197,000 comprised of our common stock and cash to repay all Patriot anticipated to be $110,500. when the acquisition closes. Our common shares will be exchanged at a ratio of approxin 0.3992 for each Patriot share, or 8,616,467 shares of our common stock for 21,584,251 Patriot shares, with such exchange decreased for any tax distributions Patriot may declare before closing. In return, we will acquire assets with an amortized c approximately $311,000 for approximately $196,000, based on an estimate of our common stock price of $10 per share ar anticipated debt outstanding at the closing, the value of either may change prior to the closing. We, in conjunction w independent valuation agent, have determined that the fair value of the assets is approximate to the anticipated purchase and do not anticipate recording any material gain on the consummation of the transaction.

On August 20, 2009, we issued 3,449,686 shares at $8.50 per share in a private stock offering. The net proceeds to us approximately $29,205 after deducting legal and advisory fees. Concurrent with the sale of these shares, we entered registration rights agreement in which we granted the purchasers certain registration rights with respect to the Shares. Und terms and conditions of the registration rights agreement, we will use our reasonable best efforts to file with the SEC v sixty (60) days a post-effective amendment to the registration statement on Form N-2 and will also use our reasonabl efforts to cause such post-effective amendment to be declared effective by the SEC within one hundred twenty (120) Under the registration rights agreement, the Corporation may be obligated to make liquidated damages payments to ho upon certain events.

On August 31, 2009, C&J repaid the $3,150 loan receivable to us and we received an additional 5% prepayment penalty to $158. We continue to hold warrants for common units in this investment.

On September 4, 2009, Peerless Manufacturing Co. repaid the $20,000 loan receivable to us.

On September 24, 2009, we issued 2,807,111 shares at $9.00 per share in a private stock offering. The net proceeds to us approximately $24,423 after deducting estimated legal and advisory fees. Concurrent with the sale of these shares, we en into a registration rights agreement in which we granted the purchasers certain registration rights with respect to the S Under the terms and conditions of the registration rights agreement, we will use our reasonable best efforts to file with the within sixty (60) days a post-effective amendment to the registration statement on Form N-2 and will also use our reaso best efforts to cause such post-effective amendment to be declared effective by the SEC within one hundred twenty (120) Under the registration rights agreement, the Corporation may be obligated to make liquidated damages payments to ho upon certain events.

On September 28, 2009, we announced the declaration of a cash distribution of $0.4075 per share to holders of reco
October 8, 2009 to be paid on October 19, 2009.

On September 29, 2009, we announced a $20,000 increase in total commitments on our revolving credit facility, increasi
facility size from $175,000 to $195,000.

On October 19, 2009, we issued 233,523 shares of our common stock in connection with the dividend reinvestment plan.

The information in this preliminary prospectus supplement is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission has been declared effective . T preliminary prospectus supplement is not an offer to sell nor does it seek an offer to buy these securities in any jurisdiction where the offer or sale is not permitted.

___________ Shares

Common Stock
$___________ per Share

Prospect Capital Corporation is a financial services company that lends to and invests in middle market, privately companies. We are organized as an externally-managed, non-diversified closed-end management investment company th elected to be treated as a business development company under the Investment Company Act of 1940. Prospect C Management LLC manages our investments, and Prospect Administration LLC provides the administrative services nece for us to operate.

We are offering _______ shares of our common stock. See “Plan of Distribution” beginning on page S-__ of this pro supplement for more information regarding this offering. These shares may be offered at a discount from our most rec determined net asset value per share pursuant to authority granted by our stockholders at the annual meeting of stockho held on December 11, 2009. Sales of common stock at prices below net asset value per share dilute the interests of ex stockholders, have the effect of reducing our net asset value per share and may reduce our market price per share. See Factors" beginning on page S-__ and "Sales of Common Stock Below Net Asset Value" beginning on page S-__ o prospectus supplement and on page 14 of the accompanying prospectus.

Our common stock is traded on the NASDAQ Global Select Market under the symbol "PSEC." The last reported closing price for our common stock on _______, 2010 was $____ per share and our most recently determined net asset value per was $10.06 as of December 31, 2009 ($10.07 on an as adjusted basis solely to give effect to the issuance of our common on January 25, 2010 in connection with our dividend reinvestment plan).

This prospectus supplement and the accompanying prospectus contain important information you should know before inv in our securities. Please read it before you invest and keep it for future reference. We file annual, quarterly and current re proxy statements and other information about us with the Securities and Exchange Commission, or the SEC. This informat available free of charge by contacting us at 10 East 40th Street, 44th Floor, New York, NY 10016 or by telephone at 448-0702. The SEC maintains a website at www.sec.gov where such information is available without charge upon writ oral request. Our Internet website address is www.prospectstreet.com. Information contained on our website is not incorpo by reference into this prospectus supplement or the accompanying prospectus and you should not consider inform contained on our website to be part of this prospectus.

Investing in our common stock involves risks. See "Risk Factors" beginning on page S-__ of this prospectus supplement a
page 14 of the accompanying prospectus.

The SEC has not approved or disapproved of these securities or determined if this prospectus supplement or the accompa
prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

	Per Share	Tota
Public offering price	$	$
Sales Load (underwriting discounts and commissions)	$	$

Proceeds to Prospect Capital Corporation, before expenses(1)	$	$

(1) Before deducting estimated offering expenses payable by us of approximately $_______.

The underwriters expect to deliver the shares to purchasers on or about_______, 2010

The underwriters have the option to purchase up to an additional ______ shares of common stock at the public offering pri
less the sales load (underwriting discounts and commissions), within 30 days from the date of this prospectus supplement s
to cover over-allotments. If the over-allotment option is exercised in full, the total public offering price will be $______, ar
total sales load (underwriting discounts and commissions) will be $______. The proceeds to us would be $______, before
deducting estimated offering expenses payable by us of approximately $______.

Prospectus Supplement dated _________, 2010

You should rely only on the information contained in this prospectus supplement and the accompanying prospectus. We
not authorized any other person to provide you with information that is different from that contained in this prosp
supplement or the accompanying prospectus. If anyone provides you with different or inconsistent information, you shou
rely on it. We are not making an offer of these securities in any jurisdiction where the offer is not permitted. You should as
that the information appearing in this prospectus supplement and the accompanying prospectus is accurate only as of
respective dates. Our business, financial condition and results of operations may have changed since those dates.
prospectus supplement supersedes the accompanying prospectus to the extent it contains information that is different from
addition to the information in that prospectus.

TABLE OF CONTENTS

PROSPECTUS SUPPLEMENT

PROSPECTUS

PROSPECTUS SUMMARY

This summary highlights some information from this prospectus supplement and the accompanying prospectus, and it ma
contain all of the information that is important to you. To understand the terms of the common stock offered hereby, you s
read this prospectus supplement and the accompanying prospectus carefully. Together, these documents describe the sp
terms of the shares we and the selling stockholders are offering. You should carefully read the sections titled "Risk Facto
this prospectus supplement and in the accompanying prospectus and the documents identified in the section "Ava
Information."

The terms "we," "us," "our" and "Company," refer to Prospect Capital Corporation; "Prospect Capital Management
"Investment Advisor" refer to Prospect Capital Management LLC; and "Prospect Administration" and the "Administrator"
to Prospect Administration LLC.

The Company

Prospect Capital Corporation is a financial services company that primarily lends to and invests in middle market privately
companies. We are a closed-end investment company that has filed an election to be treated as a business development co
under the Investment Company Act of 1940, or the 1940 Act. We invest primarily in senior and subordinated debt and equ
companies in need of capital for acquisitions, divestitures, growth, development, project financing and recapitalizatio
work with the management teams or financial sponsors to seek investments with historical cash flows, asset collate
contracted pro-forma cash flows.

Typically, we concentrate on making investments in companies with annual revenues of less than $500 million and ente
values of less than $250 million. Our typical investment involves a secured loan of less than $50 million with some fo
equity participation. From time to time, we acquire controlling interests in companies in conjunction with making secure
investments in such companies. In most cases, companies in which we invest are privately held at the time we invest in
We refer to these companies as "target" or "middle market" companies and these investments as "middle market investmen

We seek to maximize total returns to our investors, including both current yield and equity upside, by applying rigorous
analysis and asset-based and cash-flow based lending techniques to make and monitor our investments. A majority o
investments to date have been in energy-related industries. We have made no investments to date in the real estate or mor
industries, and we do not intend currently to focus on such investments.

