PROSPECT CAPITAL CORP
Form N-2/A
October 18, 2011

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As filed with the Securities and Exchange Commission on October 18, 2011

Registration No. 333-176637

U.S. SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM N-2

ý REGISTRATION STATEMENT UNDER THE SECURITIES ACT OF 1933
ý PRE-EFFECTIVE AMENDMENT NO. 2
o POST-EFFECTIVE AMENDMENT NO.

PROSPECT CAPITAL CORPORATION

(Exact Name of Registrant as Specified in Charter)

10 East 40th Street, 44th Floor
New York, NY 10016
(Address of Principal Executive Offices)

Registrant's Telephone Number, including Area Code: **(212) 448-0702**

John F. Barry III
Brian H. Oswald
c/o Prospect Capital Management LLC
10 East 40th Street, 44th Floor
New York, NY 10016
(212) 448-0702
(Name and Address of Agent for Service)

Copies of information to:

Richard T. Prins
Skadden Arps Slate Meagher & Flom LLP
4 Times Square
New York, NY 10036
(212) 735-3000

Approximate Date of Proposed Public Offering: As soon as practicable after the effective date of this Registration Statement.

If any securities being registered on this form will be offered on a delayed or continuous basis in reliance on Rule 415 under the Securities Act of 1933, other than securities offered in connection with a distribution reinvestment plan, check the following box. ý

It is proposed that this filing will become effective (check appropriate box):

o when declared effective pursuant to section 8(c).
If appropriate, check the following box:

o This post-effective amendment designates a new effective date for a previously filed post-effective amendment registration statement.

o This form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act and the Securities Act registration statement number of the earlier effective registration statement for the same offering is .

CALCULATION OF REGISTRATION FEE UNDER THE SECURITIES ACT OF 1933

Title of Securities Being Registered	Amount Being Registered	Proposed Maximum Offering Price Per Unit	Proposed Maximum Aggregate Offering Price(1)	Amount of Registration Fee
Common Stock, $.001 par value per share(2)				
Preferred Stock, $.001 par value per share(2)				
Debt Securities(3)				
Warrants(4)				
Total	$750,000,000		$750,000,000(5)	$63,301(6)

(1) Estimated solely for the purpose of calculating the registration fee. Pursuant to Rule 457(o) of the rules and regulations under the Securities Act of 1933 (the "Securities Act"), which permits the registration fee to be calculated on the basis of the maximum offering price of all the securities listed, the table does not specify by each class information as to the amount to be registered, proposed maximum offering price per unit or proposed maximum aggregate offering price. Pursuant to Rule 415(a)(6) under the Securities Act, this registration statement covers a total of $530,675,000 of unsold securities that had previously been registered under the registrant's registration statement on Form N-2, initially filed with the Securities and Exchange Commission (the "SEC") on November 19, 2010 (No. 333-170724) (the "Prior Registration Statement") and that are being carried forward to this registration statement. The Prior Registration Statement initially registered securities for a maximum aggregate offering price of $750,000,000 and of that amount the registrant has previously sold common stock for an aggregate offering price of $219,325,000, leaving a balance of unsold securities with an aggregate offering price of $530,675,000. In connection with the registration of securities on the Prior Registration Statement, the registrant paid a registration fee of $37,837 covering such unsold securities and which registration fee is being carried forward to this registration statement and will continue to be applied to such unsold securities pursuant to Rule 415(a)(6). Pursuant to Rule 415(a)(6), the offering of the unsold securities registered under the Prior Registration Statement will be deemed terminated as of the date of effectiveness of this registration statement. If the registrant sells any of such unsold securities pursuant to the Prior Registration Statement after the date of the initial filing, and prior to the date of effectiveness, of this registration statement, the registrant will file a pre-effective amendment to this registration statement which will reduce the number of such unsold securities included on this registration statement.

(2) Subject to Note 6 below, there is being registered hereunder an indeterminate principal amount of common stock or preferred stock as may be sold, from time to time.

(3) Subject to Note 6 below, there is being registered hereunder an indeterminate principal amount of debt securities as may be sold, from time to time. If any debt securities are issued at an original issue discount, then the offering price shall be in such greater principal amount as shall result in an aggregate price to investors not to exceed $750,000,000.

(4) Subject to Note 6 below, there is being registered hereunder an indeterminate principal amount of warrants as may be sold, from time to time, representing rights to purchase common stock, preferred stock or debt securities.

(5) In no event will the aggregate offering price of all securities issued from time to time pursuant to this registration statement exceed $750,000,000.

(6) Previously paid.

THE REGISTRANT HEREBY AMENDS THIS REGISTRATION STATEMENT ON SUCH DATE OR DATES AS MAY BE NECESSARY TO DELAY ITS EFFECTIVE DATE UNTIL THE REGISTRANT SHALL FILE A FURTHER AMENDMENT WHICH SPECIFICALLY STATES THAT THE REGISTRATION STATEMENT SHALL THEREAFTER BECOME EFFECTIVE IN ACCORDANCE WITH SECTION 8(A) OF THE

SECURITIES ACT OF 1933 OR UNTIL THE REGISTRATION STATEMENT SHALL BECOME EFFECTIVE ON SUCH DATES AS THE COMMISSION, ACTING PURSUANT TO SAID SECTION 8(A), MAY DETERMINE.

The information in this preliminary prospectus 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. This preliminary prospectus 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.

SUBJECT TO COMPLETION, DATED OCTOBER 18, 2011

$750,000,000

PROSPECT CAPITAL CORPORATION

Common Stock
Preferred Stock
Debt Securities
Warrants

We may offer, from time to time, in one or more offerings or series, together or separately, up to $750,000,000 of our common stock, preferred stock, debt securities, warrants representing rights to purchase shares of common stock, preferred stock or debt securities, collectively, the Securities, to provide us with additional capital. Securities may be offered at prices and on terms to be disclosed in one or more supplements to this prospectus. You should read this prospectus and the applicable prospectus supplement carefully before you invest in our Securities.

We may offer shares of common stock, or warrants, options or rights to acquire shares of common stock, at a discount to net asset value per share in certain circumstances. Sales of common stock at prices below net asset value per share dilute the interests of existing stockholders, have the effect of reducing our net asset value per share and may reduce our market price per share. At our 2010 annual meeting, held on December 10, 2010, our stockholders approved our ability to sell or otherwise issue an unlimited number of shares of our common stock at any level of discount from net asset value per share for a period of twelve months, expiring on December 10, 2011. We are currently seeking stockholder approval at our 2011 annual meeting, to be held on December 8, 2011, to continue for an additional year our ability to issue shares of common stock below net asset value, subject to the condition that the maximum number of shares salable below net asset value pursuant to this authority in any particular offering that could result in such dilution is limited to 25% of our then outstanding common stock immediately prior to each such offering.

Our Securities may be offered directly to one or more purchasers, or through agents designated from time to time by us, or to or through underwriters or dealers. The prospectus supplement relating to the offering will identify any agents or underwriters involved in the sale of our Securities, and will disclose any applicable purchase price, fee, commission or discount arrangement between us and our agents or underwriters or among our underwriters or the basis upon which such amount may be calculated. See "Plan of Distribution." We may not sell any of our Securities through agents, underwriters or dealers without delivery of the prospectus and a prospectus supplement describing the method and terms of the offering of such Securities. Our common stock is traded on The NASDAQ Global Select Market under the symbol "PSEC." As of October 17, 2011, the last reported sales price for our common stock was $8.86.

Prospect Capital Corporation, or the Company, is a company that lends to and invests in middle market privately-held companies. Prospect Capital Corporation, a Maryland corporation, has been organized as a closed-end investment company since April 13, 2004 and has filed an election to be treated as a business development company under the Investment Company Act of 1940, as amended, or the 1940 Act, and is a non-diversified investment company within the meaning of the 1940 Act.

Prospect Capital Management LLC, our investment adviser, manages our investments and Prospect Administration LLC, our administrator, provides the administrative services necessary for us to operate.

Investing in our Securities involves a heightened risk of total loss of investment and is subject to risks. Before buying any Securities, you should read the discussion of the material risks of investing in our Securities in "Risk Factors" beginning on page 10 of this prospectus.

This prospectus contains important information about us that you should know before investing in our Securities. Please read it before making an investment decision and keep it for future reference. We file annual, quarterly and current reports, proxy statements and other information about us with the Securities and Exchange Commission, or the SEC. You may make inquiries or obtain this information free of charge by writing to Prospect Capital Corporation at 10 East 40th Street, 44th Floor, New York, NY 10016, or by calling 212-448-0702. Our Internet address is http://www.prospectstreet.com. Information contained on our website is not incorporated by reference into this prospectus and you should not consider information contained on our website to be a part of this prospectus. You may also obtain information about us from our website and the SEC's website (http://www.sec.gov).

The SEC has not approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

This prospectus may not be used to consummate sales of securities unless accompanied by a prospectus supplement.

The date of this Prospectus is , 2011

Table of Contents

TABLE OF CONTENTS

Table of Contents

ABOUT THIS PROSPECTUS

This prospectus is part of a registration statement that we have filed with the SEC, using the "shelf" registration process. Under the shelf registration process, we may offer, from time to time on a delayed basis, up to $750,000,000 of our common stock, preferred stock, debt securities or warrants representing rights to purchase shares of our common stock, preferred stock or debt securities, on the terms to be determined at the time of the offering. The Securities may be offered at prices and on terms described in one or more supplements to this prospectus. This prospectus provides you with a general description of the Securities that we may offer. Each time we use this prospectus to offer Securities, we will provide a prospectus supplement that will contain specific information about the terms of that offering. The prospectus supplement may also add, update or change information contained in this prospectus. Please carefully read this prospectus and any prospectus supplement together with any exhibits and the additional information described under the heading "Available Information" and the section under the heading "Risk Factors" before you make an investment decision.

Table of Contents

PROSPECTUS SUMMARY

The following summary contains basic information about this offering. It does not contain all the information that may be important to an investor. For a more complete understanding of this offering, we encourage you to read this entire document and the documents to which we have referred.

Information contained or incorporated by reference in this prospectus may contain "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, which are statements about the future that may be identified by the use of forward-looking terminology such as "may," "will," "expect," "intend," "plans," "anticipate," "estimate" or "continue" or the negative thereof or other variations thereon or comparable terminology. These forward-looking statements do not meet the safe harbor for forward-looking statements pursuant to Section 27A of the Securities Act of 1933, as amended, or the Securities Act. The matters described in "Risk Factors" and certain other factors noted throughout this prospectus and in any exhibits to the registration statement of which this prospectus is a part, constitute cautionary statements identifying important factors with respect to any such forward-looking statements, including certain risks and uncertainties, that could cause actual results to differ materially from those in such forward-looking statements. The Company reminds all investors that no forward-looking statement can be relied upon as an accurate or even mostly accurate forecast because humans cannot forecast the future.

The terms "we," "us," "our," "Prospect," and "Company" refer to Prospect Capital Corporation; "Prospect Capital Management" or the "Investment Adviser" refers to Prospect Capital Management LLC, our investment adviser; and "Prospect Administration" or the "Administrator" refers to Prospect Administration LLC, our administrator.

The Company

We are a financial services company that lends to and invests in middle market privately-held companies.

We were originally organized under the name "Prospect Street Energy Corporation" and we changed our name to "Prospect Energy Corporation" in June 2004. We changed our name again to "Prospect Capital Corporation" in May 2007 and at the same time terminated our policy of investing at least 80% of our net assets in energy companies. From our inception to the fiscal year ended June 30, 2007, we invested primarily in industries related to the industrial/energy economy. Since then, we have widened our strategy to focus on other sectors of the economy and continue to broaden our portfolio holdings.

We have been organized as a closed-end investment company since April 13, 2004 and have filed an election to be treated as a business development company under the 1940 Act. We are a non-diversified company within the meaning of the 1940 Act. Our headquarters are located at 10 East 40th Street, 44th Floor, New York, NY 10016, and our telephone number is (212) 448-0702.

The Investment Adviser

Prospect Capital Management, an affiliate of the Company, manages our investment activities. Prospect Capital Management is an investment adviser that has been registered under the Investment Advisers Act of 1940, or the Advisers Act, since March 31, 2004. Under an investment advisory and management agreement between us and Prospect Capital Management, or the Investment Advisory Agreement, we have agreed to pay Prospect Capital Management investment advisory fees, which will consist of an annual base management fee based on our gross assets, which we define as total assets without deduction for any liabilities (and, accordingly, includes the value of assets acquired with proceeds from borrowings), as well as a two-part incentive fee based on our performance.

Table of Contents

The Offering

We may offer, from time to time, in one or more offerings or series, together or separately, up to $750,000,000 of our Securities, which we expect to use initially to maintain balance sheet liquidity, involving repayment of debt under our credit facility, investment in high quality short-term debt instruments or a combination thereof, and thereafter to make long-term investments in accordance with our investment objectives.

Our Securities may be offered directly to one or more purchasers, through agents designated from time to time by us, or to or through underwriters or dealers. The prospectus supplement relating to a particular offering will disclose the terms of that offering, including the name or names of any agents or underwriters involved in the sale of our Securities by us, the purchase price, and any fee, commission or discount arrangement between us and our agents or underwriters or among our underwriters, or the basis upon which such amount may be calculated. See "Plan of Distribution." We may not sell any of our Securities through agents, underwriters or dealers without delivery of a prospectus supplement describing the method and terms of the offering of our Securities.

We may sell our common stock, or warrants, options or rights to acquire our common stock, at a price below the current net asset value of our common stock upon approval of our directors, including a majority of our independent directors, in certain circumstances. At our 2010 annual meeting, held on December 10, 2010, our stockholders approved our ability to sell or otherwise issue an unlimited number of shares of our common stock at any level of discount from net asset value per share for a period of twelve months, expiring on December 10, 2011. We are currently seeking stockholder approval at our 2011 annual meeting, to be held on December 8, 2011, to continue for an additional year our ability to issue shares of common stock below net asset value, subject to the condition that the maximum number of shares salable below net asset value pursuant to this authority in any particular offering that could result in such dilution is limited to 25% of our then outstanding common stock immediately prior to each such offering. Similarly, our stockholders approved our ability to issue warrants, options or rights to acquire our common stock at our 2008 annual meeting of stockholders for an unlimited time period and in accordance with the 1940 Act which provides that the conversion or exercise price of such warrants, options or rights may be less than net asset value per share at the date such securities are issued or at the date such securities are converted into or exercised for shares of our common stock. See "Sales of Common Stock Below Net Asset Value" in this prospectus and in the prospectus supplement, if applicable. Sales of common stock at prices below net asset value per share dilute the interests of existing stockholders, have the effect of reducing our net asset value per share and may reduce our market price per share. We have no current intention of engaging in a rights offering, although we reserve the right to do so in the future.

Set forth below is additional information regarding the offering of our Securities:

Use of proceeds	Unless otherwise specified in a prospectus supplement, we intend to use the net proceeds from selling Securities pursuant to this prospectus initially to maintain balance sheet liquidity, involving repayment of debt under our credit facility, investments in high quality short-term debt instruments or a combination thereof, and thereafter to make long-term investments in accordance with our investment objective. See "Use of Proceeds."

Table of Contents

Distributions	In June 2010, our Board of Directors approved a change in dividend policy from quarterly distributions to monthly distributions. Since that time, we have paid monthly distributions to the holders of our common stock and generally intend to continue to do so. The amount of the monthly distributions is determined by our Board of Directors and is based on our estimate of our investment company taxable income and net short-term capital gains. Certain amounts of the monthly distributions may from time to time be paid out of our capital rather than from earnings for the month as a result of our deliberate planning or accounting reclassifications. Distributions in excess of our current or accumulated earnings or profits constitute a return of capital and will reduce the stockholder's adjusted tax basis in such stockholder's common stock. After the adjusted basis is reduced to zero, these distributions will constitute capital gains to such stockholders. Certain additional amounts may be deemed as distributed to stockholders for income tax purposes. Other types of Securities will likely pay distributions in accordance with their terms. See "Price Range of Common Stock," "Distributions" and "Material U.S. Federal Income Tax Considerations."
Taxation	We have qualified and elected to be treated for U.S. Federal income tax purposes as a regulated investment company, or a RIC, under Subchapter M of the Internal Revenue Code of 1986, or the Code. As a RIC, we generally do not have to pay corporate-level U.S. Federal income taxes on any ordinary income or capital gains that we distribute to our stockholders as dividends. To maintain our qualification as a RIC and obtain RIC tax treatment, we must maintain specified source-of-income and asset diversification requirements and distribute annually at least 90% of our ordinary income and realized net short-term capital gains in excess of realized net long-term capital losses, if any. See "Distributions" and "Material U.S. Federal Income Tax Considerations."
Dividend reinvestment plan	We have a dividend reinvestment plan for our stockholders. This is an "opt out" dividend reinvestment plan. As a result, when we declare a dividend, the dividends are automatically reinvested in additional shares of our common stock, unless a stockholder specifically "opts out" of the dividend reinvestment plan so as to receive cash dividends. Stockholders who receive distributions in the form of stock are subject to the same U.S. Federal, state and local tax consequences as stockholders who elect to receive their distributions in cash. See "Dividend Reinvestment Plan."
The NASDAQ Global Select Market Symbol	PSEC
Anti-takeover provisions	Our charter and bylaws, as well as certain statutory and regulatory requirements, contain provisions that may have the effect of discouraging a third party from making an acquisition proposal for us. These anti-takeover provisions may inhibit a change in control in circumstances that could give the holders of our common stock the opportunity to realize a premium over the market price of our common stock. See "Description Of Our Capital Stock."

Table of Contents

Management arrangements	Prospect Capital Management serves as our investment adviser. Prospect Administration serves as our administrator. For a description of Prospect Capital Management, Prospect Administration and our contractual arrangements with these companies, see "Business Management Services Investment Advisory Agreement," and "Business Management Services Administration Agreement."
Risk factors	Investment in our Securities involves certain risks relating to our structure and investment objective that should be considered by prospective purchasers of our Securities. We have a limited operating history upon which you can evaluate our business. In addition, as a business development company, our portfolio primarily includes securities issued by privately-held companies. These investments generally involve a high degree of business and financial risk, and are less liquid than public securities. We are required to mark the carrying value of our investments to fair value on a quarterly basis, and economic events, market conditions and events affecting individual portfolio companies can result in quarter-to-quarter mark-downs and mark-ups of the value of individual investments that collectively can materially affect our net asset value, or NAV. Also, our determinations of fair value of privately-held securities may differ materially from the values that would exist if there was a ready market for these investments. A large number of entities compete for the same kind of investment opportunities as we do. Moreover, our business requires a substantial amount of capital to operate and to grow and we seek additional capital from external sources. In addition, the failure to qualify as a RIC eligible for pass-through tax treatment under the Code on income distributed to stockholders could have a materially adverse effect on the total return, if any, obtainable from an investment in our Securities. See "Risk Factors" and the other information included in this prospectus for a discussion of factors you should carefully consider before deciding to invest in our Securities.
Plan of distribution	We may offer, from time to time, up to $750,000,000 of our common stock, preferred stock, debt securities or warrants representing rights to purchase shares of our common stock, preferred stock or debt securities, on the terms to be determined at the time of the offering. Securities may be offered at prices and on terms described in one or more supplements to this prospectus directly to one or more purchasers, through agents designated from time to time by us, or to or through underwriters or dealers. The supplement to this prospectus relating to the offering will identify any agents or underwriters involved in the sale of our Securities, and will set forth any applicable purchase price, fee and commission or discount arrangement or the basis upon which such amount may be calculated. We may not sell Securities pursuant to this prospectus without delivering a prospectus supplement describing the method and terms of the offering of such Securities. For more information, see "Plan of Distribution."

Table of Contents

Fees and Expenses

The following tables are intended to assist you in understanding the costs and expenses that an investor in this offering will bear directly or indirectly. We caution you that some of the percentages indicated in the table below are estimates and may vary. In these tables, we assume that we have borrowed $1,072.5 million. We do not intend to issue preferred stock during the year. Except where the context suggests otherwise, whenever this prospectus contains a reference to fees or expenses paid by "you" or "us" or that "we" will pay fees or expenses, the Company will pay such fees and expenses out of our net assets and, consequently, you will indirectly bear such fees or expenses as an investor in the Company. However, you will not be required 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)	5.00%
Offering expenses borne by us (as a percentage of offering price)(2)	0.50%
Dividend reinvestment plan expenses(3)	None
Total stockholder transaction expenses (as a percentage of offering price)(4)	5.50%
Annual expenses (as a percentage of net assets attributable to common stock)(4):	
Management fees(5)	3.98%
Incentive fees payable under Investment Advisory Agreement (20% of realized capital gains and 20% of pre-incentive fee net investment income)(6)	2.11%
Total advisory fees	6.09%
Interest payments on the credit facility	2.86%
Interest payments on the 2010 Notes(7)	0.84%
Interest payments on the 2011 Notes(8)	0.85%
Total interest expense	4.55%
Acquired Fund Fees and Expenses(9)	0.01%
Other expenses(10)	1.52%
Total annual expenses(6)(10)	12.18%

Example

The following table demonstrates the projected dollar amount of cumulative expenses we would pay out of net assets and that you would indirectly bear over various periods with respect to a hypothetical investment in our common stock. In calculating the following expense amounts, we have assumed we would have borrowed $1,072.5 million, that our annual operating expenses would remain at the levels set forth in the table above and that we would pay the 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	$ 150.09	$ 326.06	$ 484.67	$ 816.06

While the example assumes, as required by the SEC, a 5% annual return, our performance will vary and may result in a return greater or less than 5%. The income incentive fee under our Investment Advisory Agreement with Prospect Capital Management is unlikely to be material assuming a 5% annual return and is not included in the example. If we achieve sufficient returns on our investments, including through the realization of capital gains, to trigger an incentive fee of a material amount, our distributions to our common stockholders and our expenses would likely be higher. In

Table of Contents

addition, while the example assumes reinvestment of all dividends and other distributions at NAV, participants in our dividend reinvestment plan will receive a number of shares of our common stock determined by dividing the total dollar amount of the distribution payable to a participant by the market price per share of our common stock at the close of trading on the valuation date for the distribution. See "Dividend Reinvestment Plan" 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. Actual expenses (including the cost of debt, if any, and other expenses) may be greater or less than those shown.

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(1) In the event that the Securities to which this prospectus relates are sold to or through underwriters, a corresponding prospectus supplement will disclose the estimated applicable sales load.

(2) The related prospectus supplement will disclose the estimated amount of offering expenses, the offering price and the estimated offering expenses borne by us as a percentage of the offering price.

(3) The expenses of the dividend reinvestment plan are included in "other expenses."

(4) The related prospectus supplement will disclose the offering price and the total stockholder transaction expenses as a percentage of the offering price.

