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

FORM 10-K

---

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

For the fiscal year ended December 31, 2010

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

For the transition period from __________ to __________

Commission File No. 814-00735

Kohlberg Capital Corporation

(Exact name of Registrant as specified in its charter)

Delaware	**20-5951150**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

295 Madison Avenue, 6th Floor
New York, New York 10017

(Address of principal executive offices)

(212) 455-8300

(Registrant's telephone number, including area code)

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

Title of each class	Name of exchange on which registered
Common Shares, par value $0.01 per share	The NASDAQ Global Select Market

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

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

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

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

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

Large accelerated filer o	Accelerated filer x	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller Reporting Company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes o No x

The aggregate market value of the voting and non-voting common stock held by non-affiliates of the registrant as of June 30, 2010 was approximately $94 million based upon a closing price of $5.01 reported for such date by The NASDAQ Global Select Market. Common shares held by each executive officer and director and by each person who owns 5% or more of the outstanding common shares have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

The number of outstanding shares of common stock of the registrant as of February 28, 2011 was 22,808,907.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement for the annual meeting of stockholders to be held on June 16, 2011 (the "Proxy Statement") are incorporated by reference into Part III of this report.

NOTE ABOUT REFERENCES TO KOHLBERG CAPITAL CORPORATION

In this Annual Report on Form 10-K (this "Annual Report"), the "Company", "we", "us" and "our" refer to Kohlberg Capital Corporation, its subsidiaries and its wholly-owned portfolio company, Katonah Debt Advisors, L.L.C., and its controlled affiliates ("Katonah Debt Advisors" or "KDA"), and related companies, unless the context otherwise requires.

NOTE ABOUT TRADEMARKS

Kohlberg Capital Corporation, our logo and other trademarks of Kohlberg Capital Corporation are the property of Kohlberg Capital Corporation. All other trademarks or trade names referred to in this Annual Report are the property of their respective owners.

NOTE ABOUT FORWARD-LOOKING STATEMENTS

This Annual Report includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. The matters discussed in this Annual Report, as well as in future oral and written statements by management of Kohlberg Capital Corporation, that are forward-looking statements are based on current management expectations that involve substantial risks and uncertainties which could cause actual results to differ materially from the results expressed in, or implied by, these forward-looking statements. Forward-looking statements relate to future events or our future financial performance. We generally identify forward-looking statements by terminology such as "may," "will," "should," "expects," "plans," "anticipates," "could," "intends," "target," "projects," "contemplates," "believes," "estimates," "predicts," "potential" or "continue" or the negative of these terms or other similar words, although not all forward-looking statements include these words. Important assumptions include our ability to originate new investments, achieve certain margins and levels of profitability, the availability of additional capital, and the ability to maintain certain debt to asset ratios. In light of these and other uncertainties, the inclusion of a projection or forward-looking statement in this Annual Report should not be regarded as a representation by us that our plans or objectives will be achieved. The forward-looking statements contained in this Annual Report include statements as to:

- our future operating results;
- our business prospects and the prospects of our existing and prospective portfolio companies;
- the return or impact of current and future investments;
- our contractual arrangements and other 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 financial condition and ability of our existing and prospective portfolio companies to achieve their objectives;
- our expected financings and investments;
- our regulatory structure and tax treatment;
- our ability to operate as a business development company and a registered investment company, including the impact of changes in laws or regulations governing our operations, the operations of KDA or the operations of our portfolio companies;
- the adequacy of our cash resources and working capital;
- the timing of cash flows, if any, from the operations of our portfolio companies, including Katonah Debt Advisors;
- the impact of a protracted decline in the liquidity of credit markets on our business;
- the impact of fluctuations in interest rates on our business;

TABLE OF CONTENTS

- the valuation of our investments in portfolio companies, particularly those having no liquid trading market;
- our ability to recover unrealized losses;
- market conditions and our ability to access additional capital; and
- the timing, form and amount of any dividend distributions;

For a discussion of factors that could cause our actual results to differ from forward-looking statements contained in this Annual Report, please see the discussion under "Risk Factors" in Item 1A. You should not place undue reliance on these forward-looking statements. The forward-looking statements made in this Annual Report relate only to events as of the date on which the statements are made. We undertake no obligation to update any forward-looking statement to reflect events or circumstances occurring after the date of this Annual Report.

Kohlberg Capital Corporation

TABLE OF CONTENTS

PART I

Item 1. *Business*

KOHLBERG CAPITAL CORPORATION

We are an internally managed, non-diversified closed-end investment company that has elected to be regulated as a business development company ("BDC") under the Investment Company Act of 1940, as amended (the "1940 Act"). We originate, structure and invest in senior secured term loans, mezzanine debt and selected equity securities primarily in privately-held middle market companies. We define the middle market as comprising companies with earnings before interest, taxes, depreciation and amortization, which we refer to as "EBITDA," of $10 million to $50 million and/or total debt of $25 million to $150 million. In addition to our middle market investment business, our wholly-owned portfolio company, Katonah Debt Advisors and its controlled affiliates (collectively, "Katonah Debt Advisors"), manage collateralized loan obligation funds ("CLO Funds") that invest in broadly syndicated loans, high-yield bonds and other corporate credit instruments. We acquired Katonah Debt Advisors and certain related assets prior to our initial public offering from affiliates of Kohlberg & Co., L.L.C. ("Kohlberg & Co."), a leading private equity firm focused on middle market investing. As of December 31, 2010, Katonah Debt Advisors had approximately $2.1 billion of assets under management.

Our investment objective is to generate current income and capital appreciation from our investments. We also expect to receive distributions of recurring fee income and to generate capital appreciation from our investment in the asset management business of Katonah Debt Advisors. Our investment portfolio as well as the investment portfolios of the CLO Funds in which we have invested and the investment portfolios of the CLO Funds managed by Katonah Debt Advisors consist exclusively of credit instruments and other securities issued by corporations and do not include any asset-backed securities secured by commercial mortgages, residential mortgages or other consumer borrowings.

As a Regulated Investment Company ("RIC"), for U.S. federal tax purposes, we intend to distribute to our stockholders substantially all of our net taxable income and the excess of realized net short-term capital gains over realized net long-term capital losses. To qualify as a RIC, we must, among other things, meet certain source-of-income and asset diversification requirements. As a RIC, we generally will not have to pay corporate-level taxes on any income that we distribute in a timely manner to our stockholders.

Our common stock is traded on The NASDAQ Global Select Market under the symbol "KCAP." The net asset value per share of our common stock at December 31, 2010 was $8.21. On December 31, 2010, the last reported sale price of a share of our common stock on The NASDAQ Global Select Market was $6.97.

CORPORATE HISTORY AND OFFICES

We were formed in August 2006 as a Delaware limited liability company. In December 2006, we completed our initial public offering ("IPO"), which raised net proceeds of approximately $200 million after the exercise of the underwriters' over-allotment option. In connection with our IPO, we issued an additional 3,484,333 shares of our common stock to affiliates of Kohlberg & Company in exchange for the ownership interests of Katonah Debt Advisors and in securities issued by CLO Funds managed by Katonah Debt Advisors and two other asset managers.

Our principal executive offices are located at 295 Madison Avenue, 6th Floor, New York, New York 10017 and our telephone number is (212) 455-8300. Information about us may also be obtained from the website of the Securities and Exchange Commission (the "SEC" or the "Commission") at *http://www.sec.gov*. We maintain a website on the Internet at *http://www.kohlbergcapital.com*. Information contained in our website is not incorporated by reference into this Annual Report, and that information should not be considered as part of this Annual Report. We make available free of charge on our website our Annual Report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports as soon as reasonably practicable after such material is electronically filed with or furnished to the SEC.

KEY QUANTITATIVE AND QUALITATIVE FINANCIAL MEASURES AND INDICATORS

Net Asset Value

Our NAV per share was $8.21 and $9.56 as of December 31, 2010 and December 31, 2009, respectively. As we must report our assets at fair value for each reporting period, NAV also represents the amount of stockholders' equity per share for the reporting period. Our NAV is comprised mostly of investment assets less debt and other liabilities:

	December 31, 2010		December 31, 2009	
	Fair Value(1)	per Share(1)	Fair Value(1)	per Share(1)
Investments at fair value:				
Time deposits	$ 720,225	$ 0.03	$ 126	$ —
Money market account	210,311	0.01	—	—
Debt securities	91,042,928	4.00	297,356,529	13.30
CLO Fund securities	53,031,000	2.33	48,971,000	2.19
Equity securities	4,688,832	0.21	4,713,246	0.21
Asset manager affiliates	41,493,000	1.82	58,064,720	2.60
Cash	10,175,488	0.45	4,140,408	0.18
Restricted Cash	67,023,170	2.93	18,696,023	0.84
Other assets	11,437,732	0.50	7,474,005	0.33
Total Assets	$ 279,822,686	$ 12.28	$ 439,416,057	$ 19.65
Borrowings	$ 86,746,582	$ 3.81	$ 218,050,363	$ 9.75
Other liabilities	6,150,437	0.27	7,469,970	0.34
Total Liabilities	$ 92,897,019	$ 4.08	$ 225,520,333	$ 10.09
NET ASSET VALUE	$ 186,925,667	$ 8.21	$ 213,895,724	$ 9.56

(1) Our balance sheet at fair value and resultant net asset value are calculated on a basis consistent with accounting principles generally accepted in the United States of America ("GAAP"). Our per share presentation of such amounts (other than NAV per share) is an internally derived non-GAAP performance measure calculated by dividing the applicable balance sheet amount by outstanding shares. We believe that the per share amounts for such balance sheet items are helpful in analyzing our balance sheet both quantitatively and qualitatively.

Please refer to "— Investment Portfolio" below for a further description of our investment portfolio and the fair value thereof.

Leverage

We use borrowed funds, known as "leverage," to make investments and to attempt to increase returns to our shareholders by reducing our overall cost of capital. As a BDC, we are limited in the amount of leverage we can incur under the 1940 Act. We are only allowed to borrow amounts such that our asset coverage, as defined in the 1940 Act, equals at least 200% after such borrowing. As of December 31, 2010, we had approximately $87 million of outstanding borrowings and our asset coverage ratio of total assets to total borrowings was 315%, compliant with the minimum asset coverage level of 200% generally required for a BDC by the 1940 Act. We may also borrow amounts of up to 5% of the value of our total assets for temporary purposes. As of January 31, 2011, we had repaid in full the outstanding balance of our borrowings and we are currently operating fully unlevered.

Prior to the payoff of our outstanding indebtedness on January 31, 2011, our borrowings were through a secured financing facility (the "Facility"). In connection with the Facility, we were party to a Loan Funding and Servicing Agreement, dated as of February 14, 2007 (as amended, the "LFSA"), by and among us, as the servicer, our wholly-owned, special-purpose bankruptcy remote subsidiary, Kohlberg Capital Funding LLC I, as the borrower ("KCAP Funding" or the "Borrower"), BMO Capital Markets Corp, as the agent (the "Agent"), U.S. Bank National Association, a national banking association, as the trustee (the "Trustee") and the other Lender Parties and other parties thereto (the "Lender Parties"). As previously reported, the LFSA was modified on September 20, 2010 pursuant to a Forbearance and Settlement Agreement (the "Settlement

Agreement") with the Agent and Lender Parties, pursuant to which we and the Agent and the Lender Parties agreed to settle all outstanding claims thereunder and in connection with litigation previously initiated by us against the Agent and the other Lender Parties.

Prior to entering into the Settlement Agreement, the interest on outstanding amounts under the Facility accrued at a rate equal to 0.85% above the prime rate plus 0.75%, or approximately 4.9%, and we had been paying interest at such rate under protest. Under the terms of the Settlement Agreement, commencing on September 10, 2010, the advances under the Facility accrued interest at the rate provided for under the LFSA prior to the occurrence of a termination event, equal to 0.85% above the prevailing commercial paper rate, or approximately 1.2% as of such date. Under the terms of the Settlement Agreement, we calculated the advances outstanding under the Facility after consideration of amortization and pre-payments in the next scheduled distribution to the lenders. As of December 31, 2010, the Company's advances outstanding, calculated in accordance with the Settlement Agreement, were approximately $87 million. Under the Settlement Agreement, the Company was also obligated to maintain an overcollateralization ratio of at least 115%. As of December 31, 2010, our overcollateralization ratio was 177%. As a BDC, we are limited in the amount of leverage we can incur and are required to meet a coverage ratio of total asset to total senior securities of at least 200% before incurring new debt. As of December 31, 2010, our asset coverage ratio was 315%. We were in compliance with all covenants and terms set forth in the Settlement Agreement at December 31, 2010.

On January 31, 2011, we repaid in full the outstanding balance under the Facility in advance of the scheduled forbearance date of February 28, 2011. As a result, we have no outstanding indebtedness and the Lender Parties released to us approximately $73 million of collateral previously securing the Facility and also paid to us a $2 million cash settlement. In order to pay off the Facility, we utilized proceeds received from the paydown, amortization or sale of portfolio loan investments totaling approximately $133 million together with available cash.

Subject to prevailing market conditions, we intend to grow our portfolio of assets by raising additional capital, including through the prudent use of leverage. As a result, we may seek to enter into a new agreement with other lenders or into other financing arrangements as market conditions permit. Such financing arrangements may include a new secured and/or unsecured credit facility, the issuance of senior debt, preferred or convertible securities or debt guaranteed by the SBA.

The weighted average daily debt balance for the years ended December 31, 2010 and 2009 was approximately $105 million and $222 million, respectively. As of December 31, 2010, the Company had restricted cash and time deposit balances of approximately $67 million which it maintained in accordance with the terms of the Facility.

Investment Portfolio Summary Attributes as of and for the Year Ended December 31, 2010

Our investment portfolio generates net investment income, which is generally used to pay principal and interest on our borrowings and to fund our dividends. Our investment portfolio consists of three primary components: debt securities, CLO fund securities and our investment in our wholly owned asset manager, Katonah Debt Advisors. We also have investments in equity securities of approximately $5 million, which comprises approximately 2% of our investment portfolio. Below are summary attributes for each of our primary investment portfolio components (see "— Investment Portfolio" and "— Investments and Operations" for a more detailed description) as of and for the year ended December 31, 2010:

Debt Securities

- represent approximately 49% of total investment portfolio;
- represent credit instruments issued by corporate borrowers;
- no asset-backed securities such as those secured by commercial mortgages or residential mortgages and no consumer borrowings;
- primarily senior secured and junior secured loans (12% and 33%, respectively);
- spread across 16 different industries and 24 different entities;

- average balance per investment of approximately $3 million;
- all but five issuers current on their debt service obligations;
- weighted average interest rate of 8.6% on income producing debt investments.

CLO Fund Securities (as of the last monthly trustee report prior to December 31, 2010 unless otherwise specified)

- represent approximately 28% of total investment portfolio at December 31, 2010;
- 85% of CLO Fund Securities represent investments in subordinated securities or equity securities issued by CLO Funds and 15% of CLO Fund Securities are rated notes;
- all CLO Funds invest primarily in credit instruments issued by corporate borrowers;
- no asset-backed securities such as those secured by commercial mortgages or residential mortgages and no consumer borrowings;
- ten different CLO Fund securities; six of such CLO Fund securities are managed by Katonah Debt Advisors; and
- one CLO Fund security, not managed by Katonah Debt Advisors, representing a fair value of $1,000, is not currently providing a dividend payment to the Company.

Katonah Debt Advisors

- represents approximately 22% of total investment portfolio;
- represents our 100% ownership of the equity interest of a profitable CLO Fund manager focused on corporate credit investing;
- has approximately $2.1 billion of assets under management;
- receives contractual and recurring asset management fees based on par value of managed investments;
- typically receives a one-time structuring fee upon completion of a new CLO Fund;
- may receive an incentive fee upon liquidation of a CLO Fund provided that the CLO Fund achieves a minimum designated return on investment;
- dividends paid by Katonah Debt Advisors are recognized as dividend income from affiliate asset manager on our statement of operations and are an additional source of income to pay our dividend;
- for the year ended December 31, 2010, Katonah Debt Advisors had pre-tax net income of approximately $1 million; and
- for the year ended December 31, 2010, Katonah Debt Advisors made distributions of $4.5 million to the Company in the form of a dividend which is recognized as current earnings to the Company.

Time Deposits and Money Market Accounts

- time deposits, represented by overnight Eurodollar deposits, were partially restricted under terms of the Facility prior to the payoff thereof on January 31, 2011; and
- the money market account contains restricted cash held for employee flexible spending accounts.

Revenue

Revenues consist primarily of investment income from interest and dividends on our investment portfolio and various ancillary fees related to our investment holdings.

Interest from Investments in Debt Securities. We generate interest income from our investments in debt securities which consist primarily of senior and junior secured loans. Our debt securities portfolio is spread across multiple industries and geographic locations, and as such, we are broadly exposed to market conditions and business environments. As a result, although our investments are exposed to market risks, we continuously seek to limit concentration of exposure in any particular sector or issuer.

Dividends from Investments in CLO Fund Securities. We generate dividend income from our investments in the securities of CLO Funds (typically preferred shares or subordinated securities) managed by Katonah Debt Advisors and selective investments in securities issued by funds managed by other asset management companies. CLO Funds managed by Katonah Debt Advisors invest primarily in broadly syndicated non-investment grade loans, high-yield bonds and other credit instruments of corporate issuers. The Company distinguishes CLO Funds managed by Katonah Debt Advisors as "CLO fund securities managed by affiliate." The underlying assets in each of the CLO Funds in which we have an investment are generally diversified secured or unsecured corporate debt and exclude mortgage pools or mortgage securities (residential mortgage bonds, commercial mortgage backed securities, or related asset-backed securities), debt to companies providing mortgage lending and emerging markets investments. Our CLO Fund securities that are subordinated securities or preferred shares ("junior securities") are subordinated to senior bond holders who typically receive a fixed rate of return on their investment. The CLO Funds are leveraged funds and any excess cash flow or "excess spread" (interest earned by the underlying securities in the fund less payments made to senior bond holders and less fund expenses and management fees) is paid to the holders of the CLO Fund's subordinated securities or preferred shares. The level of excess spread from CLO Fund securities can be impacted from the timing and level of the resetting of the benchmark interest rate for the underlying assets (which reset at various times throughout the quarter) in the CLO Fund and the related CLO Fund bond liabilities (which reset at each quarterly distribution date); in periods of short-term and volatile changes in the benchmark interest rate, the levels of excess spread and distributions to us can vary significantly. In addition, the failure of CLO Funds in which we invest to comply with certain financial covenants my lead to the temporary suspension or deferral of cash distributions to us.

For non-junior class CLO Fund securities, such as our investment in the class B-2L notes of the Katonah 2007-1 CLO, interest is earned at a fixed spread relative to the LIBOR index.

Dividends from Affiliate Asset Manager. We generate dividend income from our investment in Katonah Debt Advisors, an asset management company, which is a wholly-owned portfolio company that manages CLO Funds that invest primarily in broadly syndicated non-investment grade loans, high yield bonds and other credit instruments issued by corporations. As a manager of CLO Funds, Katonah Debt Advisors receives contractual and recurring management fees as well as an expected one-time structuring fee from the CLO Funds for its management and advisory services. In addition, Katonah Debt Advisors may earn income related to net interest on assets accumulated for future CLO issuances on which it has provided a first loss guaranty in connection with loan warehouse arrangements for its CLO Funds. Katonah Debt Advisors generates annual operating income equal to the amount by which its fee income exceeds it operating expenses. The annual management fees which Katonah Debt Advisors receives are generally based on a fixed percentage of the par value of assets under management and are recurring in nature for the term of the CLO Fund so long as Katonah Debt Advisors manages the fund. As a result, the annual management fees earned by Katonah Debt Advisors generally are not subject to market value fluctuations in the underlying collateral. In future years, Katonah Debt Advisors may receive incentive fees upon the liquidation of CLO Funds it manages, provided such CLO Funds have achieved a minimum investment return to holders of their subordinated securities or preferred shares.

Capital Structuring Service Fees. We may earn ancillary structuring and other fees related to the origination, investment, disposition or liquidation of debt and investment securities.

Expenses

We are internally managed and directly incur the cost of management and operations; as a result, we incur no management fees or other fees to an external advisor. Our expenses consist primarily of interest expense on outstanding borrowings, compensation expense and general and administrative expenses, including professional fees.

Interest and Amortization of Debt Issuance Costs. Interest expense is dependent on the average outstanding balance on our borrowings and the base index rate for the period. Debt issuance costs represent fees and other direct costs incurred in connection with the Company's borrowings. These amounts are capitalized and amortized ratably over the contractual term of the borrowing.

Compensation Expense. Compensation expense includes base salaries, bonuses, stock compensation, employee benefits and employer related payroll costs. The largest components of total compensation costs are base salaries and bonuses; generally, base salaries are expensed as incurred and annual bonus expenses are estimated and accrued. Our compensation arrangements with our employees contain a significant profit sharing and/or performance based bonus component. Therefore, as our net revenues increase, our compensation costs may also rise. In addition, our compensation expenses may also increase to reflect increased investment in personnel as we grow our products and businesses.

Professional Fees and General and Administrative Expenses. The balance of our expenses include professional fees (primarily legal, accounting, valuation and other professional services), occupancy costs and general administrative and other costs.

Net Change in Unrealized Depreciation on Investments

During the year ended December 31, 2010, the Company's investments had net unrealized depreciation of $8 million.

The net change in unrealized depreciation for the year ended December 31, 2010 is primarily due to (i) an approximate $9 million net increase in the market value of certain loans as a result of credit considerations and current market conditions; (ii) an approximate $4 million increase in the net value of CLO Fund securities; and (iii) an approximate $20 million decrease in the value of Katonah Debt Advisors due to the receipt of approximately $5 million of previously accrued subordinate management fees during the year, the planned disposition of one of its affiliates, and current market conditions.

Net Change in Stockholders' Equity Resulting From Operations

The net change in stockholders' equity resulting from operations for the year ended December 31, 2010 was a decrease of approximately $14 million or a decrease of $0.63 per share.

Net Investment Income and Net Realized Gains (Losses)

Net investment income and net realized gains (losses) represents the net change in stockholders' equity before net unrealized appreciation or depreciation on investments. For the year ended December 31, 2010, net investment income and realized losses was approximately $6 million, or $0.26 per share. Net investment income represents the income earned on our investments less operating and interest expense before net realized gains or losses and unrealized appreciation or depreciation on investments. For the year ended December 31, 2010, net investment income was approximately $12 million, or $0.53 per share.

Generally, we seek to fund our dividends from net investment income. For the year ended December 31, 2010, dividend distributions totaled $15 million, or $0.68 per share.

Dividends

We intend to continue to distribute quarterly dividends to our stockholders. To avoid certain excise taxes imposed on RICs, we currently intend to distribute during each calendar year an amount at least equal to the sum of:

- 98.0% of our ordinary net taxable income for the calendar year;
- 98.2% of our capital gains, if any, in excess of capital losses for the one-year period ending on October 31 of the calendar year; and
- any net ordinary income and net capital gains for the preceding year that were not distributed during such year.

The amount of our declared dividends, as evaluated by management and approved by our Board of Directors, is based on our evaluation of both distributable income for tax purposes and GAAP net investment income (which excludes unrealized gains and losses). Generally, we seek to fund our dividends from GAAP current earnings, primarily from net interest and dividend income generated by our investment portfolio and without a return of capital or a high reliance on realized capital gains. The following table sets forth the quarterly dividends declared by us in the two most recently completed years, which represent an amount equal to our estimated net investment income for the specified quarter, including income distributed from Katonah Debt Advisors received by the Company, plus a portion of any prior year undistributed amounts of net investment income distributed in subsequent years:

	Dividend	Declaration Date	Record Date	Pay Date
2010:				
Fourth quarter	$ 0.17	12/13/2010	12/24/2010	1/29/2011
Third quarter	0.17	9/20/2010	10/8/2010	10/29/2010
Second quarter	0.17	6/23/2010	7/7/2010	7/29/2010
First quarter	0.17	3/19/2010	4/7/2010	4/29/2010
Total declared for 2010	$ 0.68			
2009:				
Fourth quarter	$ 0.20	12/15/2009	12/28/2009	1/25/2010
Third quarter	0.24	9/24/2009	10/9/2009	10/29/2009
Second quarter	0.24	6/12/2009	7/9/2009	7/29/2009
First quarter	0.24	3/23/2009	4/8/2009	4/29/2009
Total declared for 2009	$ 0.92			

Due to our ownership of Katonah Debt Advisors and certain timing, structural and tax considerations, our dividend distributions may include a return of capital for tax purposes. For the year ended December 31, 2010, Katonah Debt Advisors had approximately $1 million of pre-tax net income and made distributions of $4.5 million to us, a portion of which represented undistributed earnings from prior years. For the year ended December 31, 2009, Katonah Debt Advisors had approximately $2 million of pre-tax net income and made no distributions to us. Dividends are recorded as declared (where declaration date represents ex-dividend date) by Katonah Debt Advisors as income on our statement of operations.

Please refer to “Distributions” and “Certain United States Federal Income Tax Considerations” for further information regarding our dividend distributions.

INVESTMENT PORTFOLIO

Investment Objective

Our investment objective is to generate current income and capital appreciation from the investments made by our middle market investment business in senior secured term loans, mezzanine debt and selected equity investments in privately-held middle market companies, and from our investment in Katonah Debt Advisors. We intend to grow our portfolio of assets by raising additional capital, including through the prudent use of leverage, including through future borrowing facilities and issuing debt securities. We primarily invest in first and second lien term loans which, because of their priority in a company’s capital structure, we expect will have lower default rates and higher rates of recovery of principal if there is a default and which we expect will create a stable stream of interest income. While our primary investment focus is on making loans to, and selected equity investments in, privately-held middle market companies, we may also invest in other investments such as loans to larger, publicly-traded companies, high-yield bonds and distressed debt securities. We may also receive warrants or options to purchase common stock in connection with our debt investments. In addition, we may also invest in debt and equity securities issued by CLO Funds managed by Katonah Debt Advisors or by other asset managers. However, our investment strategy is to limit the value of our investments in the debt or equity securities issued by CLO Funds to not more than 15% of the value of our total investment portfolio at the time of investment. We invest almost exclusively in credit instruments issued by corporations and do not invest in asset-backed securities such as those secured by commercial mortgages, residential mortgages or other consumer borrowings.

Our middle market investment business targets companies that have strong historical cash flows, experienced management teams and identifiable and defendable market positions in industries with positive dynamics. We seek to manage risk through a rigorous credit and investment underwriting process and an active portfolio monitoring program.

We expect to continue to benefit from our ownership of Katonah Debt Advisors in four ways. First, by working with the investment professionals at Katonah Debt Advisors, we have multiple sources of investment opportunities. Second, the experienced team of credit analysts at Katonah Debt Advisors, the members of which also serve as officers of the Company, have specializations covering more than 20 industry groups and they assist us in reviewing potential investments and monitoring our portfolio. Third, we may continue to make investments in CLO Funds or other funds managed by Katonah Debt Advisors, which we believe will provide us with a current cash investment return. Fourth, we expect to continue to receive distributions of recurring fee income and the potential to generate capital appreciation from our investment in Katonah Debt Advisors as the platform grows.

The following table shows the Company's portfolio by security type at December 31, 2010 and December 31, 2009:

	December 31, 2010			December 31, 2009		
Security Type	**Cost**	**Fair Value**	**%[1]**	**Cost**	**Fair Value**	**%[1]**
Time Deposits	$ 720,225	$ 720,225	—%	$ 126	$ 126	—%
Money Market Account	210,311	210,311	—	—	—	—
Senior Secured Loan	34,183,551	22,001,256	12	179,425,767	159,075,586	39
Junior Secured Loan	76,896,867	63,944,003	34	129,016,237	114,920,499	28
Mezzanine Investment	10,744,496	250,000	—	28,606,852	19,235,444	5
Senior Subordinated Bond	4,320,596	4,490,709	2	3,007,167	2,415,000	1
Senior Unsecured Bond	—	—	—	2,000,000	1,710,000	—
CLO Fund Securities	68,280,200	53,031,000	28	68,195,049	48,971,000	12
Equity Securities	13,232,266	4,437,871	2	12,365,603	4,713,246	1
Preferred	650,961	607,921	—	—	—	—
Affiliate Asset Managers	44,532,329	41,493,000	22	40,751,511	58,064,720	14
Total	$253,771,802	$191,186,296	100%	$463,368,312	$409,105,621	100%

(1) Represents percentage of total portfolio at fair value.

Investment Securities

We invest in senior secured loans, mezzanine debt and, to a lesser extent, equity, of middle market companies in a variety of industries. We generally target companies that generate positive cash flows because we look to cash flows as the primary source for servicing debt. However, we may invest in other industries if we are presented with attractive opportunities.

We employ a disciplined approach in the selection and monitoring of our investments. Generally, we target investments that will provide a current return through interest income to provide for stability in our net income and place less reliance on realized capital gains from our investments. Our investment philosophy is focused on preserving capital with an appropriate return profile relative to risk. Our investment due diligence and selection generally focuses on an underlying issuer's net cash flow after capital expenditures to service its debt rather than on multiples of net income, valuations or other broad benchmarks which frequently miss the nuances of an issuer's business and prospective financial performance. We also avoid concentrations in any one industry or issuer. We manage risk through a rigorous credit and investment underwriting process and an active portfolio monitoring program.

Our Board of Directors is ultimately and solely responsible for making a good faith determination of the fair value of portfolio investments on a quarterly basis. Debt and equity securities for which market quotations are readily available are generally valued at such market quotations. Debt and equity securities that are not publicly traded or whose market price is not readily available are valued by the Board of Directors based on detailed analyses prepared by management, the Valuation Committee of the Board of Directors, and, in certain circumstances, third parties with valuation expertise. Valuations are conducted by management on 100% of the investment portfolio at the end of each quarter. Due to the inherent uncertainty of determining the fair value of investments that do not have a readily available market value, the fair value of our investments may differ materially from the values that would have existed had a ready market existed for such investments. Further, such investments may be generally subject to legal and other restrictions on resale or otherwise less liquid than publicly traded securities. In addition, changes in the market environment and other events may occur over the life of the investments that may cause the value realized on such investments to be different from the currently assigned valuations.

We derive fair value for our illiquid investments that do not have indicative fair values based upon active trades primarily by using a present value technique that discounts the estimated contractual cash flows for the underlying assets with discount rates imputed by broad market indices, bond spreads and yields for comparable issuers relative to the subject assets (the “Market Yield Approach”) and also consider recent loan amendments or other activity specific to the subject asset. Discount rates applied to estimated contractual cash flows for an underlying asset vary by specific investment, industry, priority and nature of the debt security (such as the seniority or security interest of the debt security) and are assessed relative to two indices, a leveraged loan index and a high-yield bond index, at the valuation date. We have identified these two indices as benchmarks for broad market information related to our loan and debt investments. Because we have not identified any market index that directly correlates to the loan and debt investments held by us and therefore use the two benchmark indices, these market indices may require significant adjustment to better correlate such market data for the calculation of fair value of the investment under the Market Yield Approach. Such adjustments require judgment and may be material to the calculation of fair value. Further adjustments to the discount rate may be applied to reflect other market conditions or the perceived credit risk of the borrower. When broad market indices are used as part of the valuation methodology, their use is subject to adjustment for many factors, including priority, collateral used as security, structure, performance and other quantitative and qualitative attributes of the asset being valued. The resulting present value determination is then weighted along with any quotes from observable transactions and broker/pricing quotes. If such quotes are indicative of actual transactions with reasonable trading volume at or near the valuation date that are not liquidation or distressed sales, relatively more reliance will be put on such quotes to determine fair value. If such quotes are not indicative of market transactions or are insufficient as to volume, reliability, consistency or other relevant factors, such quotes will be compared with other fair value indications and given relatively less weight based on their relevancy. The appropriateness of specific valuation methods and techniques may change as market conditions and available data change.

In January 2010, the Financial Accounting Standards Board (“FASB”) issued guidance that clarifies and requires new disclosures about fair value measurements. The clarifications and requirement to disclose the amounts and reasons for significant transfers between Level I and Level II, as well as significant transfers in and out of Level III of the fair value hierarchy, were adopted by us in the first quarter of 2010. Note 4 to the financial statements reflects the amended disclosure requirements. The new guidance also requires that purchases, sales, issuances and settlements be presented gross in the Level III reconciliation and that requirement is effective for fiscal years beginning after December 15, 2010 and for interim periods within those years, with early adoption permitted. The Company is evaluating the increased disclosure requirements for implementation by the effective date. Since this new guidance only amends the disclosures requirements, it did not impact our statements of financial position, statements of operations, or cash flow statements.

Accounting Standards Codification Fair Value Measurements and Disclosures (“*Fair Value Measurements and Disclosure*”) requires the disclosure in interim and annual periods of the inputs and valuation techniques used to measure fair value and a discussion of changes in valuation techniques and related inputs, if any, during the period.

We engaged Valuation Research Corporation (“VRC”), an independent valuation firm, to provide third-party valuation estimates for approximately 39% of investments at fair value as of December 31, 2009. VRC’s valuation estimates were considered as one of the relevant data inputs in the Company’s determination of fair value. Though the Board of Directors did not engage VRC to provide valuation estimates for any of the assets in the Company’s portfolio as of December 31, 2010, the Board of Directors engaged VRC to review our CLO fair value model relative to its functionality, model inputs and calculations as a reasonable method to determine CLO fair values, in the absence of Level 1 or Level 2 trading activity or observable market inputs. VRC concluded that our CLO model appropriately factored in all the necessary inputs required to build a CLO equity cash flow for fair value purposes and that the inputs were being employed correctly.

The Board of Directors may engage an independent valuation firm in the future to provide certain valuation services, including the review of certain portfolio assets, as part of its valuation processes.

The majority of our investment portfolio is composed of debt and equity securities with unique contract terms and conditions and/or complexity that requires a valuation of each individual investment that considers multiple levels of market and asset specific inputs, including historical and forecasted financial and operational performance of the individual investment, projected cash flows, market multiples, comparable market transactions, the priority of the security compared with those of other securities for such issuers, credit risk, interest rates and independent valuations and reviews.

Loans and Debt Securities.

To the extent that our investments are exchange traded and are priced or have sufficient price indications from normal course trading at or around the valuation date (financial reporting date), such pricing will determine fair value. Pricing service marks from third party pricing services may be used as an indication of fair value, depending on the volume and reliability of the marks, sufficient and reasonable correlation of bid and ask quotes, and, most importantly, the level of actual trading activity. However, most of our investments are illiquid investments with little or no trading activity. Further, we have been unable to identify directly comparable market indices or other market guidance that correlate directly to the types of investments we own. As a result, for most of our assets, we determine fair value using alternative methodologies and models using available market data, as adjusted, to reflect the types of assets we own, their structure, qualitative and credit attributes and other asset specific characteristics.

We derive fair value for our illiquid investments that do not have indicative fair values based upon active trades primarily by using the Market Yield Approach and also consider recent loan amendments or other activity specific to the subject asset. Discount rates applied to estimated contractual cash flows for an underlying asset vary by specific investment, industry, priority and nature of the debt security (such as the seniority or security interest of the debt security) and are assessed relative to two indices, a leveraged loan index and a high-yield bond index, at the valuation date. We have identified these two indices as benchmarks for broad market information related to our loan and debt investments. Because we have not identified any market index that directly correlates to the loan and debt investments held by us and therefore use the two benchmark indices, these market indices may require significant adjustment to better correlate such market data for the calculation of fair value of the investment under the Market Yield Approach. Such adjustments require judgment and may be material to the calculation of fair value. Further adjustments to the discount rate may be applied to reflect other market conditions or the perceived credit risk of the borrower. When broad market indices are used as part of the valuation methodology, their use is subject to adjustment for many factors, including priority, collateral used as security, structure, performance and other quantitative and qualitative attributes of the asset being valued. The resulting present value determination is then weighted along with any quotes from observable transactions and broker/pricing quotes. If such quotes are indicative of actual transactions with reasonable trading volume at or near the valuation date that are not liquidation or distressed sales, relatively more reliance will be put on such quotes to determine fair value. If such quotes are not indicative of market transactions or are insufficient as to volume, reliability, consistency or other relevant factors, such quotes will be compared with other fair value indications and given relatively less weight based on their relevancy.

Equity and Equity-Related Securities.

Our equity and equity-related securities in portfolio companies for which there is no liquid public market are carried at fair value based on the enterprise value of the portfolio company, which is determined using various factors, including EBITDA, cash flows from operations less capital expenditures and other pertinent factors, such as recent offers to purchase a portfolio company's securities or other liquidation events. The determined fair values are generally discounted to account for restrictions on resale and minority ownership positions. The values of our equity and equity-related securities in public companies for which market quotations are readily available are based upon the closing public market price on the balance sheet date. Securities that carry certain restrictions on sale are typically valued at a discount from the public market value of the security.

The significant inputs used to determine the fair value of equity and equity-related securities include prices, earnings, EBITDA and cash flows after capital expenditures for similar peer comparables and the investment entity itself. Equity and equity-related securities are classified as Level III when there is limited activity or less transparency around inputs to the valuation given the lack of information related to such equity investments held in nonpublic companies. Significant assumptions observed for comparable companies as applied to relevant financial data for the specific investment. Such assumptions, such as model discount rates or price/earnings multiples, vary by the specific investment, equity position and industry and incorporate adjustments for risk premiums, liquidity and company specific attributes. Such adjustments require judgment and may be material to the calculation of fair value.

At December 31, 2010 and December 31, 2009, our investments in income producing loans and debt securities, excluding CLO Fund securities, had a weighted average interest rate of approximately 8.6% and 6.5%, respectively.

The investment portfolio (excluding the Company’s investment in asset manager affiliates and CLO Funds) at December 31, 2010 was spread across 16 different industries and 24 different entities with an average balance per entity of approximately $3 million. As of December 31, 2010, all but five of our portfolio companies were current on their debt service obligations. Our portfolio, including the CLO Funds in which we invest, and the CLO Funds managed by Katonah Debt Advisors consist almost exclusively of credit instruments issued by corporations and do not include investments in asset-backed securities, such as those secured by commercial mortgages, residential mortgages or other consumer borrowings.

We may invest up to 30% of our investment portfolio in opportunistic investments in high-yield bonds, debt and equity securities of CLO Funds, distressed debt or equity securities of public companies. However, our investment strategy is to limit the value of our investments in the debt or equity securities issued by CLO Funds to not more than 15% of the value of our total investment portfolio at the time of investment. We expect that these public companies generally will have debt that is non-investment grade. We also may invest in debt of middle market companies located outside of the United States, which investments are generally not anticipated to be in excess of 10% of our investment portfolio at the time such investments are made. At December 31, 2010, approximately 29% of our investments were foreign assets (including our investments in CLO Funds, which are typically domiciled outside the U.S. and represent approximately 28% of our portfolio). We are generally prohibited from buying or selling any security from or to any portfolio company of a private equity fund managed by Kohlberg & Co. without the prior approval of the SEC. However, we may co-invest on a concurrent basis with Kohlberg & Co. or any of our affiliates, subject to compliance with existing regulatory guidance, applicable regulations and our allocation procedures. Certain types of negotiated co-investments may be made only if we receive an order from the SEC permitting us to do so. There can be no assurance that any such order will be applied for or, if applied for, obtained.

At December 31, 2010, our ten largest portfolio companies represented approximately 65% of the total fair value of our investments. Our largest investment, Katonah Debt Advisors which is our wholly-owned portfolio company, represented 22% of the total fair value of our investments. Excluding Katonah Debt Advisors and CLO Fund securities, our ten largest portfolio companies represent approximately 30% of the total fair value of our investments.

As of December 31, 2010, our investments in income producing loans and debt securities had an annual weighted average interest rate of approximately 8.6%.

TABLE OF CONTENTS

The characteristics of our investment securities at fair value, excluding CLO equity securities are presented in the following table as of each quarter end from March 31, 2009 through December 31, 2010.

	4Q10		3Q10		2Q10		1Q10	
Security Type ($ in millions)	**$**	**%**	**$**	**%**	**$**	**%**	**$**	**%**
First Lien	$ 22.0	23%	$ 95.7	49%	$123.3	53%	$143.3	51%
Second Lien/Mezzanine/Bond	68.7	72	94.9	48	103.1	44	132.8	47
Equity	4.4	5	5.7	3	6.2	3	5.6	2
Preferred	0.6	1	0.6	—	0.7	—	0.7	—
Total	$ 95.7	100%	$196.9	100%	$233.4	100%	$282.4	100%

	4Q09		3Q09		2Q09		1Q09	
Security Type ($ in millions)	**$**	**%**	**$**	**%**	**$**	**%**	**$**	**%**
First Lien	$159.1	53%	$166.6	51%	$170.8	52%	$181.3	54%
Second Lien/Mezzanine/Bond	138.3	46	156.8	48	155.6	47	151.4	45
Equity	4.7	1	4.5	1	4.7	1	4.8	1
Total	$302.1	100%	$327.9	100%	$331.1	100%	$337.5	100%

The industry concentrations, based on the fair value of the Company's investment portfolio as of December 31, 2010 and December 31, 2009, were as follows:

	December 31, 2010			December 31, 2009		
Industry Classification	**Cost**	**Fair Value**	**%[1]**	**Cost**	**Fair Value**	**%[1]**
Aerospace and Defense	$ 6,499,518	$ 5,613,844	3%	$ 33,652,058	$ 33,416,670	8%
Asset Management Companies[2]	44,532,329	41,493,000	22	40,751,511	58,064,720	14
Automobile	—	—	—	1,940,876	1,800,631	—
Broadcasting and Entertainment	—	—	—	2,986,206	2,862,000	1
Buildings and Real Estate[3]	32,845,509	6,923,963	3	36,498,537	9,840,946	2
Cargo Transport	4,940,182	4,940,182	3	13,389,865	13,359,403	3
Chemicals, Plastics and Rubber	—	—	—	3,970,688	4,000,000	1
CLO Fund Securities	68,280,200	53,031,000	28	68,195,049	48,971,000	12
Containers, Packaging and Glass	3,009,682	3,000,000	2	7,056,701	6,852,738	2
Diversified/Conglomerate Manufacturing	—	—	—	4,046,728	4,042,346	1
Diversified/Conglomerate Service	10,384,036	8,345,287	3	15,382,035	14,350,438	4
Ecological	—	—	—	2,695,103	2,699,907	1
Electronics	3,006,137	3,176,250	2	14,874,472	14,407,265	4
Farming and Agriculture	—	—	—	1,441,277	217,001	—
Finance	—	—	—	5,460,445	5,372,881	1
Healthcare, Education and Childcare	15,113,551	15,037,936	8	41,647,084	42,177,498	10
Home and Office Furnishings, Housewares, and Durable Consumer Goods	9,654,903	8,804,450	5	20,694,006	18,080,134	4
Hotels, Motels, Inns and Gaming	—	—	—	3,438,128	3,171,363	1
Insurance	4,890,322	4,049,000	2	4,861,123	4,490,000	1
Leisure, Amusement, Motion Pictures, Entertainment	2,114,458	1,983,619	1	14,572,761	14,227,907	3
Machinery (Non-Agriculture, Non-Construction, Non-Electronic)	3,477,696	3,864,600	2	33,015,472	31,956,312	8
Mining, Steel, Iron and Non-Precious Metals	14,381,863	14,430,312	8	13,861,498	13,021,854	3
Oil and Gas	—	—	—	5,998,652	6,000,000	1
Personal and Non Durable Consumer Products (Mfg. Only)	5,000,000	3,435,000	2	14,424,931	9,146,146	2
Personal, Food and Miscellaneous Services	14,730,350	4,090,000	2	14,759,522	4,559,444	1
Printing and Publishing	5,980,529	5,669,716	3	23,867,184	23,506,057	6
Retail Stores	—	—	—	3,543,046	3,521,787	1
Time Deposits and Money Market Account	930,537	930,537	—	126	126	—
Utilities	4,000,000	2,367,600	1	16,343,228	14,989,047	5
Total	$253,771,802	$191,186,296	100%	$463,368,312	$409,105,621	100%

(1) Calculated as a percentage of total portfolio at fair value.

(2) Represents Katonah Debt Advisors and other asset manager affiliates.

(3) Buildings and real estate relate to real estate ownership, builders, managers and developers and excludes mortgage debt investments and mortgage lenders or originators. As of December 31, 2010 and December 31, 2009, the Company had no exposure to mortgage securities (residential mortgage bonds, commercial mortgage backed securities, or related asset backed securities) or companies providing mortgage lending.

CLO Fund Securities

We typically make a minority investment in the subordinated securities or preferred stock of CLO Funds raised and managed by Katonah Debt Advisors and may selectively invest in securities issued by CLO Funds managed by other asset management companies. As of December 31, 2010, we had approximately $53 million invested in CLO Fund securities, including those issued by funds managed by Katonah Debt Advisors.

The CLO Funds managed by Katonah Debt Advisors invest primarily in broadly syndicated non-investment grade loans, high-yield bonds and other credit instruments of corporate issuers. The underlying assets in each of the CLO Funds in which we have an investment are generally diversified secured or unsecured corporate debt. The underlying assets in our CLO Funds exclude mortgage pools or mortgage securities (residential mortgage bonds, commercial mortgage backed securities, or related asset-backed securities), debt to companies providing mortgage lending and emerging markets investments.

Our CLO Fund investments as of December 31, 2010 and December 31, 2009 are as follows:

			December 31, 2010		December 31, 2009	
CLO Fund Securities	**Investment**	**%[1]**	**Cost**	**Fair Value**	**Cost**	**Fair Value**
Grant Grove CLO, Ltd.	Subordinated Securities	22.2%	$ 4,720,982	$ 3,150,000	$ 4,715,858	$ 2,780,000
Katonah III, Ltd.	Preferred Shares	23.1	4,500,000	470,000	4,500,000	950,000
Katonah IV, Ltd.	Preferred Shares	17.1	3,150,000	1,300,000	3,150,000	290,000
Katonah V, Ltd.[3]	Preferred Shares	26.7	3,320,000	1,000	3,320,000	1,000
Katonah VII CLO Ltd.[2]	Subordinated Securities	16.4	4,500,000	2,090,000	4,500,000	1,840,000
Katonah VIII CLO Ltd.[2]	Subordinated Securities	10.3	3,400,000	1,690,000	3,400,000	1,760,000
Katonah IX CLO Ltd.[2]	Preferred Shares	6.9	2,000,000	1,300,000	2,000,000	1,560,000
Katonah X CLO Ltd.[2]	Subordinated Securities	33.3	11,612,677	8,820,000	11,589,830	8,280,000
Katonah 2007-1 CLO Ltd.[2]	Preferred Shares	100	29,987,959	26,200,000	29,940,867	27,100,000
Katonah 2007-1 CLO Ltd.[2]	Class B-2L Notes	100	1,088,582	8,010,000	1,078,494	4,410,000
Total			$68,280,200	$53,031,000	$68,195,049	$48,971,000

(1) Represents percentage of class held.

(2) An affiliate CLO Fund managed by Katonah Debt Advisors.

(3) As of December 31, 2010, this CLO Fund Security was not providing a dividend distribution.

Our investments in CLO Fund securities are carried at fair value, which is based either on (i) the present value of the net expected cash inflows for interest income and principal repayments from underlying assets and cash outflows for interest expense, debt paydown and other fund costs for the CLO Funds that are approaching or past the end of their reinvestment period and therefore are selling assets and/or using principal repayments to pay down CLO Fund debt (or will begin to do so shortly), and for which there continue to be net cash distributions to the class of securities owned by us, or (ii) a discounted cash flow model for more recent CLO Funds that utilizes prepayment and loss assumptions based on historical experience and projected performance, economic factors, the characteristics of the underlying cash flow and comparable yields for similar securities or preferred shares to those in which we have invested. We recognize unrealized appreciation or depreciation on our investments in CLO Fund securities as comparable yields in the market change and/or based on changes in NAVs or estimated cash flows resulting from changes in prepayment or loss assumptions in the underlying collateral pool. As each investment in CLO Fund securities ages, the expected amount of losses and the expected timing of recognition of such losses in the underlying collateral pool are updated and the revised cash flows are used in determining the fair value of the CLO Fund investments. We determine the fair value of our investments in CLO Fund securities on an individual security-by-security basis.