We are currently pursuing multiple investment opportunities, including purchases of portfolios from private and p
companies, as well as originations and secondary purchases of particular securities. There can be no assurance that w
successfully consummate any investment opportunity we are currently pursuing. Motivated sellers, including comm
finance companies, hedge funds, other business development companies, total return swap counterparties, banks, collater
loan obligation funds, and other entities, are suffering from excess leverage, and we believe we are well positioned to cap
as potential buyers of such assets at attractive prices. If any of these opportunities are consummated, there can be no assu
that investors will share our view of valuation or that any assets acquired will not be subject to future write downs, ea
which could have an adverse effect on our stock price.

As of December 31, 2009, we held investments in 55 portfolio companies. The aggregate fair value as of December 31, 20
investments in these portfolio companies held on that date is approximately $648 million. Our portfolio across all our long-
debt and certain equity investments had an annualized current yield of 15.6% as of December 31, 2009. The yield includes
interest as well as dividends.

Recent Developments

On January 6, 2010, we announced a $15 million increase in total commitments on our revolving credit facility, increasi
facility size from $195 million to $210 million.

Acquisition of Patriot Capital Funding, Inc.

On December 2, 2009, we completed our previously announced acquisition of Patriot under the Agreement and Plan of M
dated as of August 3, 2009, by and among, us and Patriot. Pursuant to the terms of the merger agreement, we acquired P
for approximately $200 million comprised of our common stock and cash to repay all of Patriot's outstanding debt,
amounted to $107.3 million. In the merger, each outstanding share of Patriot common stock was converted into the ri
receive 0.363992 shares of common stock of Prospect, representing 8,444,068 shares of the Company's common stock, a
payment of cash in lieu of fractional shares of Prospect common stock of less than $200 resulting from the application
foregoing exchange ratio.

Annual Meeting of Stockholders

At our 2009 annual meeting of stockholders held on December 11, 2009, our stockholders approved our ability to s
unlimited number of shares of our common stock at any level of discount from net asset value per share during the t
month period following such approval.

The Offering

Common stock offered by us, excluding the underwriters' over-allotment option	_______ shares.
Common stock outstanding prior to this offering	_______ shares.
Common stock outstanding after this offering, excluding the underwriters' over-allotment option	_______ shares.
Use of proceeds	We expect to use the net proceeds from this offering initially to maintain balance sheet liqu involving repayment of debt under our credit facility, investments in high quality short-term instruments or a combination thereof, and thereafter to make long-term investments in accor with our investment objective. See "Use of Proceeds" in this prospectus supplement.
The NASDAQ Global Select Market symbol	PSEC
Risk factors	See "Risk Factors" in this prospectus supplement and the accompanying prospectus and information in this prospectus supplement and the accompanying prospectus for a discuss factors you should carefully consider before you decide whether to make an investment in s of our common stock.
Current distribution rate	For our second fiscal quarter of 2010, our Board of Directors declared a quarterly divide $0.40875 per share, representing an annualized dividend yield of approximately __ % bas our _______, 2010 closing stock price of $__ per share. Such dividend was payable c earnings. Our dividend is subject to change or discontinuance at any time in the discretion c Board of Directors. Our future earnings and operating cash flow may not be sufficient to sup dividend.

Fees and Expenses

The following tables are intended to assist you in understanding the costs and expenses that an investor in this offering wil directly or indirectly. In these tables, we assume that we have borrowed $195 million under our recently completed exte credit facility, which is the maximum amount currently available under the credit facility. Except where the context sug otherwise, whenever this prospectus supplement contains a reference to fees or expenses paid by "you," "us" or "Pro Capital," or that "we" will pay fees or expenses, the Company will pay such fees and expenses out of our net assets consequently, you will indirectly bear such fees or expenses as an investor in the Company. However, you will not be rec to deliver any money or otherwise bear personal liability or responsibility for such fees or expenses.

Stockholder transaction expenses:	
Sales load (as a percentage of offering price)	(1
Offering expenses borne by us (as a percentage of offering price)(2)	%

Dividend reinvestment plan expenses(3)	None
Total stockholder transaction expenses (as a percentage of offering price)	%
Annual expenses (as a percentage of net assets attributable to common stock)(4):	
Combined base management fee (___%)(5) and incentive fees payable under Investment Advisory Agreement (20% of realized capital gains and 20% of pre-incentive fee net investment income) (2.03%)(6)	%
Interest payments on borrowed funds	%

Acquired Fund Fees and Expenses	%
Other expenses	%
Total annual expenses	%

Example

The following table demonstrates the projected dollar amount of cumulative expenses we would pay out of net assets an
you would indirectly bear over various periods with respect to a hypothetical investment in our common stock. In calcu
the following expense amounts, we have assumed that our annual operating expenses would remain at the levels set forth
table above and that we pay the stockholder transaction costs shown in the table above.

	1 Year	3 Years	5 Years	10 Years
You would pay the following expenses on a $1,000 investment, assuming a 5% annual return	$	$	$	$

While the example assumes, as required by the SEC, a 5% annual return, our performance will vary and may result in a
greater or less than 5%. The income incentive fee under our Investment Advisory Agreement with Prospect Ca
Management would be zero at the 5% annual return assumption required by the SEC for this table, since no incentive fee i
until the annual return exceeds 7%. This illustration assumes that we will not realize any capital gains computed net
realized capital losses and unrealized capital depreciation in any of the indicated time periods. If we achieve sufficient re
on our investments, including through the realization of capital gains, to trigger an incentive fee of a material amoun
expenses, and returns to our investors after such expenses, would be higher. In addition, while the example ass
reinvestment of all dividends and distributions at NAV per share, participants in our dividend reinvestment plan will rec
number of shares of our common stock determined by dividing the total dollar amount of the dividend payable to a partic
by the market price per share of our common stock at the close of trading on the valuation date for the dividend. See "Div
Reinvestment Plan" in the accompanying prospectus for additional information regarding our dividend reinvestment plan.

This example and the expenses in the table above should not be considered a representation of our future expenses. A
expenses (including the cost of debt, if any, and other expenses) may be greater or less than those shown.

(1) The sales load (underwriting discounts and commissions) with respect to our common stock sold in this offe
which is a one time fee, is the only sales load paid in connection with this offering.

(2) The offering expenses of this offering are estimated to be approximately $––––________.

(3) The expenses of the dividend reinvestment plan are included in "other expenses."

(4) Net assets attributable to our common stock equal net assets (i.e., total assets less liabilities other than liabiliti
money borrowed for investment purposes) at Decemb er 31, 2009. See "Capitalization" in this prospectus supple

(5) Our base management fee is 2% of our gross assets (which include any amount borrowed, i.e., total assets wi
deduction for any liabilities). Assuming that we have borrowed $195 million (the size of our credit facility), th
management fee of gross assets equals ____% of net assets. See "Management — Management Services — I
Advisory Agreement" in the accompanying prospectus and footnote 7 below.

(6) Based on an annualized level of incentive fee paid during our quarter ended December 31, 2009, all of w
consisted of an income incentive fee. For a more detailed discussion of the calculation of the two-part incentiv
see "Management — Management Services — Investment Advisory Agreement" in the accompanying prospe

(7) We may borrow additional money before and after the proceeds of this offering are substantially invested. this offering, we will have an increased amount available for us under our $195 million extended credit facilit we will continue to seek additional lenders to upsize the facility to up to $250 million. For more informatio "Risk Factors — Risks Relating To Our Business — Changes in interest rates may affect our

cost of capital and net investment income" and "Management's Discussion and Analysis of Financial Cond and Results of Operations — Results of Operations — Operating Expenses — Financial Condition, Liquidity Resources" in the accompanying prospectus. The table above assumes that we have borrowed $195 million u our credit facility, which is the maximum amount currently available under the credit facility. If we do not bo amounts following this offering, our base management fee, as a percentage of net assets attributable to con stock, will decrease from the percentage shown in the table above, as borrowings will not represent a porti our overall assets.