(5) Our base management fee is 2% of our gross assets (which include any amount borrowed, i.e., total assets without deduction for any liabilities). Although we have no intent to borrow more than $1,072.5 million, however, assuming that we borrowed $1,072.5 million, the 2% management fee of gross assets equals approximately 3.98% of net assets. Based on our total borrowings as of October 18, 2011 of $553 million, the 2% management fee of gross assets equals approximately 3.01% of net assets. See "Business Management Services Investment Advisory Agreement" and footnote 6 below.

(6) Based on the incentive fee paid during our fiscal year ended June 30, 2011, all of which consisted of an income incentive fee. For a more detailed discussion of the calculation of the two-part incentive fee, see "Management Services Investment Advisory Agreement" in this prospectus.

(7) On December 21, 2010, the Company issued $150 million in aggregate principal amount of 6.25% Convertible Senior Notes due 2015, which we refer to as the 2010 Notes. See "Business General" and "Risk Factors Risks Related to our Business" for more detail on the 2010 Notes.

(8) On February 18, 2011, the Company issued $172.5 million in aggregate principal amount of 5.5% Convertible Senior Notes due 2016, which we refer to as the 2011 Notes. See "Business General" and "Risk Factors Risks Related to our Business" for more detail on the 2011 Notes. The 2011 Notes and the 2010 Notes are referred to collectively as the Notes.

(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 Company is invested in as of June 30, 2011. When applicable, fees and expenses are based on historic fees and expenses 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 similar 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 performance of the investment companies, which may fluctuate over time. The amount of the Company's

Table of Contents

average net assets used in calculating this percentage was based on net assets of approximately $1.1 billion as of June 30, 2011.

(10) "Other expenses" are based on estimated amounts for the current fiscal year. The amount shown above represents annualized expenses during our three months ended June 30, 2011 representing all of our estimated recurring operating expenses (except fees and expenses reported in other items of this table) that are deducted from our operating income and reflected as expenses in our Statement of Operations. The estimate of our overhead expenses, including payments under an administration agreement with Prospect Administration, or the Administration Agreement, based on our projected allocable portion of overhead and other expenses incurred by Prospect Administration in performing its obligations under the Administration Agreement. "Other expenses" does not include non-recurring expenses. See "Business Management Services Administration Agreement."

Table of Contents

SELECTED CONDENSED FINANCIAL DATA

You should read the condensed consolidated financial information below with the Consolidated Financial Statements and notes thereto included in this prospectus. Financial information below for the years ended June 30, 2011, 2010, 2009, 2008 and 2007 has been derived from the financial statements that were audited by our independent registered public accounting firm. Certain reclassifications have been made to the prior period financial information to conform to the current period presentation. See "Management's Discussion and Analysis of Financial Condition and Results of Operations" starting on page 32 for more information.

	For the Year/Period Ended June 30,				
	2011	2010	2009	2008	2007
(in thousands except data relating to shares, per share and number of portfolio companies)					
Performance Data:					
Interest income	$ 134,454	$ 86,518	$ 62,926	$ 59,033	$ 30,084
Dividend income	15,092	15,366	22,793	12,033	6,153
Other income	19,930	12,675	14,762	8,336	4,444
Total investment income	169,476	114,559	100,481	79,402	40,681
Interest and credit facility expenses	(17,598)	(8,382)	(6,161)	(6,318)	(1,903)
Investment advisory expense	(46,051)	(30,727)	(26,705)	(20,199)	(11,226)
Other expenses	(11,606)	(8,260)	(8,452)	(7,772)	(4,421)
Total expenses	(75,255)	(47,369)	(41,318)	(34,289)	(17,550)
Net investment income	94,221	67,190	59,163	45,113	23,131
Realized and unrealized gains (losses)	24,017	(47,565)	(24,059)	(17,522)	(6,403)
Net increase in net assets from operations	$ 118,238	$ 19,625	$ 35,104	$ 27,591	$ 16,728
Per Share Data:					
Net increase in net assets from operations(1)	$ 1.38	$ 0.33	$ 1.11	$ 1.17	$ 1.06
Distributions declared per share	$ (1.21)	$ (1.33)	$ (1.62)	$ (1.59)	$ (1.54)
Average weighted shares outstanding for the period	85,978,757	59,429,222	31,559,905	23,626,642	15,724,095
Assets and Liabilities Data:					
Investments	$ 1,463,010	$ 748,483	$ 547,168	$ 497,530	$ 328,222
Other assets	86,307	84,212	119,857	44,248	48,280
Total assets	1,549,317	832,695	667,025	541,778	376,502
Amount drawn on credit facility	84,200	100,300	124,800	91,167	
2010 Notes	150,000				
2011 Notes	172,500				
Amount owed to related parties	7,918	9,300	6,713	6,641	4,838
Other liabilities	20,342	11,671	2,916	14,347	71,616
Total liabilities	434,960	121,271	134,429	112,155	76,454
Net assets	$ 1,114,357	$ 711,424	$ 532,596	$ 429,623	$ 300,048
Investment Activity Data:					
No. of portfolio companies at period end	72	58	30	29(2)	24(2)

Acquisitions	$	953,337	$	364,788(3)	$	98,305	$	311,947	$	167,255
Sales, repayments, and other disposals	$	285,562	$	136,221	$	27,007	$	127,212	$	38,407
Weighted-Average Yield at end of period(4)		12.8%		14.2%		13.7%		15.5%		17.1%

(1) Per share data is based on average weighted shares for the period

(2) Includes a net profits interest in Charlevoix Energy Trading LLC ("Charlevoix"), remaining after loan was paid.

(3) Includes $207,126 of acquired portfolio investments from Patriot Acquisition.

(4) Includes dividends from certain equity investments.

Table of Contents

RISK FACTORS

Investing in our Securities involves a high degree of risk. You should carefully consider the risks described below, together with all of the other information included in this prospectus, before you decide whether to make an investment in our Securities. The risks set forth below are not the only risks we face. If any of the adverse events or conditions described below occur, our business, financial condition and results of operations could be materially adversely affected. In such case, our NAV, and the trading price of our common stock could decline, or the value of our preferred stock, debt securities, and warrants, if any are outstanding, may decline, and you may lose all or part of your investment.

Risks Relating To Our Business

We may suffer credit losses.

Investment in small and middle-market companies is highly speculative and involves a high degree of risk of credit loss. These risks are likely to increase during volatile economic periods, such as the US and many other economies have recently been experiencing. See "Risks Related to Our Investments."

Our financial condition and results of operations will depend on our ability to manage our future growth effectively.

Prospect Capital Management has been registered as an investment adviser since March 31, 2004, and we have been organized as a closed-end investment company since April 13, 2004. Our ability to achieve our investment objective depends on our ability to grow, which depends, in turn, on our Investment Adviser's ability to continue to identify, analyze, invest in and monitor companies that meet our investment criteria. Accomplishing this result on a cost-effective basis is largely a function of our Investment Adviser's structuring of investments, its ability to provide competent, attentive and efficient services to us and our access to financing on acceptable terms. As we continue to grow, Prospect Capital Management will need to continue to hire, train, supervise and manage new employees. Failure to manage our future growth effectively could have a materially adverse effect on our business, financial condition and results of operations.

We are dependent upon Prospect Capital Management's key management personnel for our future success.

We depend on the diligence, skill and network of business contacts of the senior management of our Investment Adviser. We also depend, to a significant extent, on our Investment Adviser's access to the investment professionals and the information and deal flow generated by these investment professionals in the course of their investment and portfolio management activities. The senior management team of the Investment Adviser evaluates, negotiates, structures, closes, monitors and services our investments. Our success depends to a significant extent on the continued service of the senior management team, particularly John F. Barry III and M. Grier Eliasek. The departure of any of the senior management team could have a materially adverse effect on our ability to achieve our investment objective. In addition, we can offer no assurance that Prospect Capital Management will remain our investment adviser or that we will continue to have access to its investment professionals or its information and deal flow.

We operate in a highly competitive market for investment opportunities.

A large number of entities compete with us to make the types of investments that we make in target companies. We compete with other business development companies, public and private funds, commercial and investment banks and commercial financing companies. Additionally, because competition for investment opportunities generally has increased among alternative investment vehicles, such as hedge funds, those entities have begun to invest in areas they have not traditionally invested in, including investments in middle-market companies. As a result of these new entrants, competition for investment opportunities at middle-market companies has intensified, a trend we expect to continue.

Table of Contents

Many of our existing and potential competitors are substantially larger and have considerably greater financial, technical and marketing resources than we do. For example, some competitors may have a lower cost of funds and access to funding sources that are not available to us. In addition, some of our competitors may have higher risk tolerances or different risk assessments, which could allow them to consider a wider variety of investments and establish more or fuller relationships with borrowers and sponsors than us. Furthermore, many of our competitors are not subject to the regulatory restrictions that the 1940 Act imposes on us as a business development company. We cannot assure you that the competitive pressures we face will not have a materially adverse effect on our business, financial condition and results of operations. Also, as a result of existing and increasing competition and our competitors ability to provide a total package solution, we may not be able to take advantage of attractive investment opportunities from time to time, and we can offer no assurance that we will be able to identify and make investments that are consistent with our investment objective.

We do not seek to compete primarily based on the interest rates that we offer, and we believe that some of our competitors make loans with interest rates that are comparable to or lower than the rates we offer. We may lose investment opportunities if we do not match our competitors' pricing, terms and structure. If we match our competitors' pricing, terms and structure, we may experience decreased net interest income and increased risk of credit loss.

Most of our portfolio investments are recorded at fair value as determined in good faith by our Board of Directors and, as a result, there is uncertainty as to the value of our portfolio investments.

A large percentage of our portfolio investments consist of securities of privately held companies. Hence, market quotations are generally not readily available for determining the fair values of such investments. The determination of fair value, and thus the amount of unrealized losses we may incur in any year, is to a degree subjective, and the Investment Adviser has a conflict of interest in making the determination. We value these securities quarterly at fair value as determined in good faith by our Board of Directors based on input from our Investment Adviser, a third party independent valuation firm and our audit committee. Our Board of Directors utilizes the services of an independent valuation firm to aid it in determining the fair value of any securities. The types of factors that may be considered in determining the fair values of our investments include the nature and realizable value of any collateral, the portfolio company's ability to make payments and its earnings, the markets in which the portfolio company does business, comparison to publicly traded companies, discounted cash flow, current market interest rates and other relevant factors. Because such valuations, and particularly valuations of private securities and private companies, are inherently uncertain, the valuations may fluctuate significantly over short periods of time due to changes in current market conditions. The determinations of fair value by our Board of Directors may differ materially from the values that would have been used if an active market and market quotations existed for these investments. Our net asset value could be adversely affected if the determinations regarding the fair value of our investments were materially higher than the values that we ultimately realize upon the disposal of such securities.

In addition, decreases in the market values or fair values of our investments are recorded as unrealized depreciation. Unprecedented declines in prices and liquidity in the corporate debt markets experienced during the recent financial crises resulted in significant net unrealized depreciation in our portfolio in the past. The effect of all of these factors on our portfolio reduced our NAV by increasing net unrealized depreciation in our portfolio. Depending on market conditions, we could incur substantial realized losses and may continue to suffer additional unrealized losses in future periods, which could have a material adverse impact on our business, financial condition and results of operations. We have no policy regarding holding a minimum level of liquid assets. As such, a high percentage of our portfolio generally is not liquid at any given point in time. See "   The lack of liquidity may adversely affect our business."

Table of Contents

Senior securities, including debt, expose us to additional risks, including the typical risks associated with leverage and could adversely affect our business, financial condition and results of operations.

We currently use our revolving credit facility to leverage our portfolio and we expect in the future to borrow from and issue senior debt securities to banks and other lenders and may securitize certain of our portfolio investments. We also have the Notes outstanding, which are a form of leverage and are senior in payment to our common stock.

With certain limited exceptions, as a business development company, or BDC, we are only allowed to borrow amounts such that our asset coverage, as defined in the 1940 Act, is at least 200% after such borrowing. The amount of leverage that we employ will depend on our Investment Adviser's and our Board of Directors' assessment of market conditions and other factors at the time of any proposed borrowing. There is no assurance that a leveraging strategy will be successful. Leverage involves risks and special considerations for stockholders, including the following, any of which could adversely affect our business, financial condition and result of operations:

- A likelihood of greater volatility in the net asset value and market price of our common stock;
- Diminished operating flexibility as a result of asset coverage or investment portfolio composition requirements required by lenders or investors that are more stringent than those imposed by the 1940 Act;
- The possibility that investments will have to be liquidated at less than full value or at inopportune times to comply with debt covenants or to pay interest or dividends on the leverage;
- Increased operating expenses due to the cost of leverage, including issuance and servicing costs;
- Convertible or exchangeable securities issued in the future may have rights, preferences and privileges more favorable than those of our common stock;
- Subordination to lenders' superior claims on our assets as a result of which lenders will be able to receive proceeds available in the case of our liquidation before any proceeds will be distributed to our stockholders;
- Making it more difficult for us to meet our payment and other obligations under the Notes and our other outstanding debt;
- The occurrence of an event of default if we fail to comply with the financial and/or other restrictive covenants contained in our debt agreements, including the credit agreement and each indenture governing the Notes, which event of default could result in all or some of our debt becoming immediately due and payable;
- Reduced availability of our cash flow to fund investments, acquisitions and other general corporate purposes, and limiting our ability to obtain additional financing for these purposes;
- The risk of increased sensitivity to interest rate increases on our indebtedness with variable interest rates, including borrowings under our amended senior credit facility; and
- Reduced flexibility in planning for, or reacting to, and increasing our vulnerability to, changes in our business, the industry in which we operate and the general economy.

For example, the amount we may borrow under our revolving credit facility is determined, in part, by the fair value of our investments. If the fair value of our investments declines, we may be forced to sell investments at a loss to maintain compliance with our borrowing limits. Other debt facilities we may enter into in the future may contain similar provisions. Any such forced sales would reduce our NAV and also make it difficult for the net asset value to recover. Our Investment Adviser and our Board of Directors in their best judgment nevertheless may determine to use leverage if they expect that the benefits to our stockholders of maintaining the leveraged position will outweigh the risks.

Table of Contents

In addition, our ability to meet our payment and other obligations of the Notes and our credit facility depends on our ability to generate significant cash flow in the future. This, to some extent, is subject to general economic, financial, competitive, legislative and regulatory factors as well as other factors that are beyond our control. We cannot assure you that our business will generate cash flow from operations, or that future borrowings will be available to us under our existing credit facility or otherwise, in an amount sufficient to enable us to meet our payment obligations under the Notes and our other debt and to fund other liquidity needs. If we are not able to generate sufficient cash flow to service our debt obligations, we may need to refinance or restructure our debt, including the Notes, sell assets, reduce or delay capital investments, or seek to raise additional capital. If we are unable to implement one or more of these alternatives, we may not be able to meet our payment obligations under the Notes and our other debt.

Illustration. The following table illustrates the effect of leverage on returns from an investment in our common stock assuming various annual returns, net of interest expense. The calculations in the table below are hypothetical and actual returns may be higher or lower than those appearing below. The calculation assumes (i) $1.5 billion in total assets, (ii) an average cost of funds of 4.73%, (iii) $1,072.5 million in debt outstanding and (iv) $1.1 billion of stockholders' equity.

Assumed Return on Our Portfolio (net of expenses)	**(10)%**	**(5)%**	**0%**	**5%**	**10%**
Corresponding Return to Stockholder	(24.73)%	(14.64)%	(4.55)%	5.54%	15.63%

The assumed portfolio return is required by regulation of the SEC and is not a prediction of, and does not represent, our projected or actual performance. Actual returns may be greater or less than those appearing in the table.

The Notes present other risks to holders of our common stock, including the possibility that the Notes could discourage an acquisition of the Company by a third party and accounting uncertainty.

Certain provisions of the Notes could make it more difficult or more expensive for a third party to acquire us. Upon the occurrence of certain transactions constituting a fundamental change, holders of the Notes will have the right, at their option, to require us to repurchase all of their Notes or any portion of the principal amount of such Notes in integral multiples of $1,000. We may also be required to increase the conversion rate or provide for conversion into the acquirer's capital stock in the event of certain fundamental changes. These provisions could discourage an acquisition of us by a third party.

The accounting for convertible debt securities is subject to frequent scrutiny by the accounting regulatory bodies and is subject to change. We cannot predict if or when any such change could be made and any such change could have an adverse impact on our reported or future financial results. Any such impacts could adversely affect the market price of our common stock.

We fund a portion of our investments with borrowed money, which magnifies the potential for gain or loss on amounts invested and may increase the risk of investing in us.

Borrowings and other types of financing, also known as leverage, magnify the potential for gain or loss on amounts invested and, therefore, increase the risks associated with investing in our securities. Our lenders have fixed dollar claims on our assets that are superior to the claims of our common stockholders or any preferred stockholders. If the value of our assets increases, then leveraging would cause the net asset value to increase more sharply than it would have had we not leveraged. Conversely, if the value of our assets decreases, leveraging would cause net asset value to decline more sharply than it otherwise would have had we not leveraged. Similarly, any increase in our income in excess of consolidated interest payable on the borrowed funds would cause our net income to increase more than it would without the leverage, while any decrease in our income would cause net income to decline more sharply than it would have had we not borrowed. Such a decline could negatively affect

Table of Contents

our ability to make common stock dividend payments. Leverage is generally considered a speculative investment technique.

We may in the future determine to fund a portion of our investments with preferred stock, which would magnify the potential for gain or loss and the risks of investing in us in the same way as our borrowings.

Preferred stock, which is another form of leverage, has the same risks to our common stockholders as borrowings because the dividends on any preferred stock we issue must be cumulative. Payment of such dividends and repayment of the liquidation preference of such preferred stock must take preference over any dividends or other payments to our common stockholders, and preferred stockholders are not subject to any of our expenses or losses and are not entitled to participate in any income or appreciation in excess of their stated preference.

In addition to regulatory restrictions that restrict our ability to raise capital, our credit facility contains various covenants which, if not complied with, could accelerate repayment under the facility, thereby materially and adversely affecting our liquidity, financial condition and results of operations.

The agreement governing our credit facility requires us to comply with certain financial and operational covenants. These covenants include:

- restrictions on the level of indebtedness that we are permitted to incur in relation to the value of our assets;
- restrictions on our ability to incur liens; and
- maintenance of a minimum level of stockholders' equity.

As of June 30, 2011, we were in compliance with these covenants. However, our continued compliance with these covenants depends on many factors, some of which are beyond our control. Accordingly, there are no assurances that we will continue to comply with the covenants in our credit facility. Failure to comply with these covenants would result in a default under this facility which, if we were unable to obtain a waiver from the lenders thereunder, could result in an acceleration of repayments under the facility and thereby have a material adverse impact on our business, financial condition and results of operations.

Failure to extend our existing credit facility, the revolving period of which is currently scheduled to expire on June 13, 2012, could have a material adverse effect on our results of operations and financial position and our ability to pay expenses and make distributions.

The revolving period for our credit facility with a syndicate of lenders is currently scheduled to terminate on June 13, 2012. If the credit facility is not renewed or extended by the participant banks by June 13, 2012, we will not be able to make further borrowings under the facility after such date and the outstanding principal balance on that date will be due and payable on June 13, 2013. At June 30, 2011 we had outstanding borrowings of $84.2 million under our credit facility. Interest on borrowings under the credit facility is one-month LIBOR plus 325 basis points, subject to a minimum LIBOR floor of 100 basis points. Additionally, the lenders charge a fee on the unused portion of the credit facility equal to either 75 basis points if at least half of the credit facility is used or 100 basis points otherwise. If we are unable to extend our facility or find a new source of borrowing on acceptable terms, we will be required to pay down the amounts outstanding under the facility during the one-year term-out period through one or more of the following: (1) principal collections on our securities pledged under the facility, (2) at our option, interest collections on our securities pledged under the facility and cash collections on our securities not pledged under the facility, or (3) possible liquidation of some or all of our loans and other assets, any of which could have a material adverse effect on our results of operations and financial position and may force us to decrease or stop paying certain expenses and making distributions until the facility is repaid. In addition, our stock price could decline significantly,

Table of Contents

we would be restricted in our ability to acquire new investments and, in connection with our year-end audit, our independent registered accounting firm could raise an issue as to our ability to continue as a going concern.

Changes in interest rates may affect our cost of capital and net investment income.

A significant portion of the debt investments we make bears interest at fixed rates and the value of these investments could be negatively affected by increases in market interest rates. In addition, as the interest rate on our revolving credit facility is at a variable rate based on an index, an increase in interest rates would make it more expensive to use debt to finance our investments. As a result, a significant increase in market interest rates could both reduce the value of our portfolio investments and increase our cost of capital, which would reduce our net investment income.

We need to raise additional capital to grow because we must distribute most of our income.

We need additional capital to fund growth in our investments. A reduction in the availability of new capital could limit our ability to grow. We must distribute at least 90% of our ordinary income and realized net short-term capital gains in excess of realized net long-term capital losses, if any, to our shareholders to maintain our RIC status. As a result, such earnings are not available to fund investment originations. We have sought additional capital by borrowing from financial institutions and may issue debt securities or additional equity securities. If we fail to obtain funds from such sources or from other sources to fund our investments, we could be limited in our ability to grow, which may have an adverse effect on the value of our common stock. In addition, as a business development company, we are generally required to maintain a ratio of total assets to total borrowings and other senior securities of at least 200%, which may restrict our ability to borrow in certain circumstances.

The lack of liquidity in our investments may adversely affect our business.

We generally make investments in private companies. Substantially all of these securities are subject to legal and other restrictions on resale or are otherwise less liquid than publicly traded securities. The illiquidity of our investments may make it difficult for us to sell such investments if the need arises. In addition, if we are required to liquidate all or a portion of our portfolio quickly, we may realize significantly less than the value at which we have previously recorded our investments. In addition, we may face other restrictions on our ability to liquidate an investment in a portfolio company to the extent that we or our Investment Adviser has material non-public information regarding such portfolio company.

We may experience fluctuations in our quarterly results.

We could experience fluctuations in our quarterly operating results due to a number of factors, including the interest or dividend rates payable on the debt or equity securities we hold, the default rate on debt securities, the level of our expenses, variations in and the timing of the recognition of realized and unrealized gains or losses, the degree to which we encounter competition in our markets, the seasonality of the energy industry, weather patterns, changes in energy prices and general economic conditions. As a result of these factors, results for any period should not be relied upon as being indicative of performance in future periods.

Our most recent NAV was calculated as of June 30, 2011 and our NAV when calculated as of September 30, 2011 may be higher or lower.