Due to the individual attributes of each CLO Fund security, they are classified as a Level III (as described in "— Critical Accounting Policies — Valuation of Portfolio Investments" below) investment unless specific trading activity can be identified at or near the valuation date. When available, Level II (as described in "— Critical Accounting Policies — Valuation of Portfolio Investments" below) market information will be identified, evaluated and weighted accordingly in the application of such data to the present value models and fair value determination. Significant assumptions to the present value calculations include default rates, recovery rates, prepayment rates, investment/reinvestment rates and spreads and the discount rate by which to value the resulting underlying cash flows. Such assumptions can vary significantly, depending on market data sources which often vary in depth and level of analysis, understanding of the CLO market, detailed or broad characterizations of the CLO market and the application of such data to an appropriate framework for analysis. The application of data points are based on the specific attributes of each individual CLO Fund security's underlying assets, historic, current and prospective performance, vintage, and other quantitative and qualitative factors that would be evaluated by market participants. We evaluate the source of market data for reliability as an indicative market input, consistency amongst other inputs and results and also the context in which such data is presented.

For bond rated tranches of CLO Fund securities (those above the junior class) without transactions to support a fair value for the specific CLO Fund and tranche, fair value is based on discounting estimated bond payments at current market yields, which may reflect the adjusted yield on the leveraged loan index for similarly rated tranches, as well as prices for similar tranches for other CLO Funds, and also considers other factors such as the default and recovery rates of underlying assets in the CLO Fund, as may be applicable. Such model assumptions may vary and incorporate adjustments for risk premiums and CLO Fund specific attributes. Such adjustments require judgment and may be material to the calculation of fair value.

The table below summarizes certain attributes of each CLO Fund as per their most recent trustee reports as of December 31, 2010:

CLO Fund Securities(1)	Number of Securities	Number of Issuers	Number of Industries	Average Security Position Size	Average Issuer Position Size
Grant Grove CLO, Ltd.	425	203	32	$ 660,903	$ 1,383,665
Katonah III, Ltd.	216	126	29	1,518,819	2,603,690
Katonah IV, Ltd.	184	120	25	883,807	1,355,170
Katonah V, Ltd.	231	140	29	474,946	783,660
Katonah VII CLO Ltd.	249	189	33	1,270,893	1,674,351
Katonah VIII CLO Ltd	263	196	33	1,350,822	1,812,582
Katonah IX CLO Ltd	269	204	32	1,469,049	1,937,128
Katonah X CLO Ltd	272	207	32	1,700,368	2,234,300
Katonah 2007-1 CLO Ltd	234	183	30	1,250,000	1,598,361

(1) All data from most recent trustee reports as of December 31, 2010

Katonah Debt Advisors

Katonah Debt Advisors is our wholly-owned asset management company that manages CLO Funds that invest in broadly syndicated loans, high yield bonds and other credit instruments. The CLO Funds managed by Katonah Debt Advisors consist exclusively of credit instruments issued by corporations and do not invest in asset-backed securities secured by commercial mortgages, residential mortgages or other consumer borrowings. As of December 31, 2010, Katonah Debt Advisors had approximately $2.1 billion of par value of assets under management on which it earns management fees, and was valued at approximately $42 million.

As a manager of the CLO Funds, Katonah Debt Advisors receives contractual and recurring management fees as well as an expected one-time structuring fee from the CLO Funds for its management and advisory services. In addition, Katonah Debt Advisors may also earn income related to net interest on assets accumulated for future CLO issuances on which it has provided a first loss guaranty in connection with loan warehouse arrangements for its CLO Funds. Katonah Debt Advisors generates annual operating income equal to the amount by which its fee income exceeds its operating expenses.

The annual management fees which Katonah Debt Advisors receives are generally based on a fixed percentage of the par value of assets under management and are recurring in nature for the term of the CLO Fund so long as Katonah Debt Advisors manages the fund. As a result, the annual management fees earned by Katonah Debt Advisors are not subject to market value fluctuations in the underlying collateral. The annual management fees Katonah Debt Advisors receives have two components — a senior management fee and a subordinated management fee. During 2009, certain CLO funds managed by Katonah Debt Advisors were restricted from currently paying their subordinated management fees as a result of the failure by those CLO Funds to satisfy certain restrictive covenants contained in their indenture agreements. At such time, those subordinated management fees continued to be accrued by the applicable CLO Fund to become payable to Katonah Debt Advisors when such CLO Fund becomes compliant with the applicable covenants. During the year ended December 31, 2010, all those CLO Funds which deferred payment of their subordinated management fees regained compliance with all applicable covenants in order to pay current subordinated management fees as well as all of their previously accrued subordinated management fees. During the year ended December 31, 2010, approximately $5 million of deferred subordinated management fees have been paid. Currently, all CLO Funds managed by Katonah Debt Advisors are paying both their senior and subordinated management fees on a current basis.

In future years, Katonah Debt Advisors may receive accrued incentive fees upon the liquidation of CLO Funds it manages, provided such CLO Funds have achieved a minimum investment return to holders of their subordinated securities or preferred shares.

Subject to market conditions, we expect to continue to make investments in CLO Funds managed by Katonah Debt Advisors, which we believe will provide us with a current cash investment return. We believe that these investments will provide Katonah Debt Advisors with greater opportunities to access new sources of capital which will ultimately increase Katonah Debt Advisors' assets under management and resulting management fee income. We also expect to receive distributions of recurring fee income and, if debt markets stabilize and recover, to generate capital appreciation from our investment in the asset management business of Katonah Debt Advisors.

The revenue that Katonah Debt Advisors generates through the fees it receives for managing CLO Funds and after paying the expenses pursuant to an overhead allocation agreement with the Company associated with its operations, including compensation of its employees, may be distributed to Kohlberg Capital. Cash distributions of Katonah Debt Advisors' net income are recorded as dividends from an affiliate asset manager when declared. As with all other investments, Katonah Debt Advisors' fair value is periodically determined. Our investment in Katonah Debt Advisors is carried at fair value, which is determined after taking into consideration a percentage of assets under management and a discounted cash flow model incorporating different levels of discount rates depending on the hierarchy of fees earned (including the likelihood of realization of senior, subordinate and incentive fees) and prospective modeled performance. Such valuation includes an analysis of comparable asset management companies. Katonah Debt Advisors is classified as a Level III investment. Any change in value from period to period is recognized as net change in unrealized appreciation or depreciation.

Time Deposits and Money Market Accounts

Cash time deposits primarily represent overnight Eurodollar investments of cash held in non-demand deposit accounts. Such time deposits were partially restricted under terms of the facility, and may be restructured under any borrowing facilities we enter into in the future. The money market account is restricted cash held for employee flexible spending accounts.

INVESTMENTS AND OPERATIONS

Overview

We originate, structure and invest in senior secured term loans, mezzanine debt and selected equity securities primarily in privately-held middle market companies. In addition to our middle market investment business, our wholly-owned portfolio company, Katonah Debt Advisors, manages CLO Funds, in which we also may make an investment, that invest in broadly syndicated loans, high-yield bonds and other corporate credit instruments.

Our investment objective is to generate current income and capital appreciation from our investments. In the current economic environment, capital appreciation is difficult to achieve due to real or perceived credit concerns, illiquidity in the market and the resulting impact on fair values. However, we believe our longer-term investment horizon and quality of assets will allow us to generate current income and capital appreciation on discounted assets as they amortize and repay at par.

As of December 31, 2010, we had total secured term loan, mezzanine debt, bond and equity investments of approximately $96 million, total investments in CLO Fund securities managed by our wholly-owned portfolio company Katonah Debt Advisors and three other asset managers of approximately $53 million, and total investment in 100% of Katonah Debt Advisors' asset management company of approximately $42 million.

As of December 31, 2010, we had a portfolio of investment securities that included first and second lien secured loans. Our investments generally averaged between $1 million to $10 million, although particular investments may be larger or smaller. The size of individual investments will vary according to their priority in a company's capital structure, with larger investments in more secure positions in an effort to maximize capital preservation. We expect that the size of our investments and maturity dates will vary as follows:

- senior secured term loans from $10 to $20 million maturing in five to seven years;
- second lien term loans from $5 to $20 million maturing in six to eight years;
- senior unsecured loans $5 to $10 million maturing in six to eight years;
- mezzanine loans from $5 to $10 million maturing in seven to ten years; and
- equity investments from $1 to $5 million.

When we extend senior secured term loans, we will generally take a security interest in the available assets of the portfolio company, including the equity interests of their subsidiaries, which we expect to help mitigate the risk that we will not be repaid. Nonetheless, there is a possibility that our lien could be subordinated to claims of other creditors. Structurally, mezzanine debt ranks subordinate in priority of payment to senior term loans and is often unsecured. Relative to equity, mezzanine debt ranks senior to common and preferred equity in a borrower's capital structure. Typically, mezzanine debt has elements of both debt and equity instruments, offering the fixed returns in the form of interest payments associated with a loan, while providing an opportunity to participate in the capital appreciation of a borrower, if any, through an equity interest that is typically in the form of equity purchased at the time the mezzanine loan is repaid or warrants to purchase equity at a future date at a fixed cost. Mezzanine debt generally earns a higher return than senior secured debt due to its higher risk profile and usually less restrictive covenants. The warrants associated with mezzanine debt are typically detachable, which allows lenders to receive repayment of their principal on an agreed amortization schedule while retaining their equity interest in the borrower. Mezzanine debt also may include a "put" feature, which permits the holder to sell its equity interest back to the borrower at a price determined through an agreed formula.

Investment Objective

Our investment objective is to generate current income and capital appreciation from the investments made by our middle market business in senior secured term loans, mezzanine debt and selected equity investments in privately-held middle market companies, and from our investment in Katonah Debt Advisors. Subject to prevailing market conditions, we intend to grow our portfolio of assets by raising additional capital, including through the prudent use of leverage available to us. We will primarily invest in first and second lien term loans which, because of their priority in a company's capital structure, we expect will have lower default rates and higher rates of recovery of principal if there is a default and which we expect will create a stable stream of interest income. While our primary investment focus is on making loans to, and selected equity investments in, privately-held middle market companies, we may also invest in other investments such as loans to larger, publicly-traded companies, high-yield bonds and distressed debt securities. We may also receive warrants or options to purchase common stock in connection with our debt investments. In addition, we may also invest in debt and equity securities issued by CLO Funds managed by Katonah Debt Advisors or by other asset managers. However, our investment strategy is to limit the value of our investments in the debt or equity securities issued by CLO Funds to not more than 15% of the value of our total investment portfolio. We invest almost exclusively in credit instruments issued by corporations and do not invest in asset-backed securities such as those secured by commercial or residential mortgages or other consumer borrowings.

Credit and Investment Process

We employ the same due diligence intensive investment strategy that our senior management team, Katonah Debt Advisors and Kohlberg & Co. have used over the past 22 years. Due to our ability to source transactions through multiple channels, we expect to maintain a substantial pipeline of opportunities to allow comparative risk return analysis and selectivity. By focusing on the drivers of revenue and cash flow, we develop our own underwriting cases, and multiple stress and event specific case scenarios for each company analyzed.

We focus on lending and investing opportunities in:

- companies with EBITDA of $10 to $50 million;
- companies with financing needs of $25 to $150 million;
- companies purchased by top tier equity sponsors;
- non-sponsored companies with successful management and systems;
- high-yield bonds and broadly syndicated loans to larger companies on a selective basis; and
- equity co-investment in companies where we see substantial opportunity for capital appreciation.

We expect to source investment opportunities from:

- private equity sponsors;
- regional investment banks for non-sponsored companies;
- other middle market lenders with whom we can “club” loans;
- Katonah Debt Advisors with regard to high-yield bonds and syndicated loans; and
- Kohlberg & Co. with regard to selected private equity investment opportunities.

In our experience, good credit judgment is based on a thorough understanding of both the qualitative and quantitative factors which determine a company’s performance. Our analysis begins with an understanding of the fundamentals of the industry in which a company operates, including the current economic environment and the outlook for the industry. We also focus on the company’s relative position within the industry and its historical ability to weather economic cycles. Other key qualitative factors include the experience and depth of the management team and the financial sponsor, if any.

Only after we have a comprehensive understanding of the qualitative factors do we focus on quantitative metrics. We believe that with the context provided by the qualitative analysis, we can gain a better understanding of a company’s financial performance. We analyze a potential portfolio company’s sales growth and margins in the context of its competition as well as its ability to manage its working capital requirements and its ability to generate consistent cash flow. Based upon this historical analysis, we develop a set of projections which represents a reasonable underwriting case of most likely outcomes for the company over the period of our investment. Using our Maximum Reasonable Adversity model, we also look at a variety of potential downside cases to determine a company’s ability to service its debt in a stressed credit environment.

Elements of the *qualitative analysis* we use in evaluating investment opportunities include the following:

- Industry fundamentals;
- Competitive position and market share;
- Past ability to work through historical down-cycles;
- Quality of financial and technology infrastructure;
- Sourcing risks and opportunities;
- Labor and union strategy;

- Technology risk;
- Diversity of customer base and product lines;
- Quality and experience of management;
- Quality of financial sponsor (if applicable); and
- Acquisition and integration history.

Elements of the *quantitative analysis* we use in evaluating investment opportunities include the following:

- Income statement analysis of growth and margin trends;
- Balance sheet analysis of working capital efficiency;
- Cash flow analysis of capital expenditures and free cash flow;
- Financial ratio and market share standing among comparable companies;
- Financial projections: underwriting versus stress case;
- Event specific Maximum Reasonable Adversity credit modeling;
- Future capital expenditure needs and asset sale plans;
- Downside protection to limit losses in an event of default;
- Risk adjusted returns and relative value analysis; and
- Enterprise and asset valuations.

The origination, structuring and credit approval processes are fully integrated. Our credit team is directly involved in all due diligence and analysis prior to the formal credit approval process.

Credit Monitoring

Our management team has significant experience monitoring portfolios of middle market investments and this is enhanced by the credit monitoring procedures of Katonah Debt Advisors. Along with origination and credit analysis, portfolio management is one of the key elements of our business. Most of our investments will not be liquid and, therefore, we must prepare to act quickly if potential issues arise so that we can work closely with management and the private equity sponsor, if applicable, of the portfolio company to take any necessary remedial action quickly. In addition, most of our senior management team, including the credit team at Katonah Debt Advisors, have substantial workout and restructuring experience.

In order to assist us in detecting issues with portfolio companies as early as possible, we perform a monthly financial analysis of each portfolio company. This analysis typically includes:

- reviewing financial statements with comparisons to prior year financial statements, as well as the current budget including key financial ratios such as debt/EBITDA, margins and fixed charge coverage;
- independently computing and verifying compliance with financial covenants;
- reviewing and analyzing monthly borrowing base, if any;
- a monthly discussion of MD&A with management and the private equity sponsor, if applicable;
- determining if current performance could cause future financial covenant default;
- discussing prospects with the private equity sponsor, if applicable;
- determining if a portfolio company should be added to our “watch list” (companies to be reviewed in more depth);
- if a company is not meeting expectations, reviewing original underwriting assumptions and determining if either enterprise value or asset value has deteriorated enough to warrant further action; and
- a monthly update to be reviewed by both our Chief Executive Officer and Chief Investment Officer.

Investment Securities

We invest in senior secured loans and mezzanine debt and, to a lesser extent equity capital, of middle market companies in a variety of industries. We generally target companies that generate positive cash flows because we look to cash flows as the primary source for servicing debt. As of December 31, 2010, together with our wholly-owned portfolio company Katonah Debt Advisors, we had a staff of 18 investment professionals who specialize in specific industries and generally seek to invest in companies about which we have direct expertise. However, we may invest in other industries if we are presented with attractive opportunities. For more information regarding our investment securities, see "— Investment Securities," above.

CLO Fund Securities

As of December 31, 2010, we had $53 million at fair value, invested in CLO Fund securities, including those issued by funds managed by Katonah Debt Advisors. CLO Funds managed by Katonah Debt Advisors invest primarily in broadly syndicated non-investment grade loans, high-yield bonds and other credit instruments of corporate issuers. The underlying assets in each of the CLO Funds in which we have investments are generally diversified secured or unsecured corporate debt and exclude mortgage pools or mortgage securities (residential mortgage bonds, commercial mortgage backed securities, or related asset-backed securities), debt to companies providing mortgage lending and emerging markets investments.

The CLO Funds are leveraged funds and any excess cash flow or "excess spread" (interest earned by the underlying securities in the fund less payments made to senior bond holders and less fund expenses and management fees) is paid to us and the other holders of the CLO Fund's subordinated securities or preferred shares based on the proportionate share of such class.

The securities issued by CLO Funds managed by Katonah Debt Advisors are primarily held by third parties. As of December 31, 2010, we had $48 million invested at fair value in five Katonah Debt Advisors managed CLO Funds. We typically make a minority investment in the subordinated securities or preferred shares of CLO Funds raised and managed by Katonah Debt Advisors and may selectively invest in securities issued by CLO Funds managed by other asset management companies. For more information regarding our investment securities, see "— Investment Portfolio — Investment in CLO Fund Securities."

Katonah Debt Advisors

Katonah Debt Advisors is our wholly-owned asset management company that manages CLO Funds that invest in broadly syndicated loans, high yield bonds and other credit instruments. The CLO Funds managed by Katonah Debt Advisors consist exclusively of credit instruments issued by corporations and do not invest in asset-backed securities secured by commercial mortgages, residential mortgages or other consumer borrowings. As of December 31, 2010, Katonah Debt Advisors had approximately $2.1 billion of assets under management, and was valued at approximately $42 million.

As a manager of the CLO Funds, Katonah Debt Advisors receives contractual and recurring management fees as well as a one-time structuring fee from the CLO Funds for its management and advisory services. The annual management fees which Katonah Debt Advisors receives are generally based on a fixed percentage of the par value of assets under management and are recurring in nature for the term of the CLO Fund so long as Katonah Debt Advisors manages the fund. As a result, the annual management fees earned by Katonah Debt Advisors are not subject to market value fluctuations in the underlying collateral. Katonah Debt Advisors generates annual operating income equal to the amount by which its fee income exceeds it operating expenses.

The revenue that Katonah Debt Advisors generates through the fees it receives for managing CLO Funds and after paying the expenses associated with its operations, including compensation of its employees, may be distributed to Kohlberg Capital Corporation. Cash distributions of Katonah Debt Advisors' net income are recorded as dividends from affiliate asset manager when declared. As with all other investments, Katonah Debt Advisors' fair value is periodically determined. Any change in value from period to period is recognized as unrealized gain or loss.

As a separately taxable corporation, Katonah Debt Advisors is taxed at normal corporate rates. For tax purposes, any distributions of taxable net income earned by Katonah Debt Advisors to us would generally need to be distributed to our stockholders. Katonah Debt Advisors' taxable net income differs from GAAP net income due to both deferred tax timing adjustments and permanent tax adjustments. Deferred tax timing adjustments may include differences for the recognition and timing of depreciation, bonuses to employees, stock option expense, and interest rate caps. Permanent differences may include adjustments, limitations or disallowances for meals and entertainment expenses, penalties and tax goodwill amortization.

Goodwill amortizable for tax was created upon the purchase of 100% of the equity interests in Katonah Debt Advisors prior to our initial public offering in exchange for shares of our stock valued at $33 million. Although this transaction was a stock transaction rather than an asset purchase and thus no goodwill was recognized for GAAP purposes, such exchange was considered a taxable asset purchase under the Internal Revenue Code of 1986, as amended ("Code"). At the time of the transfer, Katonah Debt Advisors had equity of approximately $1 million resulting in tax goodwill of approximately $32 million which will be amortized for tax purposes on a straight-line basis over 15 years, resulting in an annual difference between GAAP income and taxable income of approximately $2 million per year over such period.

On February 4, 2011, Katonah Debt Advisors entered to an Asset Purchase Agreement with a third-party buyer controlled by a former Katonah Debt Advisors employee to sell substantially all of the Katonah Scott's Cove Management LLC assets for a purchase price of $25,000. The transaction closed on February 28, 2011. At closing, Katonah Debt Advisors and the buyer entered into a Services Agreement, pursuant to which the buyer paid to Katonah Debt Advisors $225,000 for certain transitional services to be provided by Katonah Debt Advisors (including access to office space, secretarial services and information technology support) and agreed to pay an additional amount of $75,000 on each of the first and second anniversaries of the closing date (subject to, in the case of the first payment, deferment for up to one year under certain circumstances). Katonah Debt Advisors' obligation to provide transitional services under the Services Agreement will continue through June 30, 2011, unless the agreement is earlier terminated by the buyer in accordance with its terms. At closing, Katonah Debt Advisors and the employees that formerly managed the Katonah Scott's Cove Management LLC assets also entered into employee termination agreements, whereby they agreed to terminate their employment with Katonah Debt Advisors and to relinquish all claims against Katonah Debt Advisors or its affiliates. At December 31, 2010, Katonah Scott's Cove Management LLC had approximately $161 million of assets under management.

Revenues

We generate revenue in the form of interest income on debt securities and capital gains, if any, on warrants or other equity-related securities that we acquire from our portfolio companies. In addition, we generate revenue in the form of commitment and facility fees and, to a lesser extent, due diligence fees. Any such fees are generated in connection with our investments and recognized as earned or, in some cases, recognized over the life of the loan. We expect our investments generally to have a term of between five and eight years and bear interest at various rates ranging from 2% to 10% over the prevailing market rates for Treasury securities. Where applicable, we seek to collateralize our investments by obtaining security interests in our portfolio companies' assets. Interest on debt securities will generally be payable monthly or quarterly, with amortization of principal typically occurring over the term of the security. In those limited instances where we choose to defer amortization of the loan for a period of time from the date of the initial investment, the principal amount of the debt securities and any accrued but unpaid interest will generally become due at the maturity date.

We also generate dividend income from our investment in CLO equities. These subordinated securities are the most junior class of securities issued by the CLO Funds and are subordinated in priority of payment to each other class of securities issued by these CLO Funds. Dividends on CLO equities are generally paid quarterly.

Expenses

Because we are an internally managed BDC, we pay the costs associated with employing investment management professionals and other employees as well as running our operations. Our primary non-interest expenses include employee salaries and benefits, the costs of identifying, evaluating, negotiating, closing, monitoring and servicing our investments and our related overhead charges and expenses, including rental expense and interest expense incurred in connection with borrowings. Because we are internally managed, we do not pay any management fees to any third party.

Our Strategic Relationship with Kohlberg & Co.

We believe that we derive substantial benefits from our strategic relationship with Kohlberg & Co. The managing partners of Kohlberg & Co. are members of our Board of Directors, and are also members of our Investment Committee. Through such participation, we have access to the expertise of these individuals in middle market and leveraged investing, which we believe enhances our capital raising, due diligence, investment selection and credit analysis activities. Affiliates of Kohlberg & Co., including those who serve and have served on our Board of Directors and on our Investment Committee, own, in the aggregate, approximately 15% of our outstanding common stock. Kohlberg & Co. is a leading U.S. private equity firm which manages investment funds that acquire middle market companies.

Because we are an internally managed BDC, we do not pay any fees to Kohlberg & Co. or any of its affiliates. Under the 1940 Act, we are generally prohibited from buying or selling any security from or to any portfolio company of a private equity fund managed by Kohlberg & Co. without the prior approval of the SEC. In addition, we may co-invest on a concurrent basis with Kohlberg & Co. or any of our affiliates, subject to compliance with existing regulatory guidance, applicable regulations and our allocation procedures. Certain types of negotiated co-investments may be made only if we receive an order from the SEC permitting us to do so. There can be no assurance that any such order will be obtained.

LEVERAGE

We use borrowed funds, known as “leverage,” to make investments and to attempt to increase returns to our stockholders by reducing our overall cost of capital. As a BDC, we are limited in the amount of leverage we can incur under the 1940 Act. We are only allowed to borrow amounts such that our asset coverage, as defined in the 1940 Act, equals at least 200% after such borrowing. As of December 31, 2010, we had approximately $87 million of outstanding borrowings and our asset coverage ratio of total assets to total borrowings was 315%, compliant with the minimum asset coverage level of 200% generally required for a BDC by the 1940 Act. We may also borrow amounts of up to 5% of the value of our total assets for temporary purposes. As of January 31, 2011, we had repaid in full the outstanding balance of our borrowings and we are currently operating fully unlevered.

Prior to the payoff of our outstanding indebtedness on January 31, 2011, our borrowings were through a secured financing facility (the “Facility”). In connection with the Facility, we were party to a Loan Funding and Servicing Agreement, dated as of February 14, 2007 (as amended, the “LFSA”), by and among us, as the servicer, our wholly-owned, special-purpose bankruptcy remote subsidiary, Kohlberg Capital Funding LLC I, as the borrower, BMO Capital Markets Corp, as the agent (the “Agent”), U.S. Bank National Association, a national banking association, as the trustee (the “Trustee”) and the other Lender Parties and other parties thereto (the “Lender Parties”). As previously reported, the LFSA was modified on September 20, 2010 pursuant to a Forbearance and Settlement Agreement (the “Settlement Agreement”) with the Agent and Lender Parties, pursuant to which we and the Agent and the Lender Parties agreed to settle all outstanding claims thereunder and in connection with litigation previously initiated by us against the Agent and the other Lender Parties.

Prior to entering into the Settlement Agreement, the interest on outstanding amounts under the Facility accrued at a rate equal to 0.85% above the prime rate plus 0.75%, or approximately 4.9%, and we had been paying interest at such rate under protest. Under the terms of the Settlement Agreement, commencing on September 10, 2010, the advances under the Facility accrued interest at the rate provided for under the LFSA prior to the occurrence of a termination event, equal to 0.85% above the prevailing commercial paper rate, or approximately 1.2% as of such date. Under the terms of the Settlement Agreement, we calculated the advances outstanding under the Facility after consideration of amortization and pre-payments in the next scheduled distribution to the lenders. As of December 31, 2010, the Company's advances outstanding, calculated in accordance with the Settlement Agreement, were approximately $87 million. Under the Settlement Agreement, the Company was also obligated to maintain an overcollateralization ratio of at least 115%. As of December 31, 2010, our overcollateralization ratio was 177%. As a BDC, we are limited in the amount of leverage we can incur and are required to meet a coverage ratio of total asset to total senior securities of at least 200% before incurring new debt. As of December 31, 2010, our asset coverage ratio was 315%. We were in compliance with all covenants and terms set forth in the Settlement Agreement at December 31, 2010.

On January 31, 2011, we repaid in full the outstanding balance under the Facility in advance of the scheduled forbearance date of February 28, 2011. As a result, we have no outstanding indebtedness and the Lender Parties released to us approximately $73 million of collateral previously securing the Facility and also paid to us a $2 million cash settlement. In order to pay off the Facility, we utilized proceeds received from the paydown, amortization or sale of portfolio loan investments totaling approximately $133 million together with available cash.

Subject to prevailing market conditions, we intend to grow our portfolio of assets by raising additional capital, including through the prudent use of leverage. As a result, we may seek to enter into a new agreement with other lenders or into other financing arrangements as market conditions permit. Such financing arrangements may include a new secured and/or unsecured credit facility, the issuance of senior debt, preferred or convertible securities or debt guaranteed by the SBA.

The weighted average daily debt balance for the years ended December 31, 2010 and 2009 was approximately $105 million and $222 million, respectively. As of December 31, 2010, the Company had restricted cash and time deposit balances of approximately $67 million which it maintained in accordance with the terms of the Facility.

COMPETITION

Our primary competitors provide financing to prospective portfolio companies and include commercial banks, specialty finance companies, hedge funds, structured investment funds and investment banks. Many of these entities have greater financial and managerial resources than we have, and the 1940 Act imposes certain regulatory restrictions on us as a BDC to which many of our competitors are not subject. For additional information concerning the competitive risks we face, see "Item 1A. Risk Factors — Risks Related to Our Business — We operate in a highly competitive market for investment opportunities."

We believe that we provide a unique combination of an experienced middle market origination and credit team, an existing credit platform at Katonah Debt Advisors that includes experienced lenders with broad industry expertise and an Investment Committee that includes co-managing partners of Kohlberg & Co., a leading experienced and successful middle market private equity firm. We believe that this combination of resources provides us with a thorough credit process and multiple sources of investment opportunities to enhance our asset selection process.

COMPETITIVE ADVANTAGES

We believe that we can successfully compete with other providers of capital in the markets in which we compete for the following reasons:

- **Internally managed structure and significant management resources**. We are internally managed by our executive officers under the supervision of our Board of Directors and do not depend on a third party investment advisor. As a result, we do not pay investment advisory fees and all of our income is available to pay our operating costs and to make distributions to our stockholders.
- **Multiple sourcing capabilities for assets**. We have multiple sources of loans, mezzanine investments and equity investments through our industry relationships, Katonah Debt Advisors and our strategic relationship with Kohlberg & Co.

- **Disciplined investment process**. We employ a rigorous credit review process and due diligence intensive investment strategy which our senior management has developed over more than 20 years of lending. For each analyzed company, we develop our own underwriting case and multiple stress case scenarios and an event-specific financial model reflecting company, industry and market variables. Generally, both we and the CLO Funds managed by Katonah Debt Advisors have decided not to invest in highly leveraged or “covenant light” credit facilities.
- **Katonah Debt Advisors’ credit platform**. Katonah Debt Advisors serves as a source of our direct investment opportunities and cash flow, and certain credit analysts employed by Katonah Debt Advisors who also serve as officers of the Company serve as a resource for credit analysis.
- **Investments in a wide variety of portfolio companies in a number of different industries with no direct exposure to mortgage-backed securities**. Our investment portfolio (excluding our investments in Katonah Debt Advisors and CLO Fund securities) is spread across 16 different industries and 24 different entities with an average balance per investment of approximately $3 million. Our investment portfolio as well as the investment portfolios of the CLO Funds in which we have invested and the investment portfolios of the CLO Funds managed by Katonah Debt Advisors consist exclusively of credit instruments and other securities issued by companies and do not include any asset-backed securities secured by commercial mortgages, residential mortgages or other consumer borrowings.
- **Strategic relationship with Kohlberg & Co**. We believe that Kohlberg & Co. is one of the oldest and most well-known private equity firms focused on the middle market, and we expect to continue to derive substantial benefits from our strategic relationship with Kohlberg & Co.
- **Significant equity ownership and alignment of incentives**. Our senior management team, the senior management team of Katonah Debt Advisors and affiliates of Kohlberg & Co. together have a significant equity interest in the Company, ensuring that their incentives are strongly aligned with those of our stockholders.

EMPLOYEES

As of February 28, 2011, we had 22 employees.

DETERMINATION OF NET ASSET VALUE

We determine the net asset value per share of our common stock quarterly. The net asset value per share is equal to the value of our total assets minus liabilities and any preferred stock outstanding divided by the total number of shares of common stock outstanding. As of December 31, 2010, we did not have any preferred stock outstanding.

Value, as defined in Section 2(a)(41) of 1940 Act, is (1) the market price for those securities for which a market quotation is readily available and (2) for all other securities and assets, fair value as determined in good faith by our Board of Directors pursuant to procedures approved by our Board of Directors. Our quarterly valuation process begins with each portfolio company or investment being initially valued by the investment professionals responsible for the portfolio investment. Preliminary valuation conclusions are then documented and discussed with our senior management. The Valuation Committee of our Board of Directors reviews these preliminary valuations and makes recommendations to our Board of Directors. Where appropriate, the Valuation Committee may utilize an independent valuation firm selected by our Board of Directors for an independent determination of fair value or certain other valuation related services. Our Board of Directors discusses valuations and determines the fair value of each investment in our portfolio in good faith based on the recommendations of the Valuation Committee.

Because of the inherent uncertainty of determining the fair value of investments that do not have a readily available market value, the fair value of our investments determined under our valuation methodology may differ materially from the values that would have existed had a ready market existed for the investments.

There is no single standard for determining fair value. As a result, determining fair value requires that judgment be applied to the specific facts and circumstances of each portfolio investment. Unlike banks, we are not permitted to provide a general reserve for anticipated loan losses. Instead, we must determine the fair value of each individual investment on a quarterly basis. We record unrealized depreciation on investments when we believe that an investment has decreased in value, including where collection of a loan or realization of an equity security is doubtful. Conversely, we record unrealized appreciation if we believe that our investment has appreciated in value, for example, because the underlying portfolio company has appreciated in value.

As a BDC, we invest primarily in illiquid securities, including loans to and warrants of private companies and interests in other illiquid securities, such as interests in the underlying CLO Funds. Our investments are generally subject to restrictions on resale and generally have no established trading market. Because of the type of investments that we make and the nature of our business, our valuation process requires an analysis of various factors. Our valuation methodology includes the examination of, among other things, the underlying investment performance, financial condition and market changing events that impact valuation.

With respect to private debt and equity investments, each investment is valued using industry valuation benchmarks, and, where appropriate, such as valuing private warrants, the input value in our valuation model may be assigned a discount reflecting the illiquid nature of the investment and our minority, non-control position. When a qualifying external event such as a significant purchase transaction, public offering or subsequent loan or warrant sale occurs, the pricing indicated by the external event is considered in determining our private debt or equity valuation. Securities that are traded in the over-the-counter market or on a stock exchange generally are valued at the prevailing bid price on the valuation date. However, restricted or thinly traded public securities may be valued at discounts from the public market value due to limitations on our ability to sell the securities.

Our investments in CLO Fund securities are carried at fair value, which is based either on (i) the present value of the net expected cash inflows for interest income and principal repayments from underlying assets and cash outflows for interest expense, debt paydown and other fund costs for the CLO Funds which are approaching or are past the end of their reinvestment period and therefore are selling assets and/or using principal repayments to pay down CLO Fund debt (or will begin to do so shortly), and for which there continue to be net cash distributions to the class of securities owned by us, or (ii) the NAV of the CLO Funds which are approaching or are past the end of their reinvestment period and therefore are selling assets and/or using principal repayments to pay down CLO Fund debt (or will begin to do so shortly), and for which there are negligible net cash distributions to the class of securities owned by us, or (iii) a discounted cash flow model for more recent CLO Funds that utilizes prepayment and loss assumptions based on historical experience and projected performance, economic factors, the characteristics of the underlying cash flow and comparable yields for similar securities or preferred shares to those in which we have invested. We recognize unrealized appreciation or depreciation on our investments in CLO Fund securities as comparable yields in the market change and/or based on changes in NAVs or estimated cash flows resulting from changes in prepayment or loss assumptions in the underlying collateral pool. As each investment in CLO Fund securities ages, the expected amount of losses and the expected timing of recognition of such losses in the underlying collateral pool are updated and the revised cash flows are used in determining the fair value of the CLO Fund investments. We determine the fair value of our investments in CLO Fund securities on an individual security-by-security basis.

ELECTION TO BE REGULATED AS A BUSINESS DEVELOPMENT COMPANY AND A REGULATED INVESTMENT COMPANY

Our elections to be regulated as a BDC and to be treated as a RIC have a significant impact on our future operations:

We report our investments at market value or fair value with changes in value reported through our statement of operations.

We report all of our investments, including debt investments, at market value or, for investments that do not have a readily available market value, at their “fair value” as determined in good faith by our Board of Directors pursuant to procedures approved by our Board of Directors. Changes in these values are reported through our statement of operations under the caption of “net unrealized appreciation (depreciation) on investments.” See “— Determination of Net Asset Value.”

Our ability to use leverage as a means of financing our portfolio of investments is limited.

As a BDC, we are required to meet a coverage ratio of total assets to total senior securities of at least 200%. For this purpose, senior securities generally include all borrowings, guarantees of borrowings and any preferred stock we may issue in the future. Our ability to utilize leverage as a means of financing our portfolio of investments is limited by this asset coverage test. As of December 31, 2010, our Facility balance was approximately $87 million and our asset coverage ratio was approximately 315%, above the minimum asset coverage level generally required for a BDC by the 1940 Act. See "— Leverage" above.

We intend to distribute substantially all of our net taxable income to our stockholders. We generally will be required to pay U.S. federal income taxes only on the portion of our net taxable income and gains that we do not distribute to stockholders, although certain of our subsidiaries will be subject to corporate tax on their income.

We have elected to be treated as a RIC for U.S. federal income tax purposes, commencing with our taxable year ended December 31, 2006. As a RIC, we intend to distribute to our stockholders substantially all of our net investment company income. In addition, we may retain certain net long-term capital gains and elect to treat such net capital gains as distributed to our stockholders. If this happens, you will be treated as if you received an actual distribution of the capital gains and reinvested the net after-tax proceeds in us. You also may be eligible to claim a tax credit against your U.S. federal income tax liability (or, in certain circumstances, a tax refund) equal to your allocable share of the tax we pay on the deemed distribution. See "— Certain United States Federal Income Tax Considerations."

As a RIC, we generally are required to pay U.S. federal income taxes only on the portion of our net taxable income and gains that we do not distribute (actually or constructively). Katonah Debt Advisors, our wholly-owned taxable portfolio company, receives fee income earned with respect to its management services. We expect that we or Katonah Debt Advisors will form additional direct or indirect subsidiaries which will receive similar fee income. Some of these subsidiaries may be treated as corporations for U.S. federal income tax purposes, and as a result, such subsidiaries will be subject to income tax at regular corporate rates, for U.S. federal and state purposes, although, as a RIC, dividends and distributions of capital received by us from our taxable subsidiaries and distributed to our stockholders will not subject us to U.S. federal income taxes. As a result, the net return to us on investments in or held by such subsidiaries will be reduced to the extent that the subsidiaries are subject to income taxes.

In addition, due to the asset coverage test applicable to us as a BDC, we may be limited in our ability to make distributions. See "— Regulation" below. Also, restrictions and provisions governing our outstanding indebtedness may limit our ability to make distributions. See "Item 1A. Risk Factors" below.

We are required to comply with the provisions of the 1940 Act applicable to BDCs.

As a BDC, we are required to have a majority of directors who are not "interested" persons under the 1940 Act. In addition, we are required to comply with other applicable provisions of the 1940 Act, including those requiring the adoption of a code of ethics, fidelity bond and custody arrangements. See also "— Regulation."

REGULATION

The following discussion is a general summary of some of the material prohibitions and restrictions governing BDCs generally. It does not purport to be a complete description of all the laws and regulations affecting BDCs.

A BDC is a unique kind of investment company that primarily focuses on investing in or lending to private or relatively small publicly traded companies and making managerial assistance available to them. A BDC provides stockholders with the ability to retain the liquidity of a publicly traded stock, while sharing in the possible benefits of investing in emerging-growth or expansion-stage privately-owned companies. The 1940 Act contains prohibitions and restrictions relating to transactions between BDCs and their directors and officers and principal underwriters and certain other related persons and requires that a majority of the directors be persons other than "interested persons," as that term is defined in the 1940 Act. In the ordinary course of business, we may enter into transactions with portfolio companies that may be considered related party transactions. We have implemented certain procedures, both written and unwritten, to ensure that we do not engage in any prohibited transactions with any persons affiliated with us. If such affiliations are found to exist, we seek Board and/or committee review and approval or exemptive relief for such transactions, as appropriate.

In addition, the 1940 Act provides that we may not change the nature of our business so as to cease to be, or to withdraw our election as, a BDC unless approved by a majority of our outstanding voting securities. A majority of the outstanding voting securities of a company is defined under the 1940 Act as the lesser of (i) 67% or more of such company's shares present at a meeting or represented by proxy if more than 50% of the outstanding shares of such company are present or represented by proxy or (ii) more than 50% of the outstanding shares of such company.

Qualifying Assets

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

- Securities of an "eligible portfolio company" purchased in transactions not involving any public offering. An "eligible portfolio company" is defined in the 1940 Act as any issuer which:
  (a) is organized under the laws of, and has its principal place of business in, the United States;
  (b) is not an investment company (other than a small business investment company wholly-owned by the BDC) or a company that would be an investment company but for certain exclusions under the 1940 Act; and
  (c) satisfies any of the following:
    (i) does not have outstanding any class of securities with respect to which a broker or dealer may extend margin credit;
    (ii) is controlled by a BDC or a group of companies including a BDC and the BDC has an affiliated person who is a director of the eligible portfolio company;
    (iii) is a small and solvent company having total assets of not more than $4 million and capital and surplus of not less than $2 million; or
    (iv) does not have any class of securities listed on a national securities exchange (or, if it has a class of securities listed on a national securities exchange, has an aggregate market value of outstanding voting and non-voting common equity of less than $250 million).
- Securities of any eligible portfolio company that we control;
- Securities purchased in a private transaction from a U.S. issuer that is not an investment company and is in bankruptcy and subject to reorganization;
- Securities received in exchange for or distributed on or with respect to securities described above, or pursuant to the conversion of warrants or rights relating to such securities;
- Cash, cash equivalents, U.S. government securities or high-quality debt securities maturing in one year or less from the time of investment; and
- Under certain circumstances, securities of companies that were eligible portfolio companies at the time of the initial investment but that are not eligible portfolio companies at the time of the follow-on investment.

Significant Managerial Assistance

A BDC must be organized and have its principal place of business in the United States and must be operated for the purpose of making investments in the types of securities described above. However, to count portfolio securities as "qualifying assets" for the purpose of the 70% test discussed above, the BDC must either control the issuer of the securities or must offer to make available to the issuer of the securities (other than small and solvent companies described above) significant managerial assistance; except that, where the BDC purchases such securities in conjunction with one or more other persons acting together, one of the other persons in the group may make available such managerial assistance. Making available significant managerial assistance means, among other things, any arrangement whereby the BDC, through its directors, officers or employees, offers to provide, and, if accepted, does so provide, significant guidance and counsel concerning the management, operations or business objectives and policies of a portfolio company through monitoring of portfolio company operations, selective participation in board and management meetings, consulting with and advising a portfolio company's officers or other organizational or financial guidance.

Temporary Investments

Pending investment in other types of "qualifying assets," as described above, our investments may consist of cash, cash equivalents, U.S. government securities or high quality debt securities maturing in one year or less from the time of investment, which we refer to, collectively, as temporary investments, so that at least 70% of our assets are "qualifying assets." Typically, we invest in U.S. treasury bills or in repurchase agreements, provided that such agreements are fully collateralized by cash or securities issued by the U.S. government or its agencies. A repurchase agreement involves the purchase by an investor, such as us, of a specified security and the simultaneous agreement by the seller to repurchase it at an agreed upon future date and at a price which is greater than the purchase price by an amount that reflects an agreed-upon interest rate. There is no percentage restriction on the proportion of our assets that may be invested in such repurchase agreements. However, if more than 25% of our total assets constitute repurchase agreements that are treated, under applicable tax rules, as being issued by a single counterparty, we would not meet the diversification tests imposed on us by the Code to qualify for tax treatment as a RIC for U.S. federal income tax purposes. Thus, we do not intend to enter into repurchase agreements treated as issued, under applicable tax rules, by a single counterparty in excess of this limit. We monitor the creditworthiness of the counterparties with which we enter into repurchase agreement transactions.

Senior Securities; Coverage Ratio

We are permitted, under specified conditions, to issue multiple classes of indebtedness and one class of stock senior to our common stock if our asset coverage, as defined in the 1940 Act, is at least equal to 200% immediately after each such issuance. In addition, with respect to certain types of senior securities, we must make provisions to prohibit any dividend distribution to our stockholders or the repurchase of certain of our securities, unless we meet the applicable asset coverage ratios at the time of the dividend distribution or repurchase. We may also borrow amounts up to 5% of the value of our total assets for temporary purposes. For a discussion of the risks associated with the resulting leverage, see "Item 1A. Risk Factors — Risks Related to Our Business — The debt we incur could increase the risk of investing in our Company." As of December 31, 2010 our asset coverage ratio was 315%, above the minimum required asset coverage level of 200%.

Code of Ethics

We adopted and maintain a code of ethics pursuant to Rule 17j-1 under the 1940 Act that establishes procedures for personal investments and restricts certain personal securities transactions. Personnel subject to the code may invest in securities for their personal investment accounts, including securities that may be purchased or held by us, so long as such investments are made in accordance with the code's requirements. We may be prohibited under the 1940 Act from conducting certain transactions with our affiliates without the prior approval of our directors who are not interested persons and, in some cases, the prior approval of the SEC. A copy of the code of ethics is available on the Corporate Governance section of the Company's website at *www.kohlbergcap.com.*

Privacy Principles

We are committed to maintaining the privacy of our stockholders and safeguarding their non-public personal information. The following information is provided to help you understand what personal information we collect, how we protect that information and why, in certain cases, we may share information with select other parties.

Generally, we do not receive any non-public personal information relating to our stockholders, although some non-public personal information of our stockholders may become available to us. We do not disclose any non-public personal information about our stockholders or former stockholders to anyone, except as is necessary to service stockholder accounts, such as to a transfer agent, or as otherwise permitted by law.

We restrict access to non-public personal information about our stockholders to our employees with a legitimate business need for the information. We maintain physical, electronic and procedural safeguards designed to protect the non-public personal information of our stockholders.

Proxy Voting Policy and Procedures

Although most of the securities we hold are not voting securities, some of our investments may entitle us to vote proxies. We vote proxies relating to our portfolio securities in the best interest of our stockholders. We review on a case-by-case basis each proposal submitted to a stockholder vote to determine its impact on the portfolio securities held by us. Although we generally vote against proposals that we believe may have a negative impact on our portfolio securities, we may vote for such a proposal if we believe there exists a compelling long-term reason to do so.

Our proxy voting decisions are made by our Investment Committee, which is responsible for monitoring each of our investments. To ensure that our vote is not the product of a conflict of interest, we require that (1) anyone involved in the decision making process disclose to our Chief Compliance Officer any potential conflict that he or she is aware of and any contact that he or she has had with any interested party regarding a proxy vote; and (2) employees involved in the decision making process or vote administration are prohibited from revealing how we intend to vote on a proposal to reduce any attempted influence from interested parties.

Other

We will be periodically examined by the SEC for compliance with the 1940 Act.

We will not “concentrate” our investments, that is, invest 25% or more of our assets in any particular industry (determined at the time of investment).

We are required to provide and maintain a bond issued by a reputable fidelity insurance company to protect us against larceny and embezzlement. Furthermore, as a BDC, we are prohibited from indemnifying any director or officer against any liability to our stockholders arising from willful misfeasance, bad faith, gross negligence or reckless disregard of the duties involved in the conduct of such person’s office.

We are required to adopt and implement written policies and procedures reasonably designed to prevent violation of the federal securities laws and to review these policies and procedures annually for their adequacy and the effectiveness of their implementation. We have a designated Chief Compliance Officer who is responsible for administering these policies and procedures.

CERTAIN UNITED STATES FEDERAL INCOME TAX CONSIDERATIONS

The following discussion is a general summary of certain material U.S. federal income tax considerations applicable to us and to an investment in our shares. This summary does not purport to be a complete description of the income tax considerations applicable to such an investment. For example, we have not described tax consequences that we assume to be generally known by investors or certain considerations that may be relevant to certain types of holders subject to special treatment under U.S. federal income tax laws, including stockholders subject to the alternative minimum tax, tax-exempt organizations, insurance companies, regulated investment companies, dealers in securities, pension plans and trusts, and financial institutions. This summary assumes that investors hold our common stock as capital assets (within the meaning of the Code). The discussion is based upon the Code, Treasury regulations, and administrative and judicial interpretations, each as in effect as of the date of this filing and all of which are subject to change, possibly retroactively, which could affect the continuing validity of this discussion. This summary does not discuss any aspects of U.S. estate or gift tax or foreign, state or local tax. It does not discuss the special treatment under U.S. federal income tax laws that could result if we invested in tax-exempt securities or certain other investment assets in which we do not currently intend to invest.

A "U.S. stockholder" generally is a beneficial owner of shares of our common stock who or which is for U.S. federal income tax purposes:

- a citizen or individual resident of the United States including an alien individual who is a lawful permanent resident of the United States or meets the "substantial presence" test in Section 7701(b) of the Code;
- a corporation or other entity taxable as a corporation, for U.S. federal income tax purposes, created or organized in or under the laws of the United States or any political subdivision thereof;
- a trust over the administration of which a court in the U.S. has primary supervision or over which U.S. persons have control; or
- an estate, the income of which is subject to U.S. federal income taxation regardless of its source.

A "Non-U.S. stockholder" is a beneficial owner of shares of our common stock that is neither a U.S. stockholder nor a partnership for U.S. federal income tax purposes. If a partnership (including an entity treated as a partnership for U.S. federal income tax purposes) holds shares of our common stock, the tax treatment of a partner in the partnership will generally depend upon the status of the partner and the activities of the partnership. A prospective stockholder who is a partner of a partnership holding shares of our common stock should consult his, her or its tax advisors with respect to the purchase, ownership and disposition of shares of our common stock.

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

Election to be Taxed as a Regulated Investment Company

We have elected to be treated as a RIC under Subchapter M of the Code commencing with our taxable year ended December 31, 2006. As a RIC, we generally will not have to pay corporate-level taxes on any income or gains that we distribute to our stockholders as dividends in accordance with the timing requirements of the Code. To qualify for treatment as a RIC, we must, among other things, meet certain source-of-income and asset diversification requirements (as described below). In addition, to qualify for treatment as a RIC, we must distribute to our stockholders, for each taxable year, at least 90% of our "net investment company income," which is generally the sum of our net investment income plus the excess, if any, of realized net short-term capital gains over realized net long-term capital losses (the "Annual Distribution Requirement"), for such year.