(8) "Other expense" is based on our annualized expenses during our quarter ended December 31, 2009, as adjuste the increased costs anticipated in connection with the extended credit facility. See "Management — Mana Services — Administration Agreement" in the accompanying prospectus.

(9) The Company's stockholders indirectly bear the expenses of underlying investment companies in which the Company invests. This amount includes the fees and expenses of investment companies in which the Compan invested in as of December 31, 2009. When applicable, fees and expenses are based on historic fees and expe for the investment companies and for those investment companies with little or no operating history, fees and expenses are based on expected fees and expenses stated in the investment companies' prospectus or other sim communication without giving effect to any performance. Future fees and expenses for certain investment companies may be substantially higher or lower because certain fees and expenses are based on the performar of the investment companies, which may fluctuate over time. The amount of the Company's average net asset used in calculating this percentage was based on average monthly net assets of approximately $637 million fo six months ended December 31, 2009.

RISK FACTORS

Investing in our common stock involves a high degree of risk. You should carefully consider the risks described below a
the accompanying prospectus, together with all of the other information included in this prospectus supplement and
accompanying prospectus, before you decide whether to make an investment in our common stock. The risks set forth b
and in the accompanying prospectus are not the only risks we face. If any of the adverse events or conditions described bel
in the accompanying prospectus occur, our business, financial condition and results of operations could be materially adv
affected. In such case, our NAV and the trading price of our common stock could decline, we could reduce or elimina
dividend and you could lose all or part of your investment.

Recent developments may increase the risks associated with our business and an investment in us.

The U.S. financial markets have been experiencing a high level of volatility, disruption and distress, which was exacerbat
the failure of several major financial institutions in the last few months of 2008. In addition, the U.S. economy has ente
recession, which is likely to be severe and prolonged. Similar conditions have occurred in the financial markets and econ
of numerous other countries and could worsen, both in the U.S. and globally. These conditions have raised the level of ma
the risks described in the accompanying prospectus and could have an adverse effect on our portfolio companies as well
our business, financial condition, results of operations, dividend payments, credit facility, access to capital, valuation o
assets (including our NAV) and our stock price.

If we sell common stock at a discount to our NAV per share, stockholders who do not participate in such sale will experien
immediate dilution in an amount that may be material.

We have obtained approval from our stockholders for us to be able to sell an unlimited number of shares of our common
at any level of discount from NAV per share in certain circumstances during the one-year period ending December 11, 20
described in the accompanying prospectus. The issuance or sale by us of shares of our common stock at a discount to net
value poses a risk of dilution to our stockholders. In particular, stockholders who do not purchase additional shares at or b
the discounted price in proportion to their current ownership will experience an immediate decrease in NAV per share (a
as in the aggregate NAV of their shares if they do not participate at all). These stockholders will also experie
disproportionately greater decrease in their participation in our earnings and assets and their voting power than the increa
experience in our assets, potential earning power and voting interests from such issuance or sale. In addition, such sale
adversely affect the price at which our common stock trades. For additional information about recent sales below NA
share, see "Recent Sales of Common Stock Below Net Asset Value" in this prospectus supplement and for addit
information and hypothetical examples of these risks, see "Sales of Common Stock Below Net Asset Value" in this prosp
supplement and in the accompanying prospectus.

USE OF PROCEEDS

The net proceeds from the sale of _____ shares of our common stock in this offering will be $_______ (or $_______ over-allotment is exercised in full) after deducting estimated offering expenses of approximately $_______ payable by us.

We expect to use the net proceeds from this offering initially to maintain balance sheet liquidity, involving repayment o under our credit facility, investments in high quality short-term debt instruments or a combination thereof, and thereaf make long-term investments in accordance with our investment objective.

We are currently pursuing multiple investment opportunities, including purchases of portfolios from private and p companies, as well as originations and secondary purchases of particular securities. There can be no assurance that w successfully consummate any investment opportunity we are currently pursuing. Motivated sellers, including comm finance companies, hedge funds, other business development companies, total return swap counterparties, banks, collater loan obligation funds, and other entities, are suffering from excess leverage, and we believe we are well positioned to capi as potential buyers of such assets at attractive prices. If any of these opportunities are consummated, there can be no assu that investors will share our view of valuation or that any assets acquired will not be subject to future write downs, ea which could have an adverse effect on our stock price.

CAPITALIZATION

The following table sets forth our capitalization as of December 31, 2009:

- on an actual basis;
- on an as adjusted basis giving effect to our distribution of shares in connection with our dividend reinvestm plan on January 25, 2010 and additional borrowings;
- on an as further adjusted basis giving effect to the transactions noted in the prior column and the sale of _______ shares in this offering, at a net price of $ _______ per share after deducting estimated offering expenses of approximately $_______ payable by us, and our receipt of the estimated net proceeds from th offering.

This table should be read in conjunction with "Use of Proceeds" and our "Management's Discussion and Analysis of Fin Condition and Results of Operations" and our financial statements and notes thereto included in this prospectus suppleme the accompanying prospectus.

	As of December 31, 2009		
	Actual	As Adjusted for Stock Issuances and Additional Borrowings After December 31,2009	As furt Adjuste this Offe
	(In thousands, except shares and per share data) (Unaudited)		
Long-term debt, including current maturities:			
Borrowings under senior credit facility(1)	$ 10,000	$ 25,000	
Amount owed to affiliates	7,412	7,412	
Total long-term debt	17,412	32,412	
Stockholders' equity:			
Common stock, par value $0.001 per share (100,000,000 common shares authorized; 63,349,746 shares outstanding actual, 63,586,731(2) shares outstanding as adjusted for stock issuances in connection with our dividend reinvestment plan completed after December 31, 2009 and _______ shares outstanding as further adjusted for this offering)	63	64	
Paid-in capital in excess of par value	741,520	744,415	
Undistributed (distributions in excess of) net investment income	(14,326)	(14,326)	
Accumulated realized losses on investments	(104,279)	(104,279)	
Net unrealized depreciation on investments	14,499	14,499	
Total stockholders' equity	637,477	640,373	
Total capitalization	$ 654,889	$ 672,785	

(1) As of December 31, 2009, we had $10 million of borrowings outstanding under our credit facility. As of Februa
2010, we had $25.0 million of borrowings under our credit facility, representing a $15.0 million increase in borro
subsequent to December 31, 2009.

(2) Includes 236,985 shares of our common stock issued on January 25, 2010 in connection with our divi
reinvestment plan.

RECENT SALES OF COMMON STOCK BELOW NET ASSET VALUE

At our 2008 annual meeting of stockholders held on February 12, 2009 and our 2009 annual meeting of stockholders he December 11, 2009, our stockholders approved our ability to sell an unlimited number of shares of our common stock a level of discount to NAV per share during the twelve-month period following such approval. Accordingly, we may additional offerings of our common stock without any limitation on the total amount of dilution to stockholders. See "Sa Common Stock Below Net Asset Value" in this supplement and in the base prospectus. Pursuant to this authority, we have the following offerings:

Date of Offering	Price Per Share to Investors	Shares Issued	Estimated Net Asset Value Per Share	Percenta Dilutio
March 18, 2009	$8.20	1,500,000	$14.43	2.20
April 27, 2009	$7.75	3,680,000	$14.15	5.05
May 26, 2009	$8.25	7,762,500	$13.44	7.59
July 7, 2009	$9.00	5,175,000	$12.40	3.37
August 20, 2009	$8.50	3,449,686	$11.57	1.78
September 24, 2009	$9.00	2,807,111	$11.36	1.20

DISTRIBUTIONS AND PRICE RANGE OF COMMON STOCK

We have paid and intend to continue to distribute quarterly distributions to our stockholders out of assets legally availab distribution. Our distributions, if any, will be determined by our Board of Directors. Certain amounts of the qua distributions may from time to time be paid out of our capital rather than from earnings for the quarter as a result o deliberate planning or by accounting reclassifications.

In order to maintain RIC tax treatment, we must distribute at least 90% of our ordinary income and realized net short capital gains in excess of realized net long-term capital losses, if any, out of the assets legally available for distribution. In to avoid certain excise taxes imposed on RICs, we are required to distribute with respect to each calendar year by January the following year an amount at least equal to the sum of

- 98% of our ordinary income for the calendar year,
- 98% of our capital gains in excess of capital losses for the one-year period ending on October 31 of the calen year, and
- any ordinary income and net capital gains for preceding years that were not distributed during such years.