Our most recently estimated NAV per share is $10.04 on an as adjusted basis solely to give effect to distributions with record dates of July 29, 2011, August 31, 2011 and September 30, 2011, our issuance of common stock on July 22, 2011, August 26, 2011 and September 23, 2011 in connection with our dividend reinvestment plan, and our issuance of 1,500,000 shares of common stock on July 18, 2011 in connection with the option granted with the June 21, 2011 offering of 10,000,000 shares which were delivered June 24, 2011, versus $10.36 determined by us as of June 30, 2011. NAV per share as of September 30, 2011, may be higher or lower than $10.04 based on potential changes in valuations and earnings for the quarter then ended. Our Board of Directors has not yet determined the fair value of portfolio investments at any date subsequent to June 30, 2011. Our Board of Directors determines the fair value of our portfolio investments on a quarterly basis in connection with the preparation of quarterly financial statements and based on input from an independent valuation firm, our Investment Adviser and the audit committee of our Board of Directors.

Potential conflicts of interest could impact our investment returns.

Our executive officers and directors, and the executive officers of our Investment Adviser, Prospect Capital Management, may serve as officers, directors or principals of entities that operate in the same or related lines of business as we do or of investment funds managed by our affiliates. Accordingly, they may have obligations to investors in those entities, the fulfillment of which might not be in our best interests or those of our stockholders. Nevertheless, it is possible that new investment opportunities that meet our investment objective may come to the attention of one of these entities in connection with another investment advisory client or program, and, if so, such opportunity might not be offered, or otherwise made available, to us. However, as an investment adviser, Prospect Capital Management has a fiduciary obligation to act in the best interests of its clients, including us. To that end, if Prospect Capital Management or its affiliates manage any additional investment vehicles or client accounts in the future, Prospect Capital Management will endeavor to allocate investment opportunities in a fair and equitable manner over time so as not to discriminate unfairly against any client. If Prospect Capital Management chooses to establish another investment fund in the future, when the investment professionals of Prospect Capital Management identify an investment, they will have to choose which investment fund should make the investment.

In the course of our investing activities, under the Investment Advisory Agreement we pay base management and incentive fees to Prospect Capital Management, and reimburse Prospect Capital Management for certain expenses it incurs. As a result of the Investment Advisory Agreement, there may be times when the senior management team of Prospect Capital Management has interests that differ from those of our stockholders, giving rise to a conflict.

Prospect Capital Management receives a quarterly income incentive fee based, in part, on our pre-incentive fee net investment income, if any, for the immediately preceding calendar quarter. This income incentive fee is subject to a fixed quarterly hurdle rate before providing an income incentive fee return to the Investment Adviser. This fixed hurdle rate was determined when then current interest rates were relatively low on a historical basis. Thus, if interest rates rise, it would become easier for our investment income to exceed the hurdle rate and, as a result, more likely that our Investment Adviser will receive an income incentive fee than if interest rates on our investments remained constant or decreased. Subject to the receipt of any requisite stockholder approval under the 1940 Act, our Board of Directors may adjust the hurdle rate by amending the Investment Advisory Agreement.

The income incentive fee payable by us is computed and paid on income that may include interest that has been accrued but not yet received in cash. If a portfolio company defaults on a loan that has a deferred interest feature, it is possible that interest accrued under such loan that has previously been included in the calculation of the income incentive fee will become uncollectible. If this happens, our Investment Adviser is not required to reimburse us for any such income incentive fee payments. If we do not have sufficient liquid assets to pay this incentive fee or distributions to stockholders on such accrued income, we may be required to liquidate assets in order to do so. This fee structure could give rise to a conflict of interest for our Investment Adviser to the extent that it may encourage the Investment Adviser to favor debt financings that provide for deferred interest, rather than current cash payments of interest.

Table of Contents

We have entered into a royalty-free license agreement with Prospect Capital Management. Under this agreement, Prospect Capital Management agrees to grant us a non-exclusive license to use the name "Prospect Capital." Under the license agreement, we have the right to use the "Prospect Capital" name for so long as Prospect Capital Management or one of its affiliates remains our Investment Adviser. In addition, we rent office space from Prospect Administration, an affiliate of Prospect Capital Management, and pay Prospect Administration our allocable portion of overhead and other expenses incurred by Prospect Administration in performing its obligations as Administrator under the Administration Agreement, including rent and our allocable portion of the costs of our chief financial officer and chief compliance officer and their respective staffs. This may create conflicts of interest that our Board of Directors monitors.

Our incentive fee could induce Prospect Capital Management to make speculative investments.

The incentive fee payable by us to Prospect Capital Management may create an incentive for our Investment Adviser to make investments on our behalf that are more speculative or involve more risk than would be the case in the absence of such compensation arrangement. The way in which the incentive fee payable is determined (calculated as a percentage of the return on invested capital) may encourage the Investment Adviser to use leverage to increase the return on our investments. Increased use of leverage and this increased risk of replacement of that leverage at maturity, would increase the likelihood of default, which would disfavor holders of our common stock. Similarly, because the Investment Adviser will receive an incentive fee based, in part, upon net capital gains realized on our investments, the Investment Adviser may invest more than would otherwise be appropriate in companies whose securities are likely to yield capital gains, as compared to income producing securities. Such a practice could result in our investing in more speculative securities than would otherwise be the case, which could result in higher investment losses, particularly during economic downturns.

The incentive fee payable by us to Prospect Capital Management could create an incentive for our Investment Adviser to invest on our behalf in instruments, such as zero coupon bonds, that have a deferred interest feature. Under these investments, we would accrue interest income over the life of the investment but would not receive payments in cash on the investment until the end of the term. Our net investment income used to calculate the income incentive fee, however, includes accrued interest. For example, accrued interest, if any, on our investments in zero coupon bonds will be included in the calculation of our incentive fee, even though we will not receive any cash interest payments in respect of payment on the bond until its maturity date. Thus, a portion of this incentive fee would be based on income that we may not have yet received in cash in the event of default may never receive.

We may be obligated to pay our investment adviser incentive compensation even if we incur a loss.

Our investment adviser is entitled to incentive compensation for each fiscal quarter based, in part, on our pre-incentive fee net investment income if any, for the immediately preceeding calendar quarter above a performance threshold for that quarter. Accordingly, since the performance threshold is based on a percentage of our net asset value, decreases in our net asset value make it easier to achieve the performance threshold. Our pre-incentive fee net investment income for incentive compensation purposes excludes realized and unrealized capital losses or depreciation that we may incur in the fiscal quarter, even if such capital losses or depreciation result in a net loss on our statement of operations for that quarter. Thus, we may be required to pay Prospect Capital Management incentive compensation for a fiscal quarter even if there is a decline in the value of our portfolio or we incur a net loss for that quarter.

Table of Contents

Changes in laws or regulations governing our operations may adversely affect our business.

We and our portfolio companies are subject to regulation by laws at the local, state and U.S. Federal levels. These laws and regulations, as well as their interpretation, may be changed from time to time. Accordingly, changes in these laws or regulations could have a material adverse effect on our business. For additional information regarding the regulations we are subject to, see "Regulation."

Foreign and domestic political risk may adversely affect our business.

We are exposed to political risk to the extent that Prospect Capital Management, on its behalf and subject to its investment guidelines, transacts in securities in the U.S. and foreign markets. The governments in any of these jurisdictions could impose restrictions, regulations or other measures, which may have a material adverse impact on our strategy.

Capital markets have recently been in a period of disruption and instability. These market conditions have materially and adversely affected debt and equity capital markets in the United States and abroad, which have had, and may in the future have, a negative impact on our business and operations.

The U.S. and foreign capital markets have recently been in a period of disruption as evidenced by a lack of liquidity in the debt capital markets, significant write-offs in the financial services sector, the re-pricing of credit risk in the broadly syndicated credit market and the failure of certain major financial institutions. Despite actions of the United States federal government and foreign governments, these events contributed to worsening general economic conditions that materially and adversely impacted the broader financial and credit markets and reduced the availability of debt and equity capital for the market as a whole and financial services firms in particular. While these conditions appear to be improving, they could continue for a prolonged period of time or worsen in the future. In addition, while these conditions persist, we and other companies in the financial services sector may have to access, if available, alternative markets for debt and equity capital in order to grow. Equity capital may be difficult to raise because subject to some limited exceptions, as a BDC, we are generally not able to issue additional shares of our common stock at a price less than net asset value without first obtaining approval for such issuance from our stockholders and our independent directors. At our annual meeting of stockholders held on December 10, 2010, subject to certain determinations required to be made by our Board of Directors, our stockholders approved our ability to sell or otherwise issue shares of our common stock at a price below its then current net asset value per share for a twelve month period expiring on the anniversary of the date of stockholder approval. We are currently seeking stockholder approval at our 2011 annual meeting, to be held on December 8, 2011, to continue for an additional year our ability to issue shares of common stock below net asset value, subject to the condition that the maximum number of shares salable below net asset value pursuant to this authority in any particular offering that could result in such dilution is limited to 25% of our then outstanding common stock immediately prior to each such offering. In addition, our ability to incur indebtedness or issue other senior securities (including by issuing preferred stock) is limited by applicable regulations such that our asset coverage, as defined in the 1940 Act, must equal at least 200% immediately after each time we incur indebtedness or issue other senior securities. The debt capital that will be available, if at all, may be at a higher cost and on less favorable terms and conditions in the future. Any inability to raise capital could have a negative effect on our business, financial condition and results of operations.

Moreover, recent market conditions have made, and may in the future make, it difficult to extend the maturity of or refinance our existing indebtedness and any failure to do so could have a material adverse effect on our business. The illiquidity of our investments may make it difficult for us to sell such investments if required. As a result, we may realize significantly less than the value at which we have recorded our investments.

Given the recent extreme volatility and dislocation in the capital markets, many BDCs have faced, and may in the future face, a challenging environment in which to raise capital. Recent significant changes in the capital markets affecting our ability to raise capital have affected the pace of our investment activity. In addition, significant changes in the capital markets, including the recent extreme volatility and disruption, has had, and may in the future have, a negative effect on the valuations of our investments and on the potential for liquidity events involving our investments. An inability to raise capital, and any required sale of our investments for liquidity purposes, could have a material adverse impact on our business, financial condition or results of operations.

Risks Relating To Our Operation As A Business Development Company

A failure on our part to maintain our status as a business development company would significantly reduce our operating flexibility.

If we do not continue to qualify as a business development company, we might be regulated as a registered closed-end investment company under the 1940 Act; our failure to qualify as a BDC would make us subject to additional regulatory requirements, which may significantly decrease our operating flexibility by limiting our ability to employ leverage and issue common stock.

If we fail to qualify as a RIC, we will have to pay corporate-level taxes on our income, and our income available for distribution would be reduced.

To maintain our qualification for federal income tax purposes as a RIC under Subchapter M of the Code, and obtain RIC tax treatment, we must meet certain source of income, asset diversification and annual distribution requirements.

The source of income requirement is satisfied if we derive at least 90% of our annual gross income from interest, dividends, payments with respect to certain securities loans, gains from the sale or other disposition of securities or options thereon or foreign currencies, or other income derived with respect to our business of investing in such securities or currencies, and net income from interests in "qualified publicly traded partnerships," as defined in the Code.

The annual distribution requirement for a RIC is satisfied if we distribute at least 90% of our ordinary income and realized net short-term capital gains in excess of realized net long-term capital losses, if any, to our stockholders on an annual basis. Because we use debt financing, we are subject to certain asset coverage ratio requirements under the 1940 Act and financial covenants that could, under certain circumstances, restrict us from making distributions necessary to qualify for RIC tax treatment. If we are unable to obtain cash from other sources, we may fail to qualify for RIC tax treatment and, thus, may be subject to corporate-level income tax.

To maintain our qualification as a RIC, we must also meet certain asset diversification requirements at the end of each calendar quarter. Failure to meet these tests may result in our having to dispose of certain investments quickly in order to prevent the loss of RIC status. Because most of our investments are in private companies, any such dispositions could be made at disadvantageous prices and may result in substantial losses.

If we fail to qualify as a RIC for any reason or become subject to corporate income tax, the resulting corporate taxes would substantially reduce our net assets, the amount of income available for distribution, and the actual amount of our distributions. Such a failure would have a materially adverse effect on us and our stockholders. For additional information regarding asset coverage ratio and RIC requirements, see "Regulation Senior Securities" and "Material U.S. Federal Income Tax Considerations".

We may have difficulty paying our required distributions if we recognize income before or without receiving cash representing such income.

For U.S. federal income tax purposes, we include in income certain amounts that we have not yet received in cash, such as original issue discount or payment-in-kind interest, which represents contractual interest added to the loan balance and due at the end of the loan term. Such original issue

Table of Contents

discount, which could be significant relative to our overall investment activities, or increases in loan balances as a result of payment-in-kind arrangements, are included in our taxable income before we receive any corresponding cash payments. We also may be required to include in taxable income certain other amounts that we do not receive in cash. While we focus primarily on investments that will generate a current cash return, our investment portfolio currently includes, and we may continue to invest in, securities that do not pay some or all of their return in periodic current cash distributions.

The income incentive fee payable by us is computed and paid on income that may include interest that has been accrued but not yet received in cash. If a portfolio company defaults on a loan that is structured to provide accrued interest, it is possible that accrued interest previously used in the calculation of the income incentive fee will become uncollectible.

Since in some cases we may recognize taxable income before or without receiving cash representing such income, we may have difficulty distributing at least 90% of our ordinary income and realized net short-term capital gains in excess of realized net long-term capital losses, if any, as required to maintain RIC tax treatment. Accordingly, we may have to sell some of our investments at times we would not consider advantageous, raise additional debt or equity capital or reduce new investment originations to meet these distribution requirements. If we are not able to obtain cash from other sources, we may fail to qualify for RIC treatment and thus become subject to corporate-level income tax. See "Regulation Senior Securities" and "Material U.S. Federal Income Tax Considerations".

Regulations governing our operation as a business development company affect our ability to raise, and the way in which we raise, additional capital.

We have incurred indebtedness under our revolving credit facility and through the issuance of the Notes and, in the future, may issue preferred stock and/or borrow additional money from banks or other financial institutions, which we refer to collectively as "senior securities," up to the maximum amount permitted by the 1940 Act. Under the provisions of the 1940 Act, we are permitted, as a BDC, to incur indebtedness or issue senior securities only in amounts such that our asset coverage, as defined in the 1940 Act, equals at least 200% after each issuance of senior securities. If the value of our assets declines, we may be unable to satisfy this test, which would prohibit us from paying dividends and could prohibit us from qualifying as a RIC. If we cannot satisfy this test, we may be required to sell a portion of our investments or sell additional shares of common stock at a time when such sales may be disadvantageous in order to repay a portion of our indebtedness. In addition, issuance of additional common stock could dilute the percentage ownership of our current stockholders in us.

As a BDC regulated under provisions of the 1940 Act, we are not generally able to issue and sell our common stock at a price below the current net asset value per share. If our common stock trades at a discount to net asset value, this restriction could adversely affect our ability to raise capital. We may, however, sell our common stock, or warrants, options or rights to acquire our common stock, at a price below the current net asset value of our common stock in certain circumstances, including if (i)(1) the holders of a majority of our shares (or, if less, at least 67% of a quorum consisting of a majority of our shares) and a similar majority of the holders of our shares who are not affiliated persons of us approve the sale of our common stock at a price that is less than the current net asset value, and (2) a majority of our Directors who have no financial interest in the transaction and a majority of our independent Directors (a) determine that such sale is in our and our stockholders' best interests and (b) in consultation with any underwriter or underwriters of the offering, make a good faith determination as of a time either immediately prior to the first solicitation by us or on our behalf of firm commitments to purchase such shares, or immediately 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 closely approximates the market value of such shares, less any distributing commission or discount or if (ii) a majority of the number of the beneficial holders of our common stock entitled to vote at our annual meeting, without regard to whether a majority of such shares are voted in favor of the proposal, approve the sale of our

Table of Contents

common stock at a price that is less than the current net asset value per share. At our 2010 annual meeting of stockholders held on December 10, 2010, we obtained the first method of approval from our shareholders to sell an unlimited number of shares of common stock at any discount to net asset value per share for a period of twelve months, expiring on December 10, 2011. We are currently seeking stockholder approval at our 2011 annual meeting, to be held on December 8, 2011, to continue for an additional year our ability to issue shares of common stock below net asset value, subject to the condition that the maximum number of shares salable below net asset value pursuant to this authority in any particular offering that could result in such dilution is limited to 25% of our then outstanding common stock immediately prior to each such offering. We will not sell shares of common stock under a prospectus supplement to the registration statement (the "current registration statement") if the cumulative dilution to our NAV per share from offerings under the current registration statement exceeds 15%. See "If we sell common stock at a discount to our net asset value per share, stockholders who do not participate in such sale will experience immediate dilution in an amount that may be material" discussed below.

To generate cash for funding new investments, we pledged a substantial portion of our portfolio investments under our revolving credit facility. These assets are not available to secure other sources of funding or for securitization. Our ability to obtain additional secured or unsecured financing on attractive terms in the future is uncertain.

Alternatively, we may securitize our future loans to generate cash for funding new investments. See " Securitization of our assets subjects us to various risks."

Securitization of our assets subjects us to various risks.

We may securitize assets to generate cash for funding new investments. We refer to the term securitize to describe a form of leverage under which a company (sometimes referred to as an "originator" or "sponsor") transfers income producing assets to a single-purpose, bankruptcy-remote subsidiary (also referred to as a "special purpose entity" or SPE), which is established solely for the purpose of holding such assets and entering into a structured finance transaction. The SPE then issues notes secured by such assets. The special purpose entity may issue the notes in the capital markets either publicly or privately to a variety of investors, including banks, non-bank financial institutions and other investors. There may be a single class of notes or multiple classes of notes, the most senior of which carries less credit risk and the most junior of which may carry substantially the same credit risk as the equity of the SPE.

An important aspect of most debt securitization transactions is that the sale and/or contribution of assets into the SPE be considered a true sale and/or contribution for accounting purposes and that a reviewing court would not consolidate the SPE with the operations of the originator in the event of the originator's bankruptcy based on equitable principles. Viewed as a whole, a debt securitization seeks to lower risk to the note purchasers by isolating the assets collateralizing the securitization in an SPE that is not subject to the credit and bankruptcy risks of the originator. As a result of this perceived reduction of risk, debt securitization transactions frequently achieve lower overall leverage costs for originators as compared to traditional secured lending transactions.

In accordance with the above description, to securitize loans, we may create a wholly owned subsidiary and contribute a pool of our assets to such subsidiary. The SPE may be funded with, among other things, whole loans or interests from other pools and such loans may or may not be rated. The SPE would then sell its notes to purchasers who we would expect to be willing to accept a lower interest rate and the absence of any recourse against us to invest in a pool of income producing assets to which none of our creditors would have access. We would retain all or a portion of the equity in the SPE. An inability to successfully securitize portions of our portfolio or otherwise leverage our portfolio through secured and unsecured borrowings could limit our ability to grow our business and fully execute our business strategy, and could decrease our earnings, if any. However, the successful securitization of portions of our portfolio exposes us to a risk of loss for the equity we retain in the SPE and might expose us to greater risk on our remaining portfolio because the assets we retain may tend to be those that are riskier and more likely to generate losses. A successful securitization may also impose financial and operating covenants that restrict our business activities and may include limitations that could hinder our ability to finance additional loans and investments or to make the distributions required to maintain our status as a RIC under Subchapter M of the Code. The 1940 Act may also impose restrictions on the structure of any securitizations.

Interests we hold in the SPE, if any, will be subordinated to the other interests issued by the SPE. As such, we will only receive cash distributions on such interests if the SPE has made all cash interest and other required payments on all other interests it has issued. In addition, our subordinated interests will likely be unsecured and rank behind all of the secured creditors, known or unknown, of the SPE, including the holders of the senior interests it has issued. Consequently, to the extent that the value of the SPE's portfolio of assets has been reduced as a result of conditions in the credit markets, or as a result of defaults, the value of the subordinated interests we retain would be reduced. Securitization imposes on us the same risks as borrowing except that our risk in a securitization is limited to the amount of subordinated interests we retain, whereas in a borrowing or debt issuance by us directly we would be at risk for the entire amount of the borrowing or debt issuance.

Generally, we would expect the SPE not to be consolidated with us and in that event our only interest will be the value of our retained subordinated interest and the income allocated to us, which may be more or less than the cash we receive from the SPE, and none of the SPE's liabilities will be reflected as our liabilities. If the assets of the SPE are not consolidated with our assets and liabilities, then our interest in the SPE may be deemed not to be a qualifying asset for purposes of determining whether 70% of our assets are qualifying assets and the leverage incurred by such SPE may or may not be treated as borrowings by us for purposes of the requirement that we not issue senior securities in an amount in excess of our net assets.

We may also engage in transactions utilizing SPEs and securitization techniques where the assets sold or contributed to the SPE remain on our balance sheet for accounting purposes. If, for example, we sell the assets to the SPE with recourse or provide a guarantee or other credit support to the SPE, its assets will remain on our balance sheet. Consolidation would also generally result if we, in consultation with the SEC, determine that consolidation would result in a more accurate reflection of our assets, liabilities and results of operations. In these structures, the risks will be essentially the same as in other securitization transactions but the assets will remain our assets for purposes of the limitations described above on investing in assets that are not qualifying assets and the leverage incurred by the SPE will be treated as borrowings incurred by us for purposes of our limitation on the issuance of senior securities.

Our Investment Adviser may have conflicts of interest with respect to potential securitizations in as much as securitizations that are not consolidated may reduce our assets for purposes of determining its investment advisory fee although in some circumstances our investment adviser may be paid certain fees for managing the assets of the SPE so as to reduce or eliminate any potential bias against securitizations.

Our ability to invest in public companies may be limited in certain circumstances.

As a BDC, we must not acquire any assets other than "qualifying assets" specified in the 1940 Act unless, at the time the acquisition is made, at least 70% of our total assets are qualifying assets (with certain limited exceptions). Subject to certain exceptions for follow-on investments and distressed companies, an investment in an issuer that has outstanding securities listed on a national securities exchange may be treated as qualifying assets only if such issuer has a market capitalization that is less than $250 million at the time of such investment.

Table of Contents

Price declines and illiquidity in the corporate debt markets have adversely affected, and may in the future adversely affect, the fair value of our portfolio investments, reducing our net asset value through increased net unrealized depreciation.