Taxation as a Regulated Investment Company

For any taxable year in which we qualify as a RIC and satisfy the Annual Distribution Requirement, we generally will not be subject to U.S. federal income tax on the portion of our investment company taxable income and net capital gain (*i.e.*, net realized long-term capital gains in excess of net realized short-term capital losses) we distribute to stockholders with respect to that year. We will be subject to U.S. federal income tax at the regular corporate rates on any net ordinary income or capital gain not distributed (or deemed distributed) to our stockholders. As a RIC, we will be subject to a 4% nondeductible U.S. federal excise tax on certain net taxable undistributed income unless we distribute in a timely manner an amount at least equal to the sum of (1) 98% of our net ordinary income for each calendar year, (2) 98% of our capital gain net income for the 1-year period ending October 31 in that calendar year and (3) any net income realized, but not distributed, in the preceding year. For purposes of the required excise tax distribution, any ordinary gains and losses from the sale, exchange or other taxable disposition of property that would otherwise be taken into account after October 31 of a calendar year generally are treated as arising on January 1 of the following calendar year. We will not be subject to excise taxes on amounts on which we are required to pay corporate income tax (such as retained net capital gains). We currently intend to make sufficient distributions each taxable year and/or pay sufficient corporate income tax to avoid any excise tax liability, although we reserve the right to pay an excise tax rather than make an additional distribution when circumstances warrant (*e.g.*, the payment of an excise tax amount that we deem to be *de minimis*).

To qualify for tax treatment as a RIC for U.S. federal income tax purposes, in addition to satisfying the Annual Distribution Requirement, we must, among other things:

- have in effect at all times during each taxable year an election to be regulated as a BDC under the 1940 Act;
- in each taxable year, derive at least 90% of our gross income from (a) dividends, interest, payments with respect to certain securities loans, gains from the sale of stock or other securities, or other income derived with respect to our business of investing in such stock or securities and (b) net income derived from an interest in a “qualified publicly traded partnership” (as defined by the Code) (all such income “Qualifying Income”); and
- diversify our holdings so that at the end of each quarter of the taxable year: (i) at least 50% of the value of our assets consists of cash, cash equivalents, U.S. government securities, securities of other RICs, and other securities if such other securities of any one issuer do not represent more than 5% of the value of our assets or more than 10% of the outstanding voting securities of such issuer; and (ii) no more than 25% of the value of our assets is invested in the securities, other than U.S. government securities or securities of other RICs, of (a) one issuer, (b) two or more issuers that are controlled, as determined under applicable tax rules, by us and that are engaged in the same or similar or related trades or businesses or (c) one or more “qualified publicly traded partnerships” (the “Diversification Tests”).

We conduct the business of Katonah Debt Advisors through direct or indirect subsidiaries. Some of our subsidiaries are treated as corporations for U.S. federal income tax purposes. As a result, such subsidiaries will be subject to tax at regular corporate rates. We will recognize income from these subsidiaries to the extent that we receive dividends and distributions of capital from these subsidiaries. Some of the wholly-owned subsidiaries may be treated as disregarded entities for U.S. federal income tax purposes. As a result, we may directly recognize fee income earned by these subsidiaries. Fee income that we recognize directly through entities that are treated as disregarded entities for U.S. federal tax purposes will generally not constitute Qualifying Income. We intend to monitor our recognition of fee income to ensure that at least 90% of our gross income in each taxable year is Qualifying Income.

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

However, pursuant to guidance issued in 2009 and thereafter by the U.S. Internal Revenue Service (“IRS”), under certain circumstances it is possible for us to meet the Annual Distribution Requirement for 2009, 2010 and 2011, even though we limit how much cash (and other property which is not our stock) that we distribute in the aggregate to our stockholders (which limit can be as low as 10% of each qualifying distribution) when compared to how much cash (and other property which is not our stock) that we would need to distribute for us to meet the Annual Distribution Requirement without relying on such guidance (a “qualifying limited-cash distribution”). The portion of a qualifying limited-cash distribution that does not consist of cash (and other property which is not our stock) will be in the form of shares of our stock (based on a market-price valuation method determined pursuant to such guidance). While we have not made any qualifying limited-cash distributions to date as permitted by the IRS guidance, we reserve the right to consider making such distributions in the future, subject to compliance with applicable tax requirements. The IRS guidance is in effect for distributions declared on or before December 31, 2012 with respect to taxable years ending on or before December 31, 2011.

We could also be subject to a U.S. federal income tax (including interest charges) on distributions received from investments in passive foreign investment companies "PFICs" (defined below) or on proceeds received from the disposition of shares in PFICs, which tax cannot be eliminated by making distributions to our stockholders. A PFIC is any foreign corporation in which (i) 75% or more of the gross income for the taxable year is passive income, or (ii) the average percentage of the assets (generally by value, but by adjusted tax basis in certain cases) that produce or are held for the production of passive income is at least 50%. Generally, passive income for this purpose means dividends, interest (including income equivalent to interest), royalties, rents, annuities, the excess of gains over losses from certain property transactions and commodities transactions, and foreign currency gains. Passive income for this purpose does not include rents and royalties received by the foreign corporation from an active business and certain income received from related persons. If we are in a position to treat and do treat a PFIC as a "qualified electing fund" ("QEF") we will be required to include in income our share of the company's income and net capital gain annually, regardless of whether we receive any distribution from the company. Alternately, we may make an election to mark the gains (and to a limited extent losses) in such holdings "to the market" as though we had sold and repurchased our holdings in those PFICs on the last day of our taxable year. Such gains and losses are treated as ordinary income and loss. The QEF and mark-to-market elections may have the effect of accelerating the recognition of income (without the receipt of cash) and increasing the amount required to be distributed for us to avoid taxation.

We may also invest in "controlled foreign corporations" ("CFCs"). A non-U.S. corporation will be a CFC if "U.S. Shareholders" (*i.e.*, each U.S. investor that owns (directly or by attribution) 10% or more of the interests in the non-U.S. corporation (by vote)) own (directly or by attribution) more than 50% (by vote or value) of the outstanding interests of the non-U.S. corporation. If we are a U.S. Shareholder with respect to a CFC, we will be required each year to include in income our pro rata share of the corporation's "Subpart F income" (as defined in the Code). Therefore, investments in CFCs may have the effect of accelerating the recognition of income (without the receipt of cash) and increasing the amount required to be distributed for us to avoid taxation.

We are authorized to borrow funds and to sell assets to satisfy the Annual Distribution Requirement and to avoid any excise tax liability. However, depending on the types of debt and equity securities we have outstanding, we may be prohibited under the 1940 Act from making distributions to our stockholders while our debt obligations and other senior securities are outstanding unless certain "asset coverage" tests are met. See "Regulation — Senior Securities; Coverage Ratio." Moreover, our ability to dispose of assets to meet the Annual Distribution Requirement and to avoid any excise tax liability may be limited by (1) the illiquid nature of our portfolio, or (2) other requirements relating to our tax treatment as a RIC, including the Diversification Tests. If we dispose of assets to meet the Annual Distribution Requirements and to avoid any excise tax liability, we may make such dispositions at times that, from an investment standpoint, are not advantageous.

Gain or loss realized by us from the sale or exchange of warrants acquired by us as well as any loss attributable to the lapse of such warrants generally will be treated as capital gain or loss. Such gain or loss generally will be long-term or short-term, depending on how long we held a particular warrant. Our transactions in options, futures contracts, hedging transactions and forward contracts will be subject to special tax rules, the effect of which may be to accelerate income to us, defer losses, cause adjustments to the holding periods of our investments, convert long-term capital gains into short-term capital gains, convert short-term capital losses into long-term capital losses or have other tax consequences. These rules could affect the amount, timing and character of distributions to stockholders. We do not currently intend to engage in these types of transactions.

Capital losses in excess of capital gains ("net capital losses") are not permitted to be deducted against a RIC's net investment income. Instead, potentially subject to certain limitations, we may carry net capital losses from any taxable year forward to offset capital gains in future years, thereby reducing the amount we would otherwise be required to distribute in such future years to qualify for the special tax treatment accorded RICs and avoid a company-level tax. If we incur or have incurred net capital losses in a taxable year beginning on or before December 22, 2010 ("pre-2011 losses"), we are permitted to carry such losses forward for eight taxable years, and in the year to which they are carried forward, such losses are treated as short-term capital losses that first offset short-term capital gains, and then offset long-term capital gains. A RIC is permitted to carry forward net capital losses it incurs in taxable years beginning after December 22, 2010 without expiration. Any such carryforward losses will retain their character as short-term or long-term; this may well result in larger distributions of short-term gains (taxed as ordinary income to individual shareholders) than would have resulted under the regime applicable to pre-2011 losses. We will also generally be required to use any such carryforward losses, which will not expire, before we use any pre-2011 losses. This may increase the likelihood that pre-2011 losses, if any, will expire unused. See Note 7 — "Distributable Taxable Income" from our Notes to the Financial Statements included herein for information relating to the amount and expiration date of our capital loss carryforwards.

As a RIC we are not permitted to deduct expenses in excess of our "investment company taxable income" (which is, generally, ordinary income plus net short-term capital gains in excess of net long-term capital losses). If our expenses in a given year exceed investment company taxable income (*e.g.*, as the result of large amounts of equity-based compensation), we would experience a net operating loss for that year. However, a RIC is not permitted to carry forward net operating losses to subsequent years. In addition, expenses can be used only to offset investment company taxable income, not net capital gain (that is, the excess of net long-term capital gains over the net short-term capital losses). Due to these limits on the deductibility of expenses, we may for tax purposes have aggregate taxable income over a period of several years that we are required to distribute and that is taxable to our stockholders even if such income is greater than the net income we actually earned during those years in the aggregate. Such required distributions may be made from our cash assets or by liquidation of investments, if necessary. We may realize gains or losses from such liquidations. In the event we realize net capital gains from such transactions, you may receive a larger capital gain distribution than you would have received in the absence of such transactions. Assuming we qualify for tax treatment as a RIC, our corporate-level U.S. federal income tax should be substantially reduced or eliminated, and, as explained below in "— Taxation of U.S. Stockholders," a portion of our distributions or deemed distributions may be characterized as long-term capital gain in the hands of stockholders.

Failure to Qualify as a Regulated Investment Company

If we were to fail to meet the income or diversification requirements described above, we could in some cases cure such failure, including by paying a tax and, in the case of diversification failures, by disposing of certain assets. If we do not cure such a failure or otherwise fail to qualify for tax treatment as a RIC (including if our Board of Directors elected to temporarily or permanently revoke our RIC election), we would be subject to tax on all of our taxable income at regular corporate rates. We would not be able to deduct distributions to stockholders, nor would distributions be required to be made. Such distributions would be taxable to our stockholders as dividend income to the extent of our current and accumulated earnings and profits and (if made during a taxable year beginning before January 1, 2013) provided certain holding period and other requirements were met, could potentially qualify for treatment as "qualified dividend income" in the hands of stockholders taxed as individuals eligible for the 15% maximum rate. Subject to certain limitations under the Code, corporate distributees may be eligible for the dividends received deduction with respect to our dividend distributions. Distributions in excess of our current and accumulated earnings and profits would be treated first as a return of capital to the extent of the stockholder's tax basis, and any remaining distributions would be treated as a capital gain. To requalify as a RIC in a subsequent taxable year, we would be required to satisfy the RIC qualification requirements for that year and distribute any earnings and profits from any year in which we failed to qualify for tax treatment as a RIC. Subject to a limited exception applicable to RICs that qualified as such under Subchapter M of the Code for at least one year prior to disqualification and that requalify as a RIC no later than the second year following the nonqualifying year, we could be subject to tax on any unrealized net built-in gains in the assets held by us during the period in which we failed to qualify for tax treatment as a RIC that are recognized within the subsequent 10 years, unless we made a special election to pay corporate-level tax on such built-in gain at the time of our requalification as a RIC. Except as otherwise provided, the remainder of this discussion assumes that we qualify for tax treatment as a RIC and have satisfied the Annual Distribution Requirement.

Taxation of U.S. Stockholders

For U.S. federal income tax purposes, distributions by us generally are taxable to U.S. stockholders as ordinary income or capital gains. Distributions of our "investment company taxable income" (which is, generally, our ordinary income plus net realized short-term capital gains in excess of net realized long-term capital losses) will be taxable as ordinary income to U.S. stockholders to the extent of our current or accumulated earnings and profits, whether paid in cash or reinvested in additional common stock through our dividend reinvestment plan. For taxable years beginning before January 1, 2013, to the extent such distributions paid by us are attributable to dividends from U.S. corporations and certain qualified foreign corporations, such distributions may be reported by us as "qualified dividend income" eligible to be taxed in the hands of non-corporate stockholders at the rates applicable to long-term capital gains, provided holding period and other requirements are met at both the stockholder and company levels. In this regard, it is anticipated that distributions paid by us generally will not be attributable to dividends and, therefore, generally will not be qualified dividend income. Distributions of our net capital gains (which is generally our realized net long-term capital gains in excess of realized net short-term capital losses) properly reported by us as "capital gain dividends" will be taxable to a U.S. stockholder as long-term capital gains (currently at a maximum rate of 15% in the case of individuals, trusts or estates), regardless of the U.S. stockholder's holding period for his, her or its common stock and regardless of whether paid in cash or reinvested in additional common stock. Distributions in excess of our current and accumulated earnings and profits first will reduce a U.S. stockholder's adjusted tax basis in such stockholder's common stock and, after the adjusted basis is reduced to zero, will constitute capital gains to such U.S. stockholder.

We may retain some or all of our realized net long-term capital gains in excess of realized net short-term capital losses and designate the retained net capital gains as a "deemed distribution." In that case, among other consequences, we will pay tax on the retained amount, each U.S. stockholder will be required to include his, her or its share of the deemed distribution in income as if it had been actually distributed to the U.S. stockholder, and the U.S. stockholder will be entitled to claim a credit equal to his, her or its allocable share of the tax paid thereon by us. The amount of the deemed distribution net of such tax will be added to the U.S. stockholder's cost basis for his, her or its common stock. Since we expect to pay tax on any retained net capital gains at our regular corporate tax rate, and since that rate is in excess of the maximum rate currently payable by individuals on long-term capital gains, the amount of tax that individual stockholders will be treated as having paid and for which they will receive a credit will exceed the tax they owe on the retained net capital gain. Such excess generally may be claimed as a credit against the U.S. stockholder's other federal income tax obligations or may be refunded to the extent it exceeds a stockholder's liability for U.S. federal income tax. A stockholder that is not subject to U.S. federal income tax or otherwise required to file a U.S. federal income tax return would be required to file a U.S. federal income tax return on the appropriate form to claim a refund for the taxes we paid. To utilize the deemed distribution approach, we must provide written notice to our stockholders prior to the expiration of 60 days after the close of the relevant taxable year. We cannot treat any of our investment company taxable income as a "deemed distribution." We may also make actual distributions to our stockholders of some or all of realized net long-term capital gains in excess of realized net short-term capital losses.

For purposes of determining (1) whether the Annual Distribution Requirement is satisfied for any year and (2) the amount of capital gain dividends paid for that year, we may, under certain circumstances, elect to treat a dividend that is paid during the following taxable year as if it had been paid during the taxable year in question. If we make such an election, the U.S. stockholder will still be treated as receiving the dividend in the taxable year in which the distribution is made. However, any dividend declared by us in October, November or December of any calendar year, payable to stockholders of record on a specified date in such a month and actually paid during January of the following year, will be treated as if it had been received by our U.S. stockholders on December 31 of the year in which the dividend was declared. A U.S. stockholder generally will recognize taxable gain or loss if the U.S. stockholder sells or otherwise disposes of his, her or its shares of our common stock. Any gain arising from such sale or disposition generally will be treated as long-term capital gain or loss if the U.S. stockholder has held his, her or its shares for more than one year. Otherwise, it will be classified as short-term capital gain or loss. However, any capital loss arising from the sale or disposition of shares of our common stock held for six months or less will be treated as long-term capital loss to the extent of the amount of capital gain dividends received, or undistributed capital gain deemed received, with respect to such shares. In addition, all or a portion of any loss recognized upon a disposition of shares of our common stock may be disallowed if other shares of our common stock are purchased (whether through reinvestment of distributions or otherwise) within 30 days before or after the disposition. In such a case, the basis of the newly purchased shares will be adjusted to reflect the disallowed loss.

For taxable years beginning before January 1, 2013, individual U.S. stockholders are subject to a maximum U.S. federal income tax rate of 15% on their net capital gain (*i.e.*, the excess of realized net long-term capital gain over realized net short-term capital loss for a taxable year) including any long-term capital gain derived from an investment in our shares. Such rate is lower than the maximum rate on ordinary income currently payable by individuals. Corporate U.S. stockholders currently are subject to U.S. federal income tax on net capital gain at the maximum 35% rate also applied to ordinary income. Non-corporate stockholders with net capital losses for a year (*i.e.*, capital losses in excess of capital gains) generally may deduct up to $3,000 of such losses against their ordinary income each year ($1,500 for married individuals filing separately); any net capital losses of a non-corporate stockholder in excess of $3,000 ($1,500 for married individuals filing separately) generally may be carried forward and used in subsequent years as and to the extent provided in the Code. Corporate stockholders generally may not deduct any net capital losses for a year, but may carry back such losses for three years or carry forward such losses for five years.

Distributions are taxable to stockholders even if they are paid from income or gains earned by us before a stockholder’s investment (and thus were included in the price the stockholder paid). If an investor purchases shares of our common stock shortly before the record date of a distribution, the price of the shares will include the value of the distribution and the investor will be subject to tax on the distribution even though economically, it may represent a return of his, her or its investment.

Distributions are taxable whether stockholders receive them in cash or reinvest them in additional shares through the Dividend Reinvestment Plan. A stockholder whose distributions are reinvested in shares will be treated as having received a dividend equal to either (i) the fair market value of the shares issued to the stockholder (if we issue new shares), or (ii) the amount of cash allocated to the stockholder for the purchase of shares on its behalf (if we purchase shares on the open market). We will send to each of our U.S. stockholders, as promptly as possible after the end of each calendar year, a notice detailing, on a per share and per distribution basis, the amounts includible in such U.S. stockholder’s taxable income for such year as ordinary income and as long-term capital gain. In addition, the U.S. federal tax status of each year’s distributions generally will be reported to the IRS (including the amount of dividends, if any, eligible for the 15% “qualified dividend income” rate). Distributions may also be subject to additional state, local and foreign taxes depending on a U.S. stockholder’s particular situation. Dividends distributed by us generally will not be eligible for the corporate dividends received deduction or the preferential rate applicable to “qualified dividend income.”

We may be required to withhold U.S. federal income tax (“backup withholding”), currently at a rate of 28%, from all distributions to any non-corporate U.S. stockholder (1) who fails to furnish us with a correct taxpayer identification number or a certificate that such stockholder is exempt from backup withholding, or (2) with respect to whom the IRS notifies us that such stockholder has failed to properly report certain interest and dividend income to the IRS and to respond to notices to that effect. An individual’s taxpayer identification number is his or her social security number. The 28% rate will expire for amounts paid after December 31, 2012 and instead the backup withholding rate on such amounts will be 31% unless Congress enacts legislation proving otherwise. It is currently unclear whether such legislation will be enacted and, if enacted, what the terms of an extension will be. Backup withholding is not an additional tax. Any amount withheld under the backup withholding rules is allowed as a credit against the U.S. stockholder’s federal income tax liability, provided that proper information is provided to the IRS.

Under Treasury regulations, if a stockholder recognizes a loss with respect to our shares of $2 million or more for an individual stockholder or $10 million for a corporate stockholder, the stockholder must file with the IRS a disclosure statement on Form 8886. Direct stockholders of portfolio securities are in many cases excepted from this reporting requirement, but under current guidance, stockholders of a RIC are not excepted. Future guidance may extend the current exception from this reporting requirement to stockholders of most or all RICs. The fact that a loss is reportable under these regulations does not affect the legal determination of whether a taxpayer’s treatment of the loss is proper. Stockholders should consult their tax advisors to determine the applicability of these regulations in light of their individual circumstances.

Taxation of Non-U.S. Stockholders

Whether an investment in the shares is appropriate for a non-U.S. stockholder will depend upon that person's particular circumstances. Non-U.S. stockholders should consult their tax advisors before investing in our common stock. In general, dividend distributions (other than certain distributions derived from net long-term capital gains, certain interest income and short term capital gains, as described below) paid by us to a non-U.S. stockholder are subject to withholding of U.S. federal income tax at a rate of 30% (or lower applicable treaty rate) even if they are funded by income or gains that, if paid to a non-U.S. stockholder directly, would not be subject to withholding. If the distributions are effectively connected with a U.S. trade or business of the non-U.S. stockholder, (and, if an income tax treaty applies, attributable to a permanent establishment in the United States), we will not be required to withhold federal tax if the non-U.S. stockholder complies with applicable certification and disclosure requirements, although the distributions will be subject to U.S. federal income tax at the rates applicable to U.S. stockholders. (Special certification requirements apply to a non-U.S. stockholder that is a foreign partnership or a foreign trust and such entities are urged to consult their tax advisors.) For our taxable years beginning prior to January 1, 2012, except as provided below, we generally will not be required to withhold any amounts with respect to certain distributions of (1) U.S.-source interest income that meets certain requirements, and (2) net short-term capital gains in excess of net long-term capital losses, in each case to the extent we properly report such distributions as such to stockholders. We intend to report to stockholders the portion of our distributions that are eligible for the interest-related dividend and short-term capital gain dividend withholding tax exemptions. In respect of distributions described in clause (1) above, however, we will be required to withhold amounts with respect to distributions to a non-U.S. stockholder:

- that has not provided a satisfactory statement that the beneficial owner is not a U.S. person;
- to the extent that the dividend is attributable to certain interest on an obligation if the non-U.S. stockholder is the issuer or is a 10% stockholder of the issuer;
- that is within certain foreign countries that have inadequate information exchange with the United States; or
- to the extent the dividend is attributable to interest paid by a person that is a related person of the non-U.S. stockholder and the non-U.S. stockholder is a "controlled foreign corporation" for U.S. federal income tax purposes.

In the case of shares held through an intermediary, the intermediary may withhold even if we were to report a distribution as an interest-related or short-term capital gain dividend. Non-U.S. stockholders should contact their intermediaries regarding the application of these rules to their accounts.

Actual or deemed distributions of our net capital gain to a non-U.S. stockholder, and gains realized by a non-U.S. stockholder upon the sale of our common stock, will not be subject to U.S. federal withholding tax and generally will not be subject to U.S. federal income tax unless the distributions or gain, as the case may be, are effectively connected with a U.S. trade or business of the non-U.S. stockholder (and, if an income tax treaty applies, are attributable to a permanent establishment maintained by the non-U.S. stockholder in the U.S.), or in the case of an individual stockholder, the stockholder is present in the U.S. for a period or periods aggregating 183 days or more during the year of the sale or capital gain dividend and certain other conditions are met. If we distribute our net capital gain in the form of deemed rather than actual distributions, a non-U.S. stockholder will be entitled to a U.S. federal income tax credit or tax refund equal to the stockholder's allocable share of the tax we pay on the capital gains deemed to have been distributed. To obtain the refund, the non-U.S. stockholder must obtain a U.S. taxpayer identification number and file a U.S. federal income tax return even if the non-U.S. stockholder would not otherwise be required to obtain a U.S. taxpayer identification number or file a U.S. federal income tax return. For a corporate non-U.S. stockholder, distributions (both actual and deemed), and gains realized upon the sale of our common stock that are effectively connected to a U.S. trade or business may, under certain circumstances, be subject to an additional "branch profits tax" at a 30% rate (or at a lower rate if provided for by an applicable treaty).

A non-U.S. stockholder who is a non-resident alien individual, and who is otherwise subject to withholding of U.S. federal tax, may be subject to information reporting and backup withholding of U.S. federal income tax on dividends unless the non-U.S. stockholder provides us or the dividend paying agent a properly completed and duly executed IRS Form W-8 (or an acceptable substitute or successor form) or otherwise meets documentary evidence requirements for establishing that it is a non-U.S. stockholder or otherwise establishes an exemption from backup withholding.

Investment in the shares may not be appropriate for a non-U.S. stockholder. Non-U.S. persons should consult their tax advisors with respect to the U.S. federal income tax and withholding tax, and state, local and foreign tax consequences of an investment in the shares.

Certain Additional Reporting and Withholding Requirements

New rules enacted in March 2010 require the reporting to the IRS of direct and indirect ownership of foreign financial accounts and foreign entities by U.S. persons. Failure to provide this required information can result in a 30% withholding tax on certain payments ("withholdable payments") made after December 31, 2012. Withholdable payments include U.S.-source dividends and interest, and gross proceeds from the sale or other disposition of property that can produce U.S.-source dividends or interest.

The IRS has issued only very preliminary guidance with respect to these new rules; their scope remains unclear and potentially subject to material change. Pursuant to that guidance, it is possible that distributions and redemption payments made by us after December 31, 2012 (or such later date as may be provided in future guidance) to a stockholder will be subject to the new 30% withholding requirement. Payments to a non-U.S. stockholder that is a "foreign financial institution" will generally be subject to withholding unless such stockholder enters into an agreement with the IRS. Payments to stockholders that are U.S. persons or foreign individuals will generally not be subject to withholding, so long as such stockholders provide such certifications or other documentation as are required to comply with the new rules. Persons investing in us through an intermediary should contact their intermediaries regarding the application of the new reporting and withholding regime to their investments. Stockholders are urged to consult a tax advisor regarding this new reporting and withholding regime in light of their particular circumstances.

DIVIDEND REINVESTMENT PLAN

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

No action is required on the part of a registered stockholder to have such shareholder's cash dividend reinvested in shares of our common stock. A registered stockholder may elect to receive an entire dividend in cash by notifying American Stock Transfer & Trust Company, the plan administrator and our transfer agent and registrar, in writing so that such notice is received by the plan administrator no later than the record date for dividends to stockholders. The plan administrator will set up an account for shares acquired through the plan for each stockholder who has not elected to receive dividends in cash and hold such shares in non-certificated form. Upon request by a stockholder participating in the plan, received in writing not less than ten days prior to the record date, the plan administrator will, instead of crediting shares to the participant's account, issue a certificate registered in the participant's name for the number of whole shares of our common stock and a check for any fractional share.

Those stockholders whose shares are held by a broker or other financial intermediary may receive dividends in cash by notifying their broker or other financial intermediary of their election.

We intend to use primarily newly issued shares to implement the plan, whether our shares are trading at a premium or at a discount to net asset value. However, we reserve the right to purchase shares in the open market in connection with our implementation of the plan. The number of shares to be issued to a stockholder is determined by dividing the total dollar amount of the dividend payable to such stockholder by the market price per share of our common stock at the close of regular trading on The NASDAQ Global Select Market on the dividend payment date. Market price per share on that date will be the closing price for such shares on The NASDAQ Global Select Market or, if no sale is reported for such day, at the average of their reported bid and asked prices. The number of shares of our common stock to be outstanding after giving effect to payment of the dividend cannot be established until the value per share at which additional shares will be issued has been determined and elections of our stockholders have been tabulated.

There are no brokerage charges or other charges to stockholders who participate in the plan. The plan administrator's fees under the plan are paid by us. If a participant elects by written notice to the plan administrator to have the plan administrator sell part or all of the shares held by the plan administrator in the participant's account and remit the proceeds to the participant, the plan administrator is authorized to deduct a $15.00 transaction fee plus a $0.10 per share brokerage commission from the proceeds.

If your dividends are reinvested, you will be required to pay tax on the distributions in the same manner as if the distributions were received in cash. The taxation of dividends will not be affected by the form in which you receive them. See "Certain United States Federal Income Tax Considerations."

Participants may terminate their accounts under the plan by notifying the plan administrator via its website at *www.amstock.com*, by filling out the transaction request form located at bottom of their statement and sending it to the plan administrator at the address set forth below or by calling the plan administrator at 1-866-668-8564.

The plan may be terminated by us upon notice in writing mailed to each participant at least 30 days prior to any record date for the payment of any dividend by us. All correspondence concerning the plan should be directed to, and additional information about the plan may be obtained from, the plan administrator by mail at American Stock Transfer & Trust Company, Attn. Dividend Reinvestment Department, P.O. Box 922, Wall Street Station, New York, NY 10269-0560 or by telephone at 1-866-668-8564.

Item 1A. *Risk Factors*

Investing in our common stock involves a high degree of risk. The risks set forth below are not the only risks we face. If any of the following risks occur, our business, financial condition and results of our operations could be materially adversely affected. In such case, the net asset value and the trading price of our common stock could decline, and you may lose all or part of your investment.

Risks Related to Our Business

We are dependent upon senior management for our future success, and if we are unable to hire and retain qualified personnel or if we lose any member of our senior management team, our ability to achieve our investment objective could be significantly harmed.

We depend on the members of our senior management as well as other key personnel for the identification, final selection, structuring, closing and monitoring of our investments. These employees have critical industry experience and relationships that we rely on to implement our business plan. Our future success depends on the continued service of our senior management team and our Board of Directors. The departure of any of the members of our senior management or a significant number of our senior personnel could have a material adverse effect on our ability to achieve our investment objective. As a result, we may not be able to operate our business as we expect, and our ability to compete could be harmed, which could cause our operating results to suffer.

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 plan to make in prospective portfolio companies. We compete with other BDCs, as well as a large number of investment funds, investment banks and other sources of financing, including traditional financial services companies, such as commercial banks and finance companies. Many of our competitors are substantially larger and have considerably greater financial, technical, marketing and other 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. This may enable some of our competitors to make commercial loans with interest rates that are comparable to or lower than the rates we typically offer. We may lose prospective portfolio investments if we do not match our competitors' pricing, terms and structure. If we do match our competitors' pricing, terms or structure, we may experience decreased net interest income and increased risk of credit losses. 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, establish more relationships and build their market shares. Furthermore, many of our potential competitors have greater experience operating under, or are not subject to, the regulatory restrictions that the 1940 Act imposes on us as a BDC. As a result of this competition, there can be no assurance that we will be able to identify and take advantage of attractive investment opportunities or that we will be able to fully invest our available capital. If we are not able to compete effectively, our business and financial condition and results of operations will be adversely affected. Although Kohlberg & Co. has agreed to notify us of equity investment opportunities that are presented to Kohlberg & Co. but do not fit the investment profile of Kohlberg & Co. or its affiliates, no such referral to date has resulted in an investment by us or Katonah Debt Advisors.

If we are unable to source investments effectively, we may be unable to achieve our investment objective.

Our ability to achieve our investment objective depends on our senior management team's ability to identify, evaluate, finance and invest in suitable companies that meet our investment criteria. Accomplishing this result on a cost-effective basis is largely a function of our marketing capabilities, our management of the investment process, our ability to provide efficient services and our access to financing sources on acceptable terms. In addition to monitoring the performance of our existing investments, members of our management team and our investment professionals may also be called upon to provide managerial assistance to our portfolio companies. These demands on their time may distract them or slow the rate of investment. To grow, we need to continue to hire, train, supervise and manage new employees and to implement computer and other systems capable of effectively accommodating our growth. However, we cannot provide assurance that any such employees will contribute to the success of our business or that we will implement such systems effectively. Failure to manage our future growth effectively could have a material adverse effect on our business, financial condition and results of operations.

There is a risk that we may not make distributions.

We intend to continue to make distributions on a quarterly basis to our stockholders. We may not be able to achieve operating results that will allow us to make distributions at historical or any specific levels or to increase the amount of these distributions from time to time. In addition, due to the asset coverage test applicable to us as a BDC, depending on the types of debt and equity securities we have outstanding, we may be limited in our ability to make distributions. See "Item 1. Business — Leverage." Also, restrictions and provisions in our outstanding indebtedness may limit our ability to make distributions. If we do not distribute a certain percentage of our income annually, we could fail to qualify for tax treatment as a RIC and we would be subject to corporate level U.S. federal income tax. Furthermore, in accordance with current IRS guidance, we may make distributions under special circumstances that would allow us to meet our annual RIC distribution requirement for 2009, 2010, and 2011 by distributing shares of our stock in lieu of a significant portion of the cash (or other property other than our stock) that we would otherwise be required to distribute to satisfy such distribution requirement. See "Item 1. Business — Certain United States Federal Income Tax Considerations." We cannot ensure that we will make distributions at historical or any other specified levels or at all.

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

In accordance with GAAP and the Code, we include in income certain amounts that we have not yet received in cash, such as contracted non-cash PIK interest, which represents contractual interest added to the loan balance and due at the end of the loan term. In addition to the cash yields received on our loans, in some instances, certain loans may also include any of the following: end of term payments, exit fees, balloon payment fees or prepayment fees. The increases in loan balances as a result of contracted non-cash PIK arrangements are included in income for the period in which such non-cash PIK interest was received, which is often in advance of receiving cash payment, and are separately identified on our statements of cash flows. We also may be required to include in income certain other amounts that we will not receive in cash. Any warrants that we receive in connection with our debt investments generally are valued as part of the negotiation process with the particular portfolio company. As a result, a portion of the aggregate purchase price for the debt investments and warrants is allocated to the warrants that we receive. This generally results in "original issue discount" for tax purposes, which we must recognize as ordinary income, increasing the amounts we are required to distribute to qualify as a RIC eligible for pass-through tax treatment. Because such original issue discount income might exceed the amount of cash received in a given year with respect to such investment, we might need to obtain cash from other sources to satisfy such distribution requirements. Other features of the debt instruments that we hold may also cause such instruments to generate original issue discount, resulting in a dividend distribution requirement in excess of current cash received. Since in certain cases we may recognize income before or without receiving cash representing such income, we may have difficulty meeting the requirement to distribute at least 90% of our net ordinary income and realized net short-term capital gains in excess of realized net long-term capital losses, if any. If we are unable to meet these distribution requirements, we will not qualify for tax treatment as a RIC or, even if such distribution requirement is satisfied, we may be subject to tax on the amount that is undistributed. Accordingly, we may have to sell some of our assets, raise additional debt or equity securities or reduce new investment originations to meet these distribution requirements and avoid tax. See "Item 1. Business — Certain United States Federal Income Tax Considerations."

We may incur losses as a result of "first loss" agreements into which we or Katonah Debt Advisors may enter in connection with warehousing credit arrangements which we put in place prior to raising a CLO Fund and pursuant to which we agree to reimburse credit providers for a portion of losses (if any) on warehouse investments.

We and Katonah Debt Advisors have in the past entered, and may in the future enter, into "first loss" agreements in connection with warehouse credit lines to be established by Katonah Debt Advisors to fund the initial accumulation of loan investments for future CLO Funds that Katonah Debt Advisors will manage. Such agreements (referred to as "first loss agreements" or "first loss obligations") frequently relate to (i) losses as a result of individual loan investments being ineligible for purchase by the CLO Fund (typically due to a payment default on such loan) when such fund formation is completed or, (ii) if the CLO Fund has not been completed before the expiration of the warehouse credit line, the loss (if any, and net of any accumulated interest income) on the resale of such loans funded by the warehouse credit line. As a result, we may incur losses if loans and debt obligations that had been purchased in the warehouse facility become ineligible for inclusion in the CLO Fund or if a planned CLO Fund does not close.

Any unrealized losses we experience on our loan portfolio may be an indication of future realized losses, which could reduce our income available for distribution.

As a BDC, we are required to carry our investments at market value or, if no market value is ascertainable, at the fair value as determined in good faith by our Board of Directors pursuant to a valuation methodology approved by our Board of Directors. Decreases in the market values or fair values of our investments will be recorded as unrealized losses. An unrealized loss in our loan portfolio could be an indication of a portfolio company's inability to meet its repayment obligations with respect to the affected loans. This could result in realized losses in the future and ultimately in reductions of our income available for distribution in future periods.

We may experience fluctuations in our quarterly and annual operating results and credit spreads.

We could experience fluctuations in our quarterly and annual operating results due to a number of factors, some of which are beyond our control, including our ability to make investments in companies that meet our investment criteria, the interest rate payable on the debt securities we acquire, the default rate on such securities, our level of expenses, variations in and timing of the recognition of realized and unrealized gains or losses, the degree to which we encounter competition in our markets 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.

We are exposed to risks associated with changes in interest rates and spreads.

Changes in interest rates may have a substantial negative impact on our investments, the value of our securities and our rate of return on invested capital. A reduction in the interest spreads on new investments could also have an adverse impact on our net interest income. An increase in interest rates could decrease the value of any investments we hold which earn fixed interest rates, including mezzanine securities and high-yield bonds, and also could increase our interest expense, thereby decreasing our net income. An increase in interest rates due to an increase in credit spreads, regardless of general interest rate fluctuations, could also negatively impact the value of any investments we hold in our portfolio. Also, an increase in interest rates available to investors could make investment in our common stock less attractive if we are not able to increase our dividend rate, which could reduce the value of our common stock.

We may be exposed to additional risks associated with leverage.

Subject to prevailing market conditions, we intend to grow our portfolio of assets by raising additional capital, including through the prudent use of leverage available to us. We may borrow funds or issue senior securities to make additional investments. With certain limited exceptions, we are only allowed to borrow amounts or issue senior securities such that our asset coverage, as defined in the 1940 Act, is at least 200% immediately after such borrowing or issuance. The amount of leverage that we employ will depend on our management's and our Board of Directors' assessment of market 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 of stockholders, including:

- a likelihood of greater volatility of NAV and market price of our common stock than a comparable portfolio without leverage;
- exposure to increased risk of loss if we incur debt or issue senior securities to finance investments because a decrease in the value of our investments would have a greater negative impact on our returns and therefore the value of our common stock than if we did not use leverage;
- that the covenants contained in documents governing our indebtedness could restrict our operating flexibility. Such covenants may impose asset coverage or investment portfolio composition requirements that are more stringent than those imposed by the 1940 Act and could require us to liquidate investments at an inopportune time; and
- that we, and indirectly our stockholders, will bear the cost of leverage, including issuance and servicing costs (i.e., interest).

Any requirement that we sell assets at a loss to redeem or pay interest or dividends on any leverage, or for other reasons, would reduce our NAV and also make it difficult for the NAV to recover. Our Board of Directors, in their judgment, may authorize the use of leverage if they expect that the benefits to our stockholders of maintaining the leveraged position will outweigh the risks.

The debt we incur could increase the risk of investing in our Company and may contain various covenants that limit our discretion in operating our business and also include certain financial covenants.

As of January 31, 2011, we had no outstanding borrowings and thus our asset coverage ratio was above the minimum asset coverage level generally required by the 1940 Act for a BDC to incur new debt. However, we expect, in the future, to incur new debt, including in the form of borrowing facilities debt guaranteed by the Small Business Administration ("SBA"), preferred or convertible securities, and/or the senior debt securities. Such forms of financing may be secured or unsecured and may involve term or revolving credit. Lenders will have fixed dollar claims on our assets that are superior to the claims of our stockholders, and we may grant a security interest in our assets in connection with our borrowings. In the case of a liquidation event, those lenders would receive proceeds before our stockholders. In addition, borrowings, 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. Leverage is generally considered a speculative investment technique. If the value of our assets increases, then leveraging would cause the net asset value attributable to our common stock to increase more than it otherwise would have had we not leveraged. Conversely, if the value of our assets decreases, leveraging would cause the net asset value attributable to our common stock to decline more than it otherwise would have had we not leveraged. Similarly, any increase in our revenue in excess of interest expense on our borrowed funds would cause our net income to increase more than it would without the leverage. Any decrease in our revenue would cause our net income to decline more than it would have had we not borrowed funds and could negatively affect our ability to make distributions on our common stock. Our ability to service any debt that we incur will depend largely on our financial performance and will be subject to prevailing economic conditions and competitive pressures.

As a BDC, we generally are required to meet a coverage ratio of total assets to total borrowings and other senior securities, which include non-SBA guaranteed borrowings and any preferred stock we may issue in the future, of at least 200%. If this ratio declines below 200%, we may not be able to incur additional debt and may need to sell a portion of our investments to repay some debt when it is disadvantageous to do so, and we may not be able to make distributions.

If market constraints prevent us from obtaining debt or additional equity capital, our liquidity could be adversely affected, our business prospects could be negatively impacted, we could lose key employees and our operating results could be negatively affected.

Recent economic and capital market conditions in the U.S. have resulted in a severe reduction in the availability of debt and equity capital for the market as a whole, and financial services firms in particular. These conditions have constrained us and other companies in the financial services sector, limiting or completely preventing access to markets for debt and equity capital needed to maintain operations, continue investment originations and to grow. Reflecting concern about the stability of the financial markets, many lenders and institutional investors have reduced or ceased providing funding to borrowers. This market turmoil and tightening of credit has led to increased market volatility and widespread reduction of business activity generally. If we are unable to obtain new debt or additional equity capital, our liquidity may be impacted. We currently have no credit facility available to us. If these conditions continue for a prolonged period of time, or worsen in the future, we could lose key employees and our business prospects could be negatively impacted. Even if we are able to incur new debt, we may not be able to do so on favorable terms. In addition, the debt or equity capital that will be available, if at all, may be at a high cost and/or on unfavorable terms and conditions. Equity capital is, and may continue to be, difficult to raise because, subject to some limited exceptions, we are not generally able to issue and sell our common stock at a price below NAV per share without stockholder approval. In addition, issuing equity at depressed stock prices can be dilutive to our stockholders. These events and our inability to raise capital have resulted in a reduction in new originations, curtailed our ability to grow and have had a negative impact on our liquidity and operating results. The continued inability to raise additional capital could further constrain our liquidity, negatively impact our business prospects, cause the departure of key employees and negatively impact our operating results.

Because we intend to continue to distribute substantially all of our income and net realized capital gains to our stockholders, we will need additional capital to finance our growth.

In order to qualify as a RIC, to avoid payment of excise taxes and to minimize or avoid payment of income taxes, we intend to continue to distribute to our stockholders substantially all of our net ordinary income and realized net capital gains except for certain net long-term capital gains (which we may retain, pay applicable income taxes with respect thereto, and elect to treat as deemed distributions to our stockholders). As a BDC, in order to incur new debt, we are generally required to meet a coverage ratio of total assets to total senior securities, which includes all of our borrowings and any preferred stock we may issue in the future, of at least 200%, as measured immediately after issuance of such security. This requirement limits the amount that we may borrow. Because we will continue to need capital to grow our loan and investment portfolio, this limitation may prevent us from incurring debt and require us to issue additional equity at a time when it may be disadvantageous to do so. We cannot assure that debt and equity financing will be available to us on favorable terms, or at all, and debt financings may be restricted by the terms of such borrowings. In addition, as a BDC, we are generally not permitted to issue equity securities priced below NAV without stockholder approval. If additional funds are not available to us, we could be forced to continue to curtail or cease new lending and investment activities, and our NAV could decline.

Our Board of Directors may change our investment objective, operating policies and strategies without prior notice or stockholder approval.

Our Board of Directors has the authority to modify or waive certain of our operating policies and strategies without prior notice (except as required by the 1940 Act) and without stockholder approval. However, absent stockholder approval, we may not change the nature of our business so as to cease to be, or withdraw our election as, a BDC. We cannot predict the effect any changes to our current operating policies and strategies would have on our business, operating results and value of our stock. Nevertheless, the effects may adversely affect our business and impact our ability to make distributions.

Recent regulatory changes impact the operations of Katonah Debt Advisors and our ownership thereof.

Katonah Debt Advisors, our wholly-owned asset manager that manages CLO Funds, relies on an exemption from registration as an investment adviser set forth in Section 203(b)(3) of the Investment Advisers Act of 1940, as amended (the "Advisers Act'), which provides generally that an investment adviser with fewer than 15 clients is not required to register with the SEC (i.e., the "private adviser" exemption). However, as a result of the elimination of the "private adviser" exemption by the Private Fund Investment Advisers Registration Act of 2010, we expect that Katonah Debt Advisors will be required to register as an investment adviser under the Advisers Act. Certain provisions of the 1940 Act applicable to BDCs may prohibit BDCs from purchasing or otherwise acquiring any security issued by or any other interest in the business of a person who is a registered investment adviser. If Katonah Debt Advisors is required to register as an investment adviser under the Advisers Act, and if the 1940 Act were so interpreted, the Company may be in violation of the 1940 Act unless the Commission grants the Company exemptive relief. The Company intends to apply for this exemptive relief, however, if the Company is not successful in obtaining such exemptive relief before Katonah Debt Advisors is required to register as an investment adviser, or at all, then the Company may be in violation of the 1940 Act or Katonah Debt Advisors may be in violation of the Advisers Act until the Company is able to obtain the necessary exemptive relief or otherwise resolve the matter. The Company cannot assure you that it will be able to obtain the necessary exemptive relief in the timeframe required, or at all.

Our businesses may be adversely affected by litigation and regulatory proceedings, including those that are currently pending.

From time to time, we may be subject to legal actions as well as various regulatory, governmental and law enforcement inquiries, investigations and subpoenas. In any such claims or actions, demands for substantial monetary damages may be asserted against us and may result in financial liability or an adverse effect on our reputation among investors. We may be unable to accurately estimate our exposure to litigation risk when we record balance sheet reserves for probable loss contingencies. As a result, any reserves we establish to cover any settlements or judgments may not be sufficient to cover our actual financial exposure, which may have a material impact on our results of operations or financial condition. In regulatory enforcement matters, claims for disgorgement, the imposition of penalties and the imposition of other remedial sanctions are possible.

We are currently parties in ongoing litigation and regulatory proceedings. As described in greater detail in "Item 3. Legal Proceedings" below, pending proceedings involving us and/or our directors and officers include three purported class action lawsuits filed by our stockholders and an SEC investigation, which are at a preliminary stage, and a derivative action filed by a shareholder, which has been dismissed and in which the stockholder has appealed, all of which relate to the valuation methodology and procedures used by us to value our investments and the restatement to our financial statements for the year ended December 31, 2008 (and the quarterly periods included in such year) and the quarterly periods ended March 31, 2009 and June 30, 2009. While we believe that we have meritorious defenses in these proceedings and that the outcomes should not materially impact us, we anticipate continued elevated legal and related costs as the ultimate outcomes of the matters are uncertain.

In view of the inherent difficulty of predicting the outcome of legal actions and regulatory matters, we cannot provide assurance as to the outcome of any pending matter or, if resolved adversely, the costs associated with any such matter, particularly where the claimant seeks very large or indeterminate damages or where the matter presents novel legal theories, involves a large number of parties or is at a preliminary stage. The resolution of any such matters may be time consuming, expensive, and may distract management from the conduct of our business. The resolution of certain pending legal actions or regulatory matters, if unfavorable, could have a material adverse effect on our results of operations for the quarter in which such actions or matters are resolved or a reserve is established.

Risks Related to Our Investments

Our investments may be risky, and you could lose all or part of your investment.

We invest primarily in senior secured term loans, mezzanine debt and selected equity investments issued by middle market companies.

Secured Loans. When we extend secured term loans, we generally take a security interest (either as a first lien position or as a second lien position) in the available assets of these portfolio companies, including the equity interests of their subsidiaries, which we expect to assist in mitigating the risk that we will not be repaid. However, there is a risk that the collateral securing our loans may decrease in value over time, may be difficult to sell in a timely manner, may be difficult to appraise and may fluctuate in value based upon the success of the business and market conditions, including as a result of the inability of the portfolio company to raise additional capital, and, in some circumstances, our lien could be subordinated to claims of other creditors. In addition, deterioration in a portfolio company's financial condition and prospects, including its inability to raise additional capital, may be accompanied by deterioration in the value of the collateral for the loan. Consequently, the fact that a loan is secured does not guarantee that we will receive principal and interest payments according to the loan's terms, or at all, or that we will be able to collect on the loan should we be forced to exercise our remedies.

Mezzanine Debt. Our mezzanine debt investments generally are subordinated to senior loans and generally are unsecured. This may result in an above average amount of risk and volatility or loss of principal.

These investments may entail additional risks that could adversely affect our investment returns. To the extent interest payments associated with such debt are deferred, such debt is subject to greater fluctuations in value based on changes in interest rates and such debt could subject us to phantom income. Since we generally do not receive any cash prior to maturity of the debt, the investment is of greater risk.

Equity Investments. We have made and expect to make selected equity investments. In addition, when we invest in senior secured loans or mezzanine debt, we may acquire warrants in the equity of the portfolio company. Our goal is ultimately to dispose of such equity interests and realize gains upon our disposition of such interests. However, the equity interests we receive may not appreciate in value and, in fact, may decline in value. Accordingly, we may not be able to realize gains from our equity interests, and any gains that we do realize on the disposition of any equity interests may not be sufficient to offset any other losses we experience.