In December 2008, our Board of Directors elected to retain excess profits generated in the quarter ended September 30, and pay a 4% excise tax on such retained earnings. We paid $533,000 for the excise tax with the filing of our tax retu March 2009.

In addition, although we currently intend to distribute realized net capital gains (which we define as net long-term capital
in excess of short-term capital losses), if any, at least annually, out of the assets legally available for such distributions, w
decide in the future to retain such capital gains for investment. In such event, the consequences of our retention of net c
gains are as described under "Material U.S. Federal Income Tax Considerations" in the accompanying prospectus. We can
no assurance that we will achieve results that will permit the payment of any cash distributions and, if we issue senior secu
we will be prohibited from making distributions if doing so causes us to fail to maintain the asset coverage ratios stipula
the 1940 Act or if distributions are limited by the terms of any of our borrowings.

We maintain an "opt out" dividend reinvestment plan for our common stockholders. As a result, if we declare a dividend stockholders' cash dividends will be automatically reinvested in additional shares of our common stock, unless they specif "opt out" of the dividend reinvestment plan so as to receive cash dividends. Stockholders who receive distributions in the of stock are subject to the same U.S. Federal, state and local tax consequences as are stockholders who elect to receive distributions in cash. See "Dividend Reinvestment Plan" in the accompanying prospectus. The tax consequences of distribu to stockholders are described in the accompanying prospectus under the label "Material U.S. Federal Income Considerations" in the accompanying prospectus. To the extent prudent and practicable, we intend to declare and pay divi on a quarterly basis.

With respect to the dividends paid to stockholders, income from origination, structuring, closing, commitment and other up fees associated with investments in portfolio companies were treated as taxable income and accordingly, distribut stockholders. During the fiscal year ended June 30, 2009, we paid total dividends of approximately $56.1 million. For th and second quarters of the fiscal year ending June 30, 2010, we paid total distributions of approximately $22.3 millio $25.9 million, respectively.

Tax characteristics of all distributions will be reported to stockholders, as appropriate, on Form 1099-DIV after the end year. Our ability to pay distributions could be affected by future business performance, liquidity, capital needs, alter investment opportunities and loan covenants.

Our common stock is quoted on the NASDAQ Global Select Market under the symbol "PSEC." The following table sets for the periods indicated, our NAV per share of common stock and the high and low closing prices per share of our co stock as reported on the NASDAQ Global Select Market. Our common stock historically trades at prices both above and its NAV. There can be no assurance, however, that such premium or discount, as applicable, to NAV will be mainta Common stock of business development companies, like that of closed-end investment companies, frequently trade discount to current NAV. In the past, our common stock has traded at a discount to our NAV. The risk that our common may continue to trade at a discount to our NAV is separate and distinct from the risk that our NAV per share may decline.

	NAV(1)	Stock Price High(2)	Low(2)	Premium (Discount) of High to NAV	Premium (Discount) of Low to NAV	Divider Declare
Twelve Months Ending June 30, 2005						
First quarter	$ 13.67	$ 15.45	$ 14.42	13.0 %	5.5 %	—
Second quarter	13.74	15.15	11.63	10.3 %	(15.4)%	$ 0.100
Third quarter	13.74	13.72	10.61	(0.1)%	(22.8)%	0.125
Fourth quarter	14.59	13.47	12.27	(7.7)%	(15.9)%	0.150
Twelve Months Ending June 30, 2006						
First quarter	$ 14.60	$ 13.60	$ 11.06	(6.8)%	(24.2)%	$ 0.200
Second quarter	14.69	15.46	12.84	5.2 %	(12.6)%	0.280
Third quarter	14.81	16.64	15.00	12.4 %	1.3 %	0.300
Fourth quarter	15.31	17.07	15.83	11.5 %	3.4 %	0.340

Twelve Months Ending June 30, 2007											
First quarter	$ 14.86		$ 16.77	$ 15.30	12.9	%	3.0	%	$ 0.380
Second quarter	15.24		18.79	15.60	23.3	%	2.4	%	0.385
Third quarter	15.18		17.68	16.40	16.5	%	8.0	%	0.3875
Fourth quarter	15.04		18.68	16.91	24.2	%	12.4	%	0.390
Twelve Months Ending June 30, 2008									
First quarter	$ 15.08		$ 18.68	$ 14.16	23.9	%	(6.1	)%	$ 0.3925
Second quarter	14.58		17.17	11.22	17.8	%	(23.0	)%	0.395
Third quarter	14.15		16.00	13.55	13.1	%	(4.2	)%	0.400
Fourth quarter	14.55		16.12	13.18	10.8	%	(9.4	)%	0.4012
Twelve Months Ending June 30, 2009									
First quarter	$ 14.63		$ 14.24	$ 11.12	(2.7	)%	(24.0	)%	$ 0.4025
Second quarter	14.43		13.08	6.29	(9.4	)%	(56.4	)%	0.4037
Third quarter	14.19		12.89	6.38	(9.2	)%	(55.0	)%	0.405
Fourth quarter	12.40		10.48	7.95	(15.5	)%	(35.9	)%	0.4062
Twelve Months Ending June 30, 2010									
First quarter	$ 11.11		$ 10.99	$ 8.82	(1.1	)%	(20.6	)%	$ 0.4075
Second quarter	10.06		12.31	9.93	22.4	%	(1.3	)%	0.4087
Third quarter (to 2/25/10)	(3	)(4)	13.20	10.45	(4	)	(4	)	(5

(1) Net asset value per share is determined as of the last day in the relevant quarter and therefore may not refle net asset value per share on the date of the high or low sales price. The NAVs shown are based on outstar shares at the end of each period.

(2) The High/Low Stock Price is calculated as of the closing price on a given day in the applicable quarter.

(3) Our most recently determined NAV per share was $10.06 as of December 31, 2009 ($10.07 on an as adjusted solely to give effect to our issuance of common stock on January 25, 2010 in connection with our divi reinvestment plan). NAV as of March 31, 2010 may be higher or lower than $10.07 based on potential chang valuations as of March 31, 2010.

(4) NAV has not yet been finally determined for any day after December 31, 2009.

(5) The dividend for the third quarter of 2010 will be declared in March 2010.

On ________, 2010, the last reported sales price of our common stock was $________ per share.

As of ________, 2010, we had approximately ________ stockholders of record.

The below table sets forth each class of our outstanding securities as of ________, 2010

.

(1) Title of Class	(2) Amount Authorized	(3) Amount Held by Registrant or for its Account	(4) Amount Outstanding Exclusive of Amount Shown Under(3)
Common Stock	100,000,000	0	________

SALES OF COMMON STOCK BELOW NET ASSET VALUE

At our 2008 annual meeting of stockholders held on February 12, 2009 and our 2009 annual meeting of stockholders he December 11, 2009, our stockholders approved our ability to sell an unlimited number of shares of our common stock a level of discount from net asset value (NAV) per share during the twelve-month period following such approval. In order t shares pursuant to this authorization a majority of our directors who have no financial interest in the sale and a majority o independent directors must (a) find that the sale is in our best interests and in the best interests of our stockholders, and consultation with any underwriter or underwriters of the offering, make a good faith determination as of a time o immediately prior to the first solicitation by us or on our behalf of firm commitments to purchase such shares, or immed prior to the issuance of such shares, that the price at which such shares are to be sold is not less than a price which cl approximates the market value of such shares, less any distributing commission or discount. Any offering of common below NAV per share will be designed to raise capital for investment in accordance with our investment objective.

In making a determination that an offering below NAV per share is in our and our stockholders' best interests, our Bo Directors would consider a variety of factors including:

- The effect that an offering below NAV per share would have on our stockholders, including the potential dilu they would experience as a result of the offering;
- The amount per share by which the offering price per share and the net proceeds per share are less than the m recently determined NAV per share;
- The relationship of recent market prices of par common stock to NAV per share and the potential impact of t offering on the market price per share of our common stock;
- Whether the estimated offering price would closely approximate the market value of our shares;
- The potential market impact of being able to raise capital during the current financial market difficulties;
- The nature of any new investors anticipated to acquire shares in the offering;
- The anticipated rate of return on and quality, type and availability of investments; and
- The leverage available to us.