As a BDC, we are required to carry our investments at market value or, if no market value is ascertainable, at fair value as determined in good faith by or under the direction of our Board of Directors. As part of the valuation process, the types of factors that we may take into account in determining the fair value of our investments include, as relevant and among other factors: available current market data, including relevant and applicable market trading and transaction comparables, applicable market yields and multiples, security covenants, call protection provisions, information rights, the nature and realizable value of any collateral, the portfolio company's ability to make payments, its earnings and discounted cash flows, the markets in which the portfolio company does business, comparisons of financial ratios of peer companies that are public, merger and acquisition comparables, our principal market (as the reporting entity) and enterprise values. Decreases in the market values or fair values of our investments are recorded as unrealized depreciation. Unprecedented declines in prices and liquidity in the corporate debt markets resulted in significant net unrealized depreciation in our portfolio in the past. The effect of all of these factors on our portfolio has reduced our net asset value by increasing net unrealized depreciation in our portfolio. Depending on market conditions, we could incur substantial realized losses and may suffer additional unrealized losses in future periods, which could have a material adverse impact on our business, financial condition and results of operations.

Our common stock may trade at a discount to our net asset value per share.

Common stock of BDCs, like that of closed-end investment companies, frequently trades at a discount to current net asset value, which could adversely affect the ability to raise capital. In the past, our common stock has traded at a discount to our net asset value. The risk that our common stock may continue to trade at a discount to our net asset value is separate and distinct from the risk that our net asset value per share may decline.

If we sell common stock at a discount to our net asset value per share, stockholders who do not participate in such sale will experience immediate dilution in an amount that may be material.

At our 2010 annual meeting of stockholders held on December 10, 2010, our stockholders approved our ability to sell an unlimited number of shares of our common stock at any level of discount from net asset value per share during the 12 month period following the December 10, 2010 approval in accordance with the exception described above in " Regulations governing our operation as a business development company affect our ability to raise, and the way in which we raise, additional capital." We are currently seeking stockholder approval at our 2011 annual meeting, to be held on December 8, 2011, to continue for an additional year our ability to issue shares of common stock below net asset value, subject to the condition that the maximum number of shares salable below net asset value pursuant to this authority in any particular offering that could result in such dilution is limited to 25% of our then outstanding common stock immediately prior to each such offering. The issuance or sale by us of shares of our common stock at a discount to net asset value poses a risk of dilution to our stockholders. In particular, stockholders who do not purchase additional shares at or below the discounted price in proportion to their current ownership will experience an immediate decrease in net asset value per share (as well as in the aggregate net asset value of their shares if they do not participate at all). These stockholders will also experience a disproportionately greater decrease in their participation in our earnings and assets and their voting power than the increase we experience in our assets, potential earning power and voting interests from such issuance or sale. In addition, such sales may adversely affect the price at which our common stock trades. For additional information and hypothetical examples of these risks, see "Sales of Common Stock Below Net Asset Value" and the prospectus supplement pursuant to which such sale is made. We have sold shares of our common stock

Table of Contents

at prices below net asset value per share and may continue to do so to the future. For additional information, see "Recent Sales of Common Stock Below Net Asset Value" in the prospectus supplement pursuant to which such sale is made, if applicable.

Our ability to enter into transactions with our affiliates is restricted.

We are prohibited under the 1940 Act from knowingly participating in certain transactions with our affiliates without the prior approval of our independent directors. Any person that owns, directly or indirectly, 5% or more of our outstanding voting securities is our affiliate for purposes of the 1940 Act and we are generally prohibited from buying or selling any security or other property from or to such affiliate, absent the prior approval of our independent directors. The 1940 Act also prohibits "joint" transactions with an affiliate, which could include investments in the same portfolio company (whether at the same or different times), without prior approval of our independent directors. We are prohibited from buying or selling any security or other property from or to our Investment Adviser and its affiliates and persons with whom we are in a control relationship, or entering into joint transactions with any such person, absent the prior approval of the SEC.

Risks Relating To Our Investments

We may not realize gains or income from our investments.

We seek to generate both current income and capital appreciation. However, the securities we invest in may not appreciate and, in fact, may decline in value, and the issuers of debt securities we invest in may default on interest and/or principal payments. Accordingly, we may not be able to realize gains from our investments, and any gains that we do realize may not be sufficient to offset any losses we experience. See "Business Our Investment Objective and Policies."

Our investments in prospective portfolio companies may be risky and we could lose all or part of our investment.

Some of our portfolio companies have relatively short or no operating histories. These companies are and will be subject to all of the business risk and uncertainties associated with any new business enterprise, including the risk that these companies may not reach their investment objective and the value of our investment in them may decline substantially or fall to zero.

In addition, investment in the middle market companies that we are targeting involves a number of other significant risks, including:

- these companies may have limited financial resources and may be unable to meet their obligations under their securities that we hold, which may be accompanied by a deterioration in the value of their securities or of any collateral with respect to any securities and a reduction in the likelihood of our realizing on any guarantees we may have obtained in connection with our investment;

- they may have shorter operating histories, narrower product lines and smaller market shares than larger businesses, which tend to render them more vulnerable to competitors' actions and market conditions, as well as general economic downturns;

- because many of these companies are privately held companies, public information is generally not available about these companies. As a result, we will depend on the ability of our Investment Adviser to obtain adequate information to evaluate these companies in making investment decisions. If our Investment Adviser is unable to uncover all material information about these companies, it may not make a fully informed investment decision, and we may lose money on our investments;

Table of Contents

- they are more likely to depend on the management talents and efforts of a small group of persons; therefore, the death, disability, resignation or termination of one or more of these persons could have a materially adverse impact on our portfolio company and, in turn, on us;

- they may have less predictable operating results, may from time to time be parties to litigation, may be engaged in changing businesses with products subject to a risk of obsolescence and may require substantial additional capital to support their operations, finance expansion or maintain their competitive position;

- they may have difficulty accessing the capital markets to meet future capital needs;

- increased taxes, regulatory expense or the costs of changes to the way they conduct business due to the effects of climate change may adversely affect their business, financial structure or prospects.

In addition, our executive officers, directors and our Investment Adviser could, in the ordinary course of business, be named as defendants in litigation arising from proposed investments or from our investments in the portfolio companies.

Economic recessions or downturns could impair our portfolio companies and harm our operating results.

The U.S. and foreign financial markets have been experiencing a high level of volatility, disruption and distress, which was exacerbated by the failure of several major financial institutions in the last few months of 2008. Despite actions of the United States federal government and foreign governments, these events contributed to worsening general economic conditions that materially and adversely impacted the broader financial and credit markets and reduced the availability of debt and equity capital for the market as a whole and financial services firms in particular. While these conditions appear to be improving, they could continue for a prolonged period of time or worsen in the future both in the U.S. and globally. Our portfolio companies will generally be affected by the conditions and overall strength of the national, regional and local economies, including interest rate fluctuations, changes in the capital markets and changes in the prices of their primary commodities and products. These factors also impact the amount of residential, industrial and commercial growth in the energy industry. Additionally, these factors could adversely impact the customer base and customer collections of our portfolio companies.

Many of our portfolio companies may be susceptible to economic slowdowns or recessions and may be unable to repay our loans or meet other obligations during these periods. Therefore, our non-performing assets are likely to increase, and the value of our portfolio is likely to decrease, during these periods. Adverse economic conditions also may decrease the value of collateral securing some of our loans and the value of our equity investments. Economic slowdowns or recessions could lead to financial losses in our portfolio and a decrease in revenues, net income and assets. Unfavorable economic conditions also could increase our funding costs, limit our access to the capital markets or result in a decision by lenders not to extend credit to us. These events could prevent us from increasing investments and harm our operating results.

A portfolio company's failure to satisfy financial or operating covenants imposed by us or other lenders could lead to defaults and, potentially, termination of its loans and foreclosure on its secured assets, which could trigger cross-defaults under other agreements and jeopardize a portfolio company's ability to meet its obligations under the debt or equity securities that we hold. We may incur expenses to the extent necessary to seek recovery upon default or to negotiate new terms, which may include the waiver of certain financial covenants, with a defaulting portfolio company. In addition, if one of our portfolio companies were to go bankrupt, even though we may have structured our interest as senior debt or preferred equity, depending on the facts and circumstances, including the extent to which we actually provided managerial assistance to that portfolio company, a bankruptcy court might re-characterize our debt or equity holding and subordinate all or a portion of our claim to those of other creditors.

Our portfolio contains a limited number of portfolio companies, which subjects us to a greater risk of significant loss if any of these companies defaults on its obligations under any of its debt securities.

A consequence of the limited number of investments in our portfolio is that the aggregate returns we realize may be significantly adversely affected if one or more of our significant portfolio company investments perform poorly or if we need to write down the value of any one significant investment. Beyond our income tax diversification requirements, we do not have fixed guidelines for diversification, and our portfolio could contain relatively few portfolio companies.

Our failure to make follow-on investments in our portfolio companies could impair the value of our portfolio.

Following an initial investment in a portfolio company, we may make additional investments in that portfolio company as "follow-on" investments, in order to: (1) increase or maintain in whole or in part our equity ownership percentage; (2) exercise warrants, options or convertible securities that were acquired in the original or subsequent financing or (3) attempt to preserve or enhance the value of our investment.

We may elect not to make follow-on investments, may be constrained in our ability to employ available funds, or otherwise may lack sufficient funds to make those investments. We have the discretion to make any follow-on investments, subject to the availability of capital resources. The failure to make follow-on investments may, in some circumstances, jeopardize the continued viability of a portfolio company and our initial investment, or may result in a missed opportunity for us to increase our participation in a successful operation. Even if we have sufficient capital to make a desired follow-on investment, we may elect not to make a follow-on investment because we may not want to increase our concentration of risk, because we prefer other opportunities, or because we are inhibited by compliance with BDC requirements or the desire to maintain our tax status.

We may be unable to invest the net proceeds raised from offerings on acceptable terms, which would harm our financial condition and operating results.

Until we identify new investment opportunities, we intend to either invest the net proceeds of future offerings in interest-bearing deposits or other short-term instruments or use the net proceeds from such offerings to reduce then-outstanding obligations under our credit facility. We cannot assure you that we will be able to find enough appropriate investments that meet our investment criteria or that any investment we complete using the proceeds from an offering will produce a sufficient return.

We may have limited access to information about privately held companies in which we invest.

We invest primarily in privately-held companies. Generally, little public information exists about these companies, and we are required to rely on the ability of our Investment Adviser's investment professionals to obtain adequate information to evaluate the potential returns from investing in these companies. These companies and their financial information are not subject to the Sarbanes-Oxley Act and other rules that govern public companies. If we are unable to uncover all material information about these companies, we may not make a fully informed investment decision, and we may lose money on our investment.

We may not be in a position to control a portfolio investment when we are a debt or minority equity investor and its management may make decisions that could decrease the value of our investment.

We make both debt and minority equity investments in portfolio companies. As a result, we are subject to the risk that a portfolio company may make business decisions with which we disagree, and the management of such company, as representatives of the holders of their common equity, may take risks or otherwise act in ways that do not serve our interests. As a result, a portfolio company may make decisions that could decrease the value of our portfolio holdings.

Our portfolio companies may incur debt or issue equity securities that rank equally with, or senior to, our investments in such companies.

We may invest in mezzanine debt and dividend-paying equity securities issued by our portfolio companies. Our portfolio companies usually have, or may be permitted to incur, other debt, or issue other equity securities, that rank equally with, or senior to, the securities in which we invest. By their terms, such instruments may provide that the holders are entitled to receive payment of dividends, interest or principal on or before the dates on which we are entitled to receive payments in respect of the securities in which we invest. Also, in the event of insolvency, liquidation, dissolution, reorganization or bankruptcy of a portfolio company, holders of securities ranking senior to our investment in that portfolio company would typically be entitled to receive payment in full before we receive any distribution in respect of our investment. After repaying the senior security holders, the portfolio company may not have any remaining assets to use for repaying its obligation to us. In the case of securities ranking equally with securities in which we invest, we would have to share on an equal basis any distributions with other security holders in the event of an insolvency, liquidation, dissolution, reorganization or bankruptcy of the relevant portfolio company.

We may not be able to fully realize the value of the collateral securing our debt investments.

Although a substantial amount of our debt investments are protected by holding security interests in the assets of the portfolio companies, we may not be able to fully realize the value of the collateral securing our investments due to one or more of the following factors:

- our debt investments may be made in the form of mezzanine loans, therefore our liens on the collateral, if any, may be subordinated to those of the senior secured debt of the portfolio companies, if any. As a result, we may not be able to control remedies with respect to the collateral;

- the collateral may not be valuable enough to satisfy all of the obligations under our secured loan, particularly after giving effect to the repayment of secured debt of the portfolio company that ranks senior to our loan;

- bankruptcy laws may limit our ability to realize value from the collateral and may delay the realization process;

- our rights in the collateral may be adversely affected by the failure to perfect security interests in the collateral;

- the need to obtain regulatory and contractual consents could impair or impede how effectively the collateral would be liquidated and could affect the value received; and

- some or all of the collateral may be illiquid and may have no readily ascertainable market value. The liquidity and value of the collateral could be impaired as a result of changing economic conditions, competition, and other factors, including the availability of suitable buyers.

Our investments in foreign securities may involve significant risks in addition to the risks inherent in U.S. investments.

Our investment strategy contemplates potential investments in securities of foreign companies including those located in emerging market countries. Investing in foreign companies may expose us to additional risks not typically associated with investing in U.S. companies. These risks include changes in

Table of Contents

exchange control regulations, political and social instability, expropriation, imposition of foreign taxes, less liquid markets and less available information than is generally the case in the United States, higher transaction costs, less government supervision of exchanges, brokers and issuers, less developed bankruptcy laws, difficulty in enforcing contractual obligations, lack of uniform accounting and auditing standards and greater price volatility. Such risks are more pronounced in emerging market countries.

Although currently most of our investments are, and we expect that most of our investments will be, U.S. dollar-denominated, investments that are denominated in a foreign currency will be subject to the risk that the value of a particular currency will change in relation to one or more other currencies. Among the factors that may affect currency values are trade balances, the level of short-term interest rates, differences in relative values of similar assets in different currencies, long-term opportunities for investment and capital appreciation, and political developments.

We may expose ourselves to risks if we engage in hedging transactions.

We may employ hedging techniques to minimize certain investment risks, such as fluctuations in interest and currency exchange rates, but we can offer no assurance that such strategies will be effective. If we engage in hedging transactions, we may expose ourselves to risks associated with such transactions. We may utilize instruments such as forward contracts, currency options and interest rate swaps, caps, collars and floors to seek to hedge against fluctuations in the relative values of our portfolio positions from changes in currency exchange rates and market interest rates. Hedging against a decline in the values of our portfolio positions does not eliminate the possibility of fluctuations in the values of such positions or prevent losses if the values of such positions decline. However, such hedging can establish other positions designed to gain from those same developments, thereby offsetting the decline in the value of such portfolio positions. Such hedging transactions may also limit the opportunity for gain if the values of the portfolio positions should increase. Moreover, it may not be possible to hedge against an exchange rate or interest rate fluctuation that is so generally anticipated that we are not able to enter into a hedging transaction at an acceptable price.

The success of our hedging transactions depends on our ability to correctly predict movements, currencies and interest rates. Therefore, while we may enter into such transactions to seek to reduce currency exchange rate and interest rate risks, unanticipated changes in currency exchange rates or interest rates may result in poorer overall investment performance than if we had not engaged in any such hedging transactions. The degree of correlation between price movements of the instruments used in a hedging strategy and price movements in the portfolio positions being hedged may vary. Moreover, for a variety of reasons, we may not seek to establish a perfect correlation between such hedging instruments and the portfolio holdings being hedged. Any such imperfect correlation may prevent us from achieving the intended hedge and expose us to risk of loss. In addition, it may not be possible to hedge fully or perfectly against currency fluctuations affecting the value of securities denominated in non-U.S. currencies. The Company has no current intention of engaging in any of the hedging transaction described above, although it reserves the right to do so in the future.

Our Board of Directors may change our operating policies and strategies without prior notice or stockholder approval, the effects of which may be adverse to us and could impair the value of our stockholders' investment.

Our Board of Directors has the authority to modify or waive our current operating policies and our strategies without prior notice and without stockholder approval. We cannot predict the effect any changes to our current operating policies and strategies would have on our business, financial condition, and value of our common stock. However, the effects might be adverse, which could negatively impact our ability to pay dividends and cause stockholders to lose all or part of their investment.

Table of Contents

Risks Relating To Our Securities

Investing in our securities may involve a high degree of risk and is highly speculative.

The investments we make in accordance with our investment objective may result in a higher amount of risk than alternative investment options and volatility or loss of principal. Our investments in portfolio companies may be speculative and aggressive, and therefore, an investment in our shares may not be suitable for someone with low risk tolerance.

The market price of our securities may fluctuate significantly.

The market price and liquidity of the market for our securities may be significantly affected by numerous factors, some of which are beyond our control and may not be directly related to our operating performance. These factors include:

- significant volatility in the market price and trading volume of securities of business development companies or other companies in the energy industry, which are not necessarily related to the operating performance of these companies;
- changes in regulatory policies or tax guidelines, particularly with respect to RICs or business development companies;
- loss of RIC qualification;
- changes in earnings or variations in operating results;
- changes in the value of our portfolio of investments;
- any shortfall in revenue or net income or any increase in losses from levels expected by investors or securities analysts;
- departure of one or more of Prospect Capital Management's key personnel;
- operating performance of companies comparable to us;
- changes in prevailing interest rates;
- litigation matters;
- general economic trends and other external factors; and
- loss of a major funding source.

In the past, following periods of volatility in the market price of a company's securities, securities class action litigation has, from time to time, been brought against that company.

If our stock price fluctuates significantly, we may be the target of securities litigation in the future. Securities litigation could result in substantial costs and divert management's attention and resources from our business.

Sales of substantial amounts of our securities in the public market may have an adverse effect on the market price of our securities.

Sales of substantial amounts of our securities or the availability of such securities for sale could adversely affect the prevailing market price for our securities. If this occurs and continues it could impair our ability to raise additional capital through the sale of securities should we desire to do so.

Table of Contents

There is a risk that you may not receive distributions or that our distributions may not grow over time.

We have made and intend to continue to make distributions on a quarterly basis to our stockholders out of assets legally available for distribution. We cannot assure you that we will achieve investment results or maintain a tax status that will allow or require any specified level of cash distributions or year-to-year increases in cash distributions. In addition, due to the asset coverage test applicable to us as a business development company, we may be limited in our ability to make distributions.

Provisions of the Maryland General Corporation Law and of our charter and bylaws could deter takeover attempts and have an adverse impact on the price of our common stock.

Our charter and bylaws and the Maryland General Corporation Law contain provisions that may have the effect of delaying, deferring or preventing a transaction or a change in control that might involve a premium price for our stockholders or otherwise be in their best interest. These provisions may prevent stockholders from being able to sell shares of our common stock at a premium over the current of prevailing market prices.

Our charter provides for the classification of our Board of Directors into three classes of directors, serving staggered three-year terms, which may render a change of control or removal of our incumbent management more difficult. Furthermore, any and all vacancies on our Board of Directors will be filled generally only by the affirmative vote of a majority of the remaining directors in office, even if the remaining directors do not constitute a quorum, and any director elected to fill a vacancy will serve for the remainder of the full term until a successor is elected and qualifies.

Our Board of Directors is authorized to create and issue new series of shares, to classify or reclassify any unissued shares of stock into one or more classes or series, including preferred stock and, without stockholder approval, to amend our charter to increase or decrease the number of shares of common stock that we have authority to issue, which could have the effect of diluting a stockholder's ownership interest. Prior to the issuance of shares of common stock of each class or series, including any reclassified series, our Board of Directors is required by our governing documents to set the terms, preferences, conversion or other rights, voting powers, restrictions, limitations as to dividends or other distributions, qualifications and terms or conditions of redemption for each class or series of shares of stock.

Our charter and bylaws also provide that our Board of Directors has the exclusive power to adopt, alter or repeal any provision of our bylaws, and to make new bylaws. The Maryland General Corporation Law also contains certain provisions that may limit the ability of a third party to acquire control of us, such as:

- The Maryland Business Combination Act, which, subject to certain limitations, prohibits certain business combinations between us and an "interested stockholder" (defined generally as any person who beneficially owns 10% or more of the voting power of the common stock or an affiliate thereof) for five years after the most recent date on which the stockholder becomes an interested stockholder and, thereafter, imposes special minimum price provisions and special stockholder voting requirements on these combinations; and

- The Maryland Control Share Acquisition Act, which provides that "control shares" of a Maryland corporation (defined as shares of common stock which, when aggregated with other shares of common stock controlled by the stockholder, entitles the stockholder to exercise one of three increasing ranges of voting power in electing directors, as described more fully below) acquired in a "control share acquisition" (defined as the direct or indirect acquisition of ownership or control of "control shares") have no voting rights except to the extent approved by

Table of Contents

stockholders by the affirmative vote of at least two-thirds of all the votes entitled to be cast on the matter, excluding all interested shares of common stock.

The provisions of the Maryland Business Combination Act will not apply, however, if our Board of Directors adopts a resolution that any business combination between us and any other person will be exempt from the provisions of the Maryland Business Combination Act. Our Board of Directors has adopted a resolution that any business combination between us and any other person is exempted from the provisions of the Business Combination Act, *provided* that the business combination is first approved by the Board of Directors, including a majority of the directors who are not interested persons as defined in the 1940 Act. There can be no assurance that this resolution will not be altered or repealed in whole or in part at any time. If the resolution is altered or repealed, the provisions of the Maryland Business Combination Act may discourage others from trying to acquire control of us.

As permitted by Maryland law, our bylaws contain a provision exempting from the Maryland Control Share Acquisition Act any and all acquisitions by any person of our common stock. Although our bylaws include such a provision, such a provision may also be amended or eliminated by our Board of Directors at any time in the future, provided that we will notify the Division of Investment Management at the SEC prior to amending or eliminating this provision. It is the view of the staff of the SEC that opting into the Maryland Control Share Acquisition Act would be acting in a manner inconsistent with section 18(i) of the 1940 Act.

We may in the future choose to pay dividends in our own stock, in which case our stockholders may be required to pay tax in excess of the cash they receive.

We may distribute taxable dividends that are payable in part in our stock. Under IRS Revenue Procedure 2010-12, up to 90% of any such taxable dividend could be payable in our stock for dividends paid on or before December 31, 2012 with respect to any taxable year ending on or before December 31, 2011. The IRS has also issued private letter rulings on cash/stock dividends paid by regulated investment companies and real estate investment trusts if certain requirements are satisfied. Taxable stockholders receiving such dividends would be required to include the full amount of the dividend as ordinary income (or as long-term capital gain to the extent such distribution is properly designated as a capital gain dividend) to the extent of our current and accumulated earnings and profits for United States federal income tax purposes. As a result, a U.S. stockholder may be required to pay tax with respect to such dividends in excess of any cash received. If a U.S. stockholder sells the stock it receives as a dividend in order to pay this tax, it may be subject to transaction fees (e.g. broker fees or transfer agent fees) and the sales proceeds may be less than the amount included in income with respect to the dividend, depending on the market price of our stock at the time of the sale. Furthermore, with respect to non-U.S. stockholders, we may be required to withhold U.S. tax with respect to such dividends, including in respect of all or a portion of such dividend that is payable in stock. In addition, if a significant number of our stockholders determine to sell shares of our stock in order to pay taxes owed on dividends, it may put downward pressure on the trading price of our stock. It is unclear whether and to what extent we will be able to pay dividends in cash and our stock (whether pursuant to Revenue Procedure 2010-12, a private letter ruling, or otherwise).