Risks Associated with Middle Market Companies. Investments in middle market companies also involve a number of significant risks, including:

- limited financial resources and inability to meet their obligations, which may be accompanied by a deterioration in the value of any collateral and a reduction in the likelihood of our realizing the value of any guarantees we may have obtained in connection with our investment;
- 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;
- dependence on 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 material adverse impact on our portfolio company and, in turn, on us;
- less predictable operating results, being parties to litigation from time to time, engaging in rapidly changing businesses with products subject to a substantial risk of obsolescence and requiring substantial additional capital expenditures to support their operations, finance expansion or maintain their competitive position;
- difficulty accessing the capital markets to meet future capital needs; and
- generally less publicly available information about their businesses, operations and financial condition.

Our portfolio investments for which there is no readily available market, including our investment in Katonah Debt Advisors and our investments in CLO Funds, are recorded at fair value as determined in good faith by our Board of Directors. As a result, there is uncertainty as to the value of these investments.

Our investments consist primarily of securities issued by privately-held companies, the fair value of which is not readily determinable. In addition, we are not permitted to maintain a general reserve for anticipated loan losses. Instead, we are required by the 1940 Act to specifically value each investment and record an unrealized gain or loss for any asset that we believe has increased or decreased in value. We value these securities at fair value as determined in good faith by our Board of Directors pursuant to a valuation methodology approved by our Board of Directors. These valuations are initially prepared by our management and reviewed by our Valuation Committee, which uses its best judgment in arriving at the fair value of these securities. However, the Board of Directors retains ultimate authority to determine the appropriate valuation for each investment. From time to time, our Board of Directors has used the services of an independent valuation firm to aid it in determining fair value, including in the case of our investments in CLO Funds and in Katonah Debt Advisors. Where applicable, an independent valuation firm provides third-party valuation consulting services, which typically consist of certain limited procedures that we identify and request an independent valuation firm to perform. The types of factors that may be considered in valuing 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 and other relevant factors. Our investment in Katonah Debt Advisors is carried at fair value, which is determined after taking into consideration a percentage of assets under management and a discounted cash flow model incorporating different levels of discount rates depending on the hierarchy of fees earned (including the likelihood of realization of senior, subordinate and incentive fees) and prospective modeled performance. Such valuation includes an analysis of comparable asset management companies. Because such valuations, and particularly valuations of private investments and private companies, are inherently uncertain and may be based on estimates, our determinations of fair value may differ materially from the values that would be assessed if a ready market for these securities existed. Our NAV could be adversely affected if our determinations regarding the fair value of our illiquid investments were materially higher than the values that we ultimately realize upon the disposal of such securities.

Following our engagement of Grant Thornton, we and our Audit Committee concluded that the we would have to restate our previously issued financial statements for the year ended December 31, 2008 (and the quarterly periods included in such year) as well as the quarterly periods ended March 31, 2009 and June 30, 2009. We and our Audit Committee determined that such restatement was necessary to correct errors in the application of accounting for the fair value of our illiquid investments and the revenue recognition for certain non-cash PIK investments, which errors impact the amount of unrealized gains (losses) reported for our illiquid investments, which affects the calculation of our NAV and net income, and also impact net investment income as well as the cost basis and the net change in unrealized appreciation on certain non-cash PIK investments. In connection with the restatement, we have revised the valuation procedures applied to our illiquid investments and our accounting for our non-cash PIK investments.

We are subject to additional risks in light of the restatement of our prior period financial statements.

We have previously restated our financial statements for the year ended December 31, 2008 (and the quarterly periods included in such year) as well as the quarterly periods ended March 31, 2009 and June 30, 2009. The restatement of our financial statements was due to errors in the application of accounting for the fair value of our illiquid investments and the revenue recognition for certain non-cash PIK investments, which errors impact the amount of unrealized gains (losses) reported for our illiquid investments, which affects the calculation of our NAV and net income, and also impact net investment income as well as the cost basis and the net change in unrealized appreciation on certain non-cash PIK investments. The error related to fair value measurements was identified through the use and weighting of additional valuation techniques and a broader consideration of secondary market inputs, and with regard to our financial statements for the periods noted above, resulted from the material weaknesses in our internal control over financial reporting. A “material weakness” is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the annual or interim financial statements would not be prevented or detected on a timely basis. This restatement has exposed us to certain legal and regulatory actions described in "Item 3. Legal Proceedings" below and could expose us to additional legal or regulatory actions. In addition, the defense of any such actions could cause the diversion of management's attention and resources, and we could be required to pay damages to settle such actions if any such actions are not resolved in our favor. Even if resolved in our favor, such actions could cause us to incur significant legal and other expenses. We believe that we have addressed the material weaknesses through the adoption of the revised valuation procedures and the implementation of a review process in 2010. We may be the subject of negative publicity focusing on the restatement and negative reactions from shareholders and others with whom we do business.

We are a non-diversified investment company within the meaning of the 1940 Act, and therefore we may invest a significant portion of our assets in a relatively small number of issuers, which subjects us to a risk of significant loss if any of these issuers defaults on its obligations under any of its debt instruments or as a result of a downturn in the particular industry.

We are classified as a non-diversified investment company within the meaning of the 1940 Act, and therefore we may invest a significant portion of our assets in a relatively small number of issuers in a limited number of industries. As of December 31, 2010, our largest investment, our 100% equity interest in Katonah Debt Advisors, equaled approximately 22% of the fair value of our investments. Beyond the asset diversification requirements associated with our qualification as a RIC (as described further in "Item 1. Business — Certain United States Federal Income Tax Considerations"), we do not have fixed guidelines for diversification, and while we are not targeting any specific industries, relatively few industries may become significantly represented among our investments. In accordance with our current policy, we do not "concentrate" our investments, that is, invest 25% or more of our assets in any particular industry (determined at the time of investment). However, to the extent that we assume large positions in the securities of a small number of issuers, our NAV may fluctuate to a greater extent than that of a diversified investment company as a result of changes in the financial condition or the market's assessment of the issuer or a downturn in any particular industry. We may also be more susceptible to any single economic or regulatory occurrence than a diversified investment company.

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

Many of our portfolio companies may be susceptible to economic slowdowns or recessions and may be unable to repay our loans 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 may also 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.

Defaults by our portfolio companies could harm our operating results.

A portfolio company's failure to satisfy financial or operating covenants imposed by us or other debt holders could lead to defaults and, potentially, acceleration of the time when the loans are due and foreclosure on its secured assets. Such events could trigger cross-defaults under other agreements and jeopardize a portfolio company's ability to meet its obligations under the debt that we hold and the value of any equity securities we own. We may incur expenses to the extent necessary to seek recovery upon default or to negotiate new terms with a defaulting portfolio company.

When we are a debt or minority equity investor in a portfolio company, which generally is the case, we may not be in a position to control the entity, and its management may make decisions that could decrease the value of our investment.

Most of our investments are either debt or minority equity investments in our portfolio companies. Therefore, we are subject to the risk that a portfolio company may make business decisions with which we disagree, and the stockholders and management of such company 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. In addition, we generally are not in a position to control any portfolio company by investing in its debt securities.

Prepayments of our debt investments by our portfolio companies could negatively impact our operating results.

We are subject to the risk that the investments we make in our portfolio companies may be repaid prior to maturity. When this occurs, we generally reinvest these proceeds in temporary investments, pending their future investment in new portfolio companies. These temporary investments typically have substantially lower yields than the debt being prepaid and we could experience significant delays in reinvesting these amounts. Any future investment in a new portfolio company may also be at lower yields than the debt that was repaid. Consequently, our results of operations could be materially adversely affected if one or more of our portfolio companies elects to prepay amounts owed to us. Additionally, prepayments could negatively impact our return on equity, which could result in a decline in the market price of our common stock.

Our portfolio companies may incur debt that ranks equal with, or senior to, our investments in such companies.

We invest primarily in debt securities issued by our portfolio companies. In some cases portfolio companies are permitted to have other debt that ranks equal with, or senior to, the debt securities in which we invest. By their terms, such debt instruments may provide that the holders thereof are entitled to receive payment of interest or principal on or before the dates on which we are entitled to receive payments in respect of the debt securities in which we invest. Also, in the event of insolvency, liquidation, dissolution, reorganization or bankruptcy of a portfolio company, holders of debt instruments 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 such senior creditors, such portfolio company may not have any remaining assets to use for repaying its obligation to us. In the case of debt ranking equal with debt securities in which we invest, we would have to share on an equal basis any distributions with other creditors holding such debt in the event of an insolvency, liquidation, dissolution, reorganization or bankruptcy of a portfolio company.

There may be circumstances where our debt investments could be subordinated to claims of other creditors or we could be subject to lender liability claims.

Even though we may have structured certain of our investments as senior loans, if one of our portfolio companies were to go bankrupt, depending on the facts and circumstances, including the size of our investment and the extent to which we actually provided managerial assistance to that portfolio company, a bankruptcy court might recharacterize our debt investment and subordinate all or a portion of our claim to that of other creditors. In addition, lenders can be subject to lender liability claims for actions taken by them where they become too involved in the borrower’s business or exercise control over the borrower. It is possible that we could become subject to a lender’s liability claim, including as a result of actions taken in rendering significant managerial assistance.

Our investments in equity securities involve a substantial degree of risk.

We may purchase common stock and other equity securities, including warrants. Although equity securities have historically generated higher average total returns than fixed-income securities over the long term, equity securities have also experienced significantly more volatility in those returns. The equity securities we acquire may fail to appreciate and may decline in value or become worthless, and our ability to recover our investment depends on our portfolio company's success. Investments in equity securities involve a number of significant risks, including the risk of further dilution as a result of additional issuances, inability to access additional capital and failure to pay current distributions. Investments in preferred securities involve special risks, such as the risk of deferred distributions, credit risk, illiquidity and limited voting rights.

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

We invest in securities issued by private companies. These securities may be subject to legal and other restrictions on resale or otherwise be less liquid than publicly-traded securities. The illiquidity of these investments may make it difficult for us to sell these investments when desired. 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 had previously recorded these investments. Our investments are usually subject to contractual or legal restrictions on resale or are otherwise illiquid because there is usually no established trading market for such investments. The illiquidity of most of our investments may make it difficult for us to dispose of them at a favorable price, and, as a result, we may suffer losses.

We may not receive all or a portion of the income we expect to continue to receive from Katonah Debt Advisors.

We expect to receive distributions of recurring fee income, after the payment of its expenses, from the asset management activities of Katonah Debt Advisors. However, the existing asset management agreements pursuant to which Katonah Debt Advisors receives such fee income from the CLO Funds for which it serves as manager may be terminated for "cause" by the holders of a majority of the most senior class of securities issued by such CLO Funds and the holders of a majority of the subordinated securities issued by such CLO Funds. "Cause" is defined in the asset management agreements to include a material breach by Katonah Debt Advisors of the indenture governing the applicable CLO Fund, breaches by Katonah Debt Advisors of certain specified provisions of the indenture, material breaches of representations or warranties made by Katonah Debt Advisors, bankruptcy or insolvency of Katonah Debt Advisors, fraud or criminal activity on the part of Katonah Debt Advisors or an event of default under the indenture governing the CLO Funds. We expect that future asset management agreements will contain comparable provisions. Further, a significant portion of the asset management fees payable to Katonah Debt Advisors under the asset management agreements are subordinated to the prior payments of interest on the senior securities issued by the CLO Funds. If the asset management agreements are terminated or the CLO Funds do not generate enough income or otherwise have insufficient residual cash flow due to diversion of cash as a result of the failure by the CLO Funds to satisfy certain restrictive covenants contained in their indenture agreements to pay the subordinated management fees, we will not receive the fee income that we expect to continue to receive from Katonah Debt Advisors, which will reduce income available to make distributions to our stockholders. At December 31, 2010, Katonah Debt Advisors was receiving all (senior and subordinate) management fees payable by the CLO Funds managed by it.

We may not receive any return on our investment in the CLO Funds in which we have invested and we may be unable to raise additional CLO Funds.

As of December 31, 2010, we had $45 million invested in the subordinated securities or preferred shares issued by CLO Funds managed by Katonah Debt Advisors and certain other third party asset managers. Subject to market conditions, we expect to continue to acquire subordinated securities in the future in CLO Funds managed by Katonah Debt Advisors and/or third party managers. These subordinated securities are the most junior class of securities issued by the CLO Funds and are subordinated in priority of payment to every other class of securities issued by these CLO Funds. Therefore, they only receive cash distributions if the CLO Funds have made all cash interest payments to all other debt securities issued by the CLO Fund. The subordinated securities are also unsecured and rank behind all of the secured creditors, known or unknown, of the CLO Fund, including the holders of the senior securities issued by the CLO Fund. Consequently, to the extent that the value of a CLO Fund's loan investments has been reduced as a result of conditions in the credit markets, or as a result of default loans or individual fund assets, the value of the subordinated securities at their redemption could be reduced. Additionally, we may not be able to continue to complete new CLO Funds due to prevailing CLO market conditions or other factors.

Risks Related to Our Operation as a BDC

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

We are prohibited under the 1940 Act from participating in certain transactions with certain of our affiliates without the prior approval of our independent directors and, in some cases, the SEC. 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 generally are prohibited from buying or selling any security from or to such affiliate, absent the prior approval of our independent directors. The 1940 Act also prohibits certain "joint" transactions with certain of our affiliates, which could include investments in the same portfolio company (whether at the same or different times), without prior approval of our independent directors and, in some cases, the SEC. If a person acquires more than 25% of our voting securities, we are prohibited from buying or selling any security from or to such person or certain of that person's affiliates, or entering into prohibited joint transactions with such persons, absent the prior approval of the SEC. Similar restrictions limit our ability to transact business with our officers or directors or their affiliates. As a result of these restrictions, we may be prohibited from buying or selling any security from or to any portfolio company of a private equity fund managed by Kohlberg & Co. without the prior approval of the SEC. However, we may co-invest on a concurrent basis with Kohlberg & Co. or any of our affiliates, subject to compliance with existing regulatory guidance, applicable regulations and our allocation procedures. Certain types of negotiated co-investments may be made only if we receive an order from the SEC permitting us to do so. There can be no assurance that any such order will be applied for or, if applied for, obtained.

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

Our business requires a substantial amount of additional capital. We may acquire additional capital from the issuance of senior securities or other indebtedness, the issuance of additional shares of our common stock or from securitization transactions. However, we may not be able to raise additional capital in the future on favorable terms or at all. We may issue debt securities or preferred securities, which we refer to collectively as "senior securities," and we may borrow money from banks or other financial institutions, up to the maximum amount permitted by the 1940 Act. The 1940 Act permits us to issue senior securities or incur indebtedness only in amounts such that our asset coverage, as defined in the 1940 Act, equals at least 200% immediately after such issuance or incurrence. With respect to certain types of senior securities, we must make provisions to prohibit any dividend distribution to our stockholders or the repurchase of certain of our securities, unless we meet the applicable asset coverage ratios at the time of the dividend distribution or repurchase. If the value of our assets declines, we may be unable to satisfy the asset coverage test. If that happens, we may be required to liquidate a portion of our investments and repay a portion of our indebtedness at a time when such sales may be disadvantageous.

- *Senior Securities*. As a result of issuing senior securities, we would also be exposed to typical risks associated with leverage, including an increased risk of loss. If we issue preferred securities they would rank "senior" to common stock in our capital structure. Preferred stockholders would have separate voting rights and may have rights, preferences or privileges more favorable than those of our common stock. Furthermore, the issuance of preferred securities could have the effect of delaying, deferring or preventing a transaction or a change of control that might involve a premium price for our common stockholders or otherwise be in your best interest.
- *Additional Common Stock*. Our Board of Directors may decide to issue common stock to finance our operations rather than issuing debt or other senior securities. As a BDC, we are generally not able to issue our common stock at a price below NAV without first obtaining required approvals from our stockholders and our independent directors. In any such case, the price at which our securities are to be issued and sold may not be less than a price, that in the determination of our Board of Directors, closely approximates the market value of such securities (less any commission or discount). We may also make rights offerings to our stockholders at prices per share less than the NAV per share, subject to the 1940 Act. If we raise additional funds by issuing more common stock or senior securities convertible into, or exchangeable for, our common stock, the percentage ownership of our stockholders at that time would decrease, and you may experience dilution.

- *Securitization*. In addition to issuing securities to raise capital as described above, we may securitize a portion of the loans we may obtain to generate cash for funding new investments. If we are unable to successfully securitize our loan portfolio our ability to grow our business and fully execute our business strategy and our earnings (if any) may be adversely affected. Moreover, even successful securitization of our loan portfolio might expose us to losses, as the residual loans in which we do not sell interests tend to be those that are riskier and more apt to generate losses.

Changes in the laws or regulations governing our business, or changes in the interpretations thereof, and any failure by us to comply with these laws or regulations, could negatively affect the profitability of our operations.

Changes in the laws or regulations or the interpretations of the laws and regulations that govern BDCs, RICs or non-depository commercial lenders, could significantly affect our operations and our cost of doing business. We are subject to federal, state and local laws and regulations and are subject to judicial and administrative decisions that affect our operations, including our loan originations, maximum interest rates, fees and other charges, disclosures to portfolio companies, the terms of secured transactions, collection and foreclosure procedures and other trade practices. If these laws, regulations or decisions change, or if we expand our business into jurisdictions that have adopted more stringent requirements than those in which we currently conduct business, we may have to incur significant expenses in order to comply or we might have to restrict our operations. In addition, if we do not comply with applicable laws, regulations and decisions, we may lose licenses needed for the conduct of our business and be subject to civil fines and criminal penalties, any of which could have a material adverse effect upon our business, results of operations or financial condition.

If we do not invest a sufficient portion of our assets in “qualifying assets,” we could fail to qualify as a BDC or be precluded from investing according to our current business strategy.

As a BDC, we may not acquire any assets other than “qualifying assets” for purposes of the 1940 Act unless, at the time of and after giving effect to such acquisition, at least 70% of our total assets are “qualifying assets.” See “Item 1. Business — Regulation.”

We believe that most of the senior loans and mezzanine investments that we acquire constitute “qualifying assets.” However, investments in the equity securities of CLO Funds generally do not constitute “qualifying assets,” and we may invest in other assets that are not “qualifying assets.” If we do not invest a sufficient portion of our assets in “qualifying assets,” we may be precluded from investing in what we believe are attractive investments or could lose our status as a BDC, which would have a material adverse effect on our business, financial condition and results of operations. These restrictions could also prevent us from making investments in the equity securities of CLO Funds, which could limit Katonah Debt Advisors’ ability to organize new CLO Funds. Similarly, these rules could prevent us from making follow-on investments in existing portfolio companies (which could result in the dilution of our position) or could require us to dispose of investments at inappropriate times in order to come into compliance with the 1940 Act. If we need to dispose of such investments quickly, it would be difficult to dispose of such investments on favorable terms. For example, we may have difficulty in finding a buyer and, even if we do find a buyer, we may have to sell the investments at a substantial loss.

If we are unable to qualify as a RIC under Subchapter M of the Code, we will be subject to corporate-level U.S. federal income tax, which will adversely affect our results of operations and financial condition.

Provided we qualify as a RIC, we will generally not be subject to corporate-level U.S. federal income taxes on income distributed to our stockholders as dividends in accordance with the timing requirements of the Code. We will not continue to qualify for pass-through tax treatment as a RIC, and thus will be subject to corporate-level U.S. federal income taxes, if we are unable to comply with the source-of-income, asset diversification and distribution requirements contained in the Code, or if we fail to maintain our election to be regulated as a BDC under the 1940 Act. Failure to meet the requirements for tax treatment as a RIC would subject us to taxes, which would reduce the return on your investment. As such, our failure to qualify for tax treatment as a RIC would have a material adverse effect on us, the NAV of our common stock and the total return obtainable from your investment in our common stock. We may, from time to time, organize and conduct the business of our wholly-owned portfolio company, Katonah Debt Advisors, through additional direct or indirect wholly-owned subsidiaries which may, in some cases, be taxable as corporations. For additional information see "Item 1. Business — Regulation" and "Item 1. Business — Certain United States Federal Income Tax Considerations."

Item 1B. ***Unresolved Staff Comments***

None.

Item 2. ***Properties***

We do not own any real estate or other real property. Our wholly-owned portfolio company, Katonah Debt Advisors, is the lessee for our principal headquarters at 295 Madison Avenue, 6th Floor, New York, New York 10017. We have entered into an Overhead Allocation Agreement with Katonah Debt Advisors which provides for the sharing of the expenses under the lease agreement.

Item 3. ***Legal Proceedings***

Class Actions against the Company and Certain Directors and Officers

The Company and certain directors and officers are named as defendants in three putative class actions pending in the Southern District of New York brought by stockholders of the Company and filed in December 2009 and January 2010. The complaints in these three actions allege violations of Sections 10 and 20 of the Exchange Act based on the Company's disclosures of its year-end 2008 and first- and second-quarter 2009 financial statements. The Company believes that the above-mentioned suits are without merit and will defend each vigorously.

In addition, the Company and certain directors and officers were also named as defendants in a derivative action filed on March 2, 2010 in the Supreme Court of New York, County of New York. The complaint in this action purported to state causes of action for breaches of fiduciary duties, unjust enrichment, abuse of control, gross mismanagement, and corporate waste. On October 20, 2010, the court dismissed the complaint, and found, among other things, that the plaintiff had not alleged that any of the Company's directors "'knowingly' misrepresented or permitted others to misrepresent the Company's financial condition," or that the directors were confronted with "red flags" sufficient to put them on notice of potential problems with the Company's investment valuations so as to excuse plaintiff's requirement under Delaware law to make a demand on the Company's board before filing suit. On January 12, 2011, the court entered the final judgment dismissing the complaint and the plaintiff has subsequently filed a notice of appeal.

SEC Investigation

On January 11, 2010, the staff of the SEC's Division of Enforcement informed the Company that it was conducting an informal inquiry. The focus of the inquiry concerns the valuation methodology and procedures used by the Company to value its investments. On April 30, 2010, the SEC Staff advised the Company that a formal order of private investigation had been issued and that the informal inquiry was now a formal investigation. A subpoena has been issued to the Company in connection with the formal investigation. The subpoena requests that the Company produce documents that primarily relate to the valuation methodology and procedures used by the Company to value its investments. Since January 2010, the Company has been providing documents in response to the informal inquiry and the subpoena. The SEC Staff has also requested testimony from Company representatives. The Company is cooperating fully with the SEC Staff's investigation. The Company cannot predict the outcome of, or the timeframe for, the conclusion of this investigation.

Except as set forth above, neither the Company, nor any of its subsidiaries, is currently a party to any material legal proceedings, other than routine litigation and administrative proceedings arising in the ordinary course of business. Such proceedings are not expected to have a material adverse effect on the business, financial condition, or results of the Company's operations.

Item 4. ***[Removed and Reserved]***

PART II

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

PRICE RANGE OF COMMON STOCK

Our common stock is quoted on The NASDAQ Global Select Market under the symbol "KCAP." We completed our initial public offering on December 11, 2006 at an initial public offering price of $15.00 per share. Prior to such date there was no public market for our common stock.

The following table sets forth the range of high and low closing sales prices per share of our common stock as reported on The NASDAQ Global Select Market in respect of the periods indicated. The stock quotations are interdealer quotations and do not include markups, markdowns or commissions and may not necessarily represent actual transactions.

Quarterly Stock Prices for 2009 and 2010

	High	Low	Close	NAV(1)
2010:				
Fourth quarter	$ 7.10	$ 6.34	$ 6.97	$ 8.21
Third quarter	$ 6.69	$ 4.55	$ 6.69	$ 8.84
Second quarter	$ 5.88	$ 4.43	$ 5.01	$ 9.20
First quarter	$ 5.71	$ 3.79	$ 5.66	$ 9.62
2009:				
Fourth quarter	$ 5.99	$ 4.56	$ 4.56	$ 9.56
Third quarter	$ 6.71	$ 4.42	$ 6.03	$ 9.93
Second quarter	$ 6.32	$ 3.14	$ 6.32	$ 9.73
First quarter	$ 4.30	$ 1.26	$ 3.06	$ 9.41

(1) NAV per share is determined as of the last day in the relevant quarter and therefore may not reflect the NAV per share on the date of the high and low closing sales prices.

We began paying quarterly dividends in our first full quarter of operations following our IPO. See "Management's Discussion and Analysis of Financial Condition and Results of Operations" and Note 7 — "Distributable Tax Income" from our Notes to the Financial Statements included herein. The table below provides information relating to dividends we paid in respect of the periods indicated.

Dividend Declarations

	Dividend	Declaration Date	Record Date	Pay Date
2010:				
Fourth quarter	$ 0.17	12/13/2010	12/24/2010	1/29/2011
Third quarter	0.17	9/20/2010	10/8/2010	10/29/2010
Second quarter	0.17	6/23/2010	7/7/2010	7/29/2010
First quarter	0.17	3/19/2010	4/7/2010	4/29/2010
Total declared for 2010	$ 0.68			
2009:				
Fourth quarter	$ 0.20	12/15/2009	12/28/2009	1/25/2010
Third quarter	0.24	9/24/2009	10/9/2009	10/29/2009
Second quarter	0.24	6/12/2009	7/9/2009	7/29/2009
First quarter	0.24	3/23/2009	4/8/2009	4/29/2009
Total declared for 2009	$ 0.92			

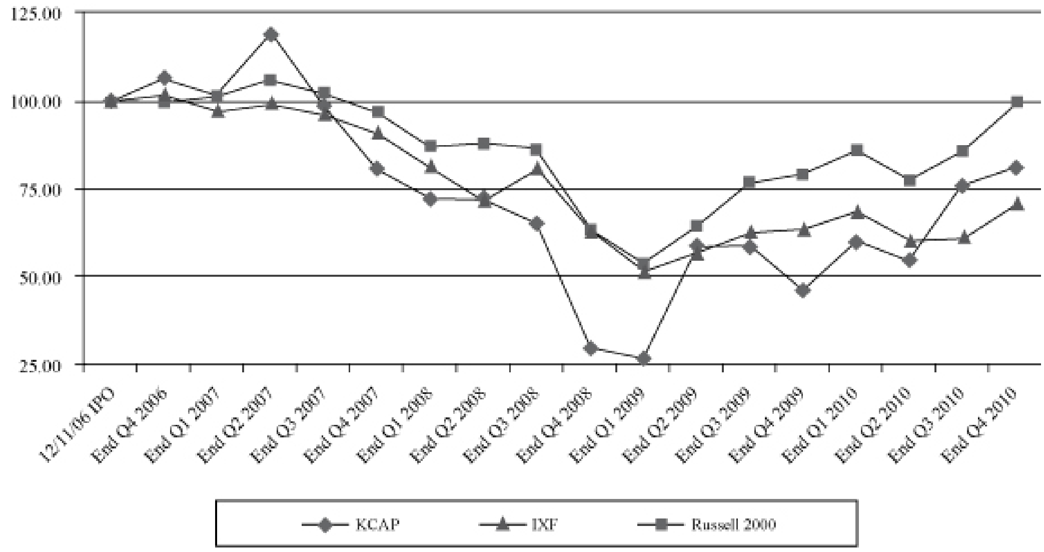
TABLE OF CONTENTS

Performance Graph

The following graph compares the return on our common stock with that of the Russell 2000 Index and the Nasdaq Financial 100 Index (IXF), for the period December 11, 2006 (the date of our initial public offering) to December 31, 2010. The graph assumes that, on December 11, 2006, a person invested $100 in each of our common stock and the Russell 2000 Index. The graph measures total shareholder return, which takes into account both changes in stock price and dividends. It assumes that dividends are reinvested.

Shareholder Return Performance Graph

Cumulative Total Return Since Initial Public Offering(1)
(Through December 31, 2010)



(1) Total return includes reinvestment of dividends through December 31, 2010. The IXF is an index of diversified financial sector stocks and, as such, the Company believes that it is representative of our industry. The Russell 2000 is a broad based equity market index that tracks companies with a market capitalization that the Company believes are comparable to Kohlberg Capital.

HOLDERS

As of December 31, 2010, there were 21 shareholders of record of our common stock and approximately 9,610 beneficial shareholders of the Company.

SALES OF UNREGISTERED SECURITIES

We did not sell any securities during the period covered by this report that were not registered under the Securities Act. However, we issued 301,663 shares of common stock pursuant to a dividend reinvestment plan. See Note 9, “Stockholders’ Equity,” of our Notes to the Consolidated Financial Statements included herein.

ISSUER PURCHASES OF EQUITY SECURITIES

In November 2008, the Board of Directors approved a $5 million share repurchase plan. Any share repurchases are subject to timing restrictions and other applicable regulations. We did not repurchase any shares of our common stock during the year ended December 31, 2010.

DIVIDEND POLICY

We intend to continue to distribute quarterly dividends to our stockholders. Our quarterly dividends, if any, will be determined by our Board of Directors. To maintain our RIC status, we must timely distribute an amount equal to 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, reduced by deductible expenses, out of the assets legally available for distribution, for each year. To avoid certain excise taxes imposed on RICs, we are generally required to distribute during each calendar year an amount at least equal to the sum of (1) 98% of our ordinary income for the calendar year, (2) 98.2% of our capital gains in excess of capital losses for the one-year period ending on October 31 of the calendar year and (3) any ordinary income and net capital gains for preceding years that were not distributed during such years. If this requirement is not met, we will be required to pay a nondeductible excise tax equal to 4% of the amount by which the required distribution amount exceeds the actual distribution for the year. The taxable income on which an excise tax is paid is generally carried forward and distributed to stockholders in the next tax year. Depending on the level of taxable income earned in a tax year, we may choose to carry forward taxable income in excess of current year distributions into the next tax year and pay a 4% excise tax on such income, to the extent required.

We cannot assure you that we will achieve results that will permit the payment of any cash distributions and, if we incur public indebtedness or issue public senior securities, we may be prohibited from making distributions if doing so causes us to fail to maintain the asset coverage ratios stipulated by the 1940 Act or if distributions are limited by the terms of any of our borrowings.

We maintain an “opt out” dividend reinvestment plan for our common stockholders. As a result, if we declare a dividend, then stockholders’ cash dividends will be automatically reinvested in additional shares of our common stock, unless they specifically “opt out” of the dividend reinvestment plan so as to receive cash dividends.

TABLE OF CONTENTS

Item 6. ***Selected Financial Data***

The following selected financial and other data for the years ended December 31, 2010, 2009, 2008, 2007, and the period December 11, 2006 (inception) through December 31, 2006 is derived from our financial statements. The data should be read in conjunction with our financial statements and notes thereto and “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” which are included in this Annual Report.

KOHLBERG CAPITAL CORPORATION

SELECTED FINANCIAL DATA

	Year Ended December 31, 2010	Year Ended December 31, 2009	Year Ended December 31, 2008	Year Ended December 31, 2007[1]	For the Period December 11, 2006 (inception) through December 31, 2010[1]
Income Statement Data:					
Interest and related portfolio income:					
Interest and Dividends	$ 24,638,631	$ 33,497,213	$ 46,208,978	$ 37,219,713	$ 1,110,109
Fees and other income	215,233	399,338	1,653,232	759,301	41,794
Dividends from affiliate asset manager	4,500,000	—	1,350,000	500,000	—
Total interest and related portfolio income	29,353,864	33,896,551	49,212,210	38,479,014	1,151,903
Expenses:					
Interest and amortization of debt issuance costs	7,088,202	9,276,563	10,925,624	7,229,597	—
Compensation	3,322,895	3,222,604	3,940,638	4,104,761	175,186
Other	7,045,648	3,066,729	3,640,031	4,385,707	487,254
Total operating expenses	17,456,745	15,565,896	18,506,293	15,720,065	662,440
Net Investment Income	11,897,119	18,330,655	30,705,917	22,758,949	489,463
Realized and unrealized gains (losses) on investments:					
Net realized gains (losses)	(17,862,984)	(15,782,121)	(575,179)	266,317	1,077
Net change in unrealized gains (losses)	(8,322,812)	31,854,736	(93,414,146)	3,116,719	4,180,000
Total net gains (losses)	(26,185,796)	16,072,615	(93,989,325)	3,383,036	4,181,077
Net increase (decrease) in net assets resulting from operations	$ (14,288,677)	$ 34,403,270	$ (63,283,408)	$ 26,141,985	$ 4,670,540
Per Share:					
Earnings per common share – basic	$ (0.63)	$ 1.56	$ (3.09)	$ 1.45	$ 0.26
Earnings per common share – diluted	$ (0.63)	$ 1.56	$ (3.09)	$ 1.45	$ 0.26
Net investment income per share – basic	$ 0.53	$ 0.83	$ 1.50	$ 1.27	$ 0.03
Net investment income per share – diluted	$ 0.53	$ 0.83	$ 1.50	$ 1.27	$ 0.03
Dividends declared per common share	$ 0.68	$ 0.92	$ 1.44	$ 1.40	$ —
Balance Sheet Data:					
Investment assets at fair value	$ 191,186,296	$ 409,105,621	$ 460,509,190	$ 521,006,947	$ 281,087,215
Total assets	$ 279,822,686	$ 439,416,057	$ 469,156,229	$ 533,141,959	$ 282,375,847
Total debt outstanding	$ 86,746,582	$ 218,050,363	$ 261,691,148	$ 255,000,000	$ —
Stockholders’ equity	$ 186,925,667	$ 213,895,724	$ 196,566,018	$ 259,068,164	$ 256,400,423
Net asset value per common share	$ 8.21	$ 9.56	$ 9.03	$ 14.38	$ 14.29
Common shares outstanding at end of year	22,767,130	22,363,281	21,771,186	18,017,699	17,946,333
Other Data:					
Investments funded[2]	11,245,300	23,482,349	109,442,643	373,852,286	191,706,724
Principal collections related to investment repayments or sales[2]	223,103,170	84,503,183	72,345,600	104,037,559	533,315
Number of portfolio investments at year end[2]	58	124	149	145	86
Weighted average yield of income producing debt investments[3]	8.6%	6.5%	7.0%	9.5%	9.0%

(1) Certain prior year amounts have been reclassified to conform to current year presentation.

(2) Does not include investments in time deposits or money markets.

(3) Weighted average yield of income producing debt investments is calculated as the average yield to par outstanding balances for investments in loans and mezzanine debt. The yields on CLO equities and investment in our wholly-owned portfolio manager, Katonah Debt Advisors, are excluded.

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

The following discussion should be read in conjunction with our financial statements and related notes and other financial information appearing elsewhere in this Annual Report. In addition to historical information, the following discussion and other parts of this Annual Report 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 "Item 1A. Risk Factors" and "Note about Forward-Looking Statements" appearing elsewhere herein.

OVERVIEW

We are an internally managed, non-diversified closed-end investment company that has elected to be regulated as a business development company ("BDC") under the Investment Company Act of 1940, as amended (the "1940 Act"). We originate, structure and invest in senior secured term loans, mezzanine debt and selected equity securities primarily in privately-held middle market companies. We define the middle market as comprising companies with earnings before interest, taxes, depreciation and amortization, which we refer to as "EBITDA," of $10 million to $50 million and/or total debt of $25 million to $150 million. In addition to our middle market investment business, our wholly-owned portfolio company, Katonah Debt Advisors and its affiliates (collectively, "Katonah Debt Advisors"), manage collateralized loan obligation funds ("CLO Funds") that invest in broadly syndicated loans, high-yield bonds and other corporate credit instruments. We acquired Katonah Debt Advisors and certain related assets prior to our initial public offering from affiliates of Kohlberg & Co., L.L.C. ("Kohlberg & Co."), a leading private equity firm focused on middle market investing. As of December 31, 2010, Katonah Debt Advisors had approximately $2.1 billion of assets under management.

Our investment objective is to generate current income and capital appreciation from our investments. We also expect to receive distributions of recurring fee income and, when debt markets stabilize and recover, to generate capital appreciation from our investment in the asset management business of Katonah Debt Advisors. Our investment portfolio as well as the investment portfolios of the CLO Funds in which we have invested and the investment portfolios of the CLO Funds managed by Katonah Debt Advisors consist exclusively of credit instruments and other securities issued by corporations and do not include any asset-backed securities secured by commercial mortgages, residential mortgages or other consumer borrowings.

As a regulated investment company ("RIC"), we intend to distribute to our stockholders substantially all of our net taxable income and the excess of realized net short-term capital gains over realized net long-term capital losses. To qualify as a RIC, we must, among other things, meet certain source-of-income and asset diversification requirements. As a RIC, we generally will not have to pay corporate-level taxes on any income that we distribute in a timely manner to our stockholders.

Our common stock is traded on The NASDAQ Global Select Market under the symbol "KCAP." The net asset value per share of our common stock at December 31, 2010 was $8.21. On December 31, 2010, the last reported sale price of a share of our common stock on The NASDAQ Global Select Market was $6.97.

CRITICAL ACCOUNTING POLICIES

The financial statements are based on the selection and application of critical accounting policies, which require management to make significant estimates and assumptions. Critical accounting policies are those that are both important to the presentation of our financial condition and results of operations and require management's most difficult, complex, or subjective judgments. Our critical accounting policies are those applicable to the basis of presentation, valuation of investments, and certain revenue recognition matters as discussed below.

Basis of Presentation

The accompanying financial statements have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States. The financial statements reflect all adjustments and reclassifications which, in the opinion of management, are necessary for the fair presentation of our results of operations and financial condition for the periods presented. Furthermore, the financial statements are based on the selection and application of critical accounting policies which may require management to make significant estimates and assumptions. Actual results could differ from those estimates. Critical accounting policies are those that are important to the presentation of our financial condition and results of operations that require management's most difficult, complex or subjective judgments.

Accounting Standards Codification. In June 2009, the Financial Accounting Standards Board ("FASB") issued a pronouncement establishing the FASB Accounting Standards Codification ("ASC") as the source of authoritative accounting principles recognized by the FASB to be applied in the preparation of financial statements in conformity with GAAP. The ASC reorganized existing U.S. accounting and reporting standards issued by the FASB and other related private sector standard setters into a single source of authoritative accounting principles arranged by topic. The standard explicitly recognizes rules and interpretive releases of the SEC under federal securities laws as authoritative GAAP for SEC registrants. The ASC supersedes all existing U.S. accounting standards; all other accounting literature not included in the ASC (other than Securities and Exchange Commission guidance for publicly-traded companies) is considered non-authoritative. The ASC was effective on a prospective basis for interim and annual reporting periods ending after September 15, 2009. The adoption of the ASC changed our references to U.S. GAAP accounting standards but did not impact our results of operations, financial position or liquidity.

Valuation of Portfolio Investments

The most significant estimate inherent in the preparation of our financial statements is the valuation of investments and the related amounts of unrealized appreciation and depreciation of investments recorded.

Value, as defined in Section 2(a)(41) of 1940 Act, is (1) the market price for those securities for which a market quotation is readily available and (2) for all other securities and assets, fair value as determined in good faith by our Board of Directors pursuant to procedures approved by our Board of Directors. Our valuation policy is intended to provide a consistent basis for determining the fair value of the portfolio based on the nature of the security, the market for the security and other considerations including the financial performance and enterprise value of the portfolio company. Because of the inherent uncertainty of valuation, the Board of Directors' determined values may differ significantly from the values that would have been used had a ready market existed for the investments, and the differences could be material.

We are, for GAAP purposes, an investment company under the AICPA Audit and Accounting Guide for Investment Companies. As a result, we reflect our investments on our balance sheet at their estimated fair value with unrealized gains and losses resulting from changes in fair value reflected as a component of unrealized gains or losses on our statements of operations. Fair value is the amount that would be received to sell the investments in an orderly transaction between market participants at the measurement date (i.e., the exit price). Additionally, we do not consolidate majority or wholly-owned and controlled investments.

Effective January 1, 2008 we adopted Statement of Financial Accounting Standards No. 157, Fair Value Measurements ("*Fair Value Measurements and Disclosures*"), which among other things, requires enhanced disclosures about financial instruments carried at fair value. See Note 4 to the financial statements for the additional information about the level of market observability associated with investments carried at fair value.

We have valued our investments, in the absence of observable market prices, using the valuation methodologies described below applied on a consistent basis. For some investments little market activity may exist; management's determination of fair value is then based on the best information available in the circumstances, and may incorporate management's own assumptions and involves a significant degree of management's judgment.

Our investments in CLO Fund securities are carried at fair value, which is based either on (i) the present value of the net expected cash inflows for interest income and principal repayments from underlying assets and the cash outflows for interest expense, debt paydown and other fund costs for the CLO Funds which are approaching or past the end of their reinvestment period and therefore begin to sell assets and/or use principal repayments to pay-down CLO Fund debt, and for which there continue to be net cash distributions to the class of we securities own, or (ii) the net asset value of the CLO Fund for CLO Funds which are approaching or past the end of their reinvestment period and therefore begin to sell assets and/or use principal repayments to pay-down CLO Fund debt, and for which there are negligible net cash distributions to the class of securities we own, or (iii) a discounted cash flow model for more recent CLO Funds that utilizes prepayment and loss assumptions based on historical experience and projected performance, economic factors, the characteristics of the underlying cash flow and comparable yields for similar securities or preferred shares to those in which the Company has invested. We recognize unrealized appreciation or depreciation on our investments in CLO Fund securities as comparable yields in the market change and/or based on changes in net asset values or estimated cash flows resulting from changes in prepayment or loss assumptions in the underlying collateral pool. As each investment in CLO Fund securities ages, the expected amount of losses and the expected timing of recognition of such losses in the underlying collateral pool are updated and the revised cash flows are used in determining the fair value of the CLO Investment. We determine the fair value of our investments in CLO Fund securities on an individual security-by-security basis.

Our investment in Katonah Debt Advisors is carried at fair value, which is determined after taking into consideration a percentage of assets under management and a discounted cash flow model incorporating different levels of discount rates depending on the hierarchy of fees earned (including the likelihood of realization of senior, subordinate and incentive fees) and prospective modeled performance. Such valuation includes an analysis of comparable asset management companies. Katonah Debt Advisors is classified as a Level III investment (as described below). Any change in value from period to period is recognized as net change in unrealized appreciation or depreciation.

Fair values of other investments for which market prices are not observable are determined by reference to public market or private transactions or valuations for comparable companies or assets in the relevant asset class and or industry when such amounts are available. Generally these valuations are derived by multiplying a key performance metric of the investee company or asset (e.g., EBITDA) by the relevant valuation multiple observed for comparable companies or transactions, adjusted by management for differences between the investment and the referenced comparable. Such investments may also be valued at cost for a period of time after an acquisition as the best indicator of fair value. If the fair value of such investments cannot be valued by reference to observable valuation measures for comparable companies, then the primary analytical method used to estimate the fair value is a discounted cash flow method and/or cap rate analysis. A sensitivity analysis is applied to the estimated future cash flows using various factors depending on the investment, including assumed growth rates (in cash flows), capitalization rates (for determining terminal values) and appropriate discount rates to determine a range of reasonable values or to compute projected return on investment.

We derive fair value for our illiquid loan investments that do not have indicative fair values based upon active trades primarily by using the Market Yield Approach, and also consider recent loan amendments or other activity specific to the subject asset as described above. Other significant assumptions, such as coupon and maturity, are asset-specific and are noted for each investment in the Schedules of Investments. Our Board of Directors may consider other methods of valuation to determine the fair value of investments as appropriate in conformity with GAAP.

The determination of fair value using this methodology takes into consideration a range of factors, including but not limited to the price at which the investment was acquired, the nature of the investment, local market conditions, trading values on public exchanges for comparable securities, current and projected operating performance and financing transactions subsequent to the acquisition of the investment. This valuation methodology involves a significant degree of management’s judgment.

After our adoption of *Fair Value Measurements and Disclosures*, investments measured and reported at fair value are classified and disclosed in one of the following categories:

- Level I — Unadjusted quoted prices are available in active markets for identical investments as of the reporting date. The type of investments included in Level I include listed equities and listed securities. As required by *Fair Value Measurements and Disclosures*, the Company does not adjust the quoted price for these investments, even in situations where the Company holds a large position and a sale could reasonably affect the quoted price.

- Level II — Pricing inputs are other than quoted prices in active markets, which are either directly or indirectly observable as of the reporting date. Such inputs may be quoted prices for similar assets or liabilities, quoted markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full character of the financial instrument, or inputs that are derived principally from, or corroborated by, observable market information. Investments which are generally included in this category include illiquid corporate loans and bonds and less liquid, privately held or restricted equity securities for which some level of recent trading activity has been observed.
- Level III — Pricing inputs are unobservable for the investment and includes situations where there is little, if any, market activity for the investment. The inputs may be based on the Company's own assumptions about how market participants would price the asset or liability or may use Level II inputs, as adjusted, to reflect specific investment attributes relative to a broader market assumption. These inputs into the determination of fair value may require significant management judgment or estimation. Even if observable market data for comparable performance or valuation measures (earnings multiples, discount rates, other financial/valuation ratios, etc.) are available, such investments are grouped as Level III if any significant data point that is not also market observable (private company earnings, cash flows, etc.) is used in the valuation methodology.

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, an investment's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. Our assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and it considers factors specific to the investment. Substantially all of our investments are classified as Level III.

Our Board of Directors may consider other methods of valuation to determine the fair value of investments as appropriate in conformity with GAAP.

Interest Income

Interest income, adjusted for amortization of premium and accretion of discount, is recorded on the accrual basis to the extent that such amounts are expected to be collected. We generally place a loan on non-accrual status and cease recognizing interest income on such loan or security when a loan or security becomes 90 days or more past due or if we otherwise do not expect the debtor to be able to service its debt obligations. Non-accrual loans remain in such status until the borrower has demonstrated the ability and intent to pay contractual amounts due or such loans become current. As of December 31, 2010, five issuers representing 4.1% of our total investments at fair value were on non-accrual status. As of December 31, 2009, ten issuers representing 2% of our total investments at fair value were on non-accrual status.

Dividend Income from CLO Fund Securities

We generate dividend income from our investments in the most junior class of securities of CLO Funds (typically preferred shares or subordinated securities) managed by Katonah Debt Advisors and selective investments in securities issued by funds managed by other asset management companies. Our CLO Fund securities are subordinate to senior bond holders who typically receive a fixed rate of return on their investment. The CLO Funds are leveraged funds and any excess cash flow or "excess spread" (interest earned by the underlying securities in the fund less payments made to senior bond holders and less fund expenses and management fees) is paid to the holders of the CLO Fund's subordinated securities or preferred shares. The level of excess spread from CLO Fund securities can be impacted from the timing and level of the resetting of the benchmark interest rate for the underlying assets (which reset at various times throughout the quarter) in the CLO Fund and the related CLO Fund bond liabilities (which reset at each quarterly distribution date); in periods of short-term and volatile changes in the benchmark interest rate, the levels of excess spread and distributions to us can vary significantly. In addition, the failure of CLO Funds in which we invest to comply with certain financial covenants may lead to the temporary suspension or deferral of cash distributions to us. We make estimated interim accruals of such dividend income based on recent historical distributions and CLO Fund performance and adjust such accruals on a quarterly basis to reflect actual distributions.

For non-junior class CLO Fund securities, such as our investment in the class B-2L notes of Katonah 2007-1 CLO, interest is earned at a fixed spread relative to the LIBOR index.

Dividends from Affiliate Asset Manager

The Company records dividend income from its affiliate asset manager on the declaration date, which represents the ex-dividend date.

Payment in Kind Interest

We may have loans in our portfolio that contain a payment-in-kind ("PIK") provision. PIK interest, computed at the contractual rate specified in each loan agreement, is added to the principal balance of the loan and recorded as interest income. To maintain our RIC status, this non-cash source of income must be paid out to stockholders in the form of dividends, even though the Company has not yet collected the cash.

Fee Income

Fee income includes fees, if any, for due diligence, structuring, commitment and facility fees, and fees, if any, for transaction services and management services rendered by us to portfolio companies and other third parties. Commitment and facility fees are generally recognized as income over the life of the underlying loan, whereas due diligence, structuring, transaction service and management service fees are generally recognized as income when the services are rendered.

Management Compensation

We may, from time to time, issue stock options or restricted stock under the Kohlberg Capital Corporation 2006 Equity Incentive Plan as amended (our "Equity Incentive Plan") to officers and employees for services rendered to us. We follow Statement of Financial Accounting Standards No. 123R (revised 2004), *Accounting for Stock-Based Compensation*, a method by which the fair value of options or restricted stock is determined and expensed. We use a Binary Option Pricing Model (American, call option) as its valuation model to establish the expected value of all stock option grants.

We are internally managed and therefore do not incur management fees payable to third parties.