Our Board of Directors would also consider the fact that sales of common stock at a discount will benefit our Advisor Advisor will earn additional investment management fees on the proceeds of such offerings, as it would from the offering o other securities of the Company or from the offering of common stock at premium to NAV per share.

We will not sell shares under a prospectus supplement to the registration statement or current post-effective amendment th of which this prospectus forms a part (the "current registration statement") if the cumulative dilution to our NAV per share offerings under the current registration statement exceeds 15%. This limit would be measured separately for each off pursuant to the current amendment by calculating the percentage dilution or accretion to aggregate NAV from that offerin then summing the percentage from each offering. For example, if our most recently determined NAV at the time of th offering is $10.07 and we have 63.59 million shares outstanding, sale of 16 million shares at net proceeds to us of $5.0

share (a 50% discount) would produce dilution of 10.04%. If we subsequently determined that our NAV per share increa
$11.00 on the then

79.59 million shares outstanding and then made an additional offering, we could, for example, sell approximately an addi 8.759 million shares at net proceeds to us of $5.50 per share, which would produce dilution of 4.96%, before we would the aggregate 15% limit. If we file a new post-effective amendment, the threshold would reset.

Sales by us of our common stock at a discount from NAV pose potential risks for our existing stockholders whether or no participate in the offering, as well as for new investors who participate in the offering.

The following three headings and accompanying tables will explain and provide hypothetical examples on the impact offering at a price less than NAV per share on three different set of investors:

- existing shareholders who do not purchase any shares in the offering
- existing shareholders who purchase a relatively small amount of shares in the offering or a relatively large amount of shares in the offering
- new investors who become shareholders by purchasing shares in the offering.

Impact On Existing Stockholders Who Do Not Participate in the Offering

Our existing stockholders who do not participate in an offering below NAV per share or who do not buy additional shares secondary market at the same or lower price we obtain in the offering (after expenses and commissions) face the gr potential risks. These stockholders will experience an immediate decrease (often called dilution) in the NAV of the share hold and their NAV per share. These stockholders will also experience a disproportionately greater decrease in participation in our earnings and assets and their voting power than the increase we will experience in our assets, pot earning power and voting interests due to the offering. These stockholders may also experience a decline in the market pr their shares, which often reflects to some degree announced or potential increases and decreases in NAV per share decrease could be more pronounced as the size of the offering and level of discounts increase.

The following chart illustrates the level of NAV dilution that would be experienced by a stockholder who does not particip the offering. NAV has not been finally determined for any day after December 31, 2009. The table below is shown based the pro-forma NAV calculated by us taking into account the effects on our NAV per share of our issuance of sha connection with our dividend reinvestment plan on January 25, 2010. For purposes of illustration, the table below assume our December 31, 2009 NAV per share has been increased to 10.07 per share as a result of the foregoing transaction following example assumes a sale of 7,000,000 shares at a sales price to the public of $10.00 with a 5.0% underwriting dis and commissions and $350,000 of expenses ($9.45 per share net). It is not possible to predict the level of market price d that may occur.

	Prior to Sale Below NAV	Following Sale	% Change
Offering Price			
Price per Share to Public		$ 10.00	—
Net Proceeds per Share to Issuer		$ 9.45	—
Decrease to NAV			
Total Shares Outstanding	63,586,731	70,586,731	11.01
NAV per Share	$ 10.07	$ 10.01	(0.61

Dilution to Nonparticipating Stockholder							
Shares Held by Stockholder A		63,587			63,587		0.00
Percentage Held by Stockholder A		0.10	%		0.09	%	(9.92
Total NAV Held by Stockholder A	$	640,375		$	636,460		(0.61
Total Investment by Stockholder A (Assumed to be $10.07 per Share)	$	640,375		$	646,375		
Total Dilution to Stockholder A (Total NAV Less Total Investment)				$	(3,915	)	
NAV per Share Held by Stockholder A after offering				$	10.01		
Investment per Share Held by Stockholder A (Assumed to be $10.07 per Share on Shares Held Prior to Sale)	$	10.82		$	10.07		
Dilution per Share Held by Stockholder A (NAV per Share Less Investment per Share)				$	(0.06	)	
Percentage Dilution to Stockholder A (Dilution per Share Divided by Investment per Share)							(0.61

Impact On Existing Stockholders Who Do Participate in the Offering

Our existing stockholders who participate in the offering or who buy additional shares in the secondary market at the sa
lower price as we obtain in the offering (after expenses and commissions) will experience the same types of NAV dilution
nonparticipating stockholders, albeit at a lower level, to the extent they purchase less than the same percentage of the disco
offering as their interest in our shares immediately prior to the offering. The level of NAV dilution will decrease as the nu
of shares such stockholders purchase increases. Existing stockholders who buy more than such percentage will experience
dilution but will, in contrast to existing stockholders who purchase less than their proportionate share of the offering, exper
an increase (often called accretion) in NAV per share over their investment per share and will also experie
disproportionately greater increase in their participation in our earnings and assets and their voting power than our incre
assets, potential earning power and voting interests due to the offering. The level of accretion will increase as the excess nu
of shares such stockholder purchases increases. Even a stockholder who overparticipates will, however, be subject to th
that we may make additional discounted offerings in which such stockholder does not participate, in which case s
stockholder will experience NAV dilution as described above in such subsequent offerings. These stockholders may
experience a decline in the market price of their shares, which often reflects to some degree announced or potential incr
and decreases in NAV per share. This decrease could be more pronounced as the size of the offering and level of disc
increases.

The following chart illustrates the level of dilution and accretion in the hypothetical 20% discount offering from the prior
(Example 3) for a stockholder that acquires shares equal to (1) 50% of its proportionate share of the offering (i.e., 3,500 s
which is 0.05% of an offering of 7,000,000 shares) rather than its 0.10% proportionate share and (2) 150% of such perce
(i.e. 10,500 shares, which is 0.15% of an offering of 7,000,000 shares rather than its 0.10% proportionate share). NAV h
been finally determined for any day after December 31, 2009. The table below is shown based upon the pro-forma
calculated by us taking into account the effects on our NAV per share of our issuance of shares in connection with our div
reinvestment plan on January 25, 2010. For purposes of illustration, the table below assumes that our December 31, 2009
per share has been increased to 10.07 per share as a result of the foregoing transaction. The following example assumes a s
7,000,000 shares at a sales price to the public of $10.00 with a 5.0% underwriting discount and commissions and $350,0
expenses ($9.45 per share net). It is not possible to predict the level of market price decline that may occur.

	Prior to Sale Below NAV	50% Participation Following Sale	50% Participation % Change	150% Participation Following Sale	150% Participation % Change
Offering Price					
Price per Share to Public		$ 10.00		$ 10.00	
Net Proceeds per Share to Issuer		$ 9.45		$ 9.45	
Decrease/Increase to NAV					
Total Shares Outstanding	63,586,731	70,586,731	11.01 %	70,586,731	11.01
NAV per Share	$ 10.07	$ 10.01	(0.61)%	$ 10.01	(0.61
Dilution/Accretion to Participating Stockholder					
Shares Held by Stockholder A	63,587	67,087	5.50 %	74,087	16.51
Percentage Held by Stockholder A	0.10 %	0.09 %	(4.96)%	0.11 %	4.96

Total NAV Held by Stockholder A	$ 640,376	$ 671,493	4.86 %	$ 741,558	15.80
Total Investment by Stockholder A (Assumed to be $10.07 per Share on Shares held Prior to Sale)		$ 675,376		$ 745,376	
Total Dilution/Accretion to Stockholder A (Total NAV Less Total Investment)		$ (3,883)		$ (3,818)	
NAV per Share Held by Stockholder A		$ 10.01		$ 10.01	
Investment per Share Held by Stockholder A (Assumed to be $10.07 on Shares Held Prior to Sale)	$ 10.07	$ 10.07	(0.04)%	$ 10.06	(0.10
Dilution/Accretion per Share Held by Stockholder A (NAV per Share Less Investment per Share)		$ (0.06)		$ (0.05)	
Percentage Dilution/Accretion to Stockholder A (Dilution/Accretion per Share Divided by Investment per Share)			(0.57)%		(0.51

Impact On New Investors

Investors who are not currently stockholders and who participate in an offering below NAV but whose investment per sh greater than the resulting NAV per share due to selling compensation and expenses paid by the issuer will experien immediate decrease, albeit small, in the NAV of their shares and their NAV per share compared to the price they pay fo shares. Investors who are not currently stockholders and who participate in an offering below NAV per share and v investment per share is also less than the resulting NAV per share due to selling compensation and expenses paid by the being significantly less than the discount per share will experience an immediate increase in the NAV of their shares and NAV per share compared to the price they pay for their shares. These investors will experience a disproportionately g participation in our earnings and assets and their voting power than our increase in assets, potential earning power and v interests. These investors will, however, be subject to the risk that we may make additional discounted offerings in which new stockholder does not participate, in which case such new stockholder will experience dilution as described above in subsequent offerings. These investors may also experience a decline in the market price of their shares, which often refle some degree announced or potential increases and decreases in NAV per share. This decrease could be more pronounced size of the offering and level of discounts increases.