Table of Contents

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

(All figures in this section are in thousands except share, per share and other data)

The following discussion should be read in conjunction with our consolidated financial statements and related notes and other financial information appearing elsewhere in this prospectus or incorporated by reference into this prospectus. In addition to historical information, the following discussion and other parts of this prospectus contain forward-looking information that involves risks and uncertainties. Our actual results could differ materially from those anticipated by such forward-looking information due to the factors discussed under "Risk Factors" and "Forward-Looking Statements" appearing elsewhere herein.

Note on Forward Looking Statements

Some of the statements in this section of the prospectus constitute forward-looking statements, which relate to future events or our future performance or financial condition. The forward-looking statements contained herein involve risks and uncertainties, including statements as to:

- our future operating results;
- our business prospects and the prospects of our portfolio companies;
- the impact of investments that we expect to make;
- our contractual arrangements and relationships with third parties;
- the dependence of our future success on the general economy and its impact on the industries in which we invest;
- the ability of our portfolio companies to achieve their objectives;
- our expected financings and investments;
- the adequacy of our cash resources and working capital; and
- the timing of cash flows, if any, from the operations of our portfolio companies.

We generally use words such as "anticipates", "believes", "expects", "intends" and similar expressions to identify forward-looking statements. Our actual results could differ materially from those projected in the forward-looking statements for any reason, including the factors set forth in "Risk Factors" and elsewhere in this prospectus. These forward-looking statements do not meet the safe harbor for forward-looking statements pursuant to Section 27A of the Securities Act.

We have based the forward-looking statements included in herein on information available to us on the date of this document, and we assume no obligation to update any such forward-looking statements. Although we undertake no obligation to revise or update any forward-looking statements, whether as a result of new information, future events or otherwise, you are advised to consult any additional disclosures that we may make directly to you or through reports that we in the future may file with the SEC, including any annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K.

Overview

We are a financial services company that primarily lends to and invests in middle market privately-held companies. We are a closed-end investment company that has filed an election to be treated as a business development company under the Investment Company Act of 1940, or the 1940 Act. We invest primarily in senior and subordinated debt and equity of companies in need of capital for

Table of Contents

acquisitions, divestitures, growth, development and recapitalization. We work with the management teams or financial sponsors to seek investments with historical cash flows, asset collateral or contracted pro-forma cash flows.

We seek to be a long-term investor with our portfolio companies. From our July 27, 2004 inception to the fiscal year ended June 30, 2007, we invested primarily in industries related to the industrial/energy economy. Since then, we have widened our strategy to focus in other sectors of the economy and continue to reduce our exposure to the energy industry, and our holdings in the energy and energy related industries now represent less than 20% of our investment portfolio.

The aggregate value of our portfolio investments was $1,463,010 and $748,483 as of June 30, 2011 and June 30, 2010, respectively. During the fiscal year ended June 30, 2011, our net cost of investments increased by $706,975, or 97.0%, as a result of twenty-eight new investments, twelve follow-on investments and revolver advances of $943,703, accrued of payment-in-kind interest of $9,634 and accretion of purchase discount of $23,035, while we received full repayment on fourteen investments, sold three investments and received several partial prepayments and revolver repayments totaling of $269,397.

Compared to the end of the fiscal year ended June 30, 2010, our net assets increased by $402,933 or 56.6% during the year ended June 30, 2011, from $711,424 to $1,114,357. This increase resulted from the issuance of new shares of our common stock (less offering costs) in the amount of $379,929, dividend reinvestments of $10,934, and another $118,238 from operations. These increases, in turn, were offset by $106,167 in dividend distributions to our stockholders. The $118,238 increase in net assets resulting from operations is net of the following: net investment income of $94,221, net realized gain on investments of $16,465, and an increase in net assets due to changes in net unrealized appreciation of investments of $7,552.

Market Opportunity

We believe that current market conditions present attractive opportunities for us to invest in middle-market companies; specifically:

We believe that the dislocation in the credit markets that began in 2007 resulted in reduced competition, a widening of interest spreads, increased fees and generally more conservative capital structures and deal terms. These previous market conditions may continue to create favorable opportunities to invest at attractive risk-adjusted returns.

We believe that many senior lenders have, in recent years, de-emphasized their service and product offerings to middle-market businesses in favor of lending to large corporate clients and managing capital markets transactions. In addition, commercial and investment banks are limited in their ability to underwrite and syndicate bank loans and high yield securities for middle-market issuers as they seek to build capital and reduce leverage, resulting in opportunities for alternative funding sources and therefore higher new-issue market opportunities.

We believe there is a large pool of un-invested private equity capital for middle-market businesses. We expect private equity firms will seek to leverage their investments by combining equity capital with senior secured loans and mezzanine debt from other sources.

A high volume of senior secured and high yield debt was originated in the calendar years 2004 through 2007 and will come due in the near term and, accordingly, we believe that new financing opportunities will increase as many companies seek to refinance this indebtedness.

To capitalize on these opportunities, expansion of the capital base has been and may continue to be necessary. We have demonstrated our continuing access to capital markets in several equity and debt transactions during the year ended June 30, 2011, From July 1, 2010 to December 15, 2010, we raised

$181,946 of equity capital through our at the market program. On December 21, 2010 and February 18, 2011, we issued $150,000 and $172,500, respectively, of senior convertible notes. On April 7, 2011, we completed a public stock offering for 9,000,000 shares of our common stock raising $102,600 of gross proceeds. On June 24, 2011, we completed a public stock offering for 10,000,000 shares of our common stock at $10.15 per share, raising $101,500 of gross proceeds. On July 18, 2011, the underwriter exercised its option to purchase an additional 1,500,000 shares of our common stock.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reported period. Changes in the economic environment, financial markets and any other parameters used in determining these estimates could cause actual results to differ.

Fourth Quarter Highlights

Investment Transactions

On April 18, 2011, we made a $13,000 secured debt investment to support the acquisition of New Meatco Provisions, LLC ("Meatco"), a leading food distributor, by Annex Capital Management. The second lien note bears interest in cash at the greater of 12.0% or Libor plus 9.0% and interest in kind of 4.0% and has a final maturity on April 18, 2016.

On April 18, 2011, Unitek Acquisition, Inc. ("Unitek") repaid the $11,500 loan receivable to us.

On April 26, 2011, we made a senior secured follow-on investment of $11,000 in ICON Health & Fitness, Inc ("ICON"). The first lien note bears interest in cash at 11.875% and has a final maturity on October 15, 2016.

On May 2, 2011, we sold our membership interests in Fischbein, LLC ("Fischbein") realizing a gain of $9,893 on the sale and received a repayment of the loan that was outstanding. We subsequently made a $3,334 senior secured second-lien term loan and invested $875 in the common equity of Fischbein with the new ownership group. The second lien note bears interest in cash at 12.0% and interest in kind of 2.0% and has a final maturity on October 31, 2016.

On May 3, 2011, we made a debt investment of $25,000 to support the acquisition of Byrider Systems Acquisition Corp. ("Byrider"), a leading used car sales and finance business, by Altamont Capital Partners. The second lien note bears interest in cash at 12.0% and interest in kind of 2.0% and has a final maturity on November 3, 2016.

On May 6, 2011, we made a $34,450 investment in NMMB Holdings, Inc. ("NMMB"), an advertising media buying business, of which $31,750 was funded at closing. $24,250 is structured as senior secured debt, $2,800 as subordinated debt and $4,400 as controlling equity. The loans bear interest in cash at 14.0% and 15.0%, respectively, and have a final maturity on May 6, 2016. The $3,000 revolver, of which $300 was drawn at closing, bears interest in cash at the greater of 10.50% or Libor plus 8.50% and has a final maturity on May 6, 2016.

On May 6, 2011, we provided $15,000 in secured second-lien acquisition financing for Mood Media Corporation ("Mood Media"), a company in the in-store media industry. The second lien note bears interest in cash at the greater of 10.25% or Libor plus 8.75% and has a final maturity on November 6, 2018.

On May 6, 2011, we provided $15,000 in secured second-lien financing for the recapitalization of Potters Holdings II, L.P. ("Potters"), a leading company in the engineered glass materials industry. The second lien note bears interest in cash at the greater of 10.25% or Libor plus 8.50% and has a final maturity on November 6, 2017.

Table of Contents

On May 25, 2011, we provided $24,000 in secured first-lien financing to Targus Group International, Inc. ("Targus"), the leading global supplier of notebook carrying cases and accessories. The first lien note bears interest in cash at the greater of 11.0% or Libor plus 9.50% and has a final maturity on May 25, 2016.

On May 31, 2011, we provided $35,000 in secured second-lien financing to Springs Window Fashions, LLC ("Springs Window"), a leading designer and manufacturer of high-quality window treatments. The second lien note bears interest in cash at the greater of 11.25% or Libor plus 9.25% and has a final maturity on November 30, 2017.

On May 31, 2011, Label Corp Holdings Inc ("Label Corp") repaid the $5,749 loan receivable to us.

On June 3, 2011, Prince Mineral Company, Inc. ("Prince") repaid the $23,540 loan receivable to us and we recognized $10,463 of accelerated purchase discount accretion.

On June 16, 2011, we made a senior secured debt investment of $26,500 to support the acquisition of ST Products, LLC ("STP"), a leading North American producer of precision redrawn, small diameter, thin wall copper, and specialty alloy tubes. The first lien note bears interest in cash at the greater of 12.0% or Libor plus 9.00% and has a final maturity date on June 16, 2016.

On June 21, 2011, we provided $25,000 in secured second lien financing for the recapitalization of U.S. HealthWorks Holding Company, Inc. ("U.S.H."), a leading company in the occupational medical services industry. The second lien note bears interest in cash at the greater of 10.50% or Libor plus 9.00% and has a final maturity on June 15, 2017.

On June 30, 2011, we made a senior secured debt investment of $82,500 in CRT MIDCO, LLC ("CRT"), a market-leading specialty media buying business, of which $75,000 was funded at closing. The first lien notes bear interest in cash at the greater of 10.50% or Libor plus 7.50% and have a final maturity on June 30, 2017. The revolver, which was undrawn at closing of $7,500, bears interest in cash at the greater of 10.50% or Libor plus 7.50% and has a final maturity on June 30, 2012.

On June 30, 2011 we provided $5,000 in secured second lien financing for the acquisition of Pre-Paid Legal Services, Inc. ("Pre-Paid Legal"), a top company in the professional services subscription market. The second lien notes bear interest in cash at the greater of 11.00% or Libor plus 9.50% and has a final maturity on December 31, 2016.

Equity Issuance

On April 7, 2011, we completed a public stock offering for 9,000,000 shares of our common stock raising $102,600 of gross proceeds and $102,164 of net proceeds.

On June 24, 2011, we completed a public stock offering for 10,000,000 shares of our common stock at $10.15 per share, raising $101,500 of gross proceeds and $100,173 of net proceeds. On July 18, 2011, the underwriter exercised its option to purchase an additional 1,500,000 shares of our common stock, raising an additional $15,225 of gross proceeds and $15,060 of net proceeds.

On April 29, 2011, May 31, 2011 and June 24, 2011, we issued 76,377, 78,689 and 92,813 shares of our common stock in connection with the dividend reinvestment plan, respectively.

Dividend

On May 9, 2011, we announced the declaration of monthly dividends in the following amounts and with the following dates:

- $0.101225 per share for May 2011 to holders of record on May 31, 2011 with a payment date of June 24, 2011;

Table of Contents

$0.101250 per share for June 2011 to holders of record on June 30, 2011 with a payment date of July 22, 2011;

$0.101275 per share for July 2011 to holders of record on July 29, 2011 with a payment date of August 26, 2011;

$0.101300 per share for August 2011 to holders of record on August 31, 2011 with a payment date of September 23, 2011.

Credit Facility

On April 21, 2011, we announced an increase in commitments to our credit facility of $40,000. The commitments to the credit facility stood at $325,000 at June 30, 2011.

Patriot Acquisition

On December 2, 2009, we acquired the outstanding shares of Patriot Capital Funding, Inc. ("Patriot") common stock for $201,083. Under the 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 connection 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 equal to its undistributed net ordinary income and capital gains of $0.38 per share. In accordance with a recent IRS revenue procedure, the dividend was paid 10% in cash and 90% in newly 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 Capital Corporation ("Prospect") in accordance with acquisition method of accounting as detailed in Accounting Standards Codification ("ASC" or "Codification") 805, *Business Combinations* ("ASC 805"). The fair value of the consideration paid was allocated to the assets acquired and liabilities assumed based on their fair values as the date of acquisition. As described in more detail in ASC 805, goodwill, if any, would have been recognized as of the acquisition date, if the consideration transferred exceeded the fair value of identifiable net assets acquired. As of the acquisition date, the fair value of the identifiable net assets acquired exceeded the fair value of the consideration transferred, and we recognized the excess as a gain. A preliminary gain of $5,714 was recorded by Prospect in the quarter ended December 31, 2009 related to the acquisition of Patriot, which was revised in the fourth quarter of the fiscal year ended June 30, 2010, to $7,708, when we settled severance accruals related to certain members of Patriot's top management, and finalized during the first quarter of the fiscal year ended June 30, 2011, to $8,632, when we settled the remaining severance accruals related to the last two members of Patriot's top management. Under ASC 805, the adjustments to our preliminary estimates were reflected in the three months ended December 31, 2009 (See Note 14 to our consolidated financial statements.). The acquisition of Patriot was negotiated in July 2009 with the purchase agreement being signed on August 3, 2009. Between July 2009 and December 2, 2009, our valuation of certain of the investments acquired from Patriot increased due to market improvement, which resulted in the recognition of the gain at closing.

Table of Contents

The purchase price has been allocated to the assets acquired and the liabilities assumed based on their estimated fair values as 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	(2,967)
Net assets acquired	209,715
Gain on Patriot acquisition(3)	$ 8,632

(1) The value of the shares of common stock exchanged with the Patriot common shareholders was based upon the closing price 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 was 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 over the remaining term of the investment.

(3) The gain has been determined after the final payments of certain liabilities were settled.

During the year ended June 30, 2011, we recognized $22,084 of interest income due to purchase discount accretion from the assets acquired from Patriot. Included in the $22,084 is $4,912 of normal accretion, $12,035 of accelerated accretion resulting from the repayment of Impact Products, LLC ("Impact Products"), Label Corp and Prince and $4,968 of accelerated accretion resulting from the recapitalization of our debt investments in Arrowhead General Insurance Agency, Inc. ("Arrowhead"), The Copernicus Group, Inc. ("Copernicus"), Fischbein and Northwestern Management Services, LLC ("Northwestern"). The restructured loans for Arrowhead, Copernicus, Fischbein and Northwestern were issued at market terms comparable to other industry transactions. In accordance with ASC 320-20-35 the cost basis of the new loan was recorded at par value, which precipitated the acceleration of original purchase discount from the loan repayment which was recognized as interest income.

During the period from the acquisition of Patriot on December 2, 2009 to June 30, 2010, we recognized $18,795 of interest income due to purchase discount accretion from the assets acquired from Patriot. Included in this amount $4,579 of normal accretion and $14,216 of accelerated accretion resulting from the early repayments of four loans, three revolving lines of credit, sale of one investment position and restructuring of our loans to Aircraft Fasteners International, LLC ("AFI"), EXL Acquisition Corp. ("EXL"), LHC Holdings Corp. ("LHC"), Prince, ROM Acquisition Corporation ("ROM"). The revised terms were more favorable than the original terms and increased the present value of the future cash flows. In accordance with ASC 320-20-35 the cost basis of the new loans were recorded at par value, which precipitated the acceleration of original purchase discount from the loan repayment which was recognized as interest income.

Table of Contents

Investment Holdings

As of June 30, 2011, we continue to pursue our investment strategy. In May 2007, we changed our name to "Prospect Capital Corporation" and the terminated of our policy to invest at least 80% of our net assets in energy companies. Since that time, we have reduced our exposure to the energy industry, and our holdings in the energy and energy related industries now represent less than 20% of our investment portfolio.

At June 30 2011, approximately $1,463,010 or 131.3% of our net assets are invested in 72 long-term portfolio investments and 5.4% of our net assets invested in money market funds.

During the year ended June 30, 2011, we originated $953,337 of new investments. Our origination efforts recently have focused primarily on secured lending and reducing the risk in the portfolio, including a higher percentage of first lien loans than in prior periods, though we also continue to close selected junior debt and equity investments. In addition to targeting investments senior in corporate capital structures with our new originations, we have also increased our origination business mix of third party private equity sponsor owned companies, which tend to have more third party equity capital supporting our debt investments than non sponsor transactions. Our portfolio's annualized current yield decreased from 14.2% as of June 30, 2010 to 12.8% as of June 30, 2011 across all long-term debt and certain equity investments. We expect Prospect's current asset yield may decline modestly over the next few quarters as we increase the size of the portfolio while reducing credit risk. Monetization of other equity positions that we hold is not included in this yield calculation. In many of our portfolio companies, we hold equity positions, ranging from minority interests to majority stakes, which we expect over time to contribute to our investment returns. Some of these equity positions include features such as contractual minimum internal rates of returns, preferred distributions, flip structures and other features expected to generate additional investment returns, as well as contractual protections and preferences over junior equity, in addition to the yield and security offered by our cash flow and collateral debt protections.

We classify our investments by level of control. As defined in the 1940 Act, control investments are those where there is the ability or power to exercise a controlling influence over the management or policies of a company. Control is generally deemed to exist when a company or individual possesses or has the right to acquire within 60 days or less, a beneficial ownership of 25% or more of the voting securities of an investee company. Affiliated investments and affiliated companies are defined by a lesser degree of influence and are deemed to exist through the possession outright or via the right to acquire within 60 days or less, beneficial ownership of 5% or more of the outstanding voting securities of another person.

As of June 30, 2011, we own controlling interests in AIRMALL USA, Inc. ("AIRMALL"), Ajax Rolled Ring & Machine, Inc. ("Ajax"), AWCNC, LLC, Borga, Inc. ("Borga"), C&J Cladding LLC, Change Clean Energy Holdings, Inc. ("CCEHI"), Freedom Marine Services LLC ("Freedom Marine"), Gas Solutions Holdings, Inc. ("GSHI"), Integrated Contract Services, Inc. ("ICS"), Iron Horse Coiled Tubing, Inc. ("Iron Horse"), Manx Energy, Inc. ("Manx"), NMMB, NRG Manufacturing, Inc. ("NRG"), Nupla Corporation ("Nupla"), R-V Industries, Inc. ("R-V") and Yatesville Coal Holdings, Inc. ("Yatesville"). We also own an affiliated interest in BNN Holdings Corp. f/k/a Biotronic NeuroNetwork ("Biotronic"), Boxercraft Incorporated ("Boxercraft"), Smart, LLC, and Sport Helmets Holdings, LLC ("Sport Helmets").