United States Federal Income Taxes

The Company has elected and intends to continue to qualify for the tax treatment applicable to RICs under Subchapter M of the Code and, among other things, intends to make the required distributions to its stockholders as specified therein. In order to qualify as a RIC, the Company is required to timely distribute to its stockholders at least 90% of investment company taxable income, as defined by the Code, for each year. Depending on the level of taxable income earned in a tax year, we may choose to carry forward taxable income in excess of current year distributions into the next tax year and pay a 4% excise tax on such income, to the extent required.

Dividends

Dividends and distributions to common stockholders are recorded on the ex-dividend date. The amount to be paid out as a dividend is determined by the Board of Directors each quarter and is generally based upon the earnings estimated by management for the period and year.

We have adopted a dividend reinvestment plan that provides for reinvestment of our distributions on behalf of our stockholders, unless a stockholder "opts out" of the plan to receive cash in lieu of having their cash dividends automatically reinvested in additional shares of our common stock.

Recent Accounting Pronouncements

Improved Disclosures Regarding Fair Value Measurements. In January 2010, the FASB issued Accounting Standards Update No. 2010-06, *Fair Value Measurements and Improving Disclosures About Fair Value Measurements (Topic 820)*, which provides for improving disclosures about fair value measurements, primarily significant transfers in and out of Levels I and II, and activity in Level III fair value measurements. The new disclosures and clarifications of existing disclosures are effective for the interim and annual reporting periods beginning after December 15, 2009, while the disclosures about the purchases, sales, issuances, and settlements in the roll forward activity in Level 3 fair value measurements are effective for fiscal years beginning after December 15, 2010 and for the interim periods within those fiscal years. Except for certain detailed Level III disclosures, which are effective for fiscal years beginning after December 15, 2010 and interim periods within those years, the new guidance became effective for the Company's fiscal 2010 second quarter. The Company had no transfers of assets into Level II or Level I fair value measurements. The adoption of this disclosure-only guidance is included in Note 4 "— Investments" and did not have a material impact on the Company's financial results.

Fair Value Measurements for Alternative Investments. In September 2009, the FASB issued Accounting Standards Update 2009-12, *Fair Value Measurements and Disclosures (Topic 820) — Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*, which provides guidance on estimating the fair value of an alternative investment, amending ASC 820-10. The amendment is effective for interim and annual periods ending after December 15, 2009. The adoption of this guidance did not have a material impact on either the Company's financial position or results of operations.

PORTFOLIO AND INVESTMENT ACTIVITY

Our primary business is lending to and investing in middle-market businesses through investments in senior secured loans, junior secured loans, subordinated/mezzanine debt investments, CLO equity investments and other equity-based investments, which may include warrants.

Total portfolio investment activity (excluding activity in time deposit and money market investments) for the years ended December 31, 2010, December 31, 2009, and December 31, 2008 was as follows:

	Debt Securities	CLO Fund Securities	Equity Securities	Affiliate Asset Managers	Total Portfolio
Fair Value at December 31, 2007	$ 410,954,082	$ 31,020,000	$ 4,752,250	$ 58,585,360	$ 505,311,692
2008 Activity:					
Purchases / originations /draws	$ 71,949,153	$ 28,859,236	$ 212,709	$ 5,478,276	$ 106,499,374
Pay-downs / pay-offs / sales	(71,671,847)	—	—	—	(71,671,847)
Net accretion of discount	717,195	1,456,095	—	—	2,173,290
Net realized gains	(575,179)	—	—	—	(575,179)
Increase (decrease) in fair value	(57,514,397)	(26,695,331)	124,406	(9,328,824)	(93,414,146)
Fair Value at December 31, 2008	$ 353,859,007	$ 34,640,000	$ 5,089,365	$ 54,734,812	$ 448,323,184
2009 Activity:					
Purchases / originations /draws	$ 1,509,987	$ 1,076,250	$ 8,625,627	$ 4,018,309	$ 15,230,173
Pay-downs / pay-offs / sales	(72,227,405)	—	—	—	(72,227,405)
Net accretion of discount	964,724	742,204	—	—	1,706,928
Net realized losses	(12,050,370)	—	(1,516,682)	(2,215,069)	(15,782,121)
Increase (decrease) in fair value	25,300,586	12,512,546	(7,485,064)	1,526,668	31,854,736
Fair Value at December 31, 2009	$ 297,356,529	$ 48,971,000	$ 4,713,246	$ 58,064,720	$ 409,105,495
2010 Activity:					
Purchases / originations /draws	$ 9,981,426	$ —	$ 1,927,366	$ 3,780,817	$ 15,689,609
Pay-downs / pay-offs / sales	(208,820,375)	—	—		(208,820,375)
Net accretion of discount	381,676	85,150	—	—	466,826
Net realized losses	(17,053,242)	—	(809,742)	—	(17,862,984)
Increase (decrease) in fair value	9,196,912	3,974,851	(1,142,038)	(20,352,537)	(8,322,812)
Fair Value at December 31, 2010	$ 91,042,926	$ 53,031,001	$ 4,688,832	$ 41,493,000	$ 190,255,759

The level of investment activity for investments funded and principal repayments for our investments can vary substantially from period to period depending on the number and size of investments that we invest in or divest of, and many other factors, including the amount and competition for the debt and equity securities available to middle market companies, the level of merger and acquisition activity for such companies and the general economic environment.

RESULTS OF OPERATIONS

The principal measure of our financial performance is the net increase (decrease) in stockholders' equity resulting from operations which includes net investment income (loss) and net realized and unrealized appreciation (depreciation). Net investment income (loss) is the difference between our income from interest, dividends, fees, and other investment income and our operating expenses. Net realized gain (loss) on investments, is the difference between the proceeds received from dispositions of portfolio investments and their amortized cost. Net change in unrealized appreciation (depreciation) on investments is the net change in the fair value of our investment portfolio.

Set forth below is a discussion of our results of operations for the years ended December 31, 2010 and 2009.

Investment Income

Investment income for the years ended December 31, 2010, 2009, and 2008 was approximately $29 million, $34 million, and $49 million, respectively. Of this amount, approximately $14 million, $24 million and $33 million, respectively, was attributable to interest income on our loan and bond investments. A portion of such interest income is attributable to net interest earned on assets accumulated for future CLO issuance on which Katonah Debt Advisors entered into a first loss agreement in connection with loan warehouse arrangements for Katonah Debt Advisors CLO Funds. For the years ended December 31, 2010 and December 31, 2009 no income related to first loss arrangements was earned. For the year ended December 31, 2008, approximately $107,000 of such net interest related to the first loss arrangements previously accrued was written off. For the years ended December 31, 2010, 2009, and 2008, approximately $10 million, $9 million and $13 million, respectively, of investment income was attributable to investments in CLO Fund securities.

Investment income is primarily dependent on the composition and credit quality of our investment portfolio. Generally, our debt securities portfolio is expected to generate predictable, recurring interest income in accordance with the contractual terms of each loan. Corporate equity securities may pay a dividend and may increase in value for which a gain may be recognized; generally such dividend payments and gains are less predictable than interest income on our loan portfolio.

Dividends from CLO Fund securities are dependent on the performance of the underlying assets in each CLO Fund; interest payments, principal amortization and prepayments of the underlying loans in each CLO Fund are primary factors which determine the level of income on our CLO Fund securities. The level of excess spread from CLO Fund securities can be impacted by the timing and level of the resetting of the benchmark interest rate for the underlying assets (which reset at various times throughout the quarter) in the CLO Fund and the related CLO Fund bond liabilities (which reset at each quarterly distribution date); in periods of short-term and volatile changes in the benchmark interest rate, the levels of excess spread and distributions to us can vary significantly.

Dividends from Affiliate Asset Manager

As of December 31, 2010, our investment in Katonah Debt Advisors was approximately $42 million. For the year ended December 31, 2010 and 2009, Katonah Debt Advisors had GAAP net income of approximately $1 million and $2 million, respectively. During the year ended December 31, 2010 distributions from Katonah Debt Advisors totaled approximately $4.5 million, a portion of which represented undistributed earnings from prior years. No distributions were made for the year ended December 31, 2009.

Distributions of Katonah Debt Advisors' net income are recorded as dividends from affiliate asset manager. The Company intends to distribute the accumulated undistributed net income of Katonah Debt Advisors in the future. For purposes of calculating distributable tax income for required quarterly dividends as a RIC, Katonah Debt Advisors' net income is further reduced by approximately $2 million per annum for tax goodwill amortization resulting from its acquisition by us prior to our initial public offering. As a result, the amount of our declared dividends, as evaluated by management and approved by our Board of Directors, is based on our evaluation of both distributable income for tax purposes and GAAP net investment income (which excludes unrealized gains and losses).

Expenses

Interest and compensation expense are generally expected to be our largest expenses each period. Interest expense is dependent on the average outstanding principal balance of our borrowings and the applicable interest rate for the period. Compensation expense includes base salaries, bonuses, stock compensation, employee benefits and employer related payroll costs. The largest components of total compensation costs are base salaries and bonuses; generally, base salaries are expensed as incurred and bonus expenses are estimated and accrued since bonuses are paid annually.

Total expenses for the years ended December 31, 2010, 2009, and 2008 were approximately $17 million, $16 million, and $19 million, respectively. Interest expense and amortization on debt issuance costs for the period, which includes facility and program fees on the unused loan balance, was approximately $7 million, $9 million, and $11 million, respectively, on average debt outstanding of $155 million, $236 million, and $248 million, respectively.

For the years ended December 31, 2010, 2009, and 2008 approximately $3 million, $3 million, and $4 million respectively, of expenses were attributable to employment compensation, including salaries, bonuses and stock option expense. For the year ended December 31, 2010, professional fees and insurance expenses totaled approximately $6 million. For the year ended December 31, 2009 and December 31, 2008, professional fees and insurance expenses totaled approximately $2 million, and $2 million, respectively. For the year ended December 31, 2010, administrative and other costs totaled approximately $1 million. For the year ended December 31, 2009 and December 31, 2008, administrative and other costs totaled approximately $1 million and $1 million, respectively. These costs include occupancy expense, technology and other office expenses.

Professional fee expenses for the year ended December 31, 2010 are significantly higher by approximately $4 million relative to the same prior year period due to increased legal expenses (approximately $2 million), accounting (approximately $1 million) and valuation services (approximately $450,000). This increase in professional fees is primarily related to legal proceedings and our complaint against our lenders and additional legal, accounting and valuation costs related to the restatement (and defense on the related class-action and SEC investigation net of reimbursable legal fees covered by directors' and officers' insurance) of our year-end 2008 and first-and second- quarter 2009 financial statements which we do not expect to recur at this level in future periods.

Net Unrealized Appreciation (Depreciation) on Investments

During the year ended December 31, 2010, our total investments had net unrealized depreciation of approximately $8 million. During the year ended December 31, 2009 and December 31, 2008, our total investments had net unrealized appreciation of approximately $32 million, and net unrealized depreciation of $93 million, respectively.

The $8 million of unrealized losses during the year ended December 31, 2010 are due to unrealized gains of $12 million on debt securities, equity securities and CLO Fund securities in our investment portfolio, and a $20 million decrease in the value of Katonah Debt Advisors. The decrease in the fair value of Katonah Debt Advisors is due to the receipt of approximately $5 million of previously accrued subordinate management fees during the year, the disposition of one of its affiliates, and current market conditions.

The $32 million of unrealized gains during the year ended December 31, 2009 were primarily due to unrealized gains of approximately $25 million and approximately $13 million on debt securities and CLO Fund securities, respectively, in our investment portfolio, offset in part by approximately a $7 million unrealized loss on equity securities. The $93 million of unrealized losses during the year ended December 31, 2008 were primarily due to unrealized losses of $58 million and $27 million on debt securities and CLO Fund securities, respectively, in our investment portfolio, as well as an approximate $9 million unrealized loss on Katonah Debt Advisors.

Net Change in Stockholders' Equity Resulting From Operations

The net decrease in stockholders' equity resulting from operations for the year ended December 31, 2010 was an approximately $14 million, or $0.63 per share. The net increase in stockholders' equity resulting from operations for the year ended December 31, 2009 was $34 million, or $1.56 per share, and the net decrease increase in stockholders' equity resulting from operations for the year ended December 31, 2008 was approximately $63 million, or $3.09 per share.

FINANCIAL CONDITION, LIQUIDITY, AND CAPITAL RESOURCES

Liquidity is a measure of our ability to meet potential cash requirements, including ongoing commitments to repay borrowings, fund and maintain investments, pay dividends to our stockholders and other general business needs. We recognize the need to have funds available for operating our business and to make investments. We seek to have adequate liquidity at all times to cover normal cyclical swings in funding availability and to allow us to meet abnormal and unexpected funding requirements. We plan to satisfy our liquidity needs through normal operations with the goal of avoiding unplanned sales of assets or emergency borrowing of funds.

In addition to the traditional sources of available funds (issuance of new equity, debt or undrawn warehouse facility capacity), we also have the ability, subject to prevailing conditions in the securitization markets, to raise additional cash funds through the securitization of assets on our balance sheet through our wholly-owned asset manager, Katonah Debt Advisors. Such a securitization would provide cash for new investments on our balance sheet as well as additional management fee income and potentially increased value (as a result of increased assets under management) for Katonah Debt Advisors. No new securitizations by Katonah Debt Advisors have closed since January 2008.

As a BDC, we are limited in the amount of leverage we can incur to finance our investment portfolio. In order to incur new debt, we are required to meet a coverage ratio of total assets to total senior securities of at least 200%. For this purpose, senior securities include all borrowings and any preferred stock. As a result, our ability to utilize leverage as a means of financing our portfolio of investments is limited by this asset coverage test. As of December 31, 2010, we had $87 million of outstanding borrowings and our asset coverage was 315%, which is above the minimum asset coverage level generally required by the 1940 Act for a BDC to incur new debt. See Item 1. Business — Leverage."

As of December 31, 2010 and December 31, 2009 the fair value of investments and cash were as follows:

	Investments at Fair Value	
Security Type	**December 31, 2010**	**December 31, 2009**
Cash	$ 10,175,488	$ 4,140,408
Time Deposits	720,225	126
Money Market Account	210,311	—
Senior Secured Loan	22,001,256	159,075,586
Junior Secured Loan	63,944,003	114,920,499
Mezzanine Investment	250,000	19,235,444
Senior Subordinated Bond	4,490,709	2,415,000
Senior Unsecured Bond	—	1,710,000
CLO Fund Securities	53,031,000	48,971,000
Equity Securities	4,437,871	4,713,246
Preferred	607,921	—
Affiliate Asset Managers	41,493,000	58,064,720
Total	$ 201,361,784	$ 413,246,029

We use borrowed funds, known as "leverage," to make investments and to attempt to increase returns to our shareholders by reducing our overall cost of capital. As a BDC, we are limited in the amount of leverage we can incur under the 1940 Act. We are only allowed to borrow amounts such that our asset coverage, as defined in the 1940 Act, equals at least 200% after such borrowing. As of December 31, 2010, we had approximately $87 million of outstanding borrowings and our asset coverage ratio of total assets to total borrowings was 315%, compliant with the minimum asset coverage level of 200% generally required for a BDC by the 1940 Act. We may also borrow amounts of up to 5% of the value of our total assets for temporary purposes. As of January 31, 2011, we had repaid in full the outstanding balance of our borrowings and we are currently operating fully unlevered.

The weighted average daily debt balance for the years ended December 31, 2010 and 2009 was approximately $105 million and $222 million, respectively. As of December 31, 2010, the Company had restricted cash and time deposit balances of approximately $67 million which it maintained in accordance with the terms of the Facility.

Subject to prevailing market conditions, we intend to grow our portfolio of assets by raising additional capital, including through the prudent use of leverage. As a result, we may seek to enter into a new agreement with other lenders or into other financing arrangements as market conditions permit. Such financing arrangements may include a new secured and/or unsecured credit facility, the issuance of senior debt preferred or convertible securities or debt guaranteed by the SBA. We also believe that our current cash position, certain loan investments and cash income earned by our investment portfolio are adequate for our current liquidity needs.

OFF-BALANCE SHEET ARRANGEMENTS

We are a party to financial instruments with off-balance sheet risk in the normal course of business in order to meet the needs of the Company’s investment in portfolio companies. Such instruments include commitments to extend credit and may involve, in varying degrees, elements of credit risk in excess of amounts recognized on our balance sheet. Prior to extending such credit, we attempt to limit our credit risk by conducting extensive due diligence, obtaining collateral where necessary and negotiating appropriate financial covenants. As of December 31, 2010 and December 31, 2009, we had committed to make a total of approximately $2 million and $2 million, respectively, of investments in various revolving senior secured loans, of which approximately $1 million was funded as of December 31, 2010 and $640,000 was funded as of December 31, 2009. As of December 31, 2010 and December 31, 2009, we had committed to make no investments in delayed draw senior secured loans.

CONTRACTUAL OBLIGATIONS

The following table summarizes our contractual cash obligations and other commercial commitments as of December 31, 2010:

	Payments Due by Period				
Contractual Obligations	**Total**	**Less than one year**	**1 – 3 years**	**3 – 5 years**	**More than 5 years**
Operating lease obligations	$ 655,415	$ 328,436	$ 326,979	$ —	$ —
Long-term debt obligations[1]	86,746,582	86,746,582	—	—	—
Unused lending commitments[2]	920,000	920,000	—	—	—
Total	$ 88,321,997	$ 87,995,018	$ 326,979	$ —	$ —

(1) On January 31, 2011, the outstanding balance of our borrowings was repaid in full.

(2) Represents the unfunded lending commitment in connection with revolving lines of credit or delayed funding draws on loans made to portfolio companies.

Item 7A. *Quantitative and Qualitative Disclosures about Market Risk*

Our business activities contain elements of market risks. We consider our principal market risks to be fluctuations in interest rates and the valuations of our investment portfolio. Managing these risks is essential to our business. Accordingly, we have systems and procedures designed to identify and analyze our risks, to establish appropriate policies and thresholds and to continually monitor these risks and thresholds by means of administrative and information technology systems and other policies and processes.

Interest Rate Risk

Interest rate risk is defined as the sensitivity of our current and future earnings to interest rate volatility, variability of spread relationships, the difference in re-pricing intervals between our assets and liabilities and the effect that interest rates may have on our cash flows. Changes in the general level of interest rates can affect our net interest income, which is the difference between the interest income earned on interest earning assets and our interest expense incurred in connection with our interest bearing debt and liabilities. Changes in interest rates can also affect, among other things, our ability to acquire and originate loans and securities and the value of our investment portfolio.

Our investment income is affected by fluctuations in various interest rates, including LIBOR and prime rates. As of December 31, 2010, approximately 95% of our loans at fair value in our portfolio were at floating rates with a spread to an interest rate index such as LIBOR or the prime rate. We generally expect that future portfolio investments will predominately be floating rate investments. As of December 31, 2010, we had $87 million of borrowings outstanding at a floating rate tied to prevailing commercial paper rates plus a margin of 0.85%. All of such borrowings were repaid in full in January 2011.

Because we borrow money to make investments, our net investment income is dependent upon the difference between the rate at which we borrow funds and the rate at which we invest the funds borrowed. Accordingly, there can be no assurance that a significant change in market interest rates will not have a material adverse effect on our net investment income. In periods of rising interest rates, our cost of funds would increase, which could reduce our net investment income if there is not a corresponding increase in interest income generated by floating rate assets in our investment portfolio.

We have analyzed the potential impact of changes in interest rates on interest income net of interest expense. Assuming that our balance sheet at December 31, 2010 were to remain constant and no actions were taken to alter the existing interest rate sensitivity, a hypothetical increase or decrease of a 1% change in interest rates would correspondingly affect net interest income proportionately by approximately $600,000 over a one-year period. Because most of our investments at December 31, 2010 were floating rate with a spread to an index similar to our Facility, we would not expect a significant impact on our net interest spread.

Although management believes that this measure is indicative of our sensitivity to interest rate changes, it does not adjust for potential changes in credit quality, size and composition of the assets on the balance sheet and other business developments that could affect a net change in assets resulting from operations or net income. Accordingly, no assurances can be given that actual results would not materially differ from the potential outcome simulated by this estimate.

We did not hold any derivative financial instruments for hedging purposes as of December 31, 2010.

Portfolio Valuation

We carry our investments at fair value, as determined in good faith by our Board of Directors pursuant to a valuation methodology approved by our Board of Directors. Investments for which market quotations are generally readily available are generally valued at such market quotations. Investments for which there is not a readily available market value are valued at fair value as determined in good faith by our Board of Directors under a valuation policy and consistently applied valuation process. However, due to the inherent uncertainty of determining the fair value of investments that cannot be marked to market, the fair value of our investments may differ materially from the values that would have been used had a ready market existed for such investments. In addition, changes in the market environment and other events that may occur over the life of the investments may cause the value realized on these investments to be different than the valuations that are assigned. The types of factors that we may take into account in fair value pricing of our investments include, as relevant, the nature and realizable value of any collateral, third party valuations, the portfolio company's ability to make payments and its earnings and discounted cash flow, the markets in which the portfolio company does business, comparison to publicly-traded securities, recent sales of or offers to buy comparable companies, and other relevant factors.

We engaged VRC, an independent valuation firm, to provide third-party valuation estimates for 39% of our investments at fair value as of December 31, 2009. VRC's valuation estimates were considered as one of the relevant data inputs in our determination of fair value. Though the Board of Directors did not engage VRC to provide valuation estimates for any of the assets in the Company's portfolio as of December 31, 2010, the Board of Directors engaged VRC to review our CLO fair value model relative to its functionality, model inputs and calculations as a reasonable method to determine CLO fair values, in the absence of Level 1 or Level 2 trading activity or observable market inputs. VRC concluded that our CLO model appropriately factors in all the necessary inputs required to build a CLO equity cash flow for fair value purposes and that the inputs were being employed correctly. The Board of Directors may engage an independent valuation firm in the future to provide certain valuation services, including the review of certain portfolio assets, as part of its valuation processes.

Item 8. *Financial Statements and Supplementary Data*

Our financial statements are annexed to this Annual Report beginning on page F-1.

Item 9. *Changes in and Disagreements with Accountants on Accounting and Financial Disclosure*

On January 12, 2010, Kohlberg Capital dismissed Deloitte as its registered public accounting firm. The Company took this action after discussions with the Staff of the SEC regarding the provisions in the 1940 Act relating to the selection and termination of a BDC's independent public accountants and the circumstances surrounding Deloitte and the Company, including the fact that on January 5, 2010, Deloitte informed the Company that, as a result of and in response to a communication from the Company on January 4, 2010, Deloitte had concluded that it was not currently independent with respect to the Company. Both the Board of Directors of the Company and the Board's Audit Committee approved the decision to dismiss Deloitte.

Prior to Deloitte's dismissal, the Company and Deloitte disagreed with respect to the appropriateness of the methodology and procedures used by the Company under *Fair Value Measurements and Disclosures* to value the Company's investments for the year ended December 31, 2008 (and the quarterly periods included in such year) and the interim periods ended March 31, 2009 and June 30, 2009. The Company does not believe that Deloitte, prior to this dismissal, provided its definitive views to the Company on the application of *Fair Value Measurements and Disclosures* to the valuation of the Company's investments, and, as a result, the Company is unable to describe the effect on its financial statements had the accounting methodology that Deloitte apparently would have concluded was required been followed.

Item 9A. *Controls and Procedures*

Evaluation of Disclosure Controls and Procedures.

The Company's management, under the supervision and with the participation of various members of management, including its Chief Executive Officer ("CEO") and its Chief Financial Officer ("CFO"), has evaluated the effectiveness of its disclosure controls and procedures (as defined in Rule 13a-15(e) or Rule 15d-15(e) of the Exchange Act) as of the end of the period covered by this report. Based upon that evaluation, the Company's CEO and CFO have concluded that the Company's disclosure controls and procedures are effective as of the end of the period covered by this report.

Management's Report on Internal Control Over Financial Reporting.

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) of the Exchange Act. The Company's internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

The Company's internal control over financial reporting includes those policies and procedures that:

- Pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Company;
- Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that the Company's receipts and expenditures are being made only in accordance with authorizations of the Company's management and directors; and
- Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the Company's financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management, including the Company's CEO and CFO, assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2010. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control — Integrated Framework. Based on management's assessment, management concluded that the Company maintained effective internal control over financial reporting as of December 31, 2010.

Attestation Report of the Independent Registered Public Accounting Firm.

The Company's independent registered public accounting firm has audited and issued a report on the Company's internal control over financial reporting, which appears in Item 15 of this report.

Changes in Internal Control Over Financial Reporting.

During the quarter ended June 30, 2010, the Company revised its valuation procedures for estimating the fair value of its illiquid investments and has revised its accounting for non-cash PIK interest income. Under the revised valuation procedures, management considers the following factors in determining the appropriate weighting of market inputs: comparability of the market input relative to the investment being valued, the source of the information, the correlation of the data to any actual observed transaction activity, the internal consistency of such inputs to other inputs noted by the same source, and other qualitative factors that may impact the reliability, comparability, or weighting of the inputs. In addition, for investments which earn non-cash PIK interest and for which there has been a substantial decline in fair value due to underlying credit concerns for an extended period, the Company no longer accrues such non-cash PIK interest as income. As of the date of filing of this report, the Company believes that it has modified its accounting for the fair value of its investments and its accounting for its non-cash PIK investments to the extent necessary to prepare the financial statements and the other financial information contained herein. During the quarter ended December 31, 2010, the Company had no further changes in its internal control over financial reporting.

Item 9B. ***Other Information***

None.

PART III

Item 10. *Directors, Executive Officers and Corporate Governance*

The information required by this item will be contained in the Proxy Statement under the headings “Proposal 1: Election of Directors,” “Control Persons and Principal Stockholders” and “Corporate Governance Principles and Director Information”, to be filed with the Securities and Exchange Commission on or prior to April 30, 2011, and is incorporated herein by reference.

We have adopted a Code of Ethics that applies to directors and officers of the Company and a Sarbanes-Oxley Code of Ethics that applies to directors, officers and employees of the Company. Both of these codes of conduct are published on our website at *www.kohlbergcap.com*. We intend to disclose any future amendments to, or waivers from, these codes of conduct within four business days of the waiver or amendment through a website posting.

Item 11. *Executive Compensation*

The information required by this item will be contained in the Proxy Statement under the headings “Proposal 1: Election of Directors,” “Executive Compensation,” “Compensation Committee Interlocks and Insider Participation” and “Compensation Committee Report”, to be filed with the Securities and Exchange Commission on or prior to April 30, 2011, and is incorporated herein by reference.

Item 12. *Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters*

The information required by this item will be contained in the Proxy Statement under the headings “Executive Compensation” and “Control Persons and Principal Stockholders”, to be filed with the Securities and Exchange Commission on or prior to April 30, 2011, and is incorporated herein by reference.

Item 13. *Certain Relationships and Related Transactions, and Director Independence*

The information required by this item will be contained in the Proxy Statement under the headings “Transactions with Related Persons” and “Proposal 1: Election of Directors”, to be filed with the Securities and Exchange Commission on or prior to April 30, 2011, and is incorporated herein by reference.

Item 14. *Principal Accountant Fees and Services*

The information required by this item will be contained in the Proxy Statement under the heading “Proposal 2: Ratification of Independent Registered Public Accounting Firm”, to be filed with the Securities and Exchange Commission on or prior to April 30, 2011, and is incorporated herein by reference.

PART IV

Item 15. *Exhibits and Financial Statement Schedules*

1. Financial Statements

The following financial statements of Kohlberg Capital Corporation (the "Company" or the "Registrant") are filed herewith:

2. Exhibits

EXHIBIT INDEX

Exhibit Number	Description
3.1	Form of Certificate of Incorporation of Kohlberg Capital Corporation (the "Company").(1)
3.2	Form of Bylaws of the Company.(2)
4.1	Specimen Certificate of the Company's common stock, par value $0.01 per share.(1)
4.2	Form of Registration Rights Agreement.(3)
4.3	Form of Dividend Reinvestment Plan.(3)
10.1	Form of the Amended and Restated 2006 Equity Incentive Plan.(9)*
10.2	Form of Company Non-Qualified Stock Option Certificate.(3)*
10.3	Form of Custodian Agreement by and among Kohlberg Capital Corporation and U.S. Bank National Association.(3)
10.4	Form of License and Referral Agreement between the Company and Kohlberg & Company, L.L.C.(1)
10.5	Form of Overhead Allocation Agreement between the Company and Katonah Debt Advisors, L.L.C.(3)
10.6	Form of Employment Agreement between the Company and Dayl W. Pearson.(3)*
10.7	Form of Employment Agreement between the Company and Michael I. Wirth.(3)*
10.8	Form of Employment Agreement between the Company and R. Jon Corless.(3)*
10.9	Form of Employment Agreement between the Company and E.A. Kratzman.(3)*
10.10	Form of Employment Agreement between Katonah Debt Advisors and E.A. Kratzman.(3)*
10.11	Letter Agreement, dated December 10, 2010, between the Company and John M. Stack.*
10.12	Consulting Agreement dated December 10, 2010, between Katonah Debt Advisors, L.L.C. and John M. Stack.*
10.13	Form of Employment Agreement between Katonah Debt Advisors and Daniel P. Gilligan.*
10.14	Form of Indemnification Agreement for Officers and Directors of the Company.(4)

TABLE OF CONTENTS

Exhibit Number	Description
10.15	Execution Copy of Loan Funding and Servicing Agreement dated as of February 14, 2007, by and among Kohlberg Capital Funding LLC I, Kohlberg Capital Corporation, each of the conduit lenders and institutional lenders from time to time party thereto, each of the lender agents from time to time party thereto, BMO Capital Markets Corp., as the Agent, Lyon Financial Services, Inc. (d/b/a U.S. Bank Portfolio Services), as the Backup Services, and U.S. Bank National Association, as Trustee.(5)
10.16	Execution Copy of First Amendment to Loan Funding and Servicing Agreement, dated as of May 30, 2007, by and among Kohlberg Capital Funding LLC I, the Company, each of the conduit lenders and institutional lenders from time to time party thereto, each of the lender agents from time to time party thereto, BMO Capital Markets Corp., as the Agent, Lyon Financial Services, Inc. (d/b/a U.S. Bank Portfolio Services), as the Backup Servicer, and U.S. Bank National Association, as Trustee.(6)
10.17	Execution Copy of Second Amendment to Loan Funding and Servicing Agreement, dated as of October 1, 2007, by and among Kohlberg Capital Funding LLC I, the Company, each of the conduit lenders and institutional lenders from time to time party thereto, each of the lender agents from time to time party thereto, BMO Capital Markets Corp., as the Agent, Lyon Financial Services, Inc. (d/b/a U.S. Bank Portfolio Services), as the Backup Servicer, and U.S. Bank National Association, as Trustee.(6)
10.18	Execution Copy of Third Amendment to Loan Funding and Servicing Agreement, dated as of November 21, 2007, by and among Kohlberg Capital Funding LLC I, the Company, each of the conduit lenders and institutional lenders from time to time party thereto, each of the lender agents from time to time party thereto, BMO Capital Markets Corp., as the Agent, Lyon Financial Services, Inc. (d/b/a U.S. Bank Portfolio Services), as the Backup Servicer, and U.S. Bank National Association, as Trustee.(8)
10.19	Execution Copy of Purchase and Sale Agreement dated as of February 14, 2007, by and among Kohlberg Capital Funding LLC I and the Company.(7)
10.20	Forbearance and Settlement Agreement, dated as of September 20, 2010, by and among the Company, BMO Capital Markets Corp. and the other lender parties thereto.(11)
10.21	Form of 2008 Non-Employee Director Plan.(10)*
21.1	List of Subsidiaries.
23.1	Consent of Grant Thornton LLP, Independent Registered Public Accounting Firm.
31.1	Chief Executive Officer Certification Pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Chief Financial Officer Certification Pursuant to Rule 13a-14 of the Securities Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Chief Executive Officer Certification pursuant to Section 1350, Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Chief Financial Officer Certification pursuant to Section 1350, Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

---

(1) Incorporated by reference to the exhibit included in Pre-Effective Amendment No. 1 on Form N-2, as filed on October 6, 2006 (File No. 333-136714).

(2) Incorporated by reference to the exhibit included on Form N-2, as filed on March 16, 2007 (File No. 333-141382).

(3) Incorporated by reference to the exhibit included in Pre-Effective Amendment No. 2 on Form N-2, as filed on November 20, 2006 (File No. 333-136714).

(4) Incorporated by reference to the exhibit included in Pre-Effective Amendment No. 3 on Form N-2, as filed on November 24, 2006 (File No. 333-136714).

(5) Incorporated by reference to Exhibit 10.15 of the Annual Report on Form 10-K, as filed on March 29, 2007 (File No. 814-00735).

(6) Incorporated by reference to the exhibit included in Pre-Effective Amendment No. 1 on Form N-2, as filed on October 18, 2007 (File No. 333-146190).

(7) Incorporated by reference to Exhibit 10.2 of the Current Report on Form 8-K, as filed on February 16, 2007 (File No. 814-00735).

(8) Incorporated by reference to Exhibit 10.15 of the Annual Report on Form 10-K, as filed on March 14, 2008 (File No. 814-00735).

(9) Incorporated by reference to Exhibit 10.1 of the Current Report on Form 8-K, as filed on June 19, 2008 (File No. 814-00735).

(10) Incorporated by reference to the exhibit included in Pre-Effective Amendment No. 1 on Form N-2, as filed on June 30, 2008 (File No. 333-151268).

(11) Incorporated by reference to Exhibit 10.1 of the Quarterly Report on Form 10-Q, as filed on November 8, 2010 (File No. 814-00735).

* Indicates a management contract or compensatory plan, contract or arrangement.

SIGNATURES

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

KOHLBERG CAPITAL CORPORATION

Date: March 4, 2011

By /s/ DAYL W. PEARSON

Dayl W. Pearson
President and Chief Executive Officer

* * * * *

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ DAYL W. PEARSON **DAYL W. PEARSON**	President and Chief Executive Officer (principal executive officer) and Member of the Board of Directors	March 4, 2011
/s/ MICHAEL I. WIRTH **MICHAEL I. WIRTH**	Chief Financial Officer, Chief Compliance Officer, Secretary and Treasurer (principal financial and accounting officer)	March 4, 2011
/s/ CHRISTOPHER LACOVARA **CHRISTOPHER LACOVARA**	Member of the Board of Directors	March 4, 2011
/s/ SAMUEL P. FRIEDER **SAMUEL P. FRIEDER**	Member of the Board of Directors	March 4, 2011
/s/ GARY CADEMARTORI **GARY CADEMARTORI**	Member of the Board of Directors	March 4, 2011
/s/ C. MICHAEL JACOBI **C. MICHAEL JACOBI**	Member of the Board of Directors	March 4, 2011
/s/ ALBERT G. PASTINO **ALBERT G. PASTINO**	Member of the Board of Directors	March 4, 2011
/s/ C. TURNEY STEVENS, JR. **C. TURNEY STEVENS, JR.**	Member of the Board of Directors	March 4, 2011

TABLE OF CONTENTS

INDEX TO FINANCIAL STATEMENTS

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Stockholders of
Kohlberg Capital Corporation

We have audited the accompanying balance sheets, including the schedule of investments, of Kohlberg Capital Corporation and subsidiary (the "Company") (a Delaware corporation) as of December 31, 2010 and 2009, and the related statements of operations, changes in net assets, cash flows and financial highlights for each of the three years in the period ended December 31, 2010. These financial statements and financial highlights are the responsibility of the Company's management. Our responsibility is to express an opinion on the financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. Our procedures included confirmation of investments owned as of December 31, 2010 and 2009. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of Kohlberg Capital Corporation and subsidiary as of December 31, 2010 and 2009, and the results of their operations, changes in their net assets and their cash flows and financial highlights for each of the three years in the period ended December 31, 2010 in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Kohlberg Capital Corporation and subsidiary's internal control over financial reporting as of December 31, 2010, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"), and our report dated March 4, 2011 expressed an unqualified opinion.

/s/ GRANT THORNTON LLP

New York, New York
March 4, 2011

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Stockholders of
Kohlberg Capital Corporation

We have audited Kohlberg Capital Corporation and subsidiary's (the "Company") (a Delaware Corporation) internal control over financial reporting as of December 31, 2010, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Kohlberg Capital Corporation maintained, in all material respects, effective internal control over financial reporting as of December 31, 2010, based on criteria established in *Internal Control — Integrated Framework* issued by COSO.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the accompanying balance sheets of the Company, including the schedule of investments as of December 31, 2010 and 2009, and the related statements of operations, changes in net assets, and cash flows and financial highlights for each of the three years in the period ended December 31, 2010, and our report dated March 4, 2011 expressed an unqualified opinion.

/s/ GRANT THORNTON LLP

New York, New York
March 4, 2011

TABLE OF CONTENTS

KOHLBERG CAPITAL CORPORATION

BALANCE SHEETS

	As of December 31, 2010	As of December 31, 2009
ASSETS		
Investments at fair value:		
Time deposits (cost: 2010 – $720,225; 2009 – $126)	$ 720,225	$ 126
Money market account (cost: 2010 – $210,311; 2009 – $0)	210,311	—
Debt securities (cost: 2010 – $126,545,510; 2009 – $342,056,023)	91,042,928	297,356,529
CLO fund securities managed by non-affiliates (cost: 2010 – $15,690,982; 2009 – $15,685,858)	4,921,000	4,021,000
CLO fund securities managed by affiliate (cost: 2010 – $52,589,218; 2009 – $52,509,191)	48,110,000	44,950,000
Equity securities (cost: 2010 – $13,483,227; 2009 – $12,365,603)	4,688,832	4,713,246
Asset manager affiliates (cost: 2010 – $44,532,329; 2009 – $40,751,511)	41,493,000	58,064,720
Total Investments at fair value	191,186,296	409,105,621
Cash	10,175,488	4,140,408
Restricted cash	67,023,170	18,696,023
Interest and dividends receivable	2,574,115	3,836,031
Receivable for open trades	7,681,536	2,953,500
Accounts Receivable	851,020	—
Due from affiliates	—	44,274
Other assets	331,061	640,200
Total assets	$279,822,686	$ 439,416,057
LIABILITIES		
Borrowings	$ 86,746,582	$ 218,050,363
Accounts payable and accrued expenses	2,337,767	3,057,742
Dividend payable	3,812,670	4,412,228
Total liabilities	$ 92,897,019	$ 225,520,333
STOCKHOLDERS' EQUITY		
Common stock, par value $0.01 per share, 100,000,000 common shares authorized; 22,767,130 and 22,363,281 common shares issued and outstanding at December 31, 2010 and December 31, 2009, respectively.	$ 224,274	$ 220,611
Capital in excess of par value	282,794,025	283,074,233
Accumulated undistributed net investment income	818,664	1,326,380
Accumulated net realized losses	(34,325,792)	(16,462,808)
Net unrealized depreciation on investments	(62,585,504)	(54,262,692)
Total stockholders' equity	$186,925,667	$ 213,895,724
Total liabilities and stockholders' equity	$279,822,686	$ 439,416,057
NET ASSET VALUE PER COMMON SHARE	$ 8.21	$ 9.56

See accompanying notes to financial statements.

TABLE OF CONTENTS

KOHLBERG CAPITAL CORPORATION

STATEMENTS OF OPERATIONS

	For the Years Ended December 31,		
	2010	2009	2008
Investment Income:			
Interest from investments in debt securities	$ 14,409,069	$ 24,157,213	$ 33,386,213
Interest from cash and time deposits	21,531	17,956	251,287
Dividends from investments in CLO fund securities managed by non-affiliates	1,837,024	1,296,349	5,946,736
Dividends from investments in CLO fund securities managed by affiliate	8,371,007	8,025,695	6,624,742
Dividends from affiliate asset manager	4,500,000	—	1,350,000
Capital structuring service fees	215,233	399,338	1,653,232
Total investment income	29,353,864	33,896,551	49,212,210
Expenses:			
Interest and amortization of debt issuance costs	7,088,202	9,276,563	10,925,624
Compensation	3,322,895	3,222,604	3,940,638
Professional fees	5,411,499	1,691,832	1,992,142
Insurance	419,942	359,062	286,456
Administrative and other	1,214,207	990,835	1,361,433
Total expenses	17,456,745	15,540,896	18,506,293
Net Investment Income before Income Tax Expense	**11,897,119**	**18,355,655**	**30,705,917**
Excise taxes	—	(25,000)	—
Net Investment Income	**11,897,119**	**18,330,655**	**30,705,917**
Realized And Unrealized Gains (Losses) On Investments:			
Net realized gain (loss) from investment transactions	(17,862,984)	(15,782,121)	(575,179)
Net change in unrealized appreciation (depreciation) on:			
Debt securities	9,196,912	25,300,586	(57,514,397)
Equity securities	(1,142,038)	(7,485,064)	124,406
CLO fund securities managed by affiliate	3,079,974	12,986,453	(20,989,960)
CLO fund securities managed by non-affiliates	894,877	(473,907)	(5,705,371)
Affiliate asset manager investments	(20,352,537)	1,526,668	(9,328,824)
Net realized and unrealized appreciation (depreciation) on investments	(26,185,796)	16,072,615	(93,989,325)
Net Increase (Decrease) In Stockholders' Equity Resulting From Operations	**$(14,288,677)**	**$ 34,403,270**	**$ (63,283,408)**
Net Increase (Decrease) in Stockholders' Equity Resulting from Operations per Common Share – Basic and Diluted	$ (0.63)	$ 1.56	$ (3.09)
Net Investment Income Per Common Share – Basic	$ 0.53	$ 0.83	$ 1.50
Net Investment Income Per Common Share – Diluted	$ 0.53	$ 0.83	$ 1.50
Net Investment Income and Net Realized Gains (Losses) Per Common Share – Basic	$ (0.26)	$ 0.12	$ 1.47
Net Investment Income and Net Realized Gains (Losses) Per Common Share – Diluted	$ (0.26)	$ 0.12	$ 1.47
Weighted Average Shares of Common Stock Outstanding – Basic	22,283,088	22,105,800	20,455,322
Weighted Average Shares of Common Stock Outstanding – Diluted	22,283,088	22,105,800	20,455,322

See accompanying notes to financial statements.

TABLE OF CONTENTS

KOHLBERG CAPITAL CORPORATION

STATEMENTS OF CHANGES IN NET ASSETS

	Year Ended December 31,		
	2010	2009	2008
Operations:			
Net investment income	$ 11,897,119	$ 18,330,655	$ 30,705,917
Net realized gain (loss) from investment transactions	(17,862,984)	(15,782,121)	(575,179)
Net change in unrealized gain (loss) on investments	(8,322,812)	31,854,736	(93,414,146)
Net increase (decrease) in net assets resulting from operations	(14,288,677)	34,403,270	(63,283,408)
Shareholder distributions:			
Dividends from net investment income to common stockholders	(11,897,119)	(18,330,654)	(29,377,019)
Dividends from net investment income to restricted stockholders	(55,404)	(125,053)	(246,626)
Common Stock Dividends in excess of net investment income	(3,269,688)	(1,747,018)	—
Net decrease in net assets resulting from stockholder distributions	(15,222,211)	(20,202,725)	(29,623,645)
Capital share transactions:			
Issuance of common stock for:			
Dividend reinvestment plan	1,621,074	2,218,818	2,591,296
Rights offering	—	—	26,925,214
Vesting of restricted stock	647	1,223	30
Stock based compensation	919,111	909,120	888,367
Net increase in net assets resulting from capital share transactions	2,540,832	3,129,161	30,404,907
Net assets at beginning of period	213,895,723	196,566,018	259,068,164
Net assets at end of period (including accumulated undistributed net investment income of $818,664, $1,326,380, and $2,865,434 in 2010, 2009, and 2008, respectively.	$186,925,667	$213,895,724	$ 196,566,018
Net asset value per common share	$ 8.21	$ 9.56	$ 9.03
Common shares outstanding at end of period	22,767,130	22,363,281	21,776,519

See accompanying notes to financial statements.

TABLE OF CONTENTS

KOHLBERG CAPITAL CORPORATION

STATEMENTS OF CASH FLOWS

	Year Ended December 31,		
	2010	2009	2008
OPERATING ACTIVITIES:			
Net increase (decrease) in stockholders' equity resulting from operations	$ (14,288,677)	$ 34,403,270	$ (63,283,408)
Adjustments to reconcile net increase (decrease) in stockholders' equity resulting from operations to net cash provided by operations:			
Net realized losses on investment transactions	17,862,984	15,782,121	575,179
Net change in unrealized (appreciation) depreciation on investments	8,322,812	(31,854,736)	93,414,146
Net accretion of discount on securities and loans	(466,826)	(1,706,928)	(2,173,290)
Amortization of debt issuance cost	595,614	824,695	522,016
Purchases of investments	(12,018,942)	(13,581,354)	(108,769,126)
Capital contribution to affiliate asset manager	(3,780,817)	(3,600,016)	—
Payment-in-kind interest income	(820,262)	(3,801)	(1,680,247)
Proceeds from sale and redemption of investments	204,092,344	81,459,787	75,181,093
Stock based compensation expense	919,112	909,121	888,367
Changes in operating assets and liabilities:			
Decrease in interest and dividends receivable	1,261,916	332,567	1,424,039
Decrease in other assets	(286,473)	251,550	255,501
Decrease in due from affiliates	44,274	346,315	150,184
Increase (decrease) in accounts payable and accrued expenses	(1,570,996)	(6,661)	(3,077,489)
Net cash provided by operating activities	199,866,063	83,555,930	(6,573,035)
FINANCING ACTIVITIES:			
Issuance of stock (net of offering costs)	647	1,223	26,925,244
Dividends paid in cash	(14,200,702)	(19,451,339)	(28,179,592)
Proceeds from issuance of debt	—	—	50,000,000
Cash paid on repayment of debt	(131,303,781)	(43,640,786)	(43,308,852)
Decrease in restricted cash	(48,327,147)	(16,576,032)	(701,123)
Net cash used in financing activities	(193,830,983)	(79,666,934)	4,735,677
CHANGE IN CASH	6,035,080	3,888,996	(1,837,358)
CASH, BEGINNING OF PERIOD	4,140,408	251,412	2,088,770
CASH, END OF PERIOD	$ 10,175,488	$ 4,140,408	$ 251,412
Supplemental Information:			
Interest paid during the period	$ 7,195,181	$ 8,297,586	$ 10,821,650
Non-cash dividends paid during the period under the dividend reinvestment plan	$ 1,621,074	$ 2,218,818	$ 2,591,296

See accompanying notes to financial statements.

TABLE OF CONTENTS

KOHLBERG CAPITAL CORPORATION
SCHEDULE OF INVESTMENTS
As of December 31, 2010

Debt Securities Portfolio

Portfolio Company/Principal Business	Investment Interest Rate[1]/Maturity	Principal	Cost	Value[2]
Advanced Lighting Technologies, Inc. *Home and Office Furnishings, Housewares, and Durable Consumer Products*	Senior Secured Loan — Revolving Loan 3.7%, Due 6/13	$ 1,080,000	$ 1,075,943	$ 979,452
Advanced Lighting Technologies, Inc.[6] Home and Office Furnishings, Housewares, and Durable Consumer Products	Junior Secured Loan — Second Lien Term Loan Note 6.3%, Due 6/14	5,000,000	5,000,000	5,000,000
Awesome Acquisition Company (CiCi's Pizza)[6] *Personal, Food and Miscellaneous Services*	Junior Secured Loan — Term Loan (Second Lien) 5.3%, Due 6/14	4,000,000	3,985,854	3,840,000
Bankruptcy Management Solutions, Inc.[6] *Diversified/Conglomerate Service*	Junior Secured Loan — Second Lien Facility 8.3%, Due 8/15	1,217,438	1,217,438	95,368
Bankruptcy Management Solutions, Inc.[6] *Diversified/Conglomerate Service*	Senior Secured Loan — Term Loan B 7.5%, Due 8/14	1,438,720	1,448,006	719,360
Bicent Power LLC[6] *Utilities*	Junior Secured Loan — Advance (Second Lien) 4.3%, Due 12/14	4,000,000	4,000,000	2,367,600
BP Metals, LLC (fka Constellation Enterprises)[6] *Mining, Steel, Iron and Non-Precious Metals*	Senior Secured Loan — Term Loan 12.0%, Due 6/13	3,982,143	3,982,143	4,002,054
Caribe Information Investments Incorporated[6] *Printing and Publishing*	Senior Secured Loan — Term Loan 2.5%, Due 3/13	1,611,045	1,608,021	1,273,692
Charlie Acquisition Corp.[9] *Personal, Food and Miscellaneous Services*	Mezzanine Investment — Senior Subordinated Notes 17.5%, Due 6/13	14,261,996	10,744,496	250,000
CoActive Technologies LLC (fka CoActive Technologies, Inc.)[6] *Machinery (Non-Agriculture, Non-Construction, Non-Electronic)*	Junior Secured Loan — Term Loan (Second Lien) 7.1%, Due 1/15	2,000,000	1,977,696	1,464,600
eInstruction Corporation[6] *Healthcare, Education and Childcare*	Junior Secured Loan — Term Loan (Second Lien) 7.8%, Due 7/14	10,000,000	10,000,000	10,000,000
Freescale Semiconductor, Inc. *Electronics*	Senior Subordinated Bond — 10.125% – 12/2016 - 35687MAP2 10.1%, Due 12/16	3,000,000	3,006,137	3,176,250
Ginn LA Conduit Lender, Inc.[9] *Buildings and Real Estate*[4]	Senior Secured Loan — First Lien Tranche A Credit-Linked Deposit 7.8%, Due 6/11	1,257,143	1,224,101	72,286
Ginn LA Conduit Lender, Inc.[9] *Buildings and Real Estate*[4]	Senior Secured Loan — First Lien Tranche B Term Loan 7.8%, Due 6/11	2,694,857	2,624,028	154,954
Ginn LA Conduit Lender, Inc.[9] *Buildings and Real Estate*[4]	Junior Secured Loan — Loan (Second Lien) 11.8%, Due 6/12	3,000,000	2,715,997	15,000
HMSC Corporation (aka Swett and Crawford)[6] *Insurance*	Junior Secured Loan — Loan (Second Lien) 5.8%, Due 10/14	5,000,000	4,890,322	4,049,000

See accompanying notes to financial statements.