The following chart illustrates the level of dilution or accretion for new investors that will be experienced by a new inv who purchases the same percentage (0.10%) of the shares in the offering as the stockholder in the prior examples immediately prior to the offering. These stockholders may also experience a decline in the market price of their shares, often reflects to some degree announced or potential increases and decreases in NAV per share. This decrease could be pronounced as the size of the offering and level of discounts increases. NAV has not been finally determined for any day December 31, 2009. The table below is shown based upon the pro-forma NAV calculated by us taking into account the e on our NAV per share of our issuance of shares in connection with our dividend reinvestment plan on January 25, 2010 purposes of illustration, the table below assumes that our December 31, 2009 NAV per share has been increased to 10.0 share as a result of the foregoing transaction. The following example assumes a sale of 7,000,000 shares at a sales price public of $10.00 with a 5.0% underwriting discount and commissions and $350,000 of expenses ($9.45 per share net). It possible to predict the level of market price decline that may occur.

	Prior to Sale Below NAV	Following Sale	% Change
Offering Price			
Price per Share to Public		$ 10.00	
Net Proceeds per Share to Issuer		$ 9.45	
Decrease/Increase to NAV			
Total Shares Outstanding	63,586,731	70,586,731	11.01
NAV per Share	$ 10.07	$ 10.01	(0.61
Dilution/Accretion to New Investor A			
Shares Held by Investor A	0	7,000	
Percentage Held by Investor A	0.00 %	0.00 %	
Total NAV Held by Investor A	$ 0	$ 70,065	
Total Investment by Investor A (At Price to Public)		$ 70,000	
Total Dilution/Accretion to Investor A (Total NAV Less Total Investment)		$ 65	
NAV per Share Held by Investor A		$ 10.01	
Investment per Share Held by Investor A	$ 0	$ 10.00	
		$ 0.01	

Dilution/Accretion per Share Held by Investor A (NAV per Share Less Investment per Share)	
Percentage Dilution/Accretion to Investor A (Dilution/Accretion per Share Divided by Investment per Share)	0.09

PLAN OF DISTRIBUTION

We are selling the shares of our common stock under this prospectus supplement ______. Subject to the terms of _____
have agreed to sell ______ shares of our common stock at a price of $______ per share in cash.

We expect to have our transfer agent deliver the shares of our common stock after we receive the payment of the total pur
price therefor in immediately available funds.

Our common stock is listed on the NASDAQ Global Select Market under the symbol "PSEC."

We will bear all of the expenses that we incur in connection with the offering of our shares of common stock unde
prospectus supplement. We estimate the total expenses payable by us in connection with the offering will be approxin
$______.

LEGAL MATTERS

Certain legal matters regarding the common stock offered hereby have been passed upon for the Company by Skadden,
Slate, Meagher & Flom LLP, New York, New York, and Venable LLP as special Maryland counsel.

INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

BDO Seidman LLP is the independent registered public accounting firm for the Company.

AVAILABLE INFORMATION

We have filed with the SEC a registration statement on Form N-2, together with all amendments and related exhibits, und
Securities Act of 1933, with respect to our common stock offered by this prospectus supplement. The registration state
contains additional information about us and the common stock being registered by this prospectus supplement. We file w
submit to the SEC annual, quarterly and current periodic reports, proxy statements and other information meetir
informational requirements of the Exchange Act. This information and the information specifically regarding how we
proxies relating to portfolio securities for the period ended June 30, 2009, are available free of charge by contacting us
East 40th Street, 44th floor, New York, NY 10016 or by telephone at toll-free (888) 748-0702. You may inspect and copy
reports, proxy statements and other information, as well as the registration statement and related exhibits and schedules,
Public Reference Room of the SEC at 100 F Street NE, Washington, D.C. 20549. You may obtain information on the ope
of the Public Reference Room by calling the SEC at (202) 551-8090. The SEC maintains an Internet site that contains re
proxy and information statements and other information filed electronically by us with the SEC which are available o
SEC's Internet site at http://www.sec.gov. Copies of these reports, proxy and information statements and other informatio
be obtained, after paying a duplicating fee, by electronic request at the following E-mail address: publicinfo@sec.gov,

writing the SEC's Public Reference Section, Washington, D.C. 20549-0102.

No dealer, salesperson or other individual has been authorized to give any information or to make any representation othe those contained in this prospectus supplement and, if given or made, such information or representations must not be upon as having been authorized by us. This prospectus supplement does not constitute an offer to sell or a solicitation of ar to buy any securities in any jurisdiction in which such an offer or solicitation is not authorized or in which the person m such offer or solicitation is not qualified to do so, or

---

to any person to whom it is unlawful to make such offer or solicitation. Neither the delivery of this prospectus suppleme
any sale made hereunder shall, under any circumstances, create any implication that there has been no change in our affa
that information contained herein is correct as of any time subsequent to the date hereof.

$500,00

Prospect Capital Corporation

Common Stock
Preferred Stock
Warrants
Debt

PROSPECTUS

PART C — OTHER INFORMATION

ITEM 25. FINANCIAL STATEMENTS AND EXHIBITS

(1) Financial Statements

The following statements of Prospect Capital Corporation (the "Company" or the "Registrant") are included in Part A c
Registration Statement:

Financial Statements

PROSPECT CAPITAL CORPORATION

(2) Exhibits

The agreements included or incorporated by reference as exhibits to this registration statement contain representation warranties by each of the parties to the applicable agreement. These representations and warranties were made solely f benefit of the other parties to the applicable agreement and (i) were not intended to be treated as categorical statements o but rather as a way of allocating the risk to one of the parties if those statements prove to be inaccurate; (ii) may have qualified in such agreement by disclosures that were made to the other party in connection with the negotiation of the appl agreement; (iii) may apply contract standards of "materiality" that are different from "materiality" under the applicable laws; and (iv) were made only as of the date of the applicable agreement or such other date or dates as may be specified agreement.

The Company acknowledges that, notwithstanding the inclusion of the foregoing cautionary statements, it is responsib considering whether additional specific disclosures of material information regarding material contractual provisior required to make the statements in this registration statement not misleading.

Exhibit No.	Description
(a)(1)	Articles of Incorporation1
(a)(2)	Articles of Amendment and Restatement2
(a)(3)	Articles of Amendment8
(b)(1)	Amended and Restated Bylaws3
(c)	Not Applicable
(d)(1)	Form of Share Certificate2
(d)(2)	Form of Indenture*
(e)	Form of Dividend Reinvestment Plan2
(f)	Not Applicable
(g)	Form of Investment Advisory Agreement between Registrant and Prospect Capital Management LLC
(h)	Form of Underwriting Agreement*
(i)	Not Applicable
(j)	Form of Custodian Agreement4
(k)(1)	Form of Administration Agreement between Registrant and Prospect Administration LLC2
(k)(2)	Form of Transfer Agency and Registrar Services Agreement4
(k)(3)	Form of Trademark License Agreement between the Registrant and Prospect Capital Management2
(k)(4)	Amended and Restated Loan and Servicing Agreement dated June 25, 2009 among Prospect Capital Funding LLC, Prospect Capital Corporation and Coöperative Centrale Raiffeisen-Boerenleenbank B.A "Rabobank Nederland," New York Branch5
(k)(5)	Agreement and Plan of Merger dated August 3, 2009 between Prospect Capital Corporation and Patri Capital Funding, Inc. 6
(l)	Opinion and Consent of Venable LLP, as special Maryland counsel for Registrant†
(m)	Not Applicable
(n) (1)	Consent of independent registered public accounting firm†
(n) (2)	Report of independent registered public accounting firm on "Senior Securities" table†
(o)	Not Applicable
(p)	Not Applicable
(q)	Not Applicable
(r)	Code of Ethics7

---

1 Incorporated by reference to the corresponding exhibit number to the Registrant's Registration Statement under the Securities Act of 1933, as amended, on Form N-2 (File No. 333-114552), filed on April 16, 2004.