Table of Contents

The following is a summary of our investment portfolio by level of control at June 30, 2011 and June 30, 2010, respectively:

	June 30, 2011				June 30, 2010			
Level of Control	**Cost**	**Percent of Portfolio**	**Fair Value**	**Percent of Portfolio**	**Cost**	**Percent of Portfolio**	**Fair Value**	**Percent of Portfolio**
Control	$ 262,301	18.0%	$ 310,072	20.4%	$ 185,720	23.3%	$ 195,958	24.0%
Affiliate	56,833	3.9%	72,337	4.7%	65,082	8.2%	73,740	9.0%
Non-control/Non-affiliate	1,116,600	74.1%	1,080,601	71.0%	477,957	59.9%	478,785	58.6%
Money Market Funds	59,903	4.0%	59,903	3.9%	68,871	8.6%	68,871	8.4%
Total Portfolio	$ 1,495,637	100.0%	$ 1,522,913	100.0%	$ 797,630	100.0%	$ 817,354	100.0%

The following is our investment portfolio presented by type of investment at June 30, 2011 and June 30, 2010, respectively:

	June 30, 2011				June 30, 2010			
Type of Investment	**Cost**	**Percent of Portfolio**	**Fair Value**	**Percent of Portfolio**	**Cost**	**Percent of Portfolio**	**Fair Value**	**Percent of Portfolio**
Money Market Funds	$ 59,903	4.0%	$ 59,903	3.9%	$ 68,871	8.6%	$ 68,871	8.4%
Revolving Line of Credit	7,144	0.5%	7,278	0.5%	4,754	0.6%	5,017	0.6%
Senior Secured Debt	822,582	55.0%	789,981	51.9%	313,755	39.4%	287,470	35.2%
Subordinated Secured Debt	491,188	32.9%	448,675	29.5%	333,453	41.8%	313,511	38.4%
Subordinated Unsecured Debt	54,687	3.7%	55,336	3.6%	30,209	3.8%	30,895	3.8%
Preferred Stock	31,979	2.1%	25,454	1.7%	16,969	2.1%	5,872	0.7%
Common Stock	19,865	1.3%	116,076	7.6%	20,243	2.5%	77,131	9.4%
Membership Interests	6,128	0.4%	15,392	1.0%	6,964	0.9%	17,730	2.2%
Overriding Royalty Interests		%	2,168	0.1%		%	2,768	0.3%
Net Profit Interests		%		%		%	1,020	0.1%
Warrants	2,161	0.1%	2,650	0.2%	2,412	0.3%	7,069	0.9%
Total Portfolio	$ 1,495,637	100.0%	$ 1,522,913	100.0%	$ 797,630	100.0%	$ 817,354	100.0%

The following is our investment portfolio presented by geographic location of the investment at June 30, 2011 and June 30, 2010, respectively:

	June 30, 2011				June 30, 2010			
Geographic Location	**Cost**	**Percent of Portfolio**	**Fair Value**	**Percent of Portfolio**	**Cost**	**Percent of Portfolio**	**Fair Value**	**Percent of Portfolio**
Canada	$ 74,239	5.0%	$ 75,207	4.9%	$ 21,002	2.6%	$ 12,054	1.5%
Ireland	14,908	1.0%	15,000	1.0%	14,903	1.9%	15,000	1.8%
Netherlands		%		%	1,397	0.2%	1,233	0.2%
Midwest US	358,540	24.0%	340,251	22.3%	170,869	21.5%	167,571	20.5%

Northeast US	242,039	16.1%	234,628	15.4%	61,813	7.7%	62,727	7.7%
Southeast US	234,528	15.7%	208,226	13.7%	193,420	24.2%	171,144	20.9%
Southwest US	189,436	12.7%	266,004	17.5%	179,641	22.6%	235,945	28.9%
Western US	322,044	21.5%	323,694	21.3%	85,714	10.7%	82,809	10.1%
Money Market Funds	59,903	4.0%	59,903	3.9%	68,871	8.6%	68,871	8.4%
Total Portfolio	$ 1,495,637	100.0%	$ 1,522,913	100.0%	$ 797,630	100.0%	$ 817,354	100.0%

Table of Contents

The following is our investment portfolio presented by industry sector of the investment at June 30, 2011 and June 30, 2010, respectively:

	June 30, 2011				June 30, 2010			
Industry	**Cost**	**Percent of Portfolio**	**Fair Value**	**Percent of Portfolio**	**Cost**	**Percent of Portfolio**	**Fair Value**	**Percent of Portfolio**
Aerospace and Defense	$ 56	%	$ 35	%	$ 56	%	$ 38	%
Automobile / Auto Finance	41,924	2.8%	42,444	2.8%	19,017	2.4%	18,615	2.3%
Biomass Power	2,540	0.2%		%	2,383	0.3%		%
Business Services	6,604	0.4%	6,787	0.4%	12,060	1.5%	12,132	1.5%
Chemicals	25,277	1.7%	25,277	1.7%	1,397	0.2%	1,233	0.2%
Commercial Services	34,625	2.3%	34,625	2.3%		%		%
Consumer Services	68,286	4.6%	68,286	4.5%		%		%
Contracting	18,220	1.2%	1,767	0.1%	16,652	2.1%	4,542	0.6%
Durable Consumer Products	141,779	9.5%	144,362	9.5%	20,000	2.5%	20,000	2.4%
Ecological	141	%	194	%	141	%	340	%
Electronics	588	%	1,374	0.1%	25,777	3.2%	25,629	3.1%
Financial Services		%		%	25,814	3.2%	25,592	3.1%
Food Products	144,503	9.7%	146,498	9.6%	53,681	6.7%	60,882	7.4%
Gas Gathering and Processing	42,003	2.8%	105,406	6.9%	37,503	4.7%	93,096	11.4%
Healthcare	156,396	10.5%	163,657	10.7%	89,026	11.2%	93,593	11.5%
Home and Office Furnishings, Housewares and Durable	1,916	0.1%	6,109	0.4%	14,112	1.8%	17,232	2.1%
Insurance	86,850	5.8%	87,448	5.7%	5,811	0.7%	5,952	0.7%
Machinery	13,179	0.9%	13,171	0.9%	15,625	2.0%	17,776	2.2%
Manufacturing	114,113	7.6%	136,039	8.9%	74,961	9.4%	64,784	7.9%
Media	121,302	8.1%	121,300	8.0%		%		%
Metal Services and Minerals	580	%	4,699	0.3%	19,252	2.4%	33,620	4.1%
Mining, Steel, Iron and Non-Precious Metals and Coal Production	1,448	0.1%		%	1,130	0.1%	808	0.1%
Oil and Gas Production	124,662	8.3%	70,923	4.7%	122,034	15.3%	96,988	11.9%
Oilfield Fabrication	23,076	1.5%	23,076	1.5%	30,429	3.8%	30,429	3.7%
Personal and Nondurable Consumer Products	15,147	1.0%	23,403	1.5%	14,387	1.8%	20,049	2.5%
Pharmaceuticals		%		%	11,955	1.5%	12,000	1.5%
		%		%	5,222	0.7%	5,284	0.6%

Printing and Publishing								
Production Services	14,387	1.0%	15,357	1.0%	21,002	2.6%	12,054	1.5%
Property Management	52,420	3.5%	51,726	3.4%		%		%
Retail	14,669	1.0%	145	0.0%	14,669	1.8%	2,148	0.3%
Shipping Vessels	11,303	0.8%	3,079	0.2%	10,040	1.3%	3,583	0.4%
Software & Computer Services	37,890	2.5%	38,000	2.5%	14,903	1.9%	15,000	1.8%
Specialty Minerals	30,169	2.0%	34,327	2.3%	15,814	2.1%	18,463	2.3%
Technical Services		%		%	11,387	1.4%	11,615	1.4%
Textiles and Leather	12,931	0.9%	15,632	1.0%	22,519	2.8%	25,006	3.1%
Transportation	76,750	5.2%	77,864	5.2%		%		%
Money Market Funds	59,903	4.0%	59,903	3.9%	68,871	8.6%	68,871	8.4%
Total Portfolio	$ 1,495,637	100.0%	$ 1,522,913	100.0%	$ 797,630	100.0%	$ 817,354	100.0%

Table of Contents

Portfolio Investment Activity

During the year ended June 30, 2011, we acquired $863,784 of new investments, completed follow-on investments in existing portfolio companies, totaling approximately $71,935, funded $7,984 of revolver advances, and recorded PIK interest of $9,634, resulting in gross investment originations of $953,337. The more significant of these investments are described briefly in the following:

On July 14, 2010, we made a senior secured investment of $38,000 in Progrexion Holdings, Inc. ("Progrexion"), a leading consumer credit enhancement services company. The $36,000 first lien note bears interest in cash at the greater of 11.0% or Libor plus 9.0% and has a final maturity on December 31, 2014. The $2,000 revolver, of which $1,400 was funded at closing, bears interest in cash at the greater of 11.0% or Libor plus 9.0% and has a final maturity on June 30, 2011.

On July 23, 2010, we made a secured debt investment of $21,000 in SonicWALL, Inc. ("SonicWALL"), a global leader in network security and data protection for small, mid-sized, and large enterprise organizations. On September 30, 2010, we made a follow-on secured debt investment of $2,000 in SonicWALL. The second lien notes bear interest in cash at the greater of 12.0% or Libor plus 2.0% and have a final maturity on January 23, 2017.

On July 30, 2010, we invested $42,500 of debt and $9,920 of equity in AIRMALL, a leading developer and manager of airport retail operations. The $30,000 first lien note bears interest in cash at the greater of 12.0% or Libor plus 9.0% and has a final maturity on June 30, 2015. The $12,500 subordinate note bears interest in cash at 12.0% and interest in kind of 6.0% and has a final maturity on December 31, 2015.

On July 30, 2010, we invested $20,000 in Northwestern, a leading dental practice management company in the Southeast Florida market. The first lien note bears interest in cash at the greater of 10.50% or Libor plus 7.50% and has a final maturity on July 30, 2015.

On September 30, 2010, we made a follow-on secured debt investment of $4,500 in GSHI to support the acquisition of a gathering pipeline system in Texas. The follow-on junior secured note bears interest in cash at 18.0% and has a final maturity on December 12, 2016.

On October 12, 2010, we made a senior secured debt investment of $32,500 in ICON, a leading manufacturer and marketer of branded health and fitness equipment. The first lien note bears interest in cash at 11.875% and has a final maturity on October 15, 2016.

On November 12, 2010, we made a senior subordinated debt investment of $15,000 in American Importing Company, Inc and Ann's House of Nuts Inc, collectively Snacks Holding Corporation, a leading manufacturer and marketer of dried fruits and trail mixes. The note bears interest in cash at 12.0% and interest in kind of 1.0% and has a final maturity on November 12, 2017.

On November 29, 2010, we made a senior subordinated debt investment of $14,000 in Royal Adhesives & Sealants, LLC ("Royal"), a leading producer of proprietary, high-performance adhesives and sealants. On December 13, 2010, we made a follow-on senior subordinated debt investment of $11,000 in Royal, an Arsenal Capital Partners portfolio company, in connection with Arsenal's acquisition of Para-Chem Southern and the creation of a leading adhesives, sealants, and coatings platform. The note bears interest in cash at 12.0% and interest in kind of 2.0% and has a final maturity on November 29, 2016.

On December 10, 2010, we made a $30,000 secured second-lien financing to American Gilsonite Company ("American Gilsonite") for a dividend recapitalization. After the financing, we received a $2,098 dividend as a result of our equity holdings in American Gilsonite and repayment of the loan that was outstanding. The second lien note bears interest in cash at the greater of

Table of Contents

12.0% or Libor plus 10.0% and interest in kind of 2.50% and has a final maturity on March 10, 2016.

On December 23, 2010, we made a second lien secured debt investment of $15,300 in JHH Holdings, Inc., a leading provider of home healthcare services in Texas. The second lien note bears interest in cash at the greater of 12.0% or Libor plus 10.0% and interest in kind of 2.50% and has a final maturity on June 23, 2016.

On December 23, 2010, we made a senior secured investment of $18,333 in VPSI, Inc., a leading market share transportation services company. The first lien note bears interest in cash at the greater of 12.0% or Libor plus 10.0% and has a final maturity on December 23, 2015.

On January 6, 2011, we made a senior secured term loan investment of $30,000 to support the acquisition of Progressive Logistics Services, LLC ("Progressive") by a middle market private equity firm. The first lien notes bear interest in cash at the greater of 8.50% or Libor plus 6.50% and the greater of 14.50% or Libor plus 12.50%, respectively, and have a final maturity on January 6, 2016.

On January 10, 2011, we made a senior secured debt investment of $20,000 to support the acquisition of Endeavor House by Pinnacle Treatment Centers, Inc. ("Pinnacle"). The $19,000 first lien note bears interest in cash at the greater of 11.0% or Libor plus 8.0% and has a final maturity on January 10, 2016. The $1,000 revolver, which was unfunded at closing, bears interest in cash at the greater of 8.0% or Libor plus 5.0% and has a final maturity on January 10, 2016.

On January 21, 2011, we provided senior secured credit facilities of $28,200 to support the acquisition of Stauber Performance Ingredients, Inc. ("Stauber"), by ICV Partners. The $25,700 first lien note bears interest in cash at the greater of 10.50% or Libor plus 7.50% and has a final maturity on January 21, 2016. The $2,500 revolver, of which $750 was funded at closing, bears interest in cash at the greater of 10.50% or Libor plus 7.50% and has a final maturity on January 21, 2016.

On January 31, 2011, we made a senior secured term investment of $7,500 to support the recapitalization of Empire Today, LLC, which is the second largest independent provider of carpet and hard surface flooring to consumers in the residential replacement flooring industry. The first lien note bears interest in cash at 11.375% and has a final maturity on February 1, 2017.

On February 3, 2011, we made a senior secured debt investment of $22,000 to support the recapitalization of Medical Security Card Company, LLC, a pharmacy services company. The $20,500 first lien note bears interest in cash at the greater of 11.25% or Libor plus 8.75% and has a final maturity on February 1, 2016. The $1,500 revolver, which was unfunded at closing, bears interest in cash at the greater of 9.50% or Libor plus 7.0% and has a final maturity on February 1, 2016.

On February 4, 2011, we made a secured second-lien debt investment of $45,000 to support the refinancing of Clearwater Seafoods LP, a leading premium seafood company based in Nova Scotia, Canada. The second lien note bears interest in cash at 12.0% and has a final maturity on February 4, 2016.

On February 9, 2011, we made a senior secured debt investment of $23,500 to support the recapitalization of Copernicus. After the financing we received a repayment of the loan that was previously outstanding. $11,250 of the first lien notes bear interest in cash at the greater of 8.0% or Libor plus 5.0% and $11,250 of the first lien notes bear interest in cash at the greater of 14.0% or Libor plus 11.0%, respectively, and both have a final maturity on February 6, 2016. The $1,000 revolver, which was unfunded at closing, bears interest in cash at the greater of 8.0% or Libor plus 5.0% and has a final maturity on February 9, 2016.

Table of Contents

On March 2, 2011, we made a senior secured first-lien debt investment of $14,000 to support the acquisition of Out Rage, LLC, a market leader in the bowhunting equipment industry. The $12,500 first lien note bears interest in cash at the greater of 11.0% or Libor plus 8.0% and has a final maturity on March 2, 2015. The $1,500 revolver, which was unfunded at closing, bears interest in cash at the greater of 11.0% or Libor plus 8.0% and has a final maturity on March 2, 2015.

On March 4, 2011, we made a $27,000 secured second-lien term loan to Arrowhead. After the financing we received a repayment of the loan that was previously outstanding. The second lien note bears interest in cash at the greater of 11.25% or Libor plus 9.50% and has a final maturity on September 30, 2017.

On March 18, 2011, we closed a $60,000 first-lien senior secured facility for SG Acquisition, Inc. ("Safe-Guard"), the leading third-party administrator of ancillary finance and insurance products and services for new, used, and leased motor vehicles. $30,000 of the first lien notes bear interest in cash at the greater of 8.50% or Libor plus 6.50% and $30,000 of the first lien notes bear interest in cash at the greater of 14.50% or Libor plus 12.50%, respectively, and both have a final maturity on March 18, 2016.

On March 31, 2011, we funded a $53,000 first-lien senior secured credit facility, funded $1,435 of a $5,000 commitment on a revolving line of credit and invested $1,500 in common equity to support the acquisition of Cargo Airport Services USA, LLC ("CAS") by ICV Partners. The $53,000 first lien note bears interest in cash at the greater of 11.50% or Libor plus 8.50% and has a final maturity on March 31, 2016. The $5,000 revolver, of which $1,435 was funded at closing, bears interest in cash at the greater of 11.50% or Libor plus 8.50% and has a final maturity on March 31, 2012.

On March 31, 2011, we provided a net $32,770 in first-lien senior secured financing for the recapitalization of Progrexion focused on the consumer credit information sector. The first lien note bears interest in cash at the greater of 10.75% or Libor plus 8.75% and has a final maturity on December 31, 2014.

On April 18, 2011, we made a $13,000 secured debt investment to support the acquisition of Meatco, a leading food distributor, by Annex Capital Management. The second lien note bears interest in cash at the greater of 12.0% or Libor plus 9.0% and interest in kind of 4.0% and has a final maturity on April 18, 2016.

On April 26, 2011, we made a senior secured follow-on investment of $11,000 in ICON. The first lien note bears interest in cash at 11.875% and has a final maturity on October 15, 2016.

On May 2, 2011, we sold our membership interests in Fischbein realizing a gain of $9,893 on the sale and received a repayment of the loan that was outstanding. We subsequently made a $3,334 senior secured second-lien term loan and invested $875 in the common equity of Fischbein with the new ownership group. The second lien note bears interest in cash at 12.0% and interest in kind of 2.0% and has a final maturity on October 31, 2016.

On May 3, 2011, we made a debt investment of $25,000 to support the acquisition of Byrider, a leading used car sales and finance business, by Altamont Capital Partners. The second lien note bears interest in cash at 12.0% and interest in kind of 2.0% and has a final maturity on November 3, 2016.

On May 6, 2011, we made a $34,450 investment in NMMB, an advertising media buying business, of which $31,750 was funded at closing. $24,250 is structured as senior secured debt, $2,800 as subordinated debt and $4,400 as controlling equity. The loans bear interest in cash at 14.0% and 15.0%, respectively, and have a final maturity on May 6, 2016. The $3,000 revolver, of

Table of Contents

which $300 was drawn at closing, bears interest in cash at the greater of 10.50% or Libor plus 8.50% and has a final maturity on May 6, 2016.

On May 6, 2011, we provided $15,000 in secured second-lien acquisition financing to Mood Media, a company in the in-store media industry. The second lien note bears interest in cash at the greater of 10.25% or Libor plus 8.75% and has a final maturity on November 6, 2018.

On May 6, 2011, we provided $15,000 in secured second-lien financing for the recapitalization of Potters, a leading company in the engineered glass materials industry. The second lien note bears interest in cash at the greater of 10.25% or Libor plus 8.50% and has a final maturity on November 6, 2017.

On May 25, 2011, we provided $24,000 in secured first-lien financing to Targus, the leading global supplier of notebook carrying cases and accessories. The first lien note bears interest in cash at the greater of 11.0% or Libor plus 9.50% and has a final maturity on May 25, 2016.

On May 31, 2011, we provide $35,000 in secured second-lien financing to Springs Window, a leading designer and manufacturer of high-quality window treatments. The second lien note bears interest in cash at the greater of 11.25% or Libor plus 9.25% and has a final maturity on November 30, 2017.

On June 16, 2011, we made a senior secured debt investment of $26,500 to support the acquisition of STP, a leading North American producer of precision redrawn, small diameter, thin wall copper, and specialty alloy tubes. The first lien note bears interest in cash at the greater of 12.0% or Libor plus 9.00% and has a final maturity date on June 16, 2016.

On June 21, 2011, we provided $25,000 in secured second lien financing for the recapitalization of U.S.H., a leading company in the occupational medical services industry. The second lien note bears interest in cash at the greater of 10.50% or Libor plus 9.00% and has a final maturity on June 15, 2017.

On June 30, 2011, we made a senior secured debt investment of $82,500 in CRT, a market-leading specialty media buying business, of which $75,000 was funded at closing. The $75,000 first lien notes bear interest in cash at the greater of 10.50% or Libor plus 7.50% and have a final maturity on June 30, 2017. The $7,500 revolver, which was unfunded at closing, bears interest in cash at the greater of 10.50% or Libor plus 7.50% and has a final maturity on June 30, 2012.

On June 30, 2011 we also provided $5,000 in secured second lien financing for the acquisition of Pre-Paid Legal, a top company in the professional services subscription market. The second lien notes bear interest in cash at the greater of 11.00% or Libor plus 9.50% and have a final maturity on December 31, 2016.

During the year ended June 30, 2011, we closed-out seventeen positions which are briefly described below.

On July 30, 2010, Northwestern repaid the $8,500 loan receivable to us.

On August 26, 2010, Regional Management Corporation ("RMC") repaid the $25,814 loan receivable to us.

On September 1, 2010, Impact Products repaid the $12,848 loan receivable to us.

On September 23, 2010, Roll Coater Acquisition Corp. repaid the $6,268 loan receivable to us.

On September 29, 2010, we sold our common stock in LyondellBasell Industries N.V. for $1,803, realizing a gain of $527.

On October 29, 2010, Castro Cheese Company, Inc. repaid the $7,732 loan receivable to us.

Table of Contents

On November 3, 2010, TriZetto Group repaid the $15,492 loan receivable to us.

On December 1, 2010, Qualitest Pharmaceuticals, Inc. repaid the $12,000 loan receivable to us.

On December 10, 2010, American Gilsonite repaid the $14,783 loan receivable to us.

On December 15, 2010, we sold Sidump'r Trailer Company, Inc. and received $430 net proceeds.

In December 2010, we exercised our warrants in Miller Petroleum, Inc. ("Miller") and received 2,013,814 shares of Miller common stock and sold 1,397,510 of these shares at $3.95 net proceeds per share, realizing a gain of $5,415. We sold the remaining 616,304 shares of Miller common stock on January 10, 2011, realizing $4.23 of net proceeds per share and an additional gain of $2,561 on this sale and a total gain of $7,976 on settlement of the investment.

On January 24, 2011, Maverick Healthcare LLC repaid the $13,122 loan receivable to us.

On March 11, 2011, EXL repaid the $22,988 loan receivable to us and we sold our 2,500 shares of EXL common stock.

On March 31, 2011, KTPS Holdings, LLC repaid the $8,414 loan receivable to us. A portion of the loan receivable was repaid at a discount, for which we realized a loss of $549.

On April 18, 2011, Unitek repaid the $11,500 loan receivable to us.

On May 31, 2011, Label Corp repaid the $5,749 loan receivable to us.

On June 3, 2011, Prince repaid the $23,540 loan receivable to us and we recognized $10,463 of accelerated purchase discount accretion.

During the year ended June 30, 2011, we also received principal amortization payments of $16,996 on several loans, and $24,450 of partial prepayments related to AIRMALL, AFI, Ajax, EXL, Fischbein, Iron Horse, LHC, Nupla, Northwestern, Progrexion, ROM, Seaton Corp and Stauber.

During the year ended June 30, 2011, we recognized $22,084 of interest income due to purchase discount accretion from the assets acquired from Patriot. Included in the $22,084 is $4,912 of normal accretion, $12,035 of accelerated accretion resulting from the repayment of Impact Products, Label Corp and Prince, and $4,968 of accelerated accretion resulting from the recapitalization of our debt investments in Arrowhead, Copernicus, Fischbein and Northwestern. The restructured loans for Arrowhead, Copernicus, Fischbein and Northwestern were issued at market terms comparable to other industry transactions. In accordance with ASC 320-20-35 the cost basis of the new loan was recorded at par value, which precipitated the acceleration of original purchase discount from the loan repayment which was recognized as interest income. We expect to recognize $836 of normal accretion during the three months ended September 30, 2011.

During the period from the acquisition of Patriot on December 2, 2009 to June 30, 2010, we recognized $18,795 of interest income due to purchase discount accretion from the assets acquired from Patriot. Included in this amount $4,579 of normal accretion and $14,216 of accelerated accretion resulting from the early repayments of four loans, three revolving lines of credit, sale of one investment position and restructuring of our loans to AFI, EXL, LHC, Prince and ROM. The revised terms were more favorable than the original terms and increased the present value of the future cash flows. In accordance with ASC 320-20-35 the cost basis of the new loans were recorded at par value, which precipitated the acceleration of original purchase discount from the loan repayment which was recognized as interest income.

On September 30, 2008, we settled our net profits interests ("NPIs") in IEC-Systems, LP ("IEC") and Advanced Rig Services, LLC ("ARS") with the companies for a combined $12,576. IEC and ARS

Table of Contents

originally issued the NPIs to us when we loaned a combined $25,600 to IEC and ARS on November 20, 2007. In conjunction with the NPI realization, we recognized other income of $12,576 and simultaneously reinvested the $12,576 as incremental senior secured debt in IEC and ARS. The incremental debt amortized over the period ending November 20, 2010.

The following is a quarter-by-quarter summary of our investment activity:

Quarter-End	Acquisitions(1)	Dispositions(2)
June 30, 2011	$ 312,301	$ 62,367
March 31, 2011	359,152	76,494
December 31, 2010	140,933	62,915
September 30, 2010	140,951	67,621
June 30, 2010	88,973	39,883
March 31, 2010	59,311	26,603
December 31, 2009(3)	210,438	45,494
September 30, 2009	6,066	24,241
June 30, 2009	7,929	3,148
March 31, 2009	6,356	10,782
December 31, 2008	13,564	2,128
September 30, 2008	70,456	10,949
June 30, 2008	118,913	61,148
March 31, 2008	31,794	28,891
December 31, 2007	120,846	19,223
September 30, 2007	40,394	17,949
June 30, 2007	130,345	9,857
March 31, 2007	19,701	7,731
December 31, 2006	62,679	17,796
September 30, 2006	24,677	2,781
June 30, 2006	42,783	5,752
March 31, 2006	15,732	901
December 31, 2005		3,523
September 30, 2005	25,342	
June 30, 2005	17,544	
March 31, 2005	7,332	
December 31, 2004	23,771	32,083
September 30, 2004	30,371	
Since inception	$ 2,128,654	$ 640,260

(1) Includes new deals, additional fundings, refinancings and PIK interest.