Portfolio Company/Principal Business	Investment Interest Rate[1]/Maturity	Principal	Cost	Value[2]
Hunter Fan Company[6] *Home and Office Furnishings, Housewares, and Durable Consumer Products*	Junior Secured Loan — Loan (Second Lien) 7.0%, Due 10/14	$ 3,000,000	$ 3,000,000	$ 2,682,900
International Architectural Products, Inc.[6],[9] *Mining, Steel, Iron and Non-Precious Metals*	Senior Secured Loan — Term Loan 12.0%, Due 5/15	967,622	948,809	929,498
Intrapac Corporation/Corona Holdco[6] *Containers, Packaging and Glass*	Junior Secured Loan — Term Loans (Second Lien) 7.8%, Due 5/13	3,000,000	3,009,682	3,000,000
Jones Stephens Corp.[6],[9] *Buildings and Real Estate*[4]	Senior Secured Loan — Term Loan (2006) 7.8%, Due 9/12	9,541,180	9,527,522	6,364,921
KIK Custom Products Inc.[6] *Personal and Non Durable Consumer Products (Mfg. Only)*	Junior Secured Loan — Loan (Second Lien) 5.3%, Due 12/14	5,000,000	5,000,000	3,435,000
LBREP/L-Suncal Master I LLC[9] *Buildings and Real Estate*[4]	Junior Secured Loan — Term Loan (Third Lien) 15.0%, Due 2/12	2,332,868	2,332,868	933
LBREP/L-Suncal Master I LLC[6],[9] *Buildings and Real Estate*[4]	Senior Secured Loan — Term Loan (First Lien) 7.5%, Due 1/10	3,875,156	3,875,156	58,127
LBREP/L-Suncal Master I LLC[6],[9] *Buildings and Real Estate*[4]	Junior Secured Loan — Term Loan (Second Lien) 9.5%, Due 1/11	2,000,000	1,920,211	7,600
Legacy Cabinets, Inc.[6] *Home and Office Furnishings, Housewares, and Durable Consumer Products*	Senior Secured Loan — Term Loan 7.3%, Due 5/14	463,380	463,380	92,676
MCCI Group Holdings, LLC[6] *Healthcare, Education and Childcare*	Junior Secured Loan — Term Loan (Second Lien) 7.5%, Due 6/13	1,000,000	1,000,000	1,000,000
Pegasus Solutions, Inc.[12] *Leisure, Amusement, Motion Pictures, Entertainment*	Senior Subordinated Bond — Senior Subordinated Second Lien PIK Notes 13.0%, Due 4/14	1,314,459	1,314,459	1,314,459
Perseus Holding Corp.[7] *Leisure, Amusement, Motion Pictures, Entertainment*	Preferred Stock — Preferred Stock 14.0%, Due 1/00	400,000	400,000	356,960
QA Direct Holdings, LLC[6] *Printing and Publishing*	Senior Secured Loan — Term Loan 8.3%, Due 8/14	4,396,024	4,372,508	4,396,024
Resco Products, Inc. *Mining, Steel, Iron and Non-Precious Metals*	Junior Secured Loan — Term Loan (Second Lien) 20.0%, Due 6/14	2,078,079	2,078,079	2,078,079
Resco Products, Inc.[6] *Mining, Steel, Iron and Non-Precious Metals*	Junior Secured Loan — Term Loan (Second Lien) 20.0%, Due 6/14	7,193,458	7,079,981	7,193,458
Specialized Technology Resources, Inc.[6] *Diversified/Conglomerate Service*	Junior Secured Loan — Loan (Second Lien) 7.3%, Due 12/14	7,500,000	$ 7,500,000	$ 7,500,000
TUI University, LLC[6] *Healthcare, Education and Childcare*	Senior Secured Loan — Term Loan (First Lien) 3.3%, Due 10/14	3,119,818	3,033,934	2,958,212
Walker Group Holdings LLC *Cargo Transport*	Junior Secured Loan — Term Loan B 13.3%, Due 12/13	470,643	470,643	470,643
Walker Group Holdings LLC[6] *Cargo Transport*	Junior Secured Loan — Term Loan B 13.3%, Due 12/13	4,469,539	4,469,539	4,469,539

See accompanying notes to financial statements.

TABLE OF CONTENTS

Portfolio Company/Principal Business	Investment Interest Rate(1)/Maturity	Principal	Cost	Value(2)
Wesco Aircraft Hardware Corp. *Aerospace and Defense*	Junior Secured Loan — Loan (Second Lien) 6.0%, Due 3/14	$ 1,720,000	$ 1,679,298	$ 1,720,000
Wesco Aircraft Hardware Corp.(6) *Aerospace and Defense*	Junior Secured Loan — Loan (Second Lien) 6.0%, Due 3/14	3,554,283	3,569,258	3,554,283
Total Investment in Debt Securities (49% of net asset value at fair value)		$ 130,939,851	$126,545,510	$ 91,042,928

Equity Portfolio

Portfolio Company/Principal Business	Investment	Percentage Interest/Shares	Cost	Value(2)
Aerostructures Holdings L.P.(7) *Aerospace and Defense*	Partnership Interests	1.2%	$ 1,000,000	$ 88,600
Aerostructures Holdings L.P.(7) *Aerospace and Defense*	Series A Preferred Interests	1.2%	250,961	250,961
Bankruptcy Management Solutions, Inc.(6),(7) *Diversified/Conglomerate Service*	Warrants	0.1%	—	—
Coastal Concrete Holding II, LLC(7) *Buildings and Real Estate*(4)	Class A Units	10.8%	8,625,626	250,143
eInstruction Acquisition, LLC(7) *Healthcare, Education and Childcare*	Membership Units	1.1%	1,079,617	1,079,724
FP WRCA Coinvestment Fund VII, Ltd.(3),(7) *Machinery (Non-Agriculture, Non-Construction, Non-Electronic)*	Class A Shares	1,500	1,500,000	2,400,000
International Architectural Products, Inc.(6),(7) *Mining, Steel, Iron and Non-Precious Metals*	Common	2.5%	292,851	227,223
Legacy Cabinets, Inc.(6),(7) *Home and Office Furnishings, Housewares, and Durable Consumer Products*	Equity	4.0%	115,580	49,422
Perseus Holding Corp.(7) *Leisure, Amusement, Motion Pictures, Entertainment*	Common	0.2%	400,000	312,200
Bankruptcy Management Solutions, Inc.(6),(7) *Diversified/Conglomerate Service*	Common Stock	1.2%	218,592	30,559
Total Investment in Equity Securities (3% of net asset value at fair value)			$13,483,227	$ 4,688,832

CLO Fund Securities

CLO Equity Investments

Portfolio Company	Investment	Percentage Interest	Cost	Value(2)
Grant Grove CLO, Ltd.(3),(12)	Subordinated Securities	22.2%	$ 4,720,982	$ 3,150,000
Katonah III, Ltd.(3),(12)	Preferred Shares	23.1%	4,500,000	470,000
Katonah IV, Ltd.(3),(12)	Preferred Shares	17.1%	3,150,000	1,300,000
Katonah V, Ltd.(3),(12),(13)	Preferred Shares	26.7%	3,320,000	1,000
Katonah VII CLO Ltd.(3),(8),(12)	Subordinated Securities	16.4%	4,500,000	2,090,000
Katonah VIII CLO Ltd(3),(8),(12)	Subordinated Securities	10.3%	3,400,000	1,690,000
Katonah IX CLO Ltd(3),(8),(12)	Prefered Shares	6.9%	2,000,000	1,300,000
Katonah X CLO Ltd (3),(8),(12)	Subordinated Securities	33.3%	11,612,677	8,820,000
Katonah 2007-I CLO Ltd.(3),(8),(12)	Preferred Shares	100.0%	29,987,959	26,200,000
Total Investment in CLO Equity Securities			$67,191,618	$ 45,021,000

See accompanying notes to financial statements.

CLO Rated-Note Investment

Portfolio Company	Investment	Percentage Interest	Cost	Value[2]
Katonah 2007-I CLO Ltd.[3],[8],[12]	Class B-2L Notes Par Value of $10,500,000 5.2%, Due 4/22	100.0%	$ 1,088,582	$ 8,010,000
Total Investment in CLO Rated-Note			$ 1,088,582	$ 8,010,000
Total Investment in CLO Fund Securities (28% of net asset value at fair value)			$68,280,200	$ 53,031,000

Asset Manager Affiliate

Portfolio Company/Principal Business	Investment	Percentage Interest	Cost	Value[2]
Katonah Debt Advisors	Asset Management Company	100.0%	$44,532,329	$ 41,493,000
Total Investment in Asset Manager Affiliate (22% of net asset value at fair value)			$44,532,329	$ 41,493,000

Time Deposits and Money Market Account

Time Deposits and Money Market Account	Investment	Yield	Par/Cost	Value[2]
JP Morgan Asset Account	Time Deposit	0.03%	$ 720,225	$ 720,225
JP Morgan Business Money Market Account[11]	Money Market Account	0.2%	210,311	210,311
Total Investment in Time Deposit and Money Market Accounts (0% of net asset value at fair value)			$ 930,536	$ 930,536
Total Investments[5] (102% of net asset value at fair value)			$253,771,802	$191,186,296

(1) A majority of the variable rate loans to the Company's portfolio companies bear interest at a rate that may be determined by reference to either LIBOR or an alternate Base Rate (commonly based on the Federal Funds Rate or the Prime Rate), which typically resets semi-annually, quarterly, or monthly. For each such loan, the Company has provided the weighted average annual stated interest rate in effect at December 31, 2010.

(2) Reflects the fair market value of all existing investments as of December 31, 2010, as determined by the Company's Board of Directors.

(3) Non-U.S. company or principal place of business outside the U.S.

(4) Buildings and real estate relate to real estate ownership, builders, managers and developers and excludes mortgage debt investments and mortgage lenders or originators. As of December 31, 2010, the Company had no exposure to mortgage securities (residential mortgage bonds, commercial mortgage backed securities, or related asset backed securities), companies providing mortgage lending or emerging markets investments either directly or through the Company's investments in CLO funds.

(5) The aggregate cost of investments for federal income tax purposes is approximately $254 million. The aggregate gross unrealized appreciation is approximately $8 million and the aggregate gross unrealized depreciation is approximately $71 million.

(6) Pledged as collateral for the secured revolving credit facility (see Note 6 to the financial statements).

(7) Non-income producing.

(8) An affiliate CLO Fund managed by Katonah Debt Advisors, L.L.C. or its affiliate.

(9) Loan or debt security is on non-accrual status and therefore is considered non-income producing.

(10) Time deposit investment partially restricted under terms of the secured credit facility (see Note 6 to financial statements).

(11) Money market account holding restricted cash for employee flexible spending accounts.

(12) These securities were acquired in a transaction that was exempt from the registration requirements of the Securities Act of 1933, as amended (the "Securities Act"), pursuant to Rule 144A thereunder. These securities may be resold only in transactions that are exempt from the registration requirements of the Securities Act, normally to qualified institutional buyers.

(13) As of December 31, 2010, this CLO Fund Security was not providing a dividend distribution.

See accompanying notes to financial statements.

KOHLBERG CAPITAL CORPORATION

SCHEDULE OF INVESTMENTS
As of December 31, 2009

Debt Securities Portfolio

Portfolio Company/Principal Business	Investment Interest Rate[1]/Maturity	Principal	Cost	Value[2]
Advanced Lighting Technologies, Inc. *Home and Office Furnishings, Housewares, and Durable Consumer Products*	Senior Secured Loan — Revolving Loan 5.0%, Due 6/13	$ 640,000	$ 634,264	$ 637,440
Advanced Lighting Technologies, Inc.[6] *Home and Office Furnishings, Housewares, and Durable Consumer Products*	Senior Secured Loan — Deferred Draw Term Loan (First Lien) 3.0%, Due 6/13	323,595	323,595	322,301
Advanced Lighting Technologies, Inc.[6] *Home and Office Furnishings, Housewares, and Durable Consumer Products*	Junior Secured Loan — Second Lien Term Loan Note 6.2%, Due 6/14	5,000,000	5,000,000	5,000,000
Advanced Lighting Technologies, Inc.[6] *Home and Office Furnishings, Housewares, and Durable Consumer Products*	Senior Secured Loan — Term Loan (First Lien) 3.0%, Due 6/13	1,580,565	1,580,565	1,574,242
Aero Products International, Inc.[6] *Personal and Non Durable Consumer Products (Mfg. Only)*	Senior Secured Loan — Term Loan 9.5%, Due 4/12	3,118,560	3,118,560	1,721,445
Aerostructures Acquisition LLC[6] *Aerospace and Defense*	Senior Secured Loan — Delayed Draw Term Loan 6.8%, Due 3/13	412,667	412,667	412,667
Aerostructures Acquisition LLC[6] *Aerospace and Defense*	Senior Secured Loan — Term Loan 6.8%, Due 3/13	5,219,471	5,219,471	5,219,471
AGA Medical Corporation[6] *Healthcare, Education and Childcare*	Senior Secured Loan — Tranche B Term Loan 2.3%, Due 4/13	1,832,209	1,831,354	1,799,230
AGS LLC[6] *Hotels, Motels, Inns, and Gaming*	Senior Secured Loan — Delayed Draw Term Loan 3.2%, Due 5/13	425,866	421,983	389,241
AGS LLC[6] *Hotels, Motels, Inns, and Gaming*	Senior Secured Loan — Initial Term Loan 3.2%, Due 5/13	3,043,896	3,016,145	2,782,121
AmerCable Incorporated[6] *Machinery (Non-Agriculture, Non-Construction, Non-Electronic)*	Senior Secured Loan — Initial Term Loan 3.8%, Due 6/14	5,840,213	5,840,213	5,606,605
Astoria Generating Company Acquisitions, L.L.C.[6] *Utilities*	Junior Secured Loan — Term C 4.0%, Due 8/13	4,000,000	4,031,898	3,800,000
Atlantic Marine Holding Company[6] *Cargo Transport*	Senior Secured Loan — Term Loan 4.6%, Due 3/14	1,681,287	1,688,586	1,681,287
Aurora Diagnostics, LLC[6] *Healthcare, Education and Childcare*	Senior Secured Loan — Tranche A Term Loan (First Lien) 4.5%, Due 12/12	4,017,152	3,993,498	4,017,152
Awesome Acquisition Company (CiCi's Pizza)[6] *Personal, Food and Miscellaneous Services*	Junior Secured Loan — Term Loan (Second Lien) 5.3%, Due 6/14	4,000,000	3,981,723	3,924,000
AZ Chem US Inc.[6] *Chemicals, Plastics and Rubber*	Junior Secured Loan — Second Lien Term Loan 5.7%, Due 2/14	4,000,000	3,970,688	4,000,000
Bankruptcy Management Solutions, Inc.[6] *Diversified/Conglomerate Service*	Junior Secured Loan — Loan (Second Lien) 6.5%, Due 7/13	2,418,750	2,441,936	1,777,781

See accompanying notes to financial statements.

TABLE OF CONTENTS

Portfolio Company/Principal Business	Investment Interest Rate[1]/Maturity	Principal	Cost	Value[2]
Bankruptcy Management Solutions, Inc.[6] *Diversified/Conglomerate Service*	Senior Secured Loan — Term Loan (First Lien) 4.2%, Due 7/12	$ 1,870,497	$ 1,876,933	$ 1,509,491
Bicent Power LLC[6] *Utilities*	Junior Secured Loan — Advance (Second Lien) 4.3%, Due 12/14	4,000,000	4,000,000	3,528,000
BP Metals, LLC (fka Constellation Enterprises)[6] *Mining, Steel, Iron and Non-Precious Metals*	Senior Secured Loan — Term Loan 10.0%, Due 6/13	4,383,929	4,383,929	4,383,929
Broadlane, Inc.[6] *Healthcare, Education and Childcare*	Senior Secured Loan — Term Loan 8.5%, Due 8/13	2,741,832	2,711,990	2,741,832
Caribe Information Investments Incorporated[6] *Printing and Publishing*	Senior Secured Loan — Term Loan 2.5%, Due 3/13	1,676,743	1,672,195	1,653,269
Cast & Crew Payroll, LLC (Payroll Acquisition)[6] *Leisure, Amusement, Motion Pictures, Entertainment*	Senior Secured Loan — Initial Term Loan 3.2%, Due 9/12	7,693,290	7,709,678	7,654,824
CEI Holdings, Inc. (Cosmetic Essence)[6],[9] *Personal and Non Durable Consumer Products (Mfg. Only)*	Senior Secured Loan — Term Loan 8.1%, Due 3/13	1,454,368	1,407,135	780,116
Charlie Acquisition Corp.[9] *Personal, Food and Miscellaneous Services*	Mezzanine Investment — Senior Subordinated Notes 15.5%, Due 6/13	10,893,401	10,777,799	635,444
CoActive Technologies, Inc.[6] *Machinery (Non-Agriculture, Non-Construction, Non-Electronic)*	Senior Secured Loan — Term Loan (First Lien) 3.3%, Due 7/14	3,916,722	3,903,782	2,882,707
CoActive Technologies, Inc.[6] *Machinery (Non-Agriculture, Non-Construction, Non-Electronic)*	Junior Secured Loan — Term Loan (Second Lien) 7.0%, Due 1/15	2,000,000	1,972,218	1,062,000
Dealer Computer Services, Inc. (Reynolds & Reynolds)[6] *Electronics*	Junior Secured Loan — Term Loan (Second Lien) 5.8%, Due 10/13	1,000,000	1,006,261	1,000,000
Dealer Computer Services, Inc. (Reynolds & Reynolds)[6] *Electronics*	Junior Secured Loan — Term Loan (Third Lien) 7.8%, Due 4/14	7,700,000	7,538,614	7,700,000
Delta Educational Systems, Inc.[6] *Healthcare, Education and Childcare*	Senior Secured Loan — Term Loan 6.0%, Due 6/12	2,301,996	2,301,996	2,281,278
Dex Media West LLC *Printing and Publishing*	Senior Secured Loan — Tranche B Term Loan 7.0%, Due 10/14	4,696,402	4,312,579	4,348,868
Dresser, Inc.[6] *Machinery (Non-Agriculture, Non-Construction, Non-Electronic)*	Junior Secured Loan — Term Loan (Second Lien) 6.0%, Due 5/15	3,000,000	2,970,206	2,991,000
DRI Holdings, Inc.[6] *Healthcare, Education and Childcare*	Junior Secured Loan — US Term Loan (Second Lien) 6.5%, Due 7/15	6,000,000	5,502,222	5,700,000
Edgestone CD Acquisition Corp. (Custom Direct)[6] *Printing and Publishing*	Junior Secured Loan — Loan (Second Lien) 6.3%, Due 12/14	5,000,000	5,000,000	5,000,000
Edgestone CD Acquisition Corp. (Custom Direct)[6] *Printing and Publishing*	Senior Secured Loan — Term Loan (First Lien) 3.1%, Due 12/13	3,982,724	3,985,832	3,982,724
eInstruction Corporation[6] *Healthcare, Education and Childcare*	Senior Secured Loan — Initial Term Loan 4.3%, Due 7/13	4,017,321	4,017,321	3,969,113

See accompanying notes to financial statements.

TABLE OF CONTENTS

Portfolio Company/Principal Business	Investment Interest Rate[1]/Maturity	Principal	Cost	Value[2]
eInstruction Corporation[6] *Healthcare, Education and Childcare*	Junior Secured Loan — Term Loan (Second Lien) 7.8%, Due 7/14	$ 10,000,000	$10,000,000	$ 10,000,000
Endeavor Energy Resources, L.P.[6] *Oil and Gas*	Junior Secured Loan — Initial Loan (Second Lien) 5.3%, Due 4/12	4,000,000	4,000,000	4,000,000
Fasteners For Retail, Inc.[6] *Diversified/Conglomerate Manufacturing*	Senior Secured Loan — Term Loan 4.8%, Due 12/12	4,042,346	4,046,728	4,042,346
FD Alpha Acquisition LLC (Fort Dearborn)[6] *Printing and Publishing*	Senior Secured Loan — US Term Loan 3.2%, Due 11/12	1,538,635	1,462,409	1,538,635
First American Payment Systems, L.P.[6] *Finance*	Senior Secured Loan — Term Loan 3.3%, Due 10/13	3,198,000	3,198,000	3,198,000
First Data Corporation *Finance*	Senior Secured Loan — Initial Tranche B-2 Term Loan 3.0%, Due 9/14	2,440,944	2,262,445	2,174,881
Ford Motor Company[6] *Automobile*	Senior Secured Loan — Tranche B-1 Term Loan 3.3%, Due 12/13	1,942,429	1,940,876	1,800,631
Freescale Semiconductor, Inc. *Electronics*	Senior Subordinated Bond — 10.1%, Due 12/16	3,000,000	3,007,167	2,415,000
Frontier Drilling USA, Inc.[6] *Oil and Gas*	Senior Secured Loan — Term B Advance 9.3%, Due 6/13	2,000,000	1,998,652	2,000,000
Ginn LA Conduit Lender, Inc.[9] *Buildings and Real Estate*[4]	Senior Secured Loan — First Lien Tranche A Credit-Linked Deposit 7.8%, Due 6/11	1,257,143	1,224,101	89,634
Ginn LA Conduit Lender, Inc.[9] *Buildings and Real Estate*[4]	Senior Secured Loan — First Lien Tranche B Term Loan 7.8%, Due 6/11	2,694,857	2,624,028	195,377
Ginn LA Conduit Lender, Inc.[9] *Buildings and Real Estate*[4]	Junior Secured Loan — Loan (Second Lien) 11.8%, Due 6/12	3,000,000	2,715,997	60,000
Harland Clarke Holdings Corp. (fka Clarke American Corp.)[6] *Printing and Publishing*	Senior Secured Loan — Tranche B Term Loan 2.7%, Due 6/14	2,925,000	2,925,000	2,442,375
HMSC Corporation (aka Swett and Crawford)[6] *Insurance*	Junior Secured Loan — Loan (Second Lien) 5.8%, Due 10/14	5,000,000	4,861,123	4,490,000
Huish Detergents Inc.[6] *Personal and Non Durable Consumer Products (Mfg. Only)*	Junior Secured Loan — Loan (Second Lien) 4.5%, Due 10/14	1,000,000	1,000,000	1,000,000
Hunter Fan Company[6] *Home and Office Furnishings, Housewares, and Durable Consumer Products*	Senior Secured Loan — Initial Term Loan (First Lien) 2.7%, Due 4/14	3,723,929	3,605,519	3,239,818
Hunter Fan Company[6] *Home and Office Furnishings, Housewares, and Durable Consumer Products*	Junior Secured Loan — Loan (Second Lien) 7.0%, Due 10/14	3,000,000	3,000,000	2,550,000

See accompanying notes to financial statements.

TABLE OF CONTENTS

Portfolio Company/Principal Business	Investment Interest Rate[1]/Maturity	Principal	Cost	Value[2]
Infiltrator Systems, Inc.[6] *Ecological*	Senior Secured Loan — Term Loan 8.5%, Due 9/12	$ 2,699,907	$ 2,695,103	$ 2,699,907
Inmar, Inc.[6] *Retail Stores*	Senior Secured Loan — Term Loan 2.5%, Due 4/13	3,543,046	3,543,046	3,521,787
International Aluminum Corporation (IAL Acquisition Co.)[6],[9] *Mining, Steel, Iron and Non-Precious Metals*	Senior Secured Loan — Term Loan 5.0%, Due 3/13	2,973,711	2,973,711	1,987,926
Intrapac Corporation/Corona Holdco[6] *Containers, Packaging and Glass*	Senior Secured Loan — 1st Lien Term Loan 3.8%, Due 5/12	4,034,281	4,042,948	3,852,738
Intrapac Corporation/Corona Holdco[6] *Containers, Packaging and Glass*	Junior Secured Loan — Term Loan (Second Lien) 7.8%, Due 5/13	3,000,000	3,013,753	3,000,000
Jones Stephens Corp.[6] *Buildings and Real Estate*[4]	Senior Secured Loan — Term Loan 7.8%, Due 9/12	9,541,180	9,526,158	8,491,650
KIK Custom Products Inc.[6] *Personal and Non Durable Consumer Products (Mfg. Only)*	Junior Secured Loan — Loan (Second Lien) 5.3%, Due 12/14	5,000,000	5,000,000	3,060,000
La Paloma Generating Company, LLC[6] *Utilities*	Junior Secured Loan — Loan (Second Lien) 3.8%, Due 8/13	2,000,000	2,011,080	1,622,000
LBREP/L-Suncal Master I LLC[9] *Buildings and Real Estate*[4]	Junior Secured Loan — Term Loan (Third Lien) 15.0%, Due 2/12	2,332,868	2,332,868	1,000
LBREP/L-Suncal Master I LLC[6],[9] *Buildings and Real Estate*[4]	Senior Secured Loan — Term Loan (First Lien) 5.5%, Due 1/10	3,875,156	3,873,404	116,255
LBREP/L-Suncal Master I LLC[6],[9] *Buildings and Real Estate*[4]	Junior Secured Loan — Term Loan (Second Lien) 9.5%, Due 1/11	2,000,000	1,920,211	7,500
Legacy Cabinets, Inc.[6],[9] *Home and Office Furnishings, Housewares, and Durable Consumer Products*	Senior Secured Loan — Term Loan 6.6%, Due 8/12	2,258,184	2,258,184	537,416
Levlad, LLC & Arbonne International, LLC[6],[9] *Personal and Non Durable Consumer Products (Mfg. Only)*	Senior Secured Loan — Term Loan 7.8%, Due 3/14	2,660,729	2,660,729	1,341,007
LN Acquisition Corp. (Lincoln Industrial)[6] *Machinery (Non-Agriculture, Non-Construction, Non-Electronic)*	Junior Secured Loan — Initial Term Loan (Second Lien) 6.0%, Due 1/15	2,000,000	2,000,000	1,978,000
MCCI Group Holdings, LLC[6] *Healthcare, Education and Childcare*	Senior Secured Loan — Term Loan (First Lien) 4.3%, Due 12/12	5,754,849	5,743,304	5,622,487
MCCI Group Holdings, LLC[6] *Healthcare, Education and Childcare*	Junior Secured Loan — Term Loan (Second Lien) 7.5%, Due 6/13	1,000,000	1,000,000	1,000,000
National Interest Security Company, L.L.C. *Aerospace and Defense*	Mezzanine Investment — Mezzanine Facility 15.0%, Due 6/13	3,000,000	3,000,000	3,300,000

See accompanying notes to financial statements.

TABLE OF CONTENTS

Portfolio Company/Principal Business	Investment Interest Rate[1]/Maturity	Principal	Cost	Value[2]
National Interest Security Company, L.L.C. *Aerospace and Defense*	Junior Secured Loan — Second Lien Term Loan 15.0%, Due 6/13	$ 1,000,000	$ 1,000,000	$ 1,100,000
National Interest Security Company, L.L.C.[6] *Aerospace and Defense*	Senior Secured Loan — Term Loan — 1st Lien 7.8%, Due 12/12	7,650,000	7,650,000	7,650,000
Northeast Biofuels, LP[6],[9] *Farming and Agriculture*	Senior Secured Loan — Construction Term Loan 8.8%, Due 6/13	1,382,120	1,383,944	208,369
Northeast Biofuels, LP[6],[9] *Farming and Agriculture*	Senior Secured Loan — Synthetic LC Term Loan 8.8%, Due 6/13	57,257	57,333	8,632
PAS Technologies Inc. *Aerospace and Defense*	Senior Secured Loan — Incremental Term Loan Add On 4.3%, Due 6/11	632,022	632,022	632,022
PAS Technologies Inc.[6] *Aerospace and Defense*	Senior Secured Loan — Term Loan 4.3%, Due 6/11	3,125,000	3,117,290	3,125,000
Pegasus Solutions, Inc.[9],[10] *Leisure, Amusement, Motion Pictures, Entertainment*	Senior Unsecured Bond — 10.5%, Due 4/15	2,000,000	2,000,000	1,710,000
Pegasus Solutions, Inc.[6] *Leisure, Amusement, Motion Pictures, Entertainment*	Senior Secured Loan — Term Loan 7.8%, Due 4/13	4,863,083	4,863,083	4,863,083
Primus International Inc.[6] *Aerospace and Defense*	Senior Secured Loan — Term Loan 2.7%, Due 6/12	1,087,032	1,088,240	1,060,944
QA Direct Holdings, LLC[6] *Printing and Publishing*	Senior Secured Loan — Term Loan 8.3%, Due 8/14	4,540,186	4,509,168	4,540,186
Resco Products, Inc.[6] *Mining, Steel, Iron and Non-Precious Metals*	Junior Secured Loan — Term Loan (Second Lien) 20.0%, Due 6/14	6,650,000	6,503,858	6,650,000
Rhodes Companies, LLC, The[6],[9] *Buildings and Real Estate*[4]	Senior Secured Loan — First Lien Term Loan 11.8%, Due 11/10	1,685,674	1,636,741	298,241
Rhodes Companies, LLC, The[6],[9] *Buildings and Real Estate*[4]	Junior Secured Loan — Second Lien Term Loan 13.0%, Due 11/11	2,013,977	2,019,403	12,720
San Juan Cable, LLC[6] *Broadcasting and Entertainment*	Junior Secured Loan — Loan (Second Lien) 5.8%, Due 10/13	3,000,000	2,986,206	2,862,000
Schneller LLC[6] *Aerospace and Defense*	Senior Secured Loan — Term Loan 3.7%, Due 6/13	4,304,174	4,278,271	4,231,003
Seismic Micro-Technology, Inc. (SMT)[6] *Electronics*	Senior Secured Loan — Term Loan 3.2%, Due 6/12	838,694	837,545	829,469
Seismic Micro-Technology, Inc. (SMT)[6] *Electronics*	Senior Secured Loan — Term Loan 3.2%, Due 6/12	1,258,041	1,256,317	1,244,203

See accompanying notes to financial statements.

TABLE OF CONTENTS

Portfolio Company/Principal Business	Investment Interest Rate[1]/Maturity	Principal	Cost	Value[2]
Specialized Technology Resources, Inc.[6] *Diversified/Conglomerate Service*	Junior Secured Loan — Loan (Second Lien) 7.2%, Due 12/14	$ 7,500,000	$ 7,500,000	$ 7,500,000
Specialized Technology Resources, Inc.[6] *Diversified/Conglomerate Service*	Senior Secured Loan — Term Loan (First Lien) 2.7%, Due 6/14	3,563,166	3,563,166	3,563,166
Standard Steel, LLC[6] *Cargo Transport*	Senior Secured Loan — Delayed Draw Term Loan 8.3%, Due 7/12	738,349	741,143	738,349
Standard Steel, LLC[6] *Cargo Transport*	Senior Secured Loan — Initial Term Loan 9.0%, Due 7/12	3,663,267	3,677,125	3,663,267
Standard Steel, LLC[6] *Cargo Transport*	Junior Secured Loan — Loan (Second Lien) 13.8%, Due 7/13	1,750,000	1,756,512	1,750,000
TPF Generation Holdings, LLC[6] *Utilities*	Junior Secured Loan — Loan (Second Lien) 4.5%, Due 12/14	2,000,000	2,023,571	1,894,000
TUI University, LLC[6] *Healthcare, Education and Childcare*	Senior Secured Loan — Term Loan (First Lien) 3.2%, Due 10/14	3,590,407	3,465,781	3,590,407
Twin-Star International, Inc.[6] *Home and Office Furnishings, Housewares, and Durable Consumer Products*	Senior Secured Loan — Term Loan 4.3%, Due 4/13	4,291,879	4,291,879	4,218,917
Walker Group Holdings LLC *Cargo Transport*	Junior Secured Loan — Term Loan B12.5%, Due 12/12	526,500	526,500	526,500
Walker Group Holdings LLC[6] *Cargo Transport*	Junior Secured Loan — Term Loan B12.8%, Due 12/12	5,000,000	5,000,000	5,000,000
Water PIK, Inc.[6] *Personal and Non Durable Consumer Products (Mfg. Only)*	Senior Secured Loan — Loan (First Lien) 3.5%, Due 6/13	1,243,577	1,238,507	1,243,577
Wesco Aircraft Hardware Corp. *Aerospace and Defense*	Junior Secured Loan — Loan (Second Lien) 6.0%, Due 3/14	2,000,000	1,938,058	2,000,000
Wesco Aircraft Hardware Corp.[6] *Aerospace and Defense*	Junior Secured Loan — Loan (Second Lien) 6.0%, Due 3/14	4,132,887	4,155,678	4,132,887
WireCo WorldGroup Inc.[10] *Machinery (Non-Agriculture, Non-Construction, Non-Electronic)*	Mezzanine Investment — 11.0%, Due 2/15	5,000,000	4,829,054	5,100,000
WireCo WorldGroup Inc.[6],[10] *Machinery (Non-Agriculture, Non-Construction, Non-Electronic)*	Mezzanine Investment — 11.0%, Due 2/15	10,000,000	10,000,000	10,200,000
Wolf Hollow I, LP[6] *Utilities*	Senior Secured Loan — Acquisition Term Loan 2.5%, Due 6/12	767,269	761,240	743,484
Wolf Hollow I, LP[6] *Utilities*	Senior Secured Loan — Synthetic Letter of Credit. 1%, Due 6/12	668,412	663,160	647,691

See accompanying notes to financial statements.

TABLE OF CONTENTS

Portfolio Company/Principal Business	Investment Interest Rate[1]/Maturity	Principal	Cost	Value[2]
Wolf Hollow I, LP[6] *Utilities*	Senior Secured Loan — Synthetic Revolver Deposit 1.2%, Due 6/12	$ 167,103	$ 165,790	$ 161,923
Wolf Hollow I, LP[6] *Utilities*	Junior Secured Loan — Term Loan (Second Lien) 4.8%, Due 12/12	2,683,177	2,686,492	2,591,949
X-Rite, Incorporated[6] *Electronics*	Junior Secured Loan — Loan (Second Lien) 14.4%, Due 10/13	649,162	649,162	649,162
X-Rite, Incorporated[6] *Electronics*	Senior Secured Loan — Term Loan (First Lien) 7.5%, Due 10/12	581,049	579,404	569,430
Total Investment in Debt Securities (139% of net asset value at fair value)		$ 344,924,114	$342,056,023	$297,356,529

Equity Portfolio

Portfolio Company/Principal Business	Investment	Percentage Interest/Shares	Cost	Value[2]
Aerostructures Holdings L.P.[7] *Aerospace and Defense*	Partnership Interests	1.2%	$ 1,000,000	$ 350,280
Aerostructures Holdings L.P.[7] *Aerospace and Defense*	Series A Preferred Interests	1.2%	160,361	202,396
Coastal Concrete Holding II, LLC[7] *Buildings and Real Estate*[4]	Class A Units	10.8%	8,625,625	568,570
eInstruction Acquisition, LLC[7] *Healthcare, Education and Childcare*	Membership Units	1.1%	1,079,617	1,456,000
FP WRCA Coinvestment Fund VII, Ltd.[3],[7] *Machinery (Non-Agriculture, Non-Construction, Non-Electronic)*	Class A Shares	15,000	1,500,000	2,136,000
Total Investment in Equity Securities (2% of net asset value at fair value)			$12,365,603	$ 4,713,246

CLO Fund Securities

CLO Equity Investments

Portfolio Company	Investment	Percentage Interest	Cost	Value[2]
Grant Grove CLO, Ltd.[3],[10],[11]	Subordinated Securities	22.2%	$ 4,715,858	$ 2,780,000
Katonah III, Ltd.[3],[10]	Preferred Shares	23.1%	4,500,000	950,000
Katonah IV, Ltd.[3],[10],[11]	Preferred Shares	17.1%	3,150,000	290,000
Katonah V, Ltd.[3],[10],[11]	Preferred Shares	26.7%	3,320,000	1,000
Katonah VII CLO Ltd.[3],[8],[10],[11]	Subordinated Securities	16.4%	4,500,000	1,840,000
Katonah VIII CLO Ltd[3],[8],[10],[11]	Subordinated Securities	10.3%	3,400,000	1,760,000
Katonah IX CLO Ltd[3],[8],[10],[11]	Preferred Shares	6.9%	2,000,000	1,560,000
Katonah X CLO Ltd[3],[8],[10]	Subordinated Securities	33.3%	11,589,830	8,280,000
Katonah 2007-I CLO Ltd.[3],[8],[10]	Preferred Shares	100.0%	29,940,867	27,100,000
Total Investment in CLO Equity Securities			$67,116,555	$ 44,561,000

See accompanying notes to financial statements.

CLO Rated-Note Investment

Portfolio Company	Investment	Percentage Interest	Cost	Value[2]
Katonah 2007-I CLO Ltd.[3],[8],[10]	Class B-2L Notes Par Value of $10,500,000 5.3%, Due 4/22	100.0%	$ 1,078,494	$ 4,410,000
Total Investment in CLO Rated-Note			$ 1,078,494	$ 4,410,000
Total Investment in CLO Fund Securities (23% of net asset value at fair value)			$68,195,049	$ 48,971,000

Asset Manager Affiliate

Portfolio Company/Principal Business	Investment	Percentage Interest	Cost	Value[2]
Katonah Debt Advisors, L.L.C.	Membership Interests	100%	$40,751,511	$ 58,064,720
Total Investment in Asset Manager Affiliate (27% of net asset value at fair value)			$40,751,511	$ 58,064,720

Time Deposits and Money Market Account

Time Deposits and Money Market Account	Investment	Yield	Par/Cost	Value[2]
JP Morgan Asset Account	Time Deposit	0.07%	126	126
Total Investment in Time Deposit and Money Market Accounts (0% of net asset value at fair value)			$ 126	$ 126
Total Investments[5] (191% of net asset value at fair value)			$463,368,313	$ 409,105,621

---

(1) A majority of the variable rate loans to the Company’s portfolio companies bear interest at a rate that may be determined by reference to either LIBOR or an alternate Base Rate (commonly based on the Federal Funds Rate or the Prime Rate), which typically resets semi-annually, quarterly, or monthly. For each such loan, the Company has provided the weighted average annual stated interest rate in effect at December 31, 2009.

(2) Reflects the fair market value of all existing investments as of December 31, 2009, as determined by the Company’s Board of Directors.

(3) Non-U.S. company or principal place of business outside the U.S.

(4) Buildings and real estate relate to real estate ownership, builders, managers and developers and excludes mortgage debt investments and mortgage lenders or originators. As of December 31, 2009, the Company had no exposure to mortgage securities (residential mortgage bonds, commercial mortgage backed securities, or related asset backed securities), companies providing mortgage lending or emerging markets investments either directly or through the Company’s investments in CLO funds.

(5) The aggregate cost of investments for federal income tax purposes is approximately $463 million. The aggregate gross unrealized appreciation is approximately $24 million and the aggregate gross unrealized depreciation is approximately $78 million.

(6) Pledged as collateral for the secured revolving credit facility (see Note 6 to the financial statements).

(7) Non-income producing.

(8) An affiliate CLO Fund managed by Katonah Debt Advisors L.L.C. or its affiliate.

(9) Loan or debt security is on non-accrual status and therefore is considered non-income producing.

(10) These securities were acquired in a transaction that was exempt from the registration requirements of the Securities Act of 1933, as amended (the “Securities Act”), pursuant to Rule 144A thereunder. These securities may be resold only in transactions that are exempt from the registration requirements of the Securities Act, normally to qualified institutional buyers.

(11) As of December 31, 2009, these CLO Fund securities were not providing a dividend distribution.

See accompanying notes to financial statements.

TABLE OF CONTENTS

KOHLBERG CAPITAL CORPORATION
FINANCIAL HIGHLIGHTS

($ per share)

	For the Years Ended December 31, 2010	2009	2008
Per Share Data:			
Net asset value, at beginning of period	$ 9.56	$ 9.03	$ 14.38
Net income (loss)			
Net investment income[1]	0.53	0.83	1.50
Net realized losses[1]	(0.79)	(0.71)	(0.03)
Net change in unrealized appreciation/depreciation on investments[1]	(0.54)	1.19	(6.80)
Net income	(0.80)	1.31	(5.33)
Net decrease in net assets resulting from distributions			
From net investment income	(0.52)	(0.84)	(1.43)
In excess of net investment income	(0.14)	(0.08)	(0.01)
Net decrease in net assets resulting from distributions	(0.66)	(0.92)	(1.44)
Net increase in net assets relating to stock-based transactions			
Issuance of common stock (not including DRIP)	—	—	1.26
Issuance of common stock under dividend reinvestment plan	0.07	0.10	0.12
Stock based compensation expense	0.04	0.04	0.04
Net increase in net assets relating to stock-based transactions	0.11	0.14	1.42
Net asset value, end of period	$ 8.21	$ 9.56	$ 9.03
Total net asset value return[2]	(7.1)%	16.0%	(27.2)%
Ratio/Supplemental Data:			
Per share market value at beginning of period	$ 4.56	$ 3.64	$ 12.00
Per share market value at end of period	$ 6.97	$ 4.56	$ 3.64
Total market return[3]	67.6%	50.5%	(57.7)%
Shares outstanding at end of period	22,767,130	22,363,281	21,771,186
Net assets at end of period	$186,925,667	$213,895,724	$196,566,018
Portfolio turnover rate	3.4%	3.2%	14.4%
Average debt outstanding	$154,952,070	$236,184,703	$248,300,441
Average debt outstanding per share	$ 6.81	$ 10.56	$ 11.41
Asset coverage ratio	315%	198%	175%
Ratio of net investment income to average net assets	5.8%	8.7%	12.0%
Ratio of total expenses to average net assets	8.5%	7.4%	7.2%
Ratio of interest expense to average net assets	3.4%	4.4%	4.3%
Ratio of non-interest expenses to average net assets	5.0%	3.0%	3.0%

(1) Based on weighted average number of common shares outstanding for the period.

(2) Total net asset value return (not annualized) equals the change in the net asset value per share over the beginning of period net asset value per share plus dividends, divided by the beginning net asset value per share.

(3) Total market return equals the change in the ending market price over the beginning of period price per share plus dividends, divided by the beginning price.

See accompanying notes to financial statements.

KOHLBERG CAPITAL CORPORATION

NOTES TO FINANCIAL STATEMENTS

1. ORGANIZATION

Kohlberg Capital Corporation ("Kohlberg Capital" or the "Company") is an internally managed, non-diversified closed-end investment company that is regulated as a business development company ("BDC") under the Investment Company Act of 1940. The Company originates, structures and invests in senior secured term loans, mezzanine debt and selected equity securities primarily in privately-held middle market companies. The Company defines the middle market as comprising companies with earnings before interest, taxes, depreciation and amortization ("EBITDA"), of $10 million to $50 million and/or total debt of $25 million to $150 million. The Company was formed as a Delaware limited liability company on August 8, 2006 and, prior to the issuance of shares of the Company's common stock in its initial public offering, converted to a corporation incorporated in Delaware on December 11, 2006. Prior to its initial public offering ("IPO"), the Company did not have material operations. The Company's IPO of 14,462,000 shares of common stock raised net proceeds of approximately $200 million. Prior to the IPO, the Company issued 3,484,333 shares to affiliates of Kohlberg & Co., L.L.C. ("Kohlberg & Co."), a leading middle market private equity firm, in exchange for the contribution of their ownership interests in Katonah Debt Advisors, L.L.C. (collectively with its affiliates, "Katonah Debt Advisors") and in securities issued by collateralized loan obligation funds ("CLO Funds") managed by Katonah Debt Advisors and two other asset managers to the Company. As of December 31, 2010, Katonah Debt Advisors had approximately $2.1 billion of assets under management.

The Company's investment objective is to generate current income and capital appreciation from investments made in senior secured term loans, mezzanine debt and selected equity investments in privately-held middle market companies. The Company also expects to continue to receive distributions of recurring fee income and to generate capital appreciation from its investment in the asset management business of Katonah Debt Advisors. Katonah Debt Advisors manages CLO Funds which invest in broadly syndicated loans, high-yield bonds and other credit instruments. The Company's investment portfolio as well as the investment portfolios of the CLO Funds in which it has invested and the investment portfolios of the CLO Funds managed by Katonah Debt Advisors consist exclusively of credit instruments and other securities issued by corporations and do not include any asset-backed securities secured by commercial mortgages, residential mortgages or other consumer borrowings.

The Company has elected to be treated as a regulated investment company ("RIC") under Subchapter M of the Internal Revenue Code of 1986, as amended (the "Code"). To qualify as a RIC, the Company must, among other things, meet certain source-of-income and asset diversification requirements. As a RIC, the Company generally will not have to pay corporate-level taxes on any income that it distributes in a timely manner to its stockholders.

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The financial statements include the accounts of the Company and the accounts of its special purpose financing subsidiary, Kohlberg Capital Funding LLC I. In accordance with Article 6 of Regulation S-X under the Securities Act of 1933 and Securities Exchange Act of 1934, the Company does not consolidate portfolio company investments, including those in which it has a controlling interest (Katonah Debt Advisors, including its affiliates, is currently the only company in which the Company has a controlling interest).

The accompanying financial statements have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America ("GAAP").

The financial statements reflect all adjustments, both normal and recurring which, in the opinion of management, are necessary for the fair presentation of the Company's results of operations and financial condition for the periods presented. Furthermore, the preparation of the financial statements requires management to make significant estimates and assumptions including the fair value of investments that do not have a readily available market value. Actual results could differ from those estimates, and the differences

2. SIGNIFICANT ACCOUNTING POLICIES – (continued)

could be material. The results of operations for the interim periods presented are not necessarily indicative of the operating results to be expected for the full year.

Accounting Standards Codification. In June 2009, the Financial Accounting Standards Board ("FASB") issued a pronouncement establishing the FASB Accounting Standards Codification ("ASC") as the source of authoritative accounting principles recognized by the FASB to be applied in the preparation of financial statements in conformity with GAAP. The ASC reorganized existing U.S. accounting and reporting standards issued by the FASB and other related private sector standard setters into a single source of authoritative accounting principles arranged by topic. The standard explicitly recognizes rules and interpretive releases of the Commission under federal securities laws as authoritative GAAP for SEC registrants. The ASC supersedes all existing U.S. accounting standards; all other accounting literature not included in the ASC (other than SEC guidance for publicly-traded companies) is considered non-authoritative. The ASC was effective on a prospective basis for interim and annual reporting periods ending after September 15, 2009. The adoption of the ASC changed the Company's references to U.S. GAAP accounting standards but did not impact its results of operations, financial position or liquidity.

Investments

Investment transactions are recorded on the applicable trade date. Realized gains or losses are determined using the specific identification method.

Valuation of Portfolio Investments. The Company's Board of Directors is ultimately and solely responsible for making a good faith determination of the fair value of portfolio investments on a quarterly basis. Debt and equity securities for which market quotations are readily available are generally valued at such market quotations. Debt and equity securities that are not publicly traded or whose market price is not readily available are valued by the Board of Directors based on detailed analyses prepared by management, the Valuation Committee of the Board of Directors, and, in certain circumstances, third parties with valuation expertise. Valuations are conducted by management on 100% of the investment portfolio at the end of each quarter. The Company follows the provisions of ASC Fair Value Measurements and Disclosures ("*Fair Value Measurements and Disclosures*"). This standard defines fair value, establishes a framework for measuring fair value, and expands disclosures about assets and liabilities measured at fair value. *Fair Value Measurements and Disclosures* defines "fair value" as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Subsequent to the adoption of *Fair Value Measurements and Disclosures*, the FASB has issued various staff positions clarifying the initial standard as noted below.