2	Incorporated by reference to the corresponding exhibit number to the Registration's Pre-Effective Amendment No. 2 to the Registration Statement under the Securities Act of 1933, as amended, on Form N-2 (File No. 333-14552), filed on July 23, 2004
3	Incorporated by reference to Exhibit 3.1 of the Registrant's Form 8-K filed on September 21, 2009.
4	Incorporated by reference to the corresponding exhibit number to the Registrant's Pre-effective Amendment No. 3 to the Registration Statement under the Securities Act of 1933, as amended, on Form N-2 (File No. 333-114552), filed on July 23, 2004.
5	Incorporated by reference to Exhibit 99.1 of the Registrant's Form 8-K filed on June 26, 2009.
6	Incorporated by reference to Exhibit 2.1 of the Registrant's Form 8-K filed on August 5, 2009.
7	Incorporated by reference to the corresponding exhibit number to the Registrant's Pre-effective Amendment No. 2 to the Registration Statement under the Securities Act of 1933, as amended, on Form N-2 (File No. 333-114552), filed on July 6, 2004.
8	Incorporated by reference to the corresponding exhibit number to the Registrant's Pre-Effective Amendment No. 3 to the Registration Statement under the Securities Act of 1933 as amended, on Form N-2 (File No. 333-143819), filed on September 5, 2007
†	Filed herewith.
*	To be filed by amendment.

ITEM 26. MARKETING ARRANGEMENTS

The information contained under the heading "Plan of Distribution" on this Registration Statement is incorporated here reference and any information concerning any underwriters will be contained in the accompanying prospectus suppleme any.

ITEM 27. OTHER EXPENSES OF ISSUANCE AND DISTRIBUTION**

Commission registration fee	$ 35,560
NASDAQ Global Select Additional Listing Fees	50,000
FINRA filing fee	35,746
Accounting fees and expenses	150,00
Legal fees and expenses	300,00
Printing and engraving	150,00
Miscellaneous fees and expenses	15,000
Total	$ 735,20

** These amounts are estimates.

All of the expenses set forth above shall be borne by the Company.

ITEM 28. PERSONS CONTROLLED BY OR UNDER COMMON CONTROL

As of December 31, 2009, the Registrant owns a controlling interest in the following companies: a 78.11% interest in Acquisitions Corp., a Delaware corporation; a 40% interest in C&J Cladding, LLC, a Delaware limited liability compa 100% interest in Change Clean Energy Holdings, Inc., a Delaware corporation (as well as an indirect controlling inter DownEast Power Company, LLC, a Delaware limited liability company); a 51% interest in Worcester Energy Corporat Maine limited liability company; a 100% interest in Worcester Energy Holdings, Inc., a Maine corporation (as well indirect controlling interest in Biochips LLC, a Maine corporation 51% owned by Worcester Energy Holdings, Inc.); a interest in Worcester Energy Partners, Inc., a Delaware corporation (as well as an indirect controlling interest in Pre Logging & Landclearing, Inc., a Delaware corporation 100% owned by Worcester Energy Partners, Inc.); a 49% inter Integrated Contract Services, Inc., a Delaware corporation; a 100% interest in The Healing Staff, f/k/a Lisamarie Fallon a Texas corporation; a 100% interest in Vets Securing America, Inc., a Delaware corporation; a 79.83% interest in Iron Coiled Tubing, Inc., an Alberta corporation; a 100% interest in Gas Solutions Holdings, Inc., a Delaware corporation; a interest in NRG Manufacturing, Inc., a Texas corporation; a 74.51% interest in R-V Industries, Inc., a Pennsylvania corpor and a 100% interest in Yatesville Coal Holdings, Inc., a Delaware corporation (as well as indirect controlling intere Eastern Kentucky Coal Holdings, Inc., a Delaware corporation, North Fork Collieries LLC, a Delaware limited lia company, E&L Construction Inc., a Kentucky corporation and C&A Construction Inc., a Kentucky corporation, each of is 100% owned by Yatesville, and Genesis Coal Corp., a Kentucky corporation 78% owned by Yatesville).

Prospect Capital Management LLC, a Delaware limited liability company, owns shares of the Registrant, representing 2.6
the common stock outstanding. Without conceding that Prospect Capital Management controls the Registrant, an affili
Prospect Capital Management is the general partner of, and may be deemed to control, the following entities:

Name	Jurisdiction of Organization
Prospect Street Ventures I, LLC	Delaware
Prospect Management Group LLC	Delaware
Prospect Street Broadband LLC	Delaware
Prospect Street Energy LLC	Delaware
Prospect Administration LLC	Delaware

ITEM 29. NUMBER OF HOLDERS OF SECURITIES

The following table sets forth the approximate number of record holders of our common stock at February 25, 2010.

Title of Class	Number Record Holders
Common Stock, par value $.001 per share	69

ITEM 30. INDEMNIFICATION

Maryland law permits a Maryland corporation to include in its charter a provision limiting the liability of its director
officers to the corporation and its stockholders for money damages except for liability resulting from (a) actual receipt
improper benefit or profit in money, property or services or (b) active and deliberate dishonesty established by a final judg
as being material to the cause of action. Our charter contains such a provision which eliminates directors' and officers' lia
to the maximum extent permitted by Maryland law, subject to the requirements of the 1940 Act.

Our charter authorizes us, to the maximum extent permitted by Maryland law and subject to the requirements of the 194
to obligate ourselves to indemnify any present or former director or officer or any individual who, while a director or offic
at our request, serves or has served another corporation, real estate investment trust, partnership, joint venture, trust, emp
benefit plan or other enterprise as a director, officer, partner or trustee, from and against any claim or liability to whic
person may become subject or which that person may incur by reason of his or her service in any such capacity and to p
reimburse their reasonable expenses in advance of final disposition of a proceeding. Our bylaws obligate us, to the max
extent permitted by Maryland law and subject to the requirements of the 1940 Act, to indemnify any present or former di
or officer or any individual who, while a director or officer and at our request, serves or has served another corporatio
estate investment trust, partnership, joint venture, trust, employee benefit plan or other enterprise as a director, officer, p
or trustee and who is made, or threatened to be made, a party to the proceeding by reason of his or her service in any
capacity from and against any claim or liability to which that person may become subject or which that person may in
reason of his or her service in any such capacity and to pay or reimburse their reasonable expenses in advance of
disposition of a proceeding. The charter and bylaws also permit us to indemnify and advance expenses to any perso
served a predecessor of us in any of the capacities described above and any of our employees or agents or any employ
agents of our predecessor. In accordance with the 1940 Act, we will not indemnify any person for any liability to which
person would be subject by reason of such person's willful misfeasance, bad faith, gross negligence or reckless disregard
duties involved in the conduct of his office.