(2) Includes scheduled principal payments, prepayments and refinancings.

(3) The $210,438 of acquisitions for the quarter ended December 31, 2009 includes $207,126 of portfolio investments acquired from Patriot.

Table of Contents

Investment Valuation

In determining the fair value of our portfolio investments at June 30, 2011 the Audit Committee considered valuations from the independent valuation firm and from management having an aggregate range of $1,435,916 to $1,548,301, excluding money market investments.

In determining the range of value for debt instruments, management and the independent valuation firm generally shadow rated the investment and then based upon the range of ratings, determined appropriate yields to maturity for a loan rated as such. A discounted cash flow analysis was then prepared using the appropriate yield to maturity as the discount rate, yielding the ranges. For equity investments, the enterprise value was determined by applying EBITDA multiples for similar recent investment sales. For stressed equity investments, a liquidation analysis was prepared.

The Board of Directors looked at several factors in determining where within the range to value the asset including: recent operating and financial trends for the asset, independent ratings obtained from third parties and comparable multiples for recent sales of companies within the industry. The composite of all these analysis, applied to each investment, was a total valuation of $1,463,010, excluding money market investments.

Our portfolio companies are generally lower middle market companies, outside of the financial sector, with less than $50,000 of annual EBITDA. We believe our market has experienced less volatility than others because we believe there are more buy and hold investors who own these less liquid investments.

During the year ended June 30, 2011, there has been a general improvement in the markets in which we operate, and market rates of interest negotiated for middle market loans have decreased.

Control investments offer increased risk and reward over straight debt investments. Operating results and changes in market multiples can result in dramatic changes in values from quarter to quarter. Significant downturns in operations can further result in our looking to recoveries on sales of assets rather than the enterprise value of the investment. Several control investments in our portfolio are under enhanced scrutiny by our senior management and our Board of Directors and are discussed below.

Ajax Rolled Ring & Machine, Inc.

We acquired a controlling equity interest in Ajax in a recapitalization of Ajax that was closed on April 4, 2008. We funded $22,000 of senior secured term debt, $11,500 of subordinated term debt and $6,300 of equity as of that closing. During the fiscal year ended June 30, 2010, we funded an additional $3,530 of secured subordinated debt to refinance a third-party revolver provider and provide working capital. Ajax repaid $3,461 of this secured subordinated debt during the quarter ended September 30, 2010. As of June 30, 2011, we control 77.68% of the fully-diluted common and preferred equity. The principal balance of our senior debt to Ajax was $20,607 and new debt was $15,035 as of June 30, 2011.

Ajax forges seamless steel rings sold to various customers. The rings are used in a range of industrial applications, including in construction equipment and wind power turbines. Ajax's business is cyclical, and the business experienced a significant decline in 2009 in light of the global macroeconomic crisis. Ajax has seen significant improvement in operating results in 2010 with EBITDA increasing over 100% from that generated in 2009.

The Board of Directors increased the fair value of our investment in Ajax to $33,877 as of June 30, 2011, a reduction of $7,822 from its amortized cost, compared to the $13,006 unrealized depreciation recorded at June 30, 2010.

Table of Contents

Change Clean Energy Holdings Inc. and Change Clean Energy, Inc., f/k/a Worcester Energy Partners, Inc.

Change Clean Energy, Inc. ("CCEI") is an investment that we originated in September 2005, which owns and operated a biomass energy plant. In March 2009, CCEI ceased operations, as the business became uneconomic based on the cost of materials and the price being received for the electricity generated. During that quarter, we instituted foreclosure proceedings against the co-borrowers of our debt. In anticipation of such proceedings, CCEHI was established. On March 11, 2009, the foreclosure was completed and the assets were assigned to a wholly owned subsidiary of CCEHI. During the year ended June 30, 2010, we provided additional funding of $296 to CCEHI to fund ongoing operations. CCEI currently has no material operations. At June 30, 2009 we determined that the impairment at both CCEI and CCEHI was other than temporary and recognized a realized loss of $41,134, which was the amount by which the amortized cost exceeded the fair value. During the years ended June 30, 2011 and June 30, 2010, we made follow-on investments of $316 and $554, respectively, in CCEHI for professional services related to ongoing litigations and plant security. At June 30, 2011, our Board of Directors, under recommendation from senior management, has set the value of the CCEHI investment with no value, a reduction of $2,540 from its amortized cost after the recognized loss recorded in 2009.

Freedom Marine Services, LLC

Freedom Marine is an investment that we initially funded in October 2006. We acquired a controlling interest in the company on October 1, 2009 as part of a broader restructuring of the company and subsequently provided additional funding to support ongoing operations. During the year ended June 30, 2011, we provided additional funding of $944 to Freedom Marine in order to provide needed liquidity and pay dry docking expenses. As of June 30, 2011, we control 86.78% of the fully-diluted equity.

Freedom Marine is an owner-operator of three offshore supply vessels operating out of Houma, Louisiana. The three vessels are leased out to various oil and gas industry participants operating in the Gulf of Mexico. Freedom Marine's business were significantly impacted by the 2010 Gulf of Mexico oil spill. Offshore activity levels remain depressed and the company has been EBITDA negative since October 2010.

Based upon an analysis of the liquidation value of the vessels and the enterprise value of Freedom Marine, our Board of Directors determined the fair value of our investment in Freedom Marine to be $3,079 at June 30, 2011, a reduction of $8,224 from its amortized cost, compared to the $6,457 unrealized loss recorded at June 30, 2010.

Gas Solutions Holdings, Inc.

GSHI is an investment that we completed in September 2004 in which we own 100% of the equity. GSHI is a midstream gathering and processing business located in east Texas. GSHI has improved its operations and experienced an increase in revenue, gross margin, and EBITDA over the past year given the increase in plant volumes and natural gas liquids prices.

GSHI continues to focus on plant projects and seeking new opportunities to help the company grow beyond its existing footprint. On September 30, 2010, we made a follow-on secured debt investment of $4,500 to GSHI to support the acquisition of an additional gathering pipeline system in Texas.

In April 2010, GSHI purchased a series of propane puts with strike prices of $1.00 per gallon and $0.95 per gallon covering the periods May 1, 2010, through April 30, 2011, and May 1, 2011, through April 30, 2012, respectively. GSHI hedged approximately 85% of its exposure to natural gas liquids based on plant volumes at the time of entering into the puts. In March 2011, GSHI purchased propane puts with strike prices of $0.95 per gallon covering the period May 1, 2012, through April 30, 2013, hedging approximately 100% of its exposure to natural gas liquids based on projected plant volumes. These hedges will reduce the volatility on earnings associated with lower prices of natural gas liquids without limiting the upside from higher prices, helping GSHI to continue to generate sufficient cash flow to make interest and dividend payments. GSHI has experienced a growth of approximately 34% in revenue and 40% in EBITDA when comparing 2010 results to 2009 results. GSHI has experienced a growth of approximately 36% in revenue and 60% in EBITDA when comparing results for the six months ended June 30, 2011 to June 30, 2010. As GSHI continues to fill the excess capacity at the plant, operating results will continue to improve.

In determining the value of GSHI, we have utilized two valuation techniques to determine the value of the investment. Our Board of Directors has determined the value to be $105,406 for our debt and equity positions at June 30, 2011 based upon a combination of a discounted cash flow analysis and a public comparables analysis. At June 30, 2011 and June 30, 2010, GSHI was valued $63,403 and $55,593 above its amortized cost, respectively.

Integrated Contract Services, Inc.

ICS is an investment that we entered into in April 2007. Prior to January 2009, ICS owned the assets of ESA Environmental Specialists, Inc. ("ESA") and 100% of the stock of The Healing Staff ("THS"). ESA originally defaulted under our contract governing our investment in ESA, prompting us to commence foreclosure actions with respect to certain ESA assets in respect of which we have a priority lien. In response to our actions, ESA filed voluntarily for reorganization under the bankruptcy code on August 1, 2007. On September 20, 2007, the U.S. Bankruptcy Court approved a Section 363 Asset Sale from ESA to us. To 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 ESA debt, we received senior secured debt in ICS of equal amount to our ESA debt, preferred stock of ICS, and 49% of the ICS common stock. ICS subsequently ceased operations and assigned the collateral back to us. ICS is in default of both payment and 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 100% ownership of THS and certain ESA assets. THS provides outsourced medical staffing and security staffing services to governmental and commercial enterprises. In November 2009, THS was informed that the U.S. Air Force would not exercise its option to renew its contract. THS continues to solicit new contracts to replace the revenue lost when the Air Force contract ended. As part of its strategy to recovery from the loss of the Air Force contract, in 2010 THS started a new business, Vets Securing America, Inc. ("VSA"), to provide out-sourced security guards staffed primarily using retired military veterans. During the year ended June 30, 2011, we made follow-on secured debt investments of $1,708 to support the ongoing operations of THS and VSA.

Based upon an analysis of the liquidation value of the ESA assets and the enterprise value of THS/VSA, our Board of Directors determined the fair value of our investment in ICS to be $1,767 at June 30, 2011, a reduction of $16,453 from its amortized cost, compared to the $12,110 unrealized loss recorded at June 30, 2010.

Iron Horse Coiled Tubing, Inc.

Iron Horse is an investment that we completed in April 2006. Iron Horse had been a provider of coiled tubing subcontractor services prior to making a strategic decision in late 2007 to directly

Table of Contents

service natural gas and oil producers in the Western Canadian Sedimentary Basin ("WCSB") as a fracturing services provider. As a result of the business transition, the Company's 2008 financial performance declined significantly from 2007 levels. Iron Horse completed its transition from a subcontractor to a direct service provider in 2009, but natural gas prices declined to trough levels due to the recession and heightened natural gas inventory levels. Since November 2009, Iron Horse has experienced increased activity in the WCSB and is now completing wells for a diversified base of large and small 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 received an additional 50.3% of the common stock in Iron Horse, which increased our total ownership to 58.8%. Through a series of subsequent loans that were used to construct equipment and facilitate the transition from a subcontractor to a direct service provider, we secured an additional 21.0% of the common stock in Iron Horse in September 2008, which increased our total ownership to 79.8% of the common stock in Iron Horse.

Effective January 1, 2010, we restructured our senior secured and bridge loans to Iron Horse and we reorganized Iron Horse's management structure. Our loans were replaced with three new tranches of senior secured debt and our total ownership of Iron Horse decreased to 70.4% on a fully-diluted basis. Our fully-diluted equity ownership will incrementally decrease as debt tranches are repaid. There was no change to fair value at the time of restructuring. In 2010, Iron Horse returned to profitability reporting EBITDA of over $12,000 for the year ended December 31, 2010. Revenues were up almost 500% from 2009 to 2010 and Iron Horse repaid $6,615 of this senior secured debt during the year ended June 30, 2011. These repayments decreased our ownership to 57.8% on a fully-diluted basis. As Iron Horse has shown an ability to continue to service the interest and principal payments as they come due, we returned Iron Horse to accrual status in December 2010.

The Board of Directors increased the fair value of our investment in Iron Horse to $15,357 as of June 30, 2011, a premium of $970 above its amortized cost, compared to the $8,948 unrealized depreciation recorded at June 30, 2010.

Manx Energy, Inc.

On January 19, 2010, we modified the terms of our senior secured debt in Appalachian Energy Holdings LLC ("AEH") and Coalbed LLC ("Coalbed") in conjunction with the formation of Manx, a new entity consisting of the assets of AEH, Coalbed and Kinley Exploration. The assets of the three companies were combined under new common management. We funded $2,800 at closing to Manx to provide for working capital. A portion of our loans to AEH and Coalbed was exchanged for Manx preferred equity, while our AEH equity interest was converted into Manx common stock. There was no change to fair value at the time of restructuring, and we continue to fully reserve any income accrued for Manx. During the year ended June 30, 2011, we made a follow-on secured debt investments of $750 in Manx to support ongoing operations.

The Board of Directors wrote-down the fair value of our investment in Manx to $1,312 as of June 30, 2011, a reduction of $17,707 from its amortized cost, compared to the $13,584 unrealized loss recorded at June 30, 2010.

Yatesville Coal Holdings, Inc.

All of our coal holdings have been consolidated under the Yatesville entity. Yatesville delivered improved operating results after the consolidation of the coal holdings, but the company mined through all of its permitted reserves by December 2008 and has not produced meaningful revenues since then. We continue to evaluate strategies for Yatesville, such as soliciting indications of interest regarding a transaction involving part or all of recoverable reserves. During the quarter

Table of Contents

ended December 31, 2009, we discontinued operations at Yatesville. At December 31, 2009, our Board of Directors determined that, consistent with the decision to discontinue operations, the impairment of Yatesville was other than temporary, and we recorded a realized loss of $51,228, which was the amount that the amortized cost exceeded the fair value at December 31, 2009. During the years ended June 30, 2011 and June 30, 2010, we made follow-on investments of $555 and $3,471, respectively, in Yatesville for professional services related to ongoing litigations. At June 30, 2011, our Board of Directors, under recommendation from senior management, has set the value of the Yatesville investment with no value, a reduction of $1,448 from its amortized cost after the recognized depreciation.

Equity positions in the portfolio are susceptible to potentially significant changes in value, both increases as well as decreases, due to changes in operating results. Four of our portfolio companies have experienced such volatility due to improved operating results GSHI, Iron Horse, NRG and R-V. NRG and GSHI experienced meaningful increases in valuation during the year ended June 30, 2011, NRG due to overall industry stabilization and increased backlog resulting from a new product line, and GSHI due to improved operating results. The value of our equity position in NRG has increased to $32,403 as of June 30, 2011, a premium of $30,086 to its amortized cost, compared to the $4,714 unrealized gain recorded at June 30, 2010. The value of our equity position in GSHI has increased to $68,406 as of June 30, 2011, a premium of $63,403 to its amortized cost, compared to the $55,593 unrealized gain recorded at June 30, 2010. Eight of the other controlled investments have been valued at discounts to the original investment. Six of the control investments are valued at premiums to the original investment amounts, including Iron Horse for which our unrealized gain increased by $9,918 during the year ended June 30, 2011 due to improved operating results. Overall, at June 30, 2011, the control investments are valued at $47,771 above their amortized cost.

We hold four affiliate investments at June 30, 2011. The affiliate investments reported strong operating results with valuations increasing for three investments Biotronic, Boxercraft and Sport Helmets. Biotronic experienced the most meaningful increase in valuation. Biotronic completed a significant acquisition in November 2010, which is driving the operating results and the increase in the value of the investment. All affiliate investments are valued at amortized cost or higher. Overall, at June 30, 2011, affiliate investments are valued $15,504 above their amortized cost.

With the Non-control/Non-affiliate investments, generally, there is less volatility related to our total investments because our equity positions tend to be smaller than with our control/affiliate investments, and debt investments are generally not as susceptible to large swings in value as equity investments. For debt investments, the fair value is limited on the high side to each loan's par value, plus any prepayment premia that could be imposed. Many of the debt investments in this category have not experienced a significant change in value, as they were previously valued at or near par value. The exception to this categorization relates to investments which were acquired in the Patriot Acquisition, many of which were acquired at significant discounts to par value, and any changes in operating results or interest rates can have a significant effect on the value of such investments. H&M Oil & Gas, LLC ("H&M"), Shearer's Food's, Inc. ("Shearer's") and Stryker Energy, LLC ("Stryker"), experienced decreases in valuations due to declines in their operating results. At June 30, 2011, H&M was placed on non-accrual status due to the inability of the company to service its debt. The remaining investments did not experience significant changes in operations or valuation. During the year ended June 30, 2011, we recognized $22,084 of interest income due to purchase discount accretion from the assets acquired from Patriot. Included in the $22,084 is $4,912 of normal accretion, $12,035 of accelerated accretion resulting from the repayment of Impact Products, Label Corp and Prince, and $4,968 of accelerated accretion resulting from the recapitalization of our debt investments in Arrowhead, Copernicus, Fischbein and Northwestern. The restructured loans for Arrowhead, Copernicus, Fischbein and Northwestern were issued at market terms comparable to other industry transactions. In accordance with ASC 320-20-35 the cost basis of the new loan was recorded at par value, which precipitated the

Table of Contents

acceleration of original purchase discount from the loan repayment which was recognized as interest income.

Capitalization

Our investment activities are capital intensive and the availability and cost of capital is a critical component of our business. We 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 Senior Convertible Notes which we issued in December 2010 and February 2011 and our equity capital is currently comprised entirely of common equity. The following table shows the Revolving Credit Facility and Senior Convertible Notes amounts and outstanding borrowings at June 30, 2011 and June 30, 2010:

	As of June 30, 2011		As of June 30, 2010	
	Facility Amount	Amount Outstanding	Facility Amount	Amount Outstanding
Revolving Credit Facility	$ 325,000	$ 84,200	$ 210,000	$ 100,300
Senior Convertible Notes	$ 322,500	$ 322,500	$	$

The following table shows the contractual maturity of our Revolving Credit Facility and Senior Convertible Notes at June 30, 2011:

	Payments Due By Period		
	Less Than 1 Year	1 - 3 Years	More Than 3 Years
Revolving Credit Facility	$	$ 84,200	$
Senior Convertible Notes	$	$	$ 322,500

We have and expect to continue to fund a portion of our cash needs through borrowings from banks, issuances of senior securities, including secured, unsecured and convertible debt securities and preferred stock, or issuances of common equity. For flexibility, we maintain a universal shelf registration statement that allows for the public offering and sale of our debt securities, common stock, preferred stock and warrants to purchase such securities in an amount up to $750,000 less issuances to date. We may from time to time issue securities pursuant to the shelf registration statement or otherwise pursuant to private offerings. The issuance of debt or equity securities will depend on future market conditions, funding needs and other factors and there can be no assurance that any such issuance will occur or be successful.

Revolving Credit Facility

On June 25, 2009, we completed a first closing on an expanded $250,000 syndicated revolving credit facility (the "Facility"). The Facility included an accordion feature which allowed the Facility to accept up to an aggregate total of $250,000 of commitments for which we had $210,000 of commitments from six lenders when the Facility was renegotiated. The revolving period of the Facility extended through June 2010, with an additional one year amortization period after the completion of the revolving period.

On June 11, 2010, we closed an extension and expansion of our revolving credit facility with a syndicate of lenders ("Syndicated Facility"). The lenders have extended current commitments of $400,000 under the Syndicated Facility as detailed in the *Recent Developments*. As we make additional investments which are eligible to be pledged under the Syndicated Facility, we will generate additional availability to the extent such investments are eligible to be placed into the borrowing base. The revolving period of the Syndicated Facility extends through June 2012, with an additional one year amortization period (with distributions allowed) after the completion of the revolving period. During such one year amortization period, all principal payments on the pledged assets will be applied to reduce the balance. At the end of the one year amortization period, the remaining balance will become due if required by the lenders.

As of June 30, 2011 and June 30, 2010, we had the ability to borrow up to $255,673 and $180,678, respectively, under our Syndicated Facility based on the assets pledged as collateral at that time, of which $84,200 and $100,300 was drawn, respectively. The Syndicated Facility requires us to pledge assets as collateral in order to borrow under the credit facility. At June 30, 2011, the investments used as collateral for the Syndicated Facility had an aggregate market value of $700,321, which represents 62.8% of net assets. Prospect Capital Funding, LLC, our wholly-owned subsidiary, holds $631,915 of these investments at market value as of June 30, 2011. The release of any assets from Prospect Capital Funding, LLC requires the approval of Rabobank as facility agent.

The borrowings under the Syndicated Facility bore interest at a rate of one-month Libor plus 250 basis points prior to June 25, 2009, which increased to one-month Libor plus 400 basis points, subject to a minimum Libor floor of 200 basis points for the period from June 26, 2009 to June 10, 2010. Beginning June 11, 2010, interest on borrowings decreased under the Syndicated Facility is one-month Libor plus 325 basis points, subject to a minimum Libor floor of 100 basis points. The maintenance of this facility requires us to pay a fee for the amount not drawn upon. Prior to June 25, 2009, this fee was assessed at the rate of 37.5 basis points per annum of the amount of that unused portion. For the period from June 26, 2010 to June 10, 2010, this rate increased to 100 basis points per annum. After June 11, 2010, the lenders charge a fee on the unused portion of the credit facility equal to either 75 basis points if at least half of the credit facility is used or 100 basis points otherwise.

Concurrent with the extension of our Syndicated Facility, in June 2010, we wrote off $759 of the unamortized debt issue costs associated with the original credit facility, in accordance with ASC 470-50, *Debt Modifications and Extinguishments.*

Senior Convertible Notes

On December 21, 2010, we issued $150,000 in aggregate principal amount of our 6.25% senior convertible notes due 2015 ("2010 Notes") for net proceeds following underwriting expenses of approximately $145,200. Interest on the 2010 Notes is paid semi-annually in arrears on June 15 and December 15, at a rate of 6.25% per year, commencing June 15, 2011. The 2010 Notes mature on December 15, 2015 unless converted earlier. The 2010 Notes are convertible into shares of common stock at an initial conversion rate and conversion rate at June 30, 2011 of 88.0902 and 88.0932 shares of common stock, respectively, per $1,000 principal amount of 2010 Notes, which is equivalent to a conversion price of approximately $11.35 per share of common stock, subject to adjustment in certain circumstances. The conversion rate for the 2010 Notes will be increased if monthly cash dividends paid to common shares exceed the rate of $0.101125 cents per share, subject to adjustment.

On February 18, 2011, we issued $172,500 in aggregate principal amount of our 5.50% senior convertible notes due 2016 ("2011 Notes") for net proceeds following underwriting expenses of approximately $167,325. Interest on the 2011 Notes is paid semi-annually in arrears on February 15 and August 15, at a rate of 5.50% per year, commencing August 15, 2011. The 2011 Notes mature on August 15, 2016 unless converted earlier. The 2011 Notes are convertible into shares of common stock at an initial conversion rate and conversion rate at June 30, 2011 of 78.3699 and 78.3717 shares, respectively, of common stock per $1,000 principal amount of 2011 Notes, which is equivalent to a conversion price of approximately $12.76 per share of common stock, subject to adjustment in certain circumstances. The conversion rate for the 2011 Notes will be increased when monthly cash dividends paid to common shares exceed the rate of $0.101150 per share.