In January 2010, the FASB issued guidance that clarifies and requires new disclosures about fair value measurements. The clarifications and requirement to disclose the amounts and reasons for significant transfers between Level I and Level II, as well as significant transfers in and out of Level III of the fair value hierarchy, were adopted by the Company in the first quarter of 2010. Note 4 below reflects the amended disclosure requirements. The new guidance also requires that purchases, sales, issuances and settlements be presented gross in the Level III reconciliation and that requirement is effective for fiscal years beginning after December 15, 2010 and for interim periods within those years. The Company is evaluating the increased disclosure requirements for implementation by the effective date. Since this new guidance only amends the disclosures requirements, it did not impact our statements of financial position, statements of operations, or cash flow statements.

Fair Value Measurements and Disclosures requires the disclosure in interim and annual periods of the inputs and valuation techniques used to measure fair value and a discussion of changes in valuation techniques and related inputs, if any, during the period.

KOHLBERG CAPITAL CORPORATION

NOTES TO FINANCIAL STATEMENTS

2. SIGNIFICANT ACCOUNTING POLICIES – (continued)

The Company engaged Valuation Research Corporation ("VRC"), an independent valuation firm, to provide third-party valuation estimates for approximately 39% of its portfolio at fair value as of December 31, 2009. VRC's valuation estimates were considered as one of the relevant data inputs in the Company's determination of fair value. Though the Board of Directors did not engage VRC to provide valuation estimates for any of the assets in the Company's portfolio as of December 31, 2010, the Board of Directors engaged VRC to review the Company's CLO fair value model relative to its functionality, model inputs and calculations as a reasonable method to determine CLO fair values, in the absence of Level 1 or Level 2 trading activity or observable market inputs. VRC concluded that the Company's CLO model appropriately factored in all the necessary inputs required to build a CLO equity cash flow for fair value purposes and that the inputs were being employed correctly. The Board of Directors may engage an independent valuation firm in the future to provide certain valuation services, including the review of certain portfolio assets, as part of the Company's valuation processes.

The Board of Directors may consider other methods of valuation than those set forth above to determine the fair value of Level III investments as appropriate in conformity with GAAP. Due to the inherent uncertainty of determining the fair value of investments that do not have a readily available market value, the fair value of the Company's investments may differ materially from the values that would have been used had a ready market existed for such investments. Further, such investments may be generally subject to legal and other restrictions on resale or otherwise be less liquid than publicly traded securities. In addition, changes in the market environment and other events may occur over the life of the investments that may cause the value realized on such investments to be different from the currently assigned valuations.

The Company's valuation methodology and procedures are as follows:

1) Each portfolio company or investment is cross-referenced to an independent pricing service to determine if a current market quote is available. The nature and quality of such quote is reviewed to determine reliability and relevance of the quote. Factors considered in this determination include whether the quote is from a transaction or is a broker quote, the date and aging of such quote, whether the transaction is arms-length, whether it is of a liquidation or distressed nature and certain other factors judged to be relevant by management within the framework of Fair Value Measurements and Disclosures.

2) If an investment does not have a market quotation on either a broad market exchange or from an independent pricing service, the investment is initially valued by the Company's investment professionals responsible for the portfolio investment in conjunction with the portfolio management team.

3) Preliminary valuation conclusions are discussed and documented by management.

4) Illiquid loans, junior and mezzanine securities, equity investments, CLO Fund securities and Katonah Debt Advisors may be selected for review by an independent valuation firm, which is engaged by the Company's Board of Directors. Such independent valuation firm reviews management's preliminary valuations and makes their own independent valuation assessment.

5) The Valuation Committee of the Board of Directors reviews the portfolio valuations, as well as the input and report of such independent valuation firm, as applicable.

KOHLBERG CAPITAL CORPORATION

NOTES TO FINANCIAL STATEMENTS

2. SIGNIFICANT ACCOUNTING POLICIES – (continued)

6) Upon approval of the investment valuations by the Valuation Committee of the Board of Directors, the Audit Committee of the Board of Directors reviews the results for inclusion in the Company's quarterly and annual financial statements, as applicable.

7) The Board of Directors discusses the valuations and determines in good faith that the fair values of each investment in the portfolio is reasonable based upon any applicable independent pricing service, input of management, estimates from independent valuation firms (if any) and the recommendations of the Valuation Committee of the Board of Directors.

The majority of the Company's investment portfolio is composed of debt and equity securities with unique contract terms and conditions and/or complexity that requires a valuation of each individual investment that considers multiple levels of market and asset specific inputs, including historical and forecasted financial and operational performance of the individual investment, projected cash flows, market multiples, comparable market transactions, the priority of the security compared with those of other securities for such issuers, credit risk, interest rates, and independent valuations and reviews.

Loans and Debt Securities. To the extent that the Company's investments are exchange traded and are priced or have sufficient price indications from normal course trading at or around the valuation date (financial reporting date), such pricing will determine fair value. Pricing service marks from third party pricing services may be used as an indication of fair value, depending on the volume and reliability of the marks, sufficient and reasonable correlation of bid and ask quotes, and, most importantly, the level of actual trading activity. However, most of the Company's investments are illiquid investments with little or no trading activity. Further, the Company has been unable to identify directly comparable market indices or other market guidance that correlate directly to the types of investments the Company owns. As a result, for most of its assets, the Company determines fair value using alternative methodologies using available market data, as adjusted, to reflect the types of assets the Company owns, their structure, qualitative and credit attributes and other asset specific characteristics.

The Company derives fair value for its illiquid investments that do not have indicative fair values based upon active trades primarily by using a present value technique that discounts the estimated contractual cash flows for the underlying assets with discount rates imputed by broad market indices, bond spreads and yields for comparable issuers relative to the subject assets (the "Market Yield Approach") and also considers recent loan amendments or other activity specific to the subject asset. Discount rates applied to estimated contractual cash flows for an underlying asset vary by specific investment, industry, priority and nature of the debt security (such as the seniority or security interest of the debt security) and are assessed relative to two indices, a leveraged loan index and a high-yield bond index, at the valuation date. The Company has identified these two indices as benchmarks for broad market information related to its loan and debt investments. Because the Company has not identified any market index that directly correlates to the loan and debt investments held by the Company and therefore uses the two benchmark indices, these market indices may require significant adjustment to better correlate such market data for the calculation of fair value of the investment under the Market Yield Approach. Such adjustments require judgment and may be material to the calculation of fair value. Further adjustments to the discount rate may be applied to reflect other market conditions or the perceived credit risk of the borrower. When broad market indices are used as part of the valuation methodology, their use is subject to adjustment for many factors, including priority, collateral used as security, structure, performance and other quantitative and qualitative attributes of the asset being valued. The resulting present value determination is then weighted along with any quotes from observable transactions and broker/pricing quotes. If such quotes are indicative of actual transactions with reasonable trading volume at or near the valuation date that are not liquidation or distressed sales, relatively more reliance will be put on such quotes to determine fair value. If such quotes are not indicative of market transactions or are insufficient as to volume, reliability, consistency or other relevant factors, such quotes will be compared with other fair value

2. SIGNIFICANT ACCOUNTING POLICIES – (continued)

indications and given relatively less weight based on their relevancy. Other significant assumptions, such as coupon and maturity, are asset-specific and are noted for each investment in the Schedules of Investments.

Equity and Equity-Related Securities. The Company's equity and equity-related securities in portfolio companies for which there is no liquid public market are carried at fair value based on the enterprise value of the portfolio company, which is determined using various factors, including EBITDA and cash flows from operations less capital expenditures and other pertinent factors, such as recent offers to purchase a portfolio company's securities or other liquidation events. The determined fair values are generally discounted to account for restrictions on resale and minority ownership positions. The values of the Company's equity and equity-related securities in public companies for which market quotations are readily available are based upon the closing public market prices on the balance sheet date. Securities that carry certain restrictions on sale are typically valued at a discount from the public market value of the security.

The significant inputs used to determine the fair value of equity and equity-related securities include prices, earnings, EBITDA and cash flows after capital expenditures for similar peer comparables and the investment entity itself. Equity and equity related securities are classified as Level III, as described in Note 4 below, when there is limited activity or less transparency around inputs to the valuation given the lack of information related to such equity investments held in nonpublic companies. Significant assumptions observed for comparable companies are applied to relevant financial data for the specific investment. Such assumptions, such as model discount rates or price/earnings multiples, vary by the specific investment, equity position and industry and incorporate adjustments for risk premiums, liquidity and company specific attributes. Such adjustments require judgment and may be material to the calculation of fair value.

Affiliate Asset Manager. The Company's investment in its wholly-owned asset management company, Katonah Debt Advisors, is carried at fair value, which is determined after taking into consideration a percentage of assets under management and a discounted cash flow model incorporating different levels of discount rates depending on the hierarchy of fees earned (including the likelihood of realization of senior, subordinate and incentive fees) and prospective modeled performance. Such valuation includes an analysis of comparable asset management companies. Katonah Debt Advisors is classified as a Level III investment (as described below). Any change in value from period to period is recognized as net change in unrealized appreciation or depreciation.

CLO Fund Securities. The Company typically makes a minority investment in the most junior class of securities of CLO Funds raised and managed by Katonah Debt Advisors and may selectively invest in securities issued by funds managed by other asset management companies (collectively "CLO Fund securities"). The Company's CLO Fund securities relate exclusively to credit instruments issued by corporations and do not include any asset-backed securities secured by commercial mortgages, residential mortgages, or consumer borrowings.

The Company's investments in CLO Fund securities are carried at fair value, which is based either on (i) the present value of the net expected cash inflows for interest income and principal repayments from underlying assets and cash outflows for interest expense, debt paydown and other fund costs for the CLO Funds that are approaching or past the end of their reinvestment period and therefore are selling assets and/or using principal repayments to pay down CLO Fund debt (or will begin to do so shortly), and for which there continue to be net cash distributions to the class of securities owned by the Company, or (ii) a discounted cash flow model for more recent CLO Funds that utilizes prepayment and loss assumptions based on historical experience and projected performance, economic factors, the characteristics of the underlying cash flow and comparable yields for similar securities or preferred shares to those in which the Company has invested. The Company recognizes unrealized appreciation or depreciation on the Company's investments in CLO Fund securities as comparable yields in the market change and/or based on changes in NAVs or estimated cash flows resulting from changes in prepayment or loss assumptions in the underlying collateral pool. As each investment in CLO Fund securities ages, the expected amount of losses and the expected timing

KOHLBERG CAPITAL CORPORATION

NOTES TO FINANCIAL STATEMENTS

2. SIGNIFICANT ACCOUNTING POLICIES – (continued)

of recognition of such losses in the underlying collateral pool are updated and the revised cash flows are used in determining the fair value of the CLO Fund investment. The Company determines the fair value of its investments in CLO Fund securities on an individual security-by-security basis.

Due to the individual attributes of each CLO Fund security, they are classified as a Level III investment unless specific trading activity can be identified at or near the valuation date. When available, observable market information will be identified, evaluated and weighted accordingly in the application of such data to the present value models and fair value determination. Significant assumptions to the present value calculations include default rates, recovery rates, prepayment rates, investment/reinvestment rates and spreads and the discount rate by which to value the resulting underlying cash flows. Such assumptions can vary significantly, depending on market data sources which often vary in depth and level of analysis, understanding of the CLO market, detailed or broad characterization of the CLO market and the application of such data to an appropriate framework for analysis. The application of data points are based on the specific attributes of each individual CLO Fund security's underlying assets, historic, current and prospective performance, vintage, and other quantitative and qualitative factors that would be evaluated by market participants. The Company evaluates the source of market data for reliability as an indicative market input, consistency amongst other inputs and results and also the context in which such data is presented.

For bond rated tranches of CLO Fund securities (those above the junior class) without transactions to support a fair value for the specific CLO Fund and tranche, fair value is based on discounting estimated bond payments at current market yields, which may reflect the adjusted yield on the leveraged loan index for similarly rated tranches, as well as prices for similar tranches for other CLO Funds and also other factors such as the default and recovery rates of underlying assets in the CLO Fund, as may be applicable. Such model assumptions may vary and incorporate adjustments for risk premiums and CLO Fund specific attributes. Such adjustments require judgment and may be material to the calculation of fair value.

Cash. The Company defines cash as demand deposits. The Company places its cash with financial institutions and, at times, cash held in checking accounts may exceed the Federal Deposit Insurance Corporation insured limit.

Restricted Cash. Restricted cash consisted mostly of cash held in an operating account pursuant to the Company's secured credit facility agreement with its lender.

Time Deposits and Money Market Accounts. Time deposits primarily represent overnight Eurodollar investments of cash held in non-demand deposit accounts. Such time deposits were partially restricted under terms of the secured credit facility. The money market account contains restricted cash held for employee flexible spending accounts.

Interest Income. Interest income, including the amortization of premium and accretion of discount, is recorded on the accrual basis to the extent that such amounts are expected to be collected. The Company generally places a loan or security on non-accrual status and ceases recognizing cash interest income on such loan or security when a loan or security becomes 90 days or more past due or if the Company otherwise does not expect the debtor to be able to service its debt obligations. Non-accrual loans remain in such status until the borrower has demonstrated the ability and intent to pay contractual amounts due or such loans become current. As of December 31, 2010, five issuers representing 4.1% of total investments at fair value were considered in default.

Dividends from Affiliate Asset Manager. The Company records dividend income from its affiliate asset manager on the declaration date, which represents the ex-dividend date.

Dividend Income from CLO Fund Securities. The Company generates dividend income from its investments in the most junior class of securities of CLO Funds (typically preferred shares or subordinated securities) managed by Katonah Debt Advisors and selective investments in securities issued by funds

2. SIGNIFICANT ACCOUNTING POLICIES – (continued)

managed by other asset management companies. The Company's CLO Fund junior class securities are subordinated to senior bond holders who typically receive a fixed rate of return on their investment. The CLO Funds are leveraged funds and any excess cash flow or "excess spread" (interest earned by the underlying securities in the fund less payments made to senior bond holders and less fund expenses and management fees) is paid to the holders of the CLO Fund's subordinated securities or preferred shares. The Company makes estimated interim accruals of such dividend income based on recent historical distributions and CLO Fund performance and adjusts such accruals on a quarterly basis to reflect actual distributions.

For non-junior class CLO Fund securities, such as the Company's investment in the Class B-2L Notes of the Katonah 2007-1 CLO, interest is earned at a fixed spread relative to the LIBOR index.

Capital Structuring Service Fees. The Company may earn ancillary structuring and other fees related to the origination, investment, disposition or liquidation of debt and investment securities. Generally, the Company will capitalize loan origination fees, then amortize these fees into interest income over the term of the loan using the effective interest rate method, recognizes prepayment and liquidation fees upon receipt and equity structuring fees as earned, which generally occurs when an investment transaction closes.

Debt Issuance Costs. Debt issuance costs represent fees and other direct costs incurred in connection with the Company's borrowings. These amounts are capitalized and amortized ratably over the contractual term of the borrowing. At December 31, 2010, there was an unamortized debt issuance cost of approximately $23,000 included in other assets in the accompanying balance sheet. Amortization expense for the year ended December 31, 2010 and 2009 was approximately $596,000 and $825,000, respectively.

Expenses. The Company is internally managed and expenses costs, as incurred, with regard to the running of its operations. Primary operating expenses include employee salaries and benefits, the costs of identifying, evaluating, negotiating, closing, monitoring and servicing the Company's investments and related overhead charges and expenses, including rental expense, and any interest expense incurred in connection with borrowings. The Company and its asset manager affiliates share office space and certain other operating expenses. The Company has entered into an Overhead Allocation Agreement with its asset manager affiliates which provides for the sharing of such expenses based on an equal sharing of office lease costs and the ratable usage of other shared resources. The aggregate net payments of such expenses under the Overhead Allocation Agreement are not material.

Dividends. Dividends and distributions to common stockholders are recorded on the ex-dividend date. The amount to be paid out as a dividend is determined by the Board of Directors each quarter and is generally based upon the earnings estimated by management for the period and year.

The Company has adopted a dividend reinvestment plan that provides for reinvestment of its distributions on behalf of its stockholders, unless a stockholder "opts out" of the plan to receive cash in lieu of having their cash dividends automatically reinvested in additional shares of the Company's common stock.

Recent Accounting Pronouncements

Improved Disclosures Regarding Fair Value Measurements. In January 2010, the FASB issued Accounting Standards Update No. 2010-06, *Fair Value Measurements and Improving Disclosures About Fair Value Measurements (Topic 820)*, which provides for improving disclosures about fair value measurements, primarily significant transfers in and out of Levels I and II, and activity in Level III fair value measurements. The new disclosures and clarifications of existing disclosures are effective for the interim and annual reporting periods beginning after December 15, 2009, while the disclosures about the purchases, sales, issuances, and settlements in the roll forward activity in Level 3 fair value measurements are effective for fiscal years beginning after December 15, 2010 and for the interim periods within those fiscal years. Except for certain detailed Level III disclosures, which are effective for fiscal years beginning after December 15, 2010 and interim periods within those years, the new guidance became effective for the Company's fiscal 2010 second

KOHLBERG CAPITAL CORPORATION

NOTES TO FINANCIAL STATEMENTS

2. SIGNIFICANT ACCOUNTING POLICIES – (continued)

quarter. The adoption of this disclosure-only guidance is included in Note 4 "— Investments" and did not have a material impact on the Company's financial results.

Fair Value Measurements for Alternative Investments. In September 2009, the FASB issued Accounting Standards Update 2009-12, *Fair Value Measurements and Disclosures (Topic 820) — Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*, which provides guidance on estimating the fair value of an alternative investment, amending ASC 820-10. The amendment is effective for interim and annual periods ending after December 15, 2009. The adoption of this guidance did not have a material impact on either the Company's financial position or results of operations.

3. EARNINGS (LOSSES) PER SHARE

The following information sets forth the computation of basic and diluted net increase (decrease) in stockholders' equity per share for the years ended December 31, 2010, 2009, and 2008:

	For the Years ended December 31,		
	2010	2009	2008
Net increase (decrease) in net assets from operations	$(14,288,677)	$34,403,269	$ (63,283,408)
Net increase (decrease) in net assets allocated to non-vested share awards	—	(482,332)	—
Net increase (decrease) in net assets available to common stockholders	(14,288,677)	33,920,937	(63,283,408)
Weighted average number of common shares outstanding for basic shares computation	22,283,088	22,105,800	20,455,322
Effect of dilutive securities – stock options	—	—	—
Weighted average number of common and common stock equivalent shares outstanding for diluted shares computation	22,283,088	22,105,800	20,455,322
Basic and diluted net increase (decrease) in net assets per common shares:			
Net increase (decrease) in net assets from operations	(0.63)	1.53	(3.09)
Net increase (decrease) in net assets allocated to non-vested share awards	—	0.03	—

KOHLBERG CAPITAL CORPORATION

NOTES TO FINANCIAL STATEMENTS

4. INVESTMENTS

The Company invests in senior secured loans and mezzanine debt and, to a lesser extent, equity capital of middle market companies in a variety of industries. The Company generally targets companies that generate positive cash flows because the Company looks to cash flows as the primary source for servicing debt. However, the Company may invest in other industries if it is presented with attractive opportunities.

The following table shows the Company's portfolio by security type at December 31, 2010 and December 31, 2009:

	December 31, 2010			December 31, 2009		
Security Type	**Cost**	**Fair Value**	**%[(1)]**	**Cost**	**Fair Value**	**%[(1)]**
Time Deposits	$ 720,225	$ 720,225	—%	$ 126	$ 126	—%
Money Market Account	210,311	210,311	—	—	—	—
Senior Secured Loan	34,183,551	22,001,256	12	179,425,767	159,075,586	74
Junior Secured Loan	76,896,867	63,944,003	34	129,016,237	114,920,499	54
Mezzanine Investment	10,744,496	250,000	—	28,606,852	19,235,444	9
Senior Subordinated Bond	4,320,596	4,490,709	3	3,007,167	2,415,000	1
Senior Unsecured Bond	—	—	—	2,000,000	1,710,000	1
CLO Fund Securities	68,280,200	53,031,000	28	68,195,049	48,971,000	23
Equity Securities	13,232,266	4,437,871	3	12,365,603	4,713,246	2
Preferred	650,961	607,921	—	—	—	—
Affiliate Asset Managers	44,532,329	41,493,000	22	40,751,511	58,064,720	27
Total	$253,771,802	$191,186,296	102%	$463,368,312	$409,105,621	191%

(1) Calculated as a percentage of net asset value

TABLE OF CONTENTS

4. INVESTMENTS – (continued)

The unaudited industry concentrations, based on the fair value of the Company's investment portfolio as of December 31, 2010 and December 31, 2009, were as follows:

	December 31, 2010			December 31, 2009		
Industry Classification	**Cost**	**Fair Value**	**%(1)**	**Cost**	**Fair Value**	**%(1)**
Aerospace and Defense	$ 6,499,518	$ 5,613,844	3%	$ 33,652,058	$ 33,416,670	16%
Asset Management Companies(2)	44,532,329	41,493,000	22	40,751,511	58,064,720	27
Automobile	—	—	—	1,940,876	1,800,631	1
Broadcasting and Entertainment	—	—	—	2,986,206	2,862,000	1
Buildings and Real Estate(3)	32,845,509	6,923,964	4	36,498,537	9,840,946	5
Cargo Transport	4,940,182	4,940,182	3	13,389,865	13,359,403	6
Chemicals, Plastics and Rubber	—	—	—	3,970,688	4,000,000	2
CLO Fund Securities	68,280,200	53,031,000	28	68,195,049	48,971,000	23
Containers, Packaging and Glass	3,009,682	3,000,000	2	7,056,701	6,852,738	3
Diversified/Conglomerate Manufacturing	—	—	—	4,046,728	4,042,346	2
Diversified/Conglomerate Service	10,384,036	8,345,287	4	15,382,035	14,350,438	7
Ecological	—	—	—	2,695,103	2,699,907	1
Electronics	3,006,137	3,176,250	2	14,874,472	14,407,265	7
Farming and Agriculture	—	—	—	1,441,277	217,001	—
Finance	—	—	—	5,460,445	5,372,881	3
Healthcare, Education and Childcare	15,113,551	15,037,936	8	41,647,084	42,177,498	20
Home and Office Furnishings, Housewares, and Durable Consumer Goods	9,654,903	8,804,450	5	20,694,006	18,080,134	8
Hotels, Motels, Inns and Gaming	—	—	—	3,438,128	3,171,363	1
Insurance	4,890,322	4,049,000	2	4,861,123	4,490,000	2
Leisure, Amusement, Motion Pictures, Entertainment	2,114,458	1,983,619	1	14,572,761	14,227,907	7
Machinery (Non-Agriculture, Non-Construction, Non-Electronic)	3,477,696	3,864,600	2	33,015,472	31,956,312	15
Mining, Steel, Iron and Non-Precious Metals	14,381,863	14,430,312	8	13,861,498	13,021,854	6
Oil and Gas	—	—	—	5,998,652	6,000,000	3
Personal and Non Durable Consumer Products (Mfg. Only)	5,000,000	3,435,000	2	14,424,931	9,146,146	4
Personal, Food and Miscellaneous Services	14,730,350	4,090,000	2	14,759,522	4,559,444	2
Printing and Publishing	5,980,529	5,669,716	3	23,867,184	23,506,057	11
Retail Stores	—	—	—	3,543,046	3,521,787	2
Time Deposits and Money Market Account	930,537	930,536	—	126	126	—
Utilities	4,000,000	2,367,600	1	16,343,228	14,989,047	6
Total	$253,771,802	$191,186,296	102%	$463,368,312	$409,105,621	191%

(1) Calculated as a percentage of net asset value.

(2) Represents Katonah Debt Advisors and related asset manager affiliates.

(3) Buildings and real estate relate to real estate ownership, builders, managers and developers and excludes mortgage debt investments and mortgage lenders or originators. As of December 31, 2010 and December 31, 2009, the Company had no exposure to mortgage securities (residential mortgage bonds, commercial mortgage backed securities, or related asset backed securities) or companies providing mortgage lending.

KOHLBERG CAPITAL CORPORATION

NOTES TO FINANCIAL STATEMENTS

4. INVESTMENTS – (continued)

The Company may invest up to 30% of the investment portfolio in opportunistic investments in high-yield bonds, debt and equity securities of CLO Funds, distressed debt or equity securities of public companies. However, the Company's investment strategy is to limit the value of its investments in debt or equity securities issued by CLO Funds to not more than 15% of the value of its total investment portfolio at the time of investment. The Company expects that these public companies generally will have debt that is non-investment grade. The Company also may invest in debt of middle market companies located outside of the United States, which investments (excluding the Company's investments in CLO Funds) are generally not anticipated to be in excess of 10% of the investment portfolio at the time such investments are made. The Company is generally prohibited from buying or selling any security from or to any portfolio company of a private equity fund managed by Kohlberg & Co. without the prior approval of the SEC. In addition, the Company may co-invest on a concurrent basis with Kohlberg & Co. or any of its affiliates, subject to compliance with existing regulatory guidance, applicable regulations and its allocation procedures. Certain types of negotiated co-investments may be made only if the Company receives an order from the SEC permitting it to do so. There can be no assurance that any such order will be applied for or, if applied for, obtained.

At December 31, 2010 and December 31, 2009, approximately 29% and 12% of the Company's investments were foreign assets (including the Company's investments in CLO Funds, which are typically domiciled outside the U.S. and represented approximately 28% and 12% of its portfolio on such dates), respectively. At December 31, 2010, no foreign assets were in U.S. dollar denominated over-night time Eurodollar deposits which revert to cash each business morning.

At December 31, 2010 and December 31, 2009, the Company's ten largest portfolio companies represented approximately 65% and 37%, respectively, of the total fair value of its investments. The Company's largest investment, Katonah Debt Advisors which is its wholly-owned asset manager affiliate, represented 22% and 14% of the total fair value of the Company's investments at December 31, 2010 and December 31, 2009, respectively. Excluding Katonah Debt Advisors and CLO Fund securities, the Company's ten largest portfolio companies represented approximately 30% and 19% of the total fair value of the Company's investments at December 31, 2010 and December 31, 2009, respectively.

Investment in CLO Fund Securities

The Company typically makes a minority investment in the most junior class of securities of CLO Funds (typically preferred shares or subordinated securities) managed by Katonah Debt Advisors and may selectively invest in securities issued by funds managed by other asset management companies. However, as noted above, the Company's investment strategy is to limit the value of its investments in the debt or equity securities issued by CLO Funds to not more than 15% of the value of its total investment portfolio at the time of investment. Preferred shares or subordinated securities issued by CLO Funds are entitled to recurring dividend distributions which generally equal the net remaining cash flow of the payments made by the underlying CLO Fund's securities less contractual payments to senior bond holders and CLO Fund expenses. CLO Funds managed by Katonah Debt Advisors ("CLO fund securities managed by affiliate") invest primarily in broadly syndicated non-investment grade loans, high-yield bonds and other credit instruments of corporate issuers. The underlying assets in each of the CLO Funds in which the Company has an investment are generally diversified secured or unsecured corporate debt and exclude mortgage pools or mortgage securities (residential mortgage bonds, commercial mortgage backed securities, or related asset-backed securities), debt to companies providing mortgage lending and emerging markets investments. The CLO Funds are leveraged funds and any excess cash flow or "excess spread" (interest earned by the underlying securities in the fund less payments made to senior bond holders, fund expenses and management fees) is paid to the holders of the CLO Fund's subordinated securities or preferred shares.

KOHLBERG CAPITAL CORPORATION

NOTES TO FINANCIAL STATEMENTS

4. INVESTMENTS – (continued)

On January 23, 2008, the Company's wholly-owned asset management company, Katonah Debt Advisors, closed the Katonah 2007-1 CLO, a $315 million CLO Fund. The Company received a structuring fee upon closing and Katonah Debt Advisors earns an ongoing asset management fee based on the par amount of the underlying investments in the CLO Fund. Securities issued by CLO Funds managed by Katonah Debt Advisors are primarily held by third parties. Kohlberg Capital invested approximately $29 million to acquire all of the shares of the most junior class of securities of this CLO Fund.

The subordinated securities and preferred share securities are considered equity positions in the CLO Funds and, as of December 31, 2010 and December 31, 2009, the Company had approximately $45 million and $45 million, respectively, of such CLO equity investments at fair value. The cost basis of the Company's investment in CLO Fund equity securities as of December 31, 2010 was approximately $67 million and aggregate unrealized depreciation on the CLO Fund securities totaled approximately $22 million. The cost basis of the Company's investment in CLO Fund equity securities as of December 31, 2009, was approximately $67 million and aggregate unrealized depreciation on the CLO Fund securities totaled approximately $23 million.

In May, 2009 the Company purchased the class B-2L notes of the Katonah 2007-1 CLO investment managed by Katonah Debt Advisors ("Katonah 2007-1 B-2L"). The Company purchased the Katonah 2007-1 B-2L for 10% of the par value. The fair value, cost basis, and aggregate unrealized appreciation of the Katonah 2007-1 B-2L investment as of December 31, 2010 were approximately $8 million, $1 million, and $7 million, respectively, and at December 31, 2009, the fair value, cost basis, and aggregate unrealized appreciation of the Katonah 2007-1 B-2L investment were $4 million, $1 million, and $3 million, respectively. Both the B-2L notes and preferred shares of Katonah 2007-1 are owned 100% by the Company and are making their required quarterly distributions.

Fair Value Measurements

The Company follows the provisions of *Fair Value Measurements and Disclosures*, which among other matters, requires enhanced disclosures about investments that are measured and reported at fair value. This standard defines fair value and establishes a hierarchal disclosure framework which prioritizes and ranks the level of market price observability used in measuring investments at fair value and expands disclosures about assets and liabilities measured at fair value. *Fair Value Measurements and Disclosures* defines "fair value" as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This fair value definition focuses on an exit price in the principal, or most advantageous market, and prioritizes, within a measurement of fair value, the use of market-based inputs (which may be weighted or adjusted for relevance, reliability and specific attributes relative to the subject investment) over entity-specific inputs. Market price observability is affected by a number of factors, including the type of investment and the characteristics specific to the investment. Investments with readily available active quoted prices or for which fair value can be measured from actively quoted prices generally will have a higher degree of market price observability and a lesser degree of judgment used in measuring fair value. Subsequent to the adoption of *Fair Value Measurements and Disclosures*, the FASB has issued various staff positions clarifying the initial standard (see Note 2, "Significant Accounting Policies — Investments").

Fair Value Measurements and Disclosures establishes the following three-level hierarchy, based upon the transparency of inputs to the fair value measurement of an asset or liability as of the measurement date:

Level I — Unadjusted quoted prices are available in active markets for identical investments as of the reporting date. The type of investments included in Level I include listed equities and listed securities. As required by *Fair Value Measurements and Disclosures*, the Company does not adjust the quoted price for these investments, even in situations where the Company holds a large position and a sale could reasonably affect the quoted price.

4. INVESTMENTS – (continued)

Level II — Pricing inputs are other than quoted prices in active markets, which are either directly or indirectly observable as of the reporting date. Such inputs may be quoted prices for similar assets or liabilities, quoted markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full character of the financial instrument, or inputs that are derived principally from, or corroborated by, observable market information. Investments which are generally included in this category include illiquid corporate loans and bonds and less liquid, privately held or restricted equity securities for which some level of recent trading activity has been observed.

Level III — Pricing inputs are unobservable for the investment and includes situations where there is little, if any, market activity for the investment. The inputs may be based on the Company's own assumptions about how market participants would price the asset or liability or may use Level II inputs, as adjusted, to reflect specific investment attributes relative to a broader market assumption. These inputs into the determination of fair value may require significant management judgment or estimation. Even if observable market data for comparable performance or valuation measures (earnings multiples, discount rates, other financial/valuation ratios, etc.) are available, such investments are grouped as Level III if any significant data point that is not also market observable (private company earnings, cash flows, etc.) is used in the valuation methodology.

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, an investment's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and the Company considers factors specific to the investment. Substantially all of the Company's investments are classified as Level III. The Company evaluates the source of inputs, including any markets in which its investments are trading, in determining fair value. Inputs that are backed by actual transactions, those that are highly correlated to the specific investment being valued and those derived from reliable or knowledgeable sources will tend to have a higher weighting in determining fair value. Ongoing reviews by the Company's investment analysts, Chief Investment Officer, Valuation Committee and independent valuation firms (if engaged) are based on an assessment of each underlying investment, its current and prospective operating and financial performance, consideration of financing and sale transactions with third parties, expected cash flows and market-based information, including comparable transactions, performance factors, and other investment or industry specific market data, among other factors.

KOHLBERG CAPITAL CORPORATION

NOTES TO FINANCIAL STATEMENTS

4. INVESTMENTS – (continued)

The following table summarizes the fair value of investments by the above *Fair Value Measurements and Disclosures* fair value hierarchy levels as of December 31, 2010 (unaudited) and December 31, 2009, respectively:

	As of December, 31 2010			
	Level I	Level II	Level III	Total
Time deposit and money market account	$ —	$ 930,536	$ —	$ 930,536
Debt securities	—	—	91,042,928	91,042,928
CLO fund securities	—	—	53,031,000	53,031,000
Equity securities	—	—	4,688,832	4,688,832
Asset manager affiliate	—	—	41,493,000	41,493,000
	As of December 31, 2009			
	Level I	**Level II**	**Level III**	**Total**
Time deposit and money market account	$ —	$ 126	$ —	$ 126
Debt securities	—	—	297,356,529	297,356,529
CLO fund securities	—	—	48,971,000	48,971,000
Equity securities	—	—	4,713,246	4,713,246
Asset manager affiliate	—	—	58,064,720	58,064,720

As a BDC, it is required that the Company invest primarily in the debt and equity of non-public companies for which there is little, if any, market-observable information. As a result, most, if not all, of the Company's investments at any given time will most likely be deemed Level III investments. The Company believes that investments classified as Level III for *Fair Value Measurements and Disclosures* have a further hierarchal framework which prioritizes and ranks such valuations based on the degree of independent and observable inputs, objectivity of data and models and the level of judgment required to adjust comparable data. The hierarchy of such methodologies are presented in the above table and discussed below in descending rank.

Investment values derived by a third party pricing service are deemed Level III values since such values are not traded on an active public exchange and may represent a traded or broker quote on an asset that is infrequently traded.

The Company derives fair value for its illiquid investments that do not have indicative fair values based upon active trades primarily by using the Market Yield Approach and also considers recent loan amendments or other activity specific to the subject asset. Discount rates applied to estimated contractual cash flows for an underlying asset vary by specific investment, industry, priority and nature of the debt security (such as the seniority or security interest of the debt security) and are assessed relative to two indices, a leveraged loan index and a high-yield bond index, at the valuation date. The Company has identified these two indices as benchmarks for broad market information related to its loan and debt investments. Because the Company has not identified any market index that directly correlates to the loan and debt investments held by the Company and therefore uses the two benchmark indices, these market indices may require significant adjustment to better correlate such market data for the calculation of fair value of the investment under the Market Yield Approach. Such adjustments require judgment and may be material to the calculation of fair value. Further adjustments to the discount rate may be applied to reflect other market conditions or the perceived credit risk of the borrower. When broad market indices are used as part of the valuation methodology, their use is subject to adjustment for many factors, including priority, collateral used as security, structure, performance and other quantitative and qualitative attributes of the asset being valued. The resulting present value determination is then weighted along with any quotes from observable transactions and broker/pricing quotes. If such quotes

4. INVESTMENTS – (continued)

are indicative of actual transactions with reasonable trading volume at or near the valuation date that are not liquidation or distressed sales, relatively more reliance will be put on such quotes to determine fair value. If such quotes are not indicative of market transactions or are insufficient as to volume, reliability, consistency or other relevant factors, such quotes will be compared with other fair value indications and given relatively less weight based on their relevancy. The appropriateness of specific valuation methods and techniques may change as market conditions and available data change.

The Company engaged VRC, an independent valuation firm, to provide third-party valuation estimates for approximately 39% of its portfolio at fair value as of December 31, 2009. VRC's valuation estimates were considered as one of the relevant data inputs in the Company's determination of fair value. Though the Board of Directors did not engage VRC to provide valuation estimates for any of the assets in the Company's portfolio as of December 31, 2010, the Board of Directors engaged VRC to review the Company's CLO fair value model relative to its functionality, model inputs and calculations as a reasonable method to determine CLO fair values, in the absence of Level 1 or Level 2 trading activity or observable market inputs. VRC concluded that the Company's CLO model appropriately factored in all the necessary inputs required to build a CLO equity cash flow for fair value purposes and that the inputs were being employed correctly. The Board of Directors may engage an independent valuation firm in the future to provide certain valuation services, including the review of certain portfolio assets, as part of the Company's valuation processes.

Values derived for debt securities using public/private company comparables generally utilize market-observable data from such comparables and specific, non-public and non-observable financial measures (such as earnings or cash flows) for the private, underlying company/issuer. Such non-observable company/issuer data is typically provided on a monthly basis, is certified as correct by the management of the company/issuer and/or audited by an independent accounting firm on an annual basis. Since such private company/issuer data is not publicly available it is not deemed market-observable data and, as a result, such investment values are grouped as Level III assets.

Values derived for asset manager affiliates using public/private company comparables generally utilize market-observable data from such comparables and specific, non-public and non-observable financial measures (such as assets under management, historical and prospective earnings) for the asset manager affiliate. The Company recognizes that comparable asset managers may not be fully comparable to its asset manager affiliates and typically identifies a range of performance measures and/or adjustments within the comparable population with which to determine value. Since any such ranges and adjustments are entity specific they are not considered market-observable data and thus require a Level III grouping. Illiquid investments that have values derived through the use of discounted cash flow models and residual enterprise value models are grouped as Level III assets.

KOHLBERG CAPITAL CORPORATION

NOTES TO FINANCIAL STATEMENTS

4. INVESTMENTS – (continued)

The changes in investments measured at fair value for which the Company has used unobservable inputs to determine fair value are as follows:

	Year Ended December 31, 2010				
	Debt Securities	CLO Fund Securities	Equity Securities	Asset Manager Affiliates	Total
Balance, December 31, 2009	$ 297,356,529	$ 48,971,000	$ 4,713,246	$ 58,064,720	$ 409,105,495
Transfers out of Level III	—	—	—	—	—
Net accretion of discount	381,677	85,149	—	—	466,826
Purchases (sales), net	(198,838,948)	—	1,927,366	3,780,817	(193,130,765)
Total loss realized and unrealized included in earnings	(7,856,330)	3,974,851	(1,951,780)	(20,352,537)	(26,185,796)
Balance, December 31, 2010	$ 91,042,928	$ 53,031,000	$ 4,688,832	$ 41,493,000	$ 190,255,760
Changes in unrealized gains (losses) included in earnings related to investments still held at reporting date	$ 9,196,912	3,974,851	(1,142,038)	(20,352,537)	(8,322,812)

	Year Ended December 31, 2009				
	Debt Securities	CLO Fund Securities	Equity Securities	Asset Manager Affiliates	Total
Balance, December 31, 2008	$353,859,007	$ 34,640,000	$ 5,087,512	$54,734,812	$448,321,331
Transfers out of Level III	—	—	—	—	—
Net accretion of discount	964,724	742,204	—	—	1,706,928
Purchases (sales), net	(70,717,418)	1,076,250	8,625,625	4,018,309	(56,997,234)
Total loss realized and unrealized included in earnings	13,250,216	12,512,546	(8,999,891)	(688,401)	16,074,470
Balance, December 31, 2009	$297,356,529	$ 48,971,000	$ 4,713,246	$58,064,720	$409,105,495
Changes in unrealized gains (losses) included in earnings related to investments still held at reporting date	$ 25,300,586	$ 12,512,546	$ (7,485,064)	$ 1,526,668	$ 31,854,736

5. AFFILIATE ASSET MANAGERS

Wholly-Owned Asset Manager

Katonah Debt Advisors is a wholly-owned portfolio company. Katonah Debt Advisors manages CLO Funds primarily for third party investors that invest in broadly syndicated loans, high yield bonds and other credit instruments issued by corporations. These CLO Funds do not invest in asset-backed securities secured by commercial mortgages, residential mortgages or other consumer borrowings. At December 31, 2010, Katonah Debt Advisors had approximately $2.1 billion of par value of assets under management, and the Company’s 100% equity interest in Katonah Debt Advisors was valued at approximately $42 million.

As a manager of the CLO Funds, Katonah Debt Advisors receives contractual and recurring management fees and may receive a one-time structuring fee from the CLO Funds for its management and advisory services. The annual fees which Katonah Debt Advisors receives are generally based on a fixed percentage of assets under management (at par value and not subject to changes in market value), and Katonah Debt Advisors generates annual operating income equal to the amount by which its fee income exceeds it operating expenses. The annual management fees Katonah Debt Advisors receives have two components — a senior management fee and a subordinated management fee. At December 31, 2010, Katonah Debt Advisors continued to receive all senior management fees payable by the CLO Funds managed by it.

5. AFFILIATE ASSET MANAGERS – (continued)

During 2009, certain CLO funds managed by Katonah Debt Advisors were restricted from currently paying their subordinated management fees as a result of the failure by those CLO Funds to satisfy certain restrictive covenants contained in their indenture agreements. At such time, those subordinated management fees continued to be accrued by the applicable CLO Fund to become payable to Katonah Debt Advisors when such CLO Fund becomes compliant with the applicable covenants. During the year ended December 31, 2010, all those CLO Funds which deferred payment of their subordinated management fees regained compliance with all applicable covenants in order to pay current subordinated management fees as well as a portion of previously accrued subordinated management fees. During the year ended December 31, 2010, approximately $5 million of deferred subordinated management fees have been paid. Currently, all CLO Funds managed by Katonah Debt Advisors are paying both their senior and subordinated management fees on a current basis.

In future years, Katonah Debt Advisors may receive accrued incentive fees upon the liquidation of CLO Funds it manages, provided such CLO Funds have achieved a minimum investment return to holders of their subordinated securities or preferred shares.

On January 2, 2008, the Katonah Debt Advisors platform acquired substantially all of the assets of Scott’s Cove Capital Management LLC (“Scott’s Cove”), an asset manager focused on an event-driven credit long short investment strategy. As a result of the acquisition, approximately $60 million of fee paying assets under management were integrated into the Katonah Debt Advisors asset management platform. In connection with the acquisition, Katonah Debt Advisors entered into employment agreements with three Scott’s Cove investment professionals, and expects these individuals will assist in structuring, raising and investing new funds to be managed by Katonah Debt Advisors. As of December 31, 2010, Scott’s Cove had approximately $161 million of assets under management.

On February 4, 2011, Katonah Debt Advisors entered to an Asset Purchase Agreement with a third-party buyer controlled by a former Katonah Debt Advisors employee to sell substantially all of the Katonah Scott’s Cove Management LLC assets for a purchase price of $25,000. The transaction closed on February 28, 2011. At closing, Katonah Debt Advisors and the buyer entered into a Services Agreement, pursuant to which the buyer paid to Katonah Debt Advisors $225,000 for certain transitional services to be provided by Katonah Debt Advisors (including access to office space, secretarial services and information technology support) and agreed to pay an additional amount of $75,000 on each of the first and second anniversaries of the closing date (subject to, in the case of the first payment, deferment for up to one year under certain circumstances). Katonah Debt Advisors’ obligation to provide transitional services under the Services Agreement will continue through June 30, 2011, unless the agreement is earlier terminated by the buyer in accordance with its terms. At closing, Katonah Debt Advisors and the employees that formerly managed the Katonah Scott’s Cove Management LLC assets also entered into employee termination agreements, whereby they agreed to terminate their employment with Katonah Debt Advisors and to relinquish all claims against Katonah Debt Advisors or its affiliates. At December 31, 2010, Katonah Scott’s Cove Management LLC had approximately $161 million of assets under management.

The revenue that Katonah Debt Advisors generates through the fees it receives for managing CLO Funds and after paying the expenses associated with its operations, including compensation of its employees, may be distributed to the Company. Any distributions of Katonah Debt Advisors’ net income are recorded as dividends from affiliate asset manager. For the year ended December 31, 2010, Katonah Debt Advisors had approximately $1 million of pre-tax net income and made distributions of $4.5 million to the Company, a portion of which represented undistributed earnings from prior years. For the year ended December 31, 2009, Katonah Debt Advisors earned approximately $2 million of pre-tax net income and made no distributions to the Company; dividends are recorded as declared (where declaration date represents ex-dividend date) by Katonah Debt Advisors as income on our statement of operations.

KOHLBERG CAPITAL CORPORATION

NOTES TO FINANCIAL STATEMENTS

5. AFFILIATE ASSET MANAGERS – (continued)

As with all other investments, Katonah Debt Advisors' fair value is periodically determined. The valuation is primarily based on an analysis of both a percentage of its assets under management and Katonah Debt Advisors' estimated operating income. Any change in value from period to period is recognized as unrealized gain or loss. See Note 2, "Significant Accounting Policies" and Note 4, "Investments" for further information relating to the Company's valuation methodology. For the year ended December 31, 2010 Katonah Debt Advisors had a decrease in fair value of approximately $20 million. The decrease in the fair value of Katonah Debt Advisors is due to the receipt of approximately $5 million of previously accrued subordinate management fees during the year, the disposition of one of its affiliates, and current market conditions.

As a separately regarded entity for tax purposes, Katonah Debt Advisors is taxed at normal corporate rates. For tax purposes, any distributions of taxable net income earned by Katonah Debt Advisors to the Company would generally need to be distributed to the Company's shareholders. Generally, such distributions of Katonah Debt Advisors' income to the Company's shareholders will be considered as qualified dividends for tax purposes. Katonah Debt Advisors' taxable net income will differ from GAAP net income because of deferred tax timing adjustments and permanent tax adjustments. Deferred tax timing adjustments may include differences for the recognition and timing of depreciation, bonuses to employees and stock option expense. Permanent differences may include adjustments, limitations or disallowances for meals and entertainment expenses, penalties, tax goodwill amortization and net operating loss carryforward.

Goodwill amortization for tax purposes was created upon the purchase of 100% of the equity interests in Katonah Debt Advisors prior to the Company's IPO in exchange for shares of the Company's stock valued at $33 million. Although this transaction was a stock transaction rather than an asset purchase and thus no goodwill was recognized for GAAP purposes, such exchange was considered an asset purchase under Section 351(a) of the Code. At the time of the transfer, Katonah Debt Advisors had equity of approximately $1 million resulting in tax goodwill of approximately $32 million which will be amortized for tax purposes on a straight-line basis over 15 years, which accounts for an annual difference between GAAP income and taxable income by approximately $2 million per year over such period.

At December 31, 2010 there were no intercompany balances with our affiliates, and at December 31, 2009 a net amount due from affiliates totaled approximately $44,000.

6. BORROWINGS

The Company's debt obligations consist of the following:

	As of December 31, 2010	As of December 31, 2009
Secured credit facility, due February 28, 2011[1]	$ 86,746,582	$ 218,050,363

(1) February 28, 2011 was the maturity date as established by a Forbearance and Settlement Agreement dated September 20, 2010

On February 14, 2007, the Company entered into an arrangement under which the Company may obtain up to $200 million in financing (the "Facility"). On October 1, 2007, the Company amended the Facility to increase the Company's borrowing capacity from $200 million to $275 million, extend the maturity date from February 12, 2012 to October 1, 2012 and increase the interest spread charged on outstanding borrowings by 15 basis points to 0.85%. The interest rate is based on prevailing commercial paper rates plus 0.85% or, if the commercial paper market is at any time unavailable, prevailing LIBOR rates plus an applicable spread. Interest is payable monthly. As a result of the assertion of BMO Capital Markets Corp., as the agent (the "Agent"), that a Termination Event occurred under the LFSA, for the period June 2009 through

6. BORROWINGS – (continued)

September 2010, interest under the LFSA had been calculated at a higher default rate (equal to 0.85% above the prime rate plus 0.75%). As of January 31, 2011, the Company repaid in full the outstanding balance of the facility and has no debt outstanding.

Fair Value of Debt. The Company records debt at cost. The fair value of the Company's outstanding debt was approximately $87 million and $220 million at December 31, 2010 and December 31, 2009, respectively. At December 31, 2010 the fair value of the Company's debt was determined as the current outstanding balance due to its near-term maturity and at December 31, 2009, fair value of the Company's debt was determined based on market interest rates for similar instruments as of such balance sheet date.