Maryland law requires a corporation (unless its charter provides otherwise, which our charter does not) to indemnify a di
or officer who has been successful, on the merits or otherwise, in the defense of any proceeding to which he or she is ma
threatened to be made, a party by reason of his or her service in that capacity. Maryland law permits a corporation to inde
its present and former directors and officers, among others, against judgments, penalties, fines, settlements and reaso
expenses actually incurred by them in connection with any proceeding to which they may be made, or threatened to be m
party by reason of their service in those or other capacities unless it is established that (a) the act or omission of the direc
officer was material to the matter giving rise to the proceeding and (1) was committed in bad faith or (2) was the result of
and deliberate dishonesty, (b) the director or officer actually received an improper personal benefit in money, prope
services or (c) in the case of any criminal proceeding, the director or officer had reasonable cause to believe that the
omission was unlawful. However, under Maryland law, a Maryland corporation may not indemnify for an adverse judgm

a suit by or in the right of the corporation or for a judgment of liability on the basis that a personal benefit was impro received, unless in either case a court orders indemnification, and then only for expenses. In addition, Maryland law per corporation to advance reasonable expenses to a director or officer upon the corporation's receipt of (a) a written affirmati the director or officer of his or her good faith belief that he or she has met the standard of conduct necessary for indemnifi by the corporation and (b) a written undertaking by

him or her or on his or her behalf to repay the amount paid or reimbursed by the corporation if it is ultimately determine
the standard of conduct was not met.

The Investment Advisory Agreement provides that, absent willful misfeasance, bad faith or gross negligence in the perforn
of its duties or by reason of the reckless disregard of its duties and obligations, Prospect Capital Management LLC
"Adviser") and its officers, managers, agents, employees, controlling persons, members and any other person or entity affi
with it are entitled to indemnification from the Company for any damages, liabilities, costs and expenses (including reaso
attorneys' fees and amounts reasonably paid in settlement) arising from the rendering of the Adviser's services und
Investment Advisory Agreement or otherwise as an Investment Adviser of the Company.

The Administration Agreement provides that, absent willful misfeasance, bad faith or negligence in the performance
duties or by reason of the reckless disregard of its duties and obligations, Prospect Administration LLC and its off
manager, agents, employees, controlling persons, members and any other person or entity affiliated with it are entit
indemnification from the Company for any damages, liabilities, costs and expenses (including reasonable attorneys' fee
amounts reasonably paid in settlement) arising from the rendering of Prospect Administration LLC's services unde
Administration Agreement or otherwise as administrator for the Company.

The Administrator is authorized to enter into one or more sub-administration agreements with other service providers (e
"Sub-Administrator") pursuant to which the Administrator may obtain the services of the service providers in fulfilli
responsibilities hereunder. Any such sub-administration agreements shall be in accordance with the requirements of the
Act and other applicable U.S. Federal and state law and shall contain a provision requiring the Sub-Administrator to co
with the same restrictions applicable to the Administrator.

ITEM 31. BUSINESS AND OTHER CONNECTIONS OF INVESTMENT ADVISER

A description of any other business, profession, vocation or employment of a substantial nature in which the Adviser, and
managing member, director or executive officer of the Adviser, is or has been during the past two fiscal years, engaged
his or her own account or in the capacity of director, officer, employee, partner or trustee, is set forth in Part A o
Registration Statement in the section entitled "Management." Additional information regarding the Adviser and its office
directors is set forth in its Form ADV, as filed with the Securities and Exchange Commission (SEC File No.801-62969),
incorporated herein by reference.

ITEM 32. LOCATION OF ACCOUNTS AND RECORDS

All accounts, books and other documents required to be maintained by Section 31(a) of the Investment Company Act of
and the rules thereunder are maintained at the offices of:

(1) the Registrant, Prospect Capital Corporation, 10 East 40th Street, 44th Floor, New York, NY 10016;

(2) the Transfer Agent, American Stock Transfer & Trust Company;

(3) the Custodian, U.S. Bank National Association; and

(4) the Adviser, Prospect Capital Management LLC, 10 East 40th Street, 44th Floor, New York, NY 10016.

ITEM 33. MANAGEMENT SERVICES

Not Applicable.

ITEM 34. UNDERTAKINGS

1. The Registrant undertakes to suspend the offering of shares until the prospectus is amended if (1) subsequent to the eff date of its registration statement, the net asset value declines more than ten percent from its net asset value as of the effe date of the registration statement; or (2) the net asset value increases to an amount greater than the net proceeds as stated prospectus.

2. Any securities not taken in a rights offering by stockholders are to be reoffered to the public, an undertaking to supple the prospectus, after the expiration of the subscription period, to set forth the results of the subscription offer, the transactio underwriters during the subscription period, the amount of unsubscribed securities to be purchased by underwriters, an terms of any subsequent reoffering thereof. If any public offering by the underwriters of the securities being registered is made on terms differing from those set forth on the cover page of the prospectus, we will file a post-effective amendment forth the terms of such offering.

3. The Registrant undertakes:

(a) to file, during any period in which offers or sales are being made, a post-effective amendment to the regist statement:

(1) to include any prospectus required by Section 10(a)(3) of the 1933 Act;

(2) to reflect in the prospectus any facts or events after the effective date of the registration statement (o most recent post-effective amendment thereof) which, individually or in the aggregate, represe fundamental change in the information set forth in the registration statement; and

(3) to include any material information with respect to the plan of distribution not previously disclosed i registration statement or any material change to such information in the registration statement;

(b) that, for the purpose of determining any liability under the 1933 Act, each such post-effective amendment be deemed to be a new registration statement relating to the securities offered therein, and the offering of t securities at that time shall be deemed to be the initial bona fide offering thereof;

(c) to remove from registration by means of a post-effective amendment any of the securities being registered w remain unsold at the termination of the offering;

(d) that, for the purpose of determining liability under the 1933 Act to any purchaser, each prospectus filed purs to Rule 497(b), (c), (d) or (e) under the 1933 Act as part of a registration statement relating to an offering, o than prospectuses filed in reliance on Rule 430A under the 1933 Act, shall be deemed to be part of and incl in the registration statement as of the date it is first used after effectiveness. Provided, however, tha statement made in a registration statement or prospectus that is part of the registration statement or made document incorporated or deemed incorporated by reference into the registration statement or prospectus th part of the registration statement will, as to a purchaser with a time of contract of sale prior to such first

supersede or modify any statement that was made in the registration statement or prospectus that was part o
registration statement or made in any such document immediately prior to such date of first use; and

(e) that, for the purpose of determining liability of the Registrant under the 1933 Act to any purchaser in the i
distribution of securities: The undersigned Registrant undertakes that in a primary offering of securities o
undersigned Registrant pursuant to this registration statement, regardless of the underwriting method used t
the securities to the purchaser, if the securities are offered or sold to such purchaser by means of any o
following communications, the undersigned Registrant will be a seller to the purchaser and will be conside
offer or sell such securities to the purchaser: (1) any preliminary prospectus or prospectus of the unders
Registrant relating to the offering required to be filed pursuant to Rule 497 under the 1933 Act; (2) the port
any advertisement pursuant to Rule 482 under the 1933 Act relating to the offering containing material inforn
about the undersigned Registrant or its securities provided by or on behalf of the undersigned Registrant; ar
any other communication that is an offer in the offering made by the undersigned Registrant to the purchaser.

SIGNATURES

Pursuant to the requirements of the Securities Act of 1933, the Registrant has duly caused this Registration Statement on N-2 to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of New York, in the State of York, on the 26th day of February, 2010.

PROSPECT CAPITAL CORPORATION

By: /s/ John F. Barry III
John F. Barry III
Chief Executive Officer and
Chairman of the Board of Directors

Pursuant to the requirements of the Securities Act of 1933, this Registration Statement has been signed by the following pe in the capacities indicated on February 26, 2010. This document may be executed by the signatories hereto on any numl counterparts, all of which constitute one and the same instrument.

Signature	Title
/s/ John F. Barry III John F. Barry III	Chief Executive Officer and Chairman of the Board of Directors (principal executive officer)
/s/ M. Grier Eliasek M. Grier Eliasek	Chief Operating Officer and Director
/s/ Brian H. Oswald Brian H. Oswald	Chief Financial Officer, Treasurer and Secretary (principal financial and accounting officer)
/s/ Graham D.S. Anderson Graham D.S. Anderson	Director
/s/ Andrew C. Cooper Andrew C. Cooper	Director
/s/ Eugene S. Stark Eugene S. Stark	Director

INDEX TO EXHIBITS

(l)	Opinion and Consent of Venable LLP, as special Maryland counsel for Registrant
(n)(i)	Consent of independent registered public accounting firm
(n)(ii)	Report of independent registered public accounting firm on "Senior Securities" table