Table of Contents

In no event will the total number of shares of common stock issuable upon conversion exceed 96.8992 per $1,000 principal amount of the 2010 Notes (the "conversion rate cap"), except that, to the extent we receive written guidance or a no-action letter from the staff of the Securities and Exchange Commission (the "Guidance") permitting us to adjust the conversion rate in certain instances without regard to the conversion rate cap and to make the 2010 Notes convertible into certain reference property in accordance with certain reclassifications, business combinations, asset sales and corporate events by us without regard to the conversion rate cap, we will make such adjustments without regard to the conversion rate cap and will also, to the extent that we make any such adjustment without regard to the conversion rate cap pursuant to the Guidance, adjust the conversion rate cap accordingly. We will use our commercially reasonable efforts to obtain such Guidance as promptly as practicable.

Prior to obtaining the Guidance, we will not engage in certain transactions that would result in an adjustment to the conversion rate increasing the conversion rate beyond what it would have been in the absence of such transaction unless we have engaged in a reverse stock split or share combination transaction such that in our reasonable best estimation, the conversion rate following the adjustment for such transaction will not be any closer to the conversion rate cap than it would have been in the absence of such transaction.

Upon conversion, unless a holder converts after a record date for an interest payment but prior to the corresponding interest payment date, the holder will receive a separate cash payment with respect to the Notes surrendered for conversion representing accrued and unpaid interest to, but not including the conversion date. Any such payment will be made on the settlement date applicable to the relevant conversion on the 2010 Notes and 2011 Notes (collectively, "Senior Convertible Notes").

No holder of Senior Convertible Notes will be entitled to receive shares of our common stock upon conversion to the extent (but only to the extent) that such receipt would cause such converting holder to become, directly or indirectly, a beneficial owner (within the meaning of Section 13(d) of the Securities Exchange Act of 1934 and the rules and regulations promulgated thereunder) of more than 5.0% of the shares of our common stock outstanding at such time. The 5.0% limitation shall no longer apply following the effective date of any fundamental change. We will not issue any shares in connection with the conversion or redemption of the Notes which would equal or exceed 20% of the shares outstanding at the time of the transaction in accordance with NASDAQ rules.

Subject to certain exceptions, holders may require us to repurchase, for cash, all or part of their Notes upon a fundamental change at a price equal to 100% of the principal amount of the Notes being repurchased plus any accrued and unpaid interest up to, but excluding, the fundamental change repurchase date. In addition, upon a fundamental change that constitutes a non-stock change of control we will also pay holders an amount in cash equal to the present value of all remaining interest payments (without duplication of the foregoing amounts) on such Senior Convertible Notes through and including the maturity date.

In connection with the issuance of the Senior Convertible Notes, we incurred $10,562 of fees which are being amortized over the term of the facility in accordance with ASC 470-50, *Debt Modifications and Extinguishments,* of which $9,845 remains to be amortized.

During the year ended June 30, 2011, we recorded $17,598 of interest costs and amortization of financing costs as interest expense.

During the year ended June 30, 2011, we raised $277,766 of additional equity, net of offering costs, by issuing 28,494,476 shares of our common stock below net asset value diluting shareholder value by

Table of Contents

$0.16 per share. The following table shows the calculation of net asset value per share as of June 30, 2011 and June 30, 2010:

	As of June 30, 2011	As of June 30, 2010
Net Assets	$ 1,114,357	$ 711,424
Shares of common stock outstanding	107,606,690	69,086,862
Net asset value per share	$ 10.36	$ 10.30

At June 30, 2011, we had 107,606,690 of our common stock issued and outstanding.

Results of Operations

Net increase in net assets resulting from operations for the years ended June 30, 2011, 2010 and 2009 was $118,238, $19,625 and $35,104, respectively, representing $1.38, $0.33 and $1.11 per weighted average share, respectively. The primary driver of the variability in the results is the recognition of realized gains and losses and changes in unrealized gains and losses in the investment portfolio. During the year ended June 30, 2011, we experienced net unrealized and realized gains of $24,017, or approximately $0.28 per weighted average share, primarily from significant write-ups of our investments in Ajax, Biotronic GSHI, Iron Horse, NRG and Sport Helmets, and our sale of our common equity in Fischbein and Miller, for which we realized gains of $9,893 and $7,977, respectively. These instances of realized and unrealized appreciation were partially offset by unrealized depreciation in H&M, Shearer's and Stryker. During the year ended June 30, 2010, we experienced net unrealized and realized losses of $47,565 or approximately $0.80 per weighted average share due primarily due to the impairment of Yatesville (See Investment Valuations for further discussion.). The $51,228 realized loss for Yatesville was partially offset by write-ups of our investments in Ajax, Freedom Marine, H&M, Manx, NRG, and R-V. During the year ended June 30, 2009, we experienced net unrealized and realized losses of $24,059 or approximately $0.76 per weighted average share. The $41,134 realized loss for CCEHI and $21,099 unrealized write-down of our investment in Yatesville was partially offset by write-ups of our investments in GSHI and NRG.

While we seek to maximize gains and minimize losses, our investments in portfolio companies can expose our capital to risks greater than those we may anticipate. These companies are typically not issuing securities rated investment grade, have limited resources, have limited operating history, have concentrated product lines or customers, are generally private companies with limited operating information available and are likely to depend on a small core of management talents. Changes in any of these factors can have a significant impact on the 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 common or preferred stock that we own, fees generated from the structuring of new deals. Our investments, if in the form of debt securities, will typically have a term of one to ten years and bear interest at a fixed or floating rate. To the extent achievable, we will seek to collateralize our investments by obtaining security interests in our portfolio companies' assets. We also may acquire minority or majority equity interests in our portfolio companies, which may pay cash or in-kind dividends on a recurring or otherwise negotiated basis. In addition, we may generate revenue in other forms including prepayment penalties and possibly consulting fees. Any such fees generated in connection with our investments are recognized as earned.

Investment income, which consists of interest income, including accretion of loan origination fees and prepayment penalty fees, dividend income and other income, including settlement of net profits interests, overriding royalty interests and structuring fees, was $169,476, $114,559, and $100,481 for the years ended June 30, 2011, June 30, 2010 and June 30, 2009, respectively. During the year ended

Table of Contents

June 30, 2011, the primary driver of the increase in investment income is the deployment of additional capital in revenue-producing assets through increased origination, for which we recognized an increase of $16,107 in structuring fee income, and $44,685 in cash and payment-in-kind interest income. This $44,685 of interest income excludes purchase discount accretion from the assets acquired from Patriot and is the result of a larger income producing investment portfolio. These increases were partially offset by a $4,650 decline in dividend income from GSHI as well as a decline, year over year, related to the one-time gain of $8,632 in the fiscal year ended June 30, 2010, recorded upon acquiring Patriot. The primary driver of the increase from the fiscal year ended June 30, 2009 to the fiscal year ended June 30, 2010 is the acquisition of additional assets from Patriot and other new investments which increased interest income for the second half of the year. This increase is partially offset by a decline in dividend income from GSHI.

The following table describes the various components of investment income and the related levels of debt investments:

	Year Ended June 30, 2011	Year Ended June 30, 2010	Year Ended June 30, 2009
Interest income	$ 134,454	$ 86,518	$ 62,926
Dividend income	15,092	15,366	22,793
Other income	19,930	12,675	14,762
Total investment income	$ 169,476	$ 114,559	$ 100,481
Average debt principal of investments	$ 980,557	$ 615,638	$ 523,189
Weighted-average interest rate earned	13.7%	14.1%	12.0%

Average interest income producing assets have increased from $523,189 for the year ended June 30, 2009 to $615,638 for the year ended June 30, 2010 and $980,557 for the year ended June 30, 2011. The average yield on interest bearing assets increased from 12.0% for the year ended June 30, 2009 to 14.1% for the year ended June 30, 2010 and 13.7% for the year ended June 30, 2011. This increase in annual returns is primarily the accelerated accretion on the assets acquired from Patriot on which we recognized $17,172 and $14,216 during the years ended June 30, 2011 and June 30, 2010, respectively. Without these adjustments, the weighted average interest rates earned on debt investments would have been 12.0% and 11.7% for the years ended June 30, 2011 and 2010, respectively. Generally, interest returns have remained relatively stable over the three year period, but we have seen a decrease in interest rates on loans issued during our fourth fiscal quarter ended June 30, 2011.

Investment income is also generated from dividends and other income. Dividend income decreased from $15,366 for the year ended June 30, 2010 to $15,092 for the year ended June 30, 2011. The decrease in dividend income is primarily attributable to a decrease in the level of dividends received from our investment in GSHI. We received dividends from GSHI of $9,850 and $14,500 during the years ended June 30, 2011 and June 30, 2010, respectively. The decrease in dividends from GSHI is primarily the a consequence of GSHI distributing dividends in excess of their current earnings in 2009, as GSHI had accumulated excess earnings and profits available for distribution. GSHI remains profitable and has increased its EBITDA in 2010 in comparison with 2009. We anticipate that GSHI may be able to increase its dividends in the future as the result of organic growth and add-on acquisitions. This decrease was offset by a $4,178 increase in dividends received from American Gilsonite and NRG during the year ended June 30, 2011.

Other income has come primarily from structuring fees, overriding royalty interests, and settlement of net profits interests. Comparing the year ended June 30, 2010 to the year ended June 30, 2011, income from other sources, excluding the $8,632 gain on the Patriot acquisition, increased from $4,043 to $19,930. This $15,887 increase is primarily due to $18,494 of structuring fees recognized during the year ended June 30, 2011 primarily from the AIRMALL, CAS, CRT, Progrexion, Safe-Guard, Springs

Table of Contents

Window and NMMB originations, in comparison to $2,388 of structuring fees recognized during the year ended June 30, 2010.

Comparing the year ended June 30, 2009 to the year ended June 30, 2010, income from other sources, excluding the $8,632 gain on the Patriot acquisition, decreased from $14,762 to $4,043. This decrease in other income is largely due to the settlement of our net profit interests in IEC/ARS for $12,576 during the year ended June 30, 2009. During the year ended June 30, 2009, structuring fees of $1,274 were received primarily related to Biotronic and GSHI, in comparison to $2,388 of structuring fees recognized during the year ended June 30, 2010.

Operating Expenses

Our primary operating expenses consist of investment advisory fees (base and incentive fees), credit facility costs, legal and professional fees and other operating and overhead-related expenses. These expenses include our allocable portion of overhead under the Administration Agreement with Prospect Administration under which Prospect Administration provides administrative services and facilities for us. Our investment advisory fees compensate our Investment Adviser for its work in identifying, evaluating, negotiating, closing and monitoring our investments. We bear all other costs and expenses of our operations and transactions in accordance with our Administration Agreement with Prospect Administration. Operating expenses were $75,255, $47,369 and $41,318 for the years ended June 30, 2011, June 30, 2010 and June 30, 2009, respectively.

The base investment advisory expenses were $22,496, $13,929 and $11,915 for the years ended June 30, 2011, June 30, 2010 and June 30, 2009, respectively. These increases are directly related to our growth in total assets. $23,555, $16,798 and $14,790 in income incentive fees were earned for the years ended June 30, 2011, June 30, 2010 and June 30, 2009, respectively. The increases have occurred as net interest income has increased due primarily to an increase in the asset base. No capital gains incentive fee has yet been incurred pursuant to the Investment Advisory Agreement.

During the years ended June 30, 2011, June 30, 2010 and June 30, 2009, we incurred $17,598, $8,382 and $6,161, respectively, of expenses related to our Syndicated Facility and Senior Convertible Notes. These expenses are related directly to the leveraging capacity put into place for each of those years and the levels of indebtedness actually undertaken in those years. The table below describes the various expenses of our Syndicated Facility and Senior Convertible Notes and the related indicators of leveraging capacity and indebtedness during these years.

	Year Ended June 30, 2011	**Year Ended June 30, 2010**	**Year Ended June 30, 2009**
Interest expense	$ 9,861	$ 1,338	$ 5,075
Amortization of deferred financing costs	5,366	5,297	759
Commitment and other fees	2,371	1,747	327
Total	$ 17,598	$ 8,382	$ 6,161
Weighted average debt outstanding	$ 176,277	$ 23,147	$ 132,013
Weighted average interest rate	5.59%	5.78%	3.84%
Facility amount at beginning of year	$ 210,000	$ 175,000	$ 200,000

The increase in interest expense for the year ended June 30, 2011 is due to the issuance of Senior Convertible Notes on December 21, 2010 and February 18, 2011 for which we incurred $8,374 of interest expense. The increase in our interest rate incurred for the year ended June 30, 2010 is primarily due to an increase of 150 basis points in our borrowing rate effective June 25, 2009 and the concurrent introduction of a Libor floor at 200 basis points. This increase was partially amended on June 11, 2010 with the closing of our current facility. The borrowing rate and Libor floor decreased by 75 basis points and 100 basis points, respectively.

Table of Contents

As our asset base has grown and we have added complexity to our capital raising activities, due, in part, to our assumption of the sub-administration role from Vastardis Fund Services LLC ("Vastardis"), we have commensurately increased the size of our administrative and financial staff, accounting for a significant increase in the overhead allocation from Prospect Administration. Over the last two years, Prospect Administration has increased staffing levels along with costs passed through. The allocation of overhead expense from Prospect Administration were $2,856, $3,361 and $4,979 for the years ended June 30, 2009, 2010 and 2011, respectively. As our portfolio continues to grow, we expect to continue to increase the size of our administrative and financial staff on a basis that provides increasing returns to scale. However, initial investments in administrative and financial staff may not provide returns to scale immediately, perhaps not until the portfolio increases to a greater size. Other allocated expenses from Prospect Administration will continue to increase along with the increase in staffing and asset base.

Total operating expenses, net of management fees, interest costs and allocation of overhead from Prospect Administration ("Other Operating Expenses"), were $6,627, $4,899 and $5,596 for the years ended June 30, 2011, 2010 and 2009, respectively. The increase in Other Operating Expenses during the year ended June 30, 2011 when compared to the year ended June 30, 2010 is primarily the result of a $1,058 increase in costs expensed in connection with abandoned originations and portfolio company acquisitions, an $818 increase in administrative expenses incurred to support of our growing portfolio and a $589 increase in unreimbursed legal and consulting fees incurred related to the management of loans. These increases were offset by the non-recurrence of the costs incurred in connection with the merger discussions with Allied Capital Corporation ("Allied") expensed in the 2010 period. The decrease in Other Operating Expenses during the year ended June 30, 2010 when compared to the year ended June 30, 2009 is primarily the result operating efficiencies realized upon the termination of the sub-administration agreement and no excise taxes being paid in 2010 offset by the costs incurred in connection with merger discussions with Allied expensed in the 2010 period.

Net Investment Income

Net investment income represents the difference between investment income and operating expenses. Our net investment income was $94,221, $67,190 and $59,163 for the years ended June 30, 2011, June 30, 2010 and June 30, 2009, respectively, or $1.10 per share, $1.13 per share and $1.87 per share, respectively. The $27,031 increase for the year ended June 30, 2011 is primarily due to increases of $47,936 and $7,255 in interest income and other income, respectively, due to the increased size of our portfolio for which we have recognized additional interest income and structuring fees. The $27,031 increase is offset by an increase in operating expenses of $27,886, primarily due to a $15,324 increase in advisory fees due to the growing size of our portfolio and related income, and $9,216 of additional interest and credit facility expenses. The per share decrease for the year ended June 30, 2011 is primarily due to a decrease in dividends from existing equity investments along with new equity investments in the portfolio which have not yet declared any dividends and the non-recurring nature of the gain from the Patriot Acquisition during the year ended June 30, 2010 offset by an increase in structuring fees collected in the fiscal year ended June 30, 2011.

The $8,027 increase in net investment income for the year ended June 30, 2010 in comparison to the year ended June 30, 2009 is primarily due to an increase in investment income of $14,078. This $14,078 is due to a $23,592 increase in interest income offset by decreases in dividend income from GSHI and other income. Income from other sources, excluding the $8,632 gain on the Patriot acquisition, decreased from $14,762 to $4,043. This decrease in other income is largely due to the settlement of our net profit interests in IEC/ARS for $12,576 during the year ended June 30, 2009. The per share decrease for the year ended June 30, 2010 is primarily result of our increasing our asset mix in financings with private equity sponsors. We believe that such financings offer less risk, and

Table of Contents

consequently lower yields, due, in part, to lesser risk to our capital resulting from larger equity at risk underneath our capital.

Net Realized Gains (Losses), Increase (Decrease) in Net Assets from Net Changes in Unrealized Appreciation/Depreciation

Net realized gains (losses) were $16,465, ($51,545) and ($39,078) for the years ended June 30, 2011, June 30, 2010 and June 30, 2009, respectively. The net realized gain for the year ended June 30, 2011 was due primarily to gains from the sales of our common equity in Fischbein and Miller of $9,893 and $7,977, respectively. The net realized loss of $51,545 for the year ended June 30, 2010 was due primarily to the impairment of Yatesville. (See Investment Valuations for further discussion.) On June 30, 2009, we determined that the impairment of the CCEHI investment was other than temporarily impaired and recognized a realized loss of $41,134 for the amount by which the amortized cost exceeded the current fair value. This loss was partially offset by realized gains of $423 and $1,641 from sales of the Arctic warrants and Deep Down, Inc. ("Deep Down") common stock, respectively.

Net increase in net assets from changes in unrealized appreciation was $7,552, $3,980 and $15,019 for the years ended June 30, 2011, June 30, 2010 and June 30, 2009, respectively, or $0.09 per share, $0.07 per share and $0.48 per share, respectively. For the year ended June 30, 2011, the $7,552 increase in net assets from the net change in unrealized appreciation was driven by significant write-ups of $54,916 related to our investments in Ajax, Biotronic, GSHI, Iron Horse, NRG and Sport Helmets. These instances of unrealized appreciation were partially offset by unrealized depreciation of approximately $35,689 related to our investments in H&M, ICS, Manx, Shearer's, Stryker, and $10,840 related to the repayment of Prince. For the year ended June 30, 2010, the net unrealized appreciation was driven by $25,184 of write-ups in our investments in Fischbein, GSHI, Prince, Shearer's, and RMC, and by the disposition of previously written-down investment in Yatesville mentioned above with an unrealized net appreciation of $35,471, which, in turn, were offset by $56,954 of write-downs in our investments in Deb Shops, Inc. ("Deb Shops"), Freedom Marine, H&M, Manx, NRG, R-V and Wind River Resources Corp. and Wind River II Corp. For the year ended June 30, 2009, the net unrealized appreciation was driven by significant write-ups of our investments in American Gilsonite, GSHI, NRG, R-V, Shearer's and Stryker, and by the disposition of previously written-down investment in CCEI mentioned above, which, in turn, were offset by significant write-downs our investments in Ajax, AEH, Conquest Cherokee, LLC, Deb Shops, Iron Horse and Yatesville as well as the elimination of the unrealized appreciation resulting from the sale of Deep Down mentioned above.

Financial Condition, Liquidity and Capital Resources

For the years ended June 30, 2011, June 30, 2010 and Jun 30, 2009, our operating activities (used) provided ($581,609), $54,838 and ($74,000) of cash, respectively. Investing activities used $106,586 for the acquisition of Patriot for the year ended June 30, 2010. There were no investing activities for the years ended June 30, 2011 and June 30, 2009. Financing activities provided cash flows of $582,020, $42,887 and $83,387 for the years ended June 30, 2011, June 30, 2010 and June 30, 2009, respectively. Dividends paid were $91,247, $82,908 and $43,257 for the years ended June 30, 2011, June 30, 2010 and June 30, 2009, respectively.

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

Our primary sources of funds have been issuances of debt and equity. We have and may continue to fund a portion of our cash needs through borrowings from banks, issuances of senior securities or secondary offerings. We may also securitize a portion of our investments in mezzanine or senior secured loans or other assets. Our objective is to put in place such borrowings in order to enable us to expand our portfolio. During the year ended June 30, 2011, we borrowed $465,900 and made repayments totaling $482,000 under our revolving credit facility. As of June 30, 2011, we had $84,200 outstanding borrowings on our revolving credit facility and $322,500 outstanding on our Senior Convertible notes (See Note 6 to our consolidated financial statements).

On March 16, 2011, our Registration Statement on Form N-2 was declared effective by the SEC. Under this Shelf Registration Statement, we can issue up to $547,000 of additional equity securities as of June 30, 2011.

Over the past three years, we have been active in completing public and private stock offerings.

On July 7, 2009 we completed a public stock offering for 5,175,000 shares of our common stock at $9.00 per share, raising $46,575 of gross proceeds. On August 20, 2009 and September 24, 2009, we issued 3,449,686 shares and 2,807,111 shares, respectively, of our common stock at $8.50 and $9.00 per share, respectively, in private stock offerings, raising $29,322, and $25,264 of gross proceeds, respectively. Concurrent with the sale of these shares, we entered into a registration rights agreement in which we granted the purchasers certain registration rights with respect to the shares. Under the terms and conditions of the registration rights agreement, we filed with the SEC a post-effective amendment to the registration statement on Form N-2 on November 6, 2009. Such 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. Under the 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 connection with the transaction, we repaid all the outstanding borrowings of Patriot, in compliance with the merger agreement.

On March 17, 2010, we established an at-the-market program through which we could sell, from time to time and at our discretion, 8,000,000 shares of our common stock. Through this program we issued 5,251,400 shares of our common stock at an average price of $11.50 per share, raising $60,378 of gross proceeds, from March 23, 2010 through June 30, 2010 and $26,799 from July 1, 2010 to July 21, 2010.

On July 19, 2010, we established a second at-the-market program, as we had sold all the shares authorized in the original at-the-market program. We engaged three broker-dealers to act as potential agents and sell our common stock directly into the market over a period of time. We paid a 2% commission to the broker-dealer on shares sold. Through this program we issued 6,000,000 shares of our common stock at an average price of $9.73 per share, raising $58,403 of gross proceeds, from July 22, 2010 through September 28, 2010.

On September 24, 2010, we established a third at-the-market program, as we had sold all the shares authorized in the preceding at-the-market programs, through which we could sell, from time to time and at our discretion, 6,000,000 shares of our common stock. We engaged three broker-dealers to act as potential agents and sell our common stock directly into the market over a period of time. We currently pay a 2% commission to the broker-dealer on shares sold. Through this program we issued 302,400 shares of our common stock at an average price of $9.87 per share, raising $2,986 of gross proceeds, from September 29, 2010 through September 30, 2010. During the period from October 1, 2010 to November 3, 2010, we continued this program and issued an additional 4,929,556 shares of our common stock at an average price of $9.86 per share, raising $48,611 of gross proceeds.

On November 10, 2010, we established a fourth at-the-market program, through which we could sell, from time to time and at our discretion, 9,750,000 shares of our common stock. We engaged four broker-dealers to act as potential agents and sell our common stock directly into the market over a period of time. We pay a 2% commission to the broker-dealer on shares sold. Through this program we