Prior to the payoff of the Company's outstanding indebtedness on January 31, 2011, the Company's borrowings were through a secured financing facility (the "Facility"). In connection with the Facility, the Company was a party to a Loan Funding and Servicing Agreement, dated as of February 14, 2007 (as amended, the "LFSA"), by and among the Company, as the servicer, the Company's wholly-owned, special-purpose bankruptcy remote subsidiary, Kohlberg Capital Funding LLC I, as the borrower, BMO Capital Markets Corp, as the agent (the "Agent"), U.S. Bank National Association, a national banking association, as the trustee (the "Trustee") and the other Lender Parties and other parties thereto (the "Lender Parties"). The LFSA was modified on September 20, 2010 pursuant to a Forbearance and Settlement Agreement (the "Settlement Agreement") with the Agent and Lender Parties, pursuant to which we and the Agent and the Lender Parties agreed to settle all outstanding claims thereunder and in connection with litigation previously initiated by the Company against the Agent and the other Lender Parties.

Prior to entering into the Settlement Agreement, the interest on outstanding amounts under the Facility accrued at a rate equal to 0.85% above the prime rate plus 0.75%, or approximately 4.9%, and the Company had been paying interest at such rate under protest. Under the terms of the Settlement Agreement, commencing on September 10, 2010, the advances under the Facility accrued interest at the rate provided for under the LFSA prior to the occurrence of a termination event, equal to 0.85% above the prevailing commercial paper rate, or 1.2% as of such date. Under the terms of the Settlement Agreement, the Company calculated the advances outstanding under the Facility after consideration of amortization and pre-payments in the next scheduled distribution to the lenders. As of December 31, 2010, the Company's advances outstanding, calculated in accordance with the Settlement Agreement, were approximately $87 million. Under the Settlement Agreement, the Company was also obligated to maintain an overcollateralization ratio of at least 115%. As of December 31, 2010, the Company's overcollateralization ratio was 177%. As a BDC, the Company is limited in the amount of leverage it can incur and is required to meet a coverage ratio of total asset to total senior securities of at least 200% before incurring new debt. As of December 31, 2010, the Company's asset coverage ratio was 315%. The Company was in compliance with all covenants and terms set forth in the Settlement Agreement at December 31, 2010.

On January 31, 2011, the Company repaid in full the outstanding balance under the Facility in advance of the scheduled forbearance date of February 28, 2011. As a result, the Company has no outstanding indebtedness and the Lender Parties released to the Company approximately $73 million of collateral previously securing the Facility and had also paid a $2 million cash settlement to the Company. In order to pay off the Facility, the Company utilized proceeds received from the paydown, amortization or sale of portfolio loan investments totaling approximately $133 million together with available cash.

The weighted average daily debt balance for the years ended December 31, 2010 and 2009 was approximately $105 million and $222 million, respectively. As of December 31, 2010, the Company had restricted cash and time deposit balances of approximately $67 million which it maintained in accordance with the terms of the Facility.

7. DISTRIBUTABLE TAX INCOME

Effective December 11, 2006, the Company elected to be treated as a RIC under the Code and adopted a December 31 calendar year end. As a RIC, the Company is not subject to federal income tax on the portion of its taxable income and gains distributed currently to its stockholders as a dividend. The Company's quarterly dividends, if any, are determined by the Board of Directors. The Company anticipates distributing at least 90% of its taxable income and gains, within the Subchapter M rules, and thus the Company anticipates that it will not incur any federal or state income tax at the RIC level. As a RIC, the Company is also subject to a federal excise tax based on distributive requirements of its taxable income on a calendar year basis (e.g., calendar year 2010). Depending on the level of taxable income earned in a tax year, the Company may choose to carry forward taxable income in excess of current year distributions into the next tax year and pay a 4% excise tax on such income, to the extent required. The Company anticipates timely distribution of its taxable income within the tax rules, and the Company anticipates that it will not incurr a US federal excise tax for the calendar year 2010.

The following reconciles net decrease in shareholders' equity resulting from operations to taxable income for the year ended December 31, 2010:

	Year Ended December 31,	
	2010	2009
Net increase (decrease) in stockholders' equity resulting from operations	$(14,288,677)	$ 34,403,270
Net change in unrealized (appreciation) depreciation from investments	8,322,812	(31,854,736)
Excess capital losses over capital gains	17,862,984	15,782,121
Income not on GAAP books currently taxable	241,110	2,859,846
Income not currently taxable	(76,990)	(812,945)
Expenses not currently deductible	347,883	658,834
Expenses not on GAAP books currently deductible	(3,978)	(1,166,682)
Taxable income before deductions for distributions	$ 12,405,144	$ 19,869,708
Taxable income before deductions for distributions per weighted average shares for the period	$ 0.55	$ 0.91

Taxable income differs from net increase (decrease) in stockholders' equity resulting from operations primarily due to: (1) unrealized appreciation (depreciation) on investments, as investment gains and losses are not included in taxable income until they are realized; (2) amortization of discount on CLO Fund Securities; (3) amortization of organizational costs; (4) non-deductible expenses; (5) stock compensation expense that is not currently deductible for tax purposes; (6) excess of capital losses over capital gains; and (7) recognition of interest income on certain loans.

Distributions which exceed tax distributable income (tax net investment income and realized gains, if any) are reported as distributions of paid-in capital (*i.e.*, return of capital). The tax character of distributions paid during the years ended December 31, 2010, 2009, and 2008 was as follows:

	Year Ended December 31,		
	2010	2009	2008
Distributions paid from:			
Ordinary income	$ 12,405,144	$ 19,869,708	$ 26,920,884
	12,405,144	19,869,708	26,920,884
Return of Capital	2,817,067	333,017	2,702,761
	$ 15,222,211	$ 20,202,725	$ 29,623,645

7. DISTRIBUTABLE TAX INCOME – (continued)

As of December 31, 2010 and 2009, the components of accumulated earnings on a tax basis were as follows:

	Year Ended December 31, 2010	Year Ended December 31, 2009
Distributable ordinary income	$ 818,664	$ 1,326,380
Capital loss carryforward	(32,024,811)	(14,161,827)
Net unrealized depreciation	(62,585,504)	(54,262,692)

At December 31, 2010, the Company had a net capital loss carryforward of $32 million to offset net capital gains, to the extent provided by federal tax law. The capital loss carryforward will begin to expire in the tax year ending December 31, 2015.

The Company adopted Financial Accounting Standards Board ASC Topic 740 Accounting for Uncertainty in Income Taxes (“ASC 740”) as of January 1, 2007. ASC 740 provides guidance for how uncertain tax positions should be recognized, measured, presented, and disclosed in the financial statements. ASC 740 requires the evaluation of tax positions taken or expected to be taken in the course of preparing the Company’s tax returns to determine whether the tax positions are “more-likely-than-not” of being sustained by the applicable tax authority. Tax positions not deemed to meet the more-likely-than-not threshold are recorded as a tax benefit or expense in the current year. Adoption of ASC 740 was applied to all open taxable years (the last three fiscal years) as of the effective date. The adoption of ASC 740 did not have an effect on the financial position or results of operations of the Company as there was no liability for unrecognized tax benefits and no change to the beginning capital of the Company. Management’s determinations regarding ASC 740 may be subject to review and adjustment at a later date based upon factors including, but not limited to, an ongoing analysis of tax laws, regulations and interpretations thereof.

8. COMMITMENTS AND CONTINGENCIES

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business in order to meet the needs of the Company’s investment in portfolio companies. Such instruments include commitments to extend credit and may involve, in varying degrees, elements of credit risk in excess of amounts recognized on the Company’s balance sheet. Prior to extending such credit, the Company attempts to limit its credit risk by conducting extensive due diligence, obtaining collateral where necessary and negotiating appropriate financial covenants. As of both December 31, 2010 and December 31, 2009, the Company had committed to make a total of approximately $2 million of investments in various revolving senior secured loans, of which approximately $1 million had been funded as of December 31, 2010 and $640,000 had been funded as of December 31, 2009.

The Company and certain directors and officers are named as defendants in three putative class actions pending in the Southern District of New York brought by shareholders of the Company and filed in December 2009 and January 2010. The complaints in these three actions allege violations of Sections 10 and 20 of the Exchange Act based on the Company’s disclosures of its year-end 2008 and first- and second-quarter 2009 financial statements. The Company believes that the above-mentioned suits are without merit and will defend itself vigorously.

In addition, the Company and certain directors and officers were also named as defendants in a derivative action filed on March 2, 2010 in the Supreme Court of New York, County of New York. The complaint in this action purported to state causes of action for breaches of fiduciary duties, unjust enrichment, abuse of control, gross mismanagement, and corporate waste. On October 20, 2010, the court dismissed the complaint, and found, among other things, that the plaintiff had not alleged that any of the Company’s directors “‘knowingly’ misrepresented or permitted others to misrepresent KCAP’s financial condition,” or that the directors were confronted with “red flags” sufficient to put them on notice of potential problems with KCAP’s investment

KOHLBERG CAPITAL CORPORATION

NOTES TO FINANCIAL STATEMENTS

8. COMMITMENTS AND CONTINGENCIES – (continued)

valuations so as to excuse plaintiff's requirement under Delaware law to make a demand on KCAP's board before filing suit. On January 12, 2011, the court entered the final judgment dismissing the complaint and the plaintiff has subsequently filed a notice of appeal.

9. STOCKHOLDERS' EQUITY

On April 28, 2008 the Company completed a rights offering which resulted in the issuance of 3.1 million common shares and net proceeds of approximately $27 million. During the year ended December 31, 2010 and December 31, 2009, the Company issued 301,663 and 501,873 shares, respectively, of common stock under its dividend reinvestment plan. For the year ended December 31, 2010, the Company issued 103,519 shares of restricted stock for which 4,667 shares were forfeited and 64,667 shares were converted to common stock during the year due to vesting. The total number of shares issued and outstanding as of December 31, 2010 was and 22,767,130, respectively and shares issued and outstanding as of December 31, 2009 was 22,363,281.

10. EQUITY INCENTIVE PLAN

During 2006 and as amended in 2008, the Company established an equity incentive plan (the "Plan") and reserved 2,000,000 shares of common stock for issuance under the Plan. The purpose of the Plan is to provide officers and prospective employees of the Company with additional incentives and align the interests of its employees with those of its shareholders. Options granted under the Plan are exercisable at a price equal to the fair market value (market closing price) of the shares on the day the option is granted. Restricted stock granted under the Plan is granted at a price equal to the fair market value (market closing price) of the shares on the day such restricted stock is granted.

Stock Options

During the years ended December 31, 2008, December 31, 2009, and December 31, 2010, 20,000 options per year were granted to non-employee directors as partial annual compensation for their services as director. Each of these annual options grants have a vesting period by which 50% of such options vest on the grant date and 50% vest on the first grant date anniversary. The exercise price of these grants and other characteristics of these grants are as follows:

Options granted for the year ended:	Exercise Price	Exercise Period (years)	Risk Free Rate	Volatility Rate	Weighted Average Grant Date Fair Value per Share
December 31, 2008	$ 11.97	10	4.6%	28%	$ 1.50
December 31, 2009	$ 4.93	10	4.3%	41%	$ 0.90
December 31, 2010	$ 4.83	10	3.1%	59%	$ 1.46

On June 13, 2008, the Company's Board of Directors authorized the Company to allow employees who agree to cancel options that they hold to receive one share of restricted stock for every five options so cancelled. The shares of restricted stock received by employees through any such transaction will vest annually generally over the remaining vesting schedule as was applicable to the cancelled options. During the year ended December 31, 2008, employees holding options to purchase 1,295,000 shares individually entered into agreements to cancel such options and to receive 259,000 shares of restricted stock. As a result, as of December 31, 2008, all options granted to employees had been converted to restricted stock.

KOHLBERG CAPITAL CORPORATION

NOTES TO FINANCIAL STATEMENTS

10. EQUITY INCENTIVE PLAN – (continued)

Information with respect to options granted, exercised and forfeited under the Plan for the period January 1, 2008 through December 31, 2010 is as follows:

Options Outstanding as of:	Shares	Weighted Average Exercise Price per Share	Weighted Average Contractual Remaining Term (years)	Aggregate Intrinsic Value[(1)]	Weighted Average Grant Date Fair Value per Share
January 1, 2008	1,315,000	$ 15.52			
Granted	20,000	$ 11.97			$ 1.50
Exercised	—	$ —			
Forfeited	(1,315,000)	$ —			$ 1.58
December 31, 2008	20,000	$ 11.97			
Granted	20,000	$ 4.93			$ 0.90
Exercised	—	$ —			
Forfeited	—	$ —			
December 31, 2009	40,000	$ 8.45			
Granted	20,000	4.83			$ 1.46
Exercised	—	—			
Forfeited	—	—			
December 31, 2010	60,000	$ 7.24	8.5	$ —	
Total vested at December 31, 2010	50,000	7.73	8.3		

(1) Represents the difference between the market value of shares of the Company upon exercise of the options at December 31, 2010 and the cost for the option holders to exercise the options.

The Company uses a Binary Option Pricing Model (American, call option) to establish the expected value of all stock option grants. For the year ended December 31, 2010, the Company recognized non-cash compensation expense related to stock options of approximately $25,000. For the year ended December 31, 2009, the Company recognized non-cash compensation expense related to stock options of approximately $21,000. For the year ended December 31, 2008, non-cash compensation expense related to stock options was approximately $329,000; of this amount approximately $260,000 was expensed at the Company and approximately $69,000 was a reimbursable expense allocated to Katonah Debt Advisors. At December 31, 2010, the Company had approximately $8,000 of remaining compensation cost related to unvested stock-based awards, the cost for which is expected to be recognized by the Company over a weighted average period of 0.5 years.

Restricted Stock

On June 13, 2008, the Company's shareholders approved the Company's 2006 Equity Incentive Plan, as amended and the board of directors approved the grant of awards of 100,250 shares of restricted stock to certain executive officers of the Company. On July 22, 2010 and August 5, 2009, the board of directors approved the grant of an additional 103,519 and 84,889 shares of restricted stock, respectively, to a certain executive officer of the Company. Such awards of restricted stock will vest as to 50% of the shares on the third anniversary of the grant date and the remaining 50% of the shares on the fourth anniversary of the grant date.

As noted above, on June 13, 2008, the Company's Board of Directors authorized the Company to allow employees who agree to cancel options that they hold to receive shares of the Company's common stock to receive one share of restricted stock for every five options so cancelled.

KOHLBERG CAPITAL CORPORATION

NOTES TO FINANCIAL STATEMENTS

10. EQUITY INCENTIVE PLAN – (continued)

On June 13, 2008, the Company's Board of Directors authorized the Company to allow employees who agree to cancel options that they hold to receive shares of the Company's common stock to receive 1 share of restricted stock for every 5 options so cancelled. The shares of restricted stock received by employees through any such transaction will vest annually generally over the remaining vesting schedule as was applicable to the cancelled options. Subsequently, employees holding options to purchase 1,295,000 shares individually entered into agreements to cancel such options and to receive 259,000 shares of restricted stock. As of December 31, 2010, 191,333 of such shares were vested and converted to common shares, and 47,666 of such shares had yet to vest. The remaining 20,001 shares have been forfeited.

Information with respect to restricted stock granted, exercised and forfeited under the Plan for the period January 1, 2008 through December 31, 2010 is as follows:

Non-Vested Shares Outstanding as of:	Non-Vested Restricted Shares	Weighted Average Price per Share	Weighted Average Contractual Remaining Term (years)
January 1, 2008	—	$ —	
Granted	359,250	$ 10.89	
Vested	(3,000)	$ 10.29	
Forfeited	(16,667)	$ 9.41	
December 31, 2008	339,583	$ 10.83	
Granted	84,889	$ 5.89	
Vested	(122,333)	$ 10.37	
Forfeited	—	$ —	
December 31, 2009	302,139	$ 9.63	
Granted	103,519	$ 4.83	
Vested	(64,667)	$ 10.39	
Forfeited	(4,667)	$ 9.82	
December 31, 2010	336,324	$ 8.01	2.3
Total non-vested shares at December 31, 2010	336,324	$ 8.01	2.3

The Company determines the cost of restricted stock as the closing price of the Company's stock on the date of grant and amortizes such cost over the vesting period. For the year ended December 31, 2010, non-cash compensation expense related to restricted stock was approximately $894,000 of this amount approximately $654,000 was expensed at the Company and approximately $240,000 was a reimbursable expense allocated to Katonah Debt Advisors. For the year ended December 31, 2009, non-cash compensation expense related to restricted stock was approximately $890,000 of this amount approximately $609,000 was expensed at the Company and approximately $281,000 was a reimbursable expense allocated to Katonah Debt Advisors. For the year ended December 31, 2008, non-cash compensation expense related to restricted stock was approximately $559,000; of this amount approximately $463,000 was expensed at the Company and approximately $96,000 was a reimbursable expense allocated to Katonah Debt Advisors. Dividends are paid on all issued shares of restricted stock, whether or not vested. In general, shares of unvested restricted stock are forfeited upon the recipient's termination of employment. At December 31, 2010, the Company had approximately $1 million of compensation cost related to unvested restricted stock based awards, the cost for which is expected to be recognized by the Company over a weighted average period of 2.3 years.

KOHLBERG CAPITAL CORPORATION

NOTES TO FINANCIAL STATEMENTS

11. OTHER EMPLOYEE COMPENSATION

The Company adopted a 401(k) plan ("401K Plan") effective January 1, 2007. The 401K Plan is open to all full time employees. The Plan permits an employee to defer a portion of their total annual compensation up to the Internal Revenue Service annual maximum based on age and eligibility. The Company makes contributions to the 401K Plan of up to 2.67% of the employee's first 74.9% of maximum eligible compensation, which fully vest at the time of contribution. For the years ended December 31, 2010 and 2009, the Company made contributions to the 401K Plan of approximately $29,000 and $28,000, respectively.

The Company has also adopted a deferred compensation plan ("Profit-Sharing Plan") effective January 1, 2007. Employees are eligible for the Profit-Sharing Plan provided that they are employed and working with the Company for at least 100 days during the year and remain employed as of the last day of the year. Employees do not make contributions to the Profit-Sharing Plan. On behalf of the employee, the Company may contribute to the Profit-Sharing Plan 1) up to 8.0% of all compensation up to the Internal Revenue Service annual maximum and 2) up to 5.7% excess contributions on any incremental amounts above the social security wage base limitation and up to the Internal Revenue Service annual maximum. Employees vest 100% in the Profit-Sharing Plan after five years of service. For the years ended December 31, 2010 and 2009, the Company made no contributions to the Profit-Sharing Plan.

12. IMPACT OF NEW ACCOUNTING STANDARDS

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities ("SFAS 159"), which provides companies with an option to report selected financial assets and liabilities at fair value. The objective of SFAS 159 is to reduce both complexity in accounting for financial instruments and the volatility in earnings caused by measuring related assets and liabilities differently. SFAS 159 establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities and to more easily understand the effect of a company's choice to use fair value on its earnings. SFAS 159 also requires entities to display the fair value of the selected assets and liabilities on the face of the balance sheet. SFAS 159 does not eliminate disclosure requirements of other accounting standards, including fair value measurement disclosures in SFAS 157. This statement is effective as of the beginning of an entity's first fiscal year beginning after November 15, 2007. The Company has determined that adoption of SFAS 159 does not have an impact on the Company's financial position or results of operations.

KOHLBERG CAPITAL CORPORATION

NOTES TO FINANCIAL STATEMENTS

13. SELECTED QUARTERLY DATA (Unaudited)

	Q1 2010	Q2 2010	Q3 2010	Q4 2010
Total interest and related portfolio income	$ 6,963,826	$ 7,382,805	$ 8,091,217	$ 6,916,015
Net investment income and realized gains	$ 306,353	$(5,136,467)	$ 784,510	$ (1,920,261)
Net increase (decrease) in net assets resulting from operations	$ 1,594,909	$(5,690,916)	$(3,319,312)	$ (6,873,359)
Net increase (decrease) in net assets resulting from operations per share – basic	$ 0.07	$ (0.26)	$ (0.15)	$ (0.31)
Net increase (decrease) in net assets resulting from operations per share – diluted	$ 0.07	$ (0.26)	$ (0.15)	$ (0.31)
Net investment income and realized gains per share – basic	$ 0.01	$ (0.23)	$ 0.04	$ (0.09)
Net investment income and realized gains per share – diluted	$ 0.01	$ (0.23)	$ 0.04	$ (0.09)

	Q1 2009	Q2 2009	Q3 2009	Q4 2009
Total interest and related portfolio income	$ 9,452,254	$ 8,819,471	$ 8,244,845	$ 7,379,981
Net investment income and realized gains	$ 4,446,251	$ 2,633,818	$ (292,418)	$ (4,239,118)
Net increase (decrease) in net assets resulting from operations	$ 8,895,499	$12,982,360	$10,665,810	$ 1,859,600
Net increase (decrease) in net assets resulting from operations per share – basic and diluted	$ 0.41	$ 0.60	$ 0.48	$ 0.08
Net increase (decrease) in net assets resulting from operations per share – diluted	$ 0.41	$ 0.59	$ 0.48	$ 0.08
Net investment income and realized gains per share – basic and diluted	$ 0.20	$ 0.12	$ (0.01)	$ (0.19)
Net investment income and realized gains per share – diluted	$ 0.20	$ 0.12	$ (0.01)	$ (0.19)

14. SUBSEQUENT EVENTS

None, other than those noted above.

TABLE OF CONTENTS

EXHIBIT INDEX

Exhibit Number	Description
3.1	Form of Certificate of Incorporation of Kohlberg Capital Corporation (the “Company”).(1)
3.2	Form of Bylaws of the Company.(2)
4.1	Specimen certificate of the Company’s common stock, par value $0.01 per share.(1)
4.2	Form of Registration Rights Agreement.(3)
4.3	Form of Dividend Reinvestment Plan.(3)
10.1	Form of the Amended and Restated 2006 Equity Incentive Plan.(9)*
10.2	Form of Company Non-Qualified Stock Option Certificate.(3)*
10.3	Form of Custodian Agreement by and among Kohlberg Capital Corporation and U.S. Bank National Association.(3)
10.4	Form of License and Referral Agreement between the Company and Kohlberg & Company, L.L.C. (1)
10.5	Form of Overhead Allocation Agreement between the Company and Katonah Debt Advisors, L.L.C. (3)
10.6	Form of Employment Agreement between the Company and Dayl W. Pearson.(3)*
10.7	Form of Employment Agreement between the Company and Michael I. Wirth.(3)*
10.8	Form of Employment Agreement between the Company and R. Jon Corless.(3)*
10.9	Form of Employment Agreement between the Company and E.A. Kratzman.(3)*
10.10	Form of Employment Agreement between Katonah Debt Advisors and E.A. Kratzman.(3)*
10.11	Letter Agreement, dated December 10, 2010, between the Company and John M. Stack.*
10.12	Consulting Agreement, dated December 10, 2010, between Katonah Debt Advisors, L.L.C. and John M. Stack.*
10.13	Form of Employment Agreement between Katonah Debt Advisors and Daniel P. Gilligan.*
10.14	Form of Indemnification Agreement for Officers and Directors of the Company.(4)
10.15	Execution Copy of Loan Funding and Servicing Agreement dated as of February 14, 2007, by and among Kohlberg Capital Funding LLC I, Kohlberg Capital Corporation, each of the conduit lenders and institutional lenders from time to time party thereto, each of the lender agents from time to time party thereto, BMO Capital Markets Corp., as the Agent, Lyon Financial Services, Inc. (d/b/a U.S. Bank Portfolio Services), as the Backup Services, and U.S. Bank National Association, as Trustee.(5)
10.16	Execution Copy of First Amendment to Loan Funding and Servicing Agreement, dated as of May 30, 2007, by and among Kohlberg Capital Funding LLC I, the Company, each of the conduit lenders and institutional lenders from time to time party thereto, each of the lender agents from time to time party thereto, BMO Capital Markets Corp., as the Agent, Lyon Financial Services, Inc. (d/b/a U.S. Bank Portfolio Services), as the Backup Servicer, and U.S. Bank National Association, as Trustee.(6)
10.17	Execution Copy of Second Amendment to Loan Funding and Servicing Agreement, dated as of October 1, 2007, by and among Kohlberg Capital Funding LLC I, the Company, each of the conduit lenders and institutional lenders from time to time party thereto, each of the lender agents from time to time party thereto, BMO Capital Markets Corp., as the Agent, Lyon Financial Services, Inc. (d/b/a U.S. Bank Portfolio Services), as the Backup Servicer, and U.S. Bank National Association, as Trustee.(6)

TABLE OF CONTENTS

Exhibit Number	Description
10.17	Execution Copy of Third Amendment to Loan Funding and Servicing Agreement, dated as of November 21, 2007, by and among Kohlberg Capital Funding LLC I, the Company, each of the conduit lenders and institutional lenders from time to time party thereto, each of the lender agents from time to time party thereto, BMO Capital Markets Corp., as the Agent, Lyon Financial Services, Inc. (d/b/a U.S. Bank Portfolio Services), as the Backup Servicer, and U.S. Bank National Association, as Trustee.(8)
10.18	Execution Copy of Purchase and Sale Agreement dated as of February 14, 2007, by and among Kohlberg Capital Funding LLC I and the Company.(7)
10.19	Forebearance and Settlement Agreement, dated as of September 20, 2010, by and among the Company, BMO Capital Markets Corp. and the other lender parties thereto.(11)
10.20	Form of 2008 Non-Employee Director Plan.(10)*
21.1	List of Subsidiaries.
23.1	Consent of Grant Thornton LLP, Independent Registered Public Accounting Firm.
31.1	Chief Executive Officer Certification Pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Chief Financial Officer Certification Pursuant to Rule 13a-14 of the Securities Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Chief Executive Officer Certification pursuant to Section 1350, Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Chief Financial Officer Certification pursuant to Section 1350, Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(1) Incorporated by reference to the exhibit included in Pre-Effective Amendment No. 1 on Form N-2, as filed on October 6, 2006 (File No. 333-136714).

(2) Incorporated by reference to the exhibit included on Form N-2, as filed on March 16, 2007 (File No. 333-141382).

(3) Incorporated by reference to the exhibit included in Pre-Effective Amendment No. 2 on Form N-2, as filed on November 20, 2006 (File No. 333-136714).

(4) Incorporated by reference to the exhibit included in Pre-Effective Amendment No. 3 on Form N-2, as filed on November 24, 2006 (File No. 333-136714).

(5) Incorporated by reference to Exhibit 10.15 of the Annual Report on Form 10-K, as filed on March 29, 2007 (File No. 814-00735).

(6) Incorporated by reference to the exhibit included in Pre-Effective Amendment No. 1 on Form N-2, as filed on October 18, 2007 (File No. 333-146190).

(7) Incorporated by reference to Exhibit 10.2 of the Current Report on Form 8-K, as filed on February 16, 2007 (File No. 814-00735).

(8) Incorporated by reference to Exhibit 10.15 of the Annual Report on Form 10-K, as filed on March 14, 2008 (File No. 814-00735).

(9) Incorporated by reference to Exhibit 10.1 of the Current Report on Form 8-K, as filed on June 19, 2008 (File No. 814-00735).

(10) Incorporated by reference to the exhibit included in Pre-Effective Amendment No. 1 on Form N-2, as filed on June 30, 2008 (File No. 333-151268).

(11) Incorporated by reference to Exhibit 10.1 of the Quarterly Report on Form 10-Q, as filed on November 8, 2010 (File No. 333-814-00735).

* Indicates a management contract or compensatory plan, contract or agreement.

Exhibit 10.11

Katonah Debt Advisors, L.L.C.
295 Madison Avenue, 6th Floor
New York, NY 10017

December 10, 2010

Mr. John M. Stack
167 West Trail
Stamford, CT 06903

Dear Jack:

As we discussed, effective as of 12:01 a.m. on December 30, 2010 (the "Separation Date"), you have determined to voluntarily terminate your employment with Katonah Debt Advisors, L.L.C. ("Katonah") and as Vice President of Kohlberg Capital Corporation ("KCAP" and together with Katonah, the "Company"). The purpose of this Separation Agreement (the "Agreement") is to confirm the agreement between you and the Company concerning your separation from the Company, as follows:

1. **Termination; Duties Until Separation Date.** Effective as of the Separation Date, your employment with the Company will terminate, and you will resign from all other positions and offices that you hold with the Company or any of its affiliates or subsidiaries. From the date first written above until the Separation Date, you shall continue to provide services to the Company on the terms contained in the Employment Agreement between you and Katonah dated December 14, 2009 (the "Employment Agreement"). Your right to receive the benefits under this Agreement is conditioned on your continued compliance with the covenants contained in the Employment Agreement and the fulfillment of your duties thereunder. As of the Separation Date, the Employment Agreement will terminate, except as expressly provided in this Agreement. Contemporaneously with your termination of employment, you shall begin to serve as a consultant to the Company pursuant to the terms of a consulting agreement to be entered into by you and the Company on or about the Separation Date (the "Consulting Agreement").

2. **Final Wages and Business Expenses.** In accordance with Section 5(b) of the Employment Agreement, you will receive base salary earned but not paid through the date of termination and pay for any vacation time accrued but not used to that date on December 30, 2010 whether or not you accept this Agreement, provided that any reimbursement for business expenses shall be paid in accordance with the Company's reimbursement policies in effect on the Separation Date. Subsequent to the Separation Date, the Company will not provide you with any additional benefits described in the Employment Agreement, provided that you will be eligible to elect COBRA health care continuation coverage as permitted by law.

3. **Bonus.** The Company will pay you any bonus compensation you have earned for actual performance during all of 2010 in accordance with the terms of the Employment Agreement. The payment of this amount will be made during 2011 (but not later than March 31, 2011).

4. **Restricted Stock.** In accordance with the terms of your Restricted Stock Agreement with KCAP, dated July 1, 2008 (the "Restricted Stock Agreement"), your unvested shares of restricted stock in KCAP will terminate on the Separation Date.

5. **Tax Withholding Prior to Termination.** All payments by the Company under this Agreement on or prior to the Separation Date will be reduced by all taxes and other amounts that the Company is required to withhold under applicable law and all other deductions authorized by you.

6. **Acknowledgement of Full Payment and Status of Benefits.** You agree that the payments provided under Sections 2 and 3 of this Agreement are in complete satisfaction of any and all compensation due to you from the Company or any of its affiliates, whether arising under the Employment Agreement or otherwise, in connection with your employment or the termination thereof, and that, except as expressly provided in this Agreement, nothing further is owed to you by the Company or any of its affiliates as a result of your termination from employment. You will not continue to earn vacation or other paid time off after the Separation Date.

7. **Directors and Officers Coverage; Indemnification.** The Company agrees that it will continue to provide you with director's and officer's liability insurance coverage, on the same basis as is provided to other directors and officers of the Company, with respect to your service as an employee of the Company and relating to claims incurred prior to your Separation Date

8. **Confidentiality.** You agree that you will not disclose this Agreement or any of its terms or provisions, directly or by implication, except to members of your immediate family and to your legal, financial and tax advisors, and then only on condition that they agree not to further disclose this Agreement or any of its terms or provisions to others, except as required by law.

9. **Release of Claims.**

(a) In exchange for the parties' agreement to enter into the Consulting Agreement, you agree to execute the Release. Any obligation of the Company or its affiliates under this Agreement is conditioned upon (i) your executing this Agreement (which includes the Release) and (ii) your executing the Release and delivering it to the Company within twenty-one (21) calendar days of the Separation Date.

(b) You also acknowledge that you have been advised by the Company and its subsidiaries and other affiliates to seek the advice of an attorney prior to executing this Agreement, and that you have had sufficient time to consider this Agreement and to consult with an attorney, if you wished to do so, or, subject to Section 8 of this Agreement, to consult with any other person of your choosing before signing, and you are signing this Agreement voluntarily and with a full understanding of its terms. You further acknowledge that, in signing this Agreement, you have not relied on any promises or representations, express or implied, that are not set forth expressly in this Agreement.

10. **Entire Agreement.** This Agreement constitutes the entire agreement between you and the Company and supersedes all prior and contemporaneous communications, agreements and understandings, whether written or oral, with respect to your employment, its termination and all related matters, excluding only your rights and obligations under or with respect to the Consulting Agreement, Restricted Stock Agreement and your post-employment obligations under Section 3 of the Employment Agreement and the Company's and your rights and remedies under the Employment Agreement, including those other provisions of the Employment Agreement that are necessary or desirable for the enforcement of the aforementioned surviving provisions, all of which shall remain in full force and effect in accordance with their terms.

11. **Miscellaneous.** This Agreement may not be modified or amended, and no breach shall be deemed to be waived, unless agreed to in writing by you and the Company. The captions and headings in this Agreement are for convenience only and in no way define or describe the scope or content of any provision of this Agreement. This Agreement may be executed in one or more counterparts, each of which shall be an original and all of which together shall constitute one and the same instrument. This Agreement shall be governed by the laws of the State of Delaware, without giving effect to the principles of comity or conflicts of laws thereof.

[The remainder of this page is left intentionally blank.]

If the terms of this Agreement are acceptable to you, please sign, date and return it to the Company. The enclosed copy of this Agreement, which you should also sign and date, is for your records.

Sincerely,

KATONAH DEBT ADVISORS, L.L.C.

By: /s/ E.A. Kratzman

Name: E.A. Kratzman

Title: President

Accepted and agreed:

Signature: /s/ John M. Stack

Date: December 10, 2010

EXHIBIT A

RELEASE

We advise you to consult an attorney before you sign this Release. You have until the date which is seven (7) days after the Release is signed and returned to Katonah Debt Advisors, L.L.C. to change your mind and revoke your Release. Your Release shall not become effective or enforceable until after that date.

In consideration for the benefits provided under the Separation Agreement between you and the Company dated December 10, 2010 (the “Agreement”) (other than those provided in Sections 2 and 3 of the Agreement)), to which this Release is attached, the benefits to be provided to you in connection with your termination of employment as set forth in the Agreement, and the release provided by the Company in the next paragraph hereof, by your signature below, you, for yourself and on behalf of your heirs, executors, agents, representatives, successors and assigns, hereby release and forever discharge Katonah Debt Advisors, L.L.C., its past and present parent corporations (including, without limitation, Kohlberg Capital Corporation), subsidiaries, divisions, subdivisions, affiliates and related companies (collectively, the “Company”) and the Company’s past, present and future agents, directors, officers, employees, representatives, successors and assigns (hereinafter “those associated with the Company”) with respect to any and all claims, demands, actions and liabilities, whether in law or equity, which you may have against the Company or those associated with the Company of whatever kind arising out of or in connection with your employment with the Company or the termination of that employment. You agree that this release covers, but is not limited to, claims arising under the Age Discrimination in Employment Act of 1967, 29 U.S.C. § 621 et seq., Title VII of the Civil Rights Act of 1964, 42 U.S.C. § 2000e et seq., the Americans with Disabilities Act of 1990, 42 U.S.C. § 12101 et seq., the Fair Labor Standards Act, 29 U.S.C. § 201 et seq., the Employee Retirement Income Security Act of 1974, 29 U.S.C. § 1001 et seq., and any other local, state or federal law, regulation or order dealing with discrimination in employment on the basis of sex, race, color, national origin, veteran status, marital status, religion, disability, handicap, or age. You also agree that this release includes claims based on wrongful termination of employment, breach of contract (express or implied), tort, or claims otherwise related to your employment or termination of employment with the Company and any claim for attorneys’ fees, expenses or costs of litigation.

In consideration for the release provided by you in the preceding paragraph, the Company (as defined herein), by the signature of a duly authorized officer below, hereby releases and forever discharges you with respect to any and all claims, demands, actions and liabilities, whether in law or equity, which the Company may have against you of whatever kind arising out of, and within the scope of your employment with the Company or the termination of that employment. The Company agrees that this release covers, but is not limited to, claims arising under any local, state or federal law or regulation but does not apply to any fraudulent or criminal acts or breaches of fiduciary duty or other acts that were not within the scope of your employment.

This Release covers all claims based on any facts or events, whether known or unknown by you or the Company, that occurred on or before the date of this Release. Except to enforce this Release, you and the Company agree that neither party will ever commence, prosecute, or cause to be commenced or prosecuted any lawsuit or proceeding of any kind against the other party to the extent released hereunder in any forum and agree to withdraw with prejudice all complaints or charges, if any, that you or the Company have filed against the other.

Anything in this Release to the contrary notwithstanding, this Release does not include a release of (i) any rights you may have to indemnification or insurance under any agreement, law, Company organizational document or policy, or otherwise; (ii) any rights you may have to compensation or benefits under the Company's compensation or benefit plans that were accrued and unpaid prior to the date hereof and payable hereafter; (iii) either party's right to enforce this Release; or (iv) the Company's and your rights and remedies under the Employment Agreement that survive.

By signing this Release, you further agree as follows:

You have read this Release carefully and fully understand its terms;

You have had at least twenty-one (21) days to consider the terms of the Release;

You have seven (7) days from the date you sign this Release to revoke it by written notification to the Company. After this seven (7) day period, this Release is final and binding and may not be revoked;

You have been advised to seek legal counsel and have had an opportunity to do so;

You would not otherwise be entitled to the benefits provided under your Employment Agreement (as defined in the Agreement) or the Agreement had you not agreed to execute this Release; and

Your agreement to the terms set forth above is voluntary.

Name: ______________________________

Signature: ______________________________ Date: ______________________________

Received by: ______________________________ Date: ______________________________

KATONAH DEBT ADVISORS, L.L.C.

CONSULTING AGREEMENT

This Consulting Agreement is entered into by and between Katonah Debt Advisors, L.L.C. and John M. Stack ("Consultant"), effective as of January 1, 2011 (the "Effective Date").

1. **Consulting Services.** During the one-year period commencing on the Effective Date, Consultant will provide consultancy services (the "Services") to Katonah Debt Advisors, L.L.C. and Kohlberg Capital Corporation (collectively, the "Company"). The Services shall include assisting the Company connection with the transition of oversight of investment analysts and credit processes and such other consultancy services as may be mutually agreed to by Consultant and the Company from time to time (the "Services"). Consultant shall devote that amount of time as is reasonably required by the Company for Consultant to perform the Services, taking into account Consultant's other business obligations as in effect from time to time. Consultant shall use Consultant's best efforts to perform the Services such that the results are satisfactory to the Company. In no event shall the level of Services exceed 20% of the average level of services Consultant provided to the Company over the 36-month period immediately preceding the Effective Date.

2. **Term.** The initial term of this Agreement shall be the one-year period beginning on the Effective Date (the "Term") on the terms and conditions set forth herein. The Company shall have the right (but not the obligation) to renew this Agreement for additional one-year periods by written notice to the Consultant within 30 days prior to the end of the Term (as extended by subsequent renewals hereof) on conditions (including amounts payable) that may differ from those contained herein.

3. **Consulting Payments.** In consideration of the performance of Services under this Agreement, the Company will pay to Consultant the amounts described in Sections 3(a) and 3(b).

(a) **Monthly Payments.** On the last day of each calendar month (in arrears) during the Term, the Company will pay to Consultant the following amounts:

i. **Initial Consultancy Fee**. The Company shall pay Consultant a consultancy fee (the "Initial Consulting Fee") of $16,030 per month for the period beginning on the Effective Date and ending on the six-month anniversary of the Effective Date (the "Initial Term").

ii. **Subsequent Consultancy Fee**. Following the end of the Initial Term, Consultant shall continue to provide Services for an additional six month period and, in consideration thereof, the Company shall pay Consultant a consultancy fee (the "Subsequent Consulting Fee") of $20,180 per month (together, the Initial Consulting Fee and the Subsequent Consulting Fee are referred to as the "Consultancy Fee").

(b) **Lump-Sum Payment.** On July 31, 2011, the Company shall pay Consultant a lump-sum payment of $20,000, subject to his continued provision of Services hereunder on such date.

4. **Expenses, Office Space, etc.** The Company shall reimburse Consultant for all expenses reasonably incurred in connection with the performance of the Services. As a condition to receipt of reimbursement, Consultant shall be required to submit to the Company reasonable evidence that the amount involved was expended and related to Services provided under this Agreement in accordance with the Company's reimbursement policy. Reimbursements shall be made no later than December 31 of the year following the year in which the related expenses were incurred. During the Term, the Company shall provide Consultant with reasonable office space at the Company's headquarters, when available, and access to secretarial and administrative assistance so that he may perform his duties hereunder.

5. **Termination of Consulting Services.** The consultancy relationship may be terminated by the Company for Cause. In the event of a termination of the consultancy relationship by the Company for Cause, the Company's only obligation shall be to pay Consultant any earned but unpaid Consultancy Fee as of the termination date. For purposes of this Agreement, "Cause" shall mean the conviction or a plea of *nolo contendere* of the Consultant for the commission of a felony, or willful misconduct by the Consultant in connection with his consultancy with the Company that results in material and demonstrable financial harm to the Company, or the breach of any restrictive covenants described Section 7 of this Agreement.

6. **Termination by Consultant**. The Consultant may terminate the consultancy relationship for any reason upon giving the Company ten (10) days' advance notice of such termination. In the event of the Consultant's termination of the consultancy relationship, the Company's only obligation shall be to pay Consultant any earned but unpaid Consultancy Fee as of the termination date.

7. **Confidential Information and Restrictive Covenants.**

(a) **Confidential Information.** During the course of Consultant's prior employment with the Company and his provision of services as a Consultant under this Agreement, he has and will learn of Confidential Information, as defined below, and he may develop Confidential Information on behalf of the Company. Consultant agrees that he will not use or disclose to any Person (except as required by applicable law or for the proper performance of Consultant's regular duties and responsibilities for the Company) any Confidential Information obtained by him incident to his employment or consulting services or any other association with the Company or any of its Affiliates. Consultant understands that this restriction shall continue to apply after his service terminates, regardless of the reason for such termination.

(b) **Protection of Documents.** All documents, records and files, in any media of whatever kind and description, relating to the business, present or otherwise, of the Company or any of its Affiliates, and any copies, in whole or in part, thereof (the "Documents"), whether or not prepared by Consultant shall be the sole and exclusive property of the Company. Consultant agrees to safeguard all Documents and to surrender to the Company, at the time his service terminates or at such earlier time or times as the Company or its designee may specify, all Documents then in Consultant's possession or control.

(c) **Non-Competition.** Consultant acknowledges that in connection with his prior employment and his present consultancy services with the Company he has had and will have access to Confidential Information which, if disclosed, would assist in competition against the Company and its Affiliates and that he will also generate goodwill for the Company and its Affiliates in the course of his performing Services hereunder. Therefore, Consultant agrees that the following restrictions on his activities during and after the Term is necessary protect the goodwill, Confidential Information and other legitimate interests of the Company and its Affiliates:

i. While Consultant is performing services for the Company (the "Non-Competition Period"), Consultant agrees that he will not, without the prior written consent of the Company, directly or indirectly, own, manage, operate, join, control, finance, or participate in the ownership, marketing, management, operation, control, fundraising or financing of, or be connected as an officer, director, employee, partner, principal, agent, representative, consultant, or otherwise use or permit his name to be used in connection with any business or enterprise engaged in the United States in the business of structuring CDO or CLO securitization vehicles, analyzing and acquiring loans and other assets to be held by CDO or CLO vehicles, arranging for the issuance of debt and preferred securities by CDO or CLO vehicles, acting as collateral managers for such securitizations, or performing similar functions.

ii. Consultant agrees that during the Non-Competition Period, he will not, directly or through any other Person, (i) hire any employee of the Company or any of its Affiliates or seek to persuade any employee of the Company or any of its Affiliates to discontinue employment, (ii) solicit or encourage any customer or investor of the Company or any of its Affiliates or independent contractor providing services to the Company or any of its Affiliates to terminate or diminish its relationship with them or (iii) seek to persuade any customer or investor or prospective customer or investor of the Company or any of its Affiliates to conduct with anyone else any business or activity that such customer or investor or prospective customer or investor conducts or could conduct with the Company or any of its Affiliates.

(d) **Remedies.** In signing this agreement, Consultant gives the Company assurance that he has carefully read and considered all the terms and conditions of this agreement, including the restraints imposed on him under this Section 7. Consultant agrees without reservation that these restraints are necessary for the reasonable and proper protection of the Company and its Affiliates and that each and every one of the restraints is reasonable in respect to subject matter, length of time and geographic area. He further agrees that, were he to breach any of the covenants contained in this Section 7, the damage to the Company and its Affiliates would be irreparable. Consultant therefore agrees that the Company, in addition to any other remedies available to it, shall be entitled to preliminary and permanent injunctive relief against any breach or threatened breach by him of any of those covenants, without having to post bond. Consultant and the Company further agree that, in the event that any provision of this Section 7 is determined by any court of competent jurisdiction to be unenforceable by reason of its being extended over too great a time, too large a geographic area or too great a range of activities, that provision shall be deemed to be modified to permit its enforcement to the maximum extent permitted by law. It is also agreed that each of the Company's Affiliates shall have the right to enforce all of Consultant's obligations to that Affiliate under this agreement, including without limitation pursuant to this Section 7.

8. **Independent Contractor.** Consultant's relationship with the Company will be that of an independent contractor and not that of an employee.

(a) **Method of Provision of Services.** Consultant shall be solely responsible for determining the method, details and means of performing the Services.

(b) **No Authority to Bind Company.** Neither Consultant, nor any of his partners, agents or employees, has authority to enter into contracts that bind the Company or create obligations on the part of the Company without the prior written authorization of the Company.

(c) **No Benefits.** Consultant acknowledges and agrees that Consultant will not be eligible for any Company employee benefits under this Agreement.

(d) **Withholding During Consultancy Period; Indemnification.** Following the Effective Date, Consultant shall have full responsibility for applicable withholding taxes for all compensation paid to him, his partners, agents or employees under this Agreement, and for compliance with all applicable labor and employment requirements with respect to his self-employment, sole proprietorship or other form of business organization, and his partners, agents and employees, including state worker's compensation insurance coverage requirements and any US immigration visa requirements. Consultant agrees to indemnify, defend and hold the Company harmless from any liability for, or assessment of, any claims or penalties with respect to such withholding taxes, labor or employment requirements, including any liability for, or assessment of, withholding taxes imposed on the Company by the relevant taxing authorities with respect to any compensation paid to Consultant or Consultant's partners, agents or employees.

(e) **Supervision of Consultant's Services.** All of the services to be performed by Consultant, including but not limited to the Services, will be as agreed between Consultant and E.A. Kratzman III, President, Katonah Debt Advisors, L.L.C. The nature and frequency of these reports will be left to the discretion of Mr. Kratzman.

9. **Conflicts with this Agreement.** Consultant represents and warrants that he is not under any pre-existing obligation in conflict or in any way inconsistent with the provisions of this Agreement. Consultant represents and warrants that Consultant's performance of all the terms of this Agreement will not breach any agreement to keep in confidence proprietary information acquired by Consultant in confidence or in trust prior to commencement of this Agreement. Consultant warrants that Consultant has the right to disclose and/or or use all ideas, processes, techniques and other information, if any, which Consultant has gained from third parties, and which Consultant discloses to the Company or uses in the course of performance of this Agreement, without liability to such third parties. Notwithstanding the foregoing, Consultant agrees that he shall not bundle with or incorporate into any deliveries provided to the Company herewith any third party products, ideas, processes, or other techniques, without the express, written prior approval of the Company. Consultant represents and warrants that Consultant has not granted and will not grant any rights or licenses to any intellectual property or technology that would conflict with Consultant's obligations under this Agreement. Consultant will not knowingly infringe upon any copyright, patent, trade secret or other property right of any former client, employer or third party in the performance of the Services required by this Agreement.

10. **Miscellaneous.**

(a) **Amendments and Waivers.** Any term of this Agreement may be amended or waived only with the written consent of the parties.

(b) **Sole Agreement.** This Agreement constitutes the sole agreement of the parties and supersedes all oral negotiations and prior writings with respect to the subject matter hereof.

(c) **Choice of Law, Attorneys' Fees.** The validity, interpretation, construction and performance of this Agreement shall be governed by the laws of the State of Delaware, without giving effect to the principles of conflict of laws.

(d) **Severability.** If one or more provisions of this Agreement are held to be unenforceable under applicable law, such portion shall be deemed to be modified or altered to the extent necessary to conform thereto or, if that is not possible, to be omitted from this Agreement. The invalidity of any such portion shall not affect the force, effect, and validity of the remaining portion hereof.

(e) **Counterparts.** This Agreement may be executed in counterparts, each of which shall be deemed an original, but all of which together will constitute one and the same instrument.

(f) **Successors.** This Agreement is personal to Consultant and, without the prior written consent of the Company, shall not be assignable by Consultant otherwise than by will or the laws of descent and distribution. This Agreement shall inure to the benefit of and be enforceable by Consultant's legal representatives. This Agreement shall inure to the benefit of and be binding upon the Company and its successors and assigns. As used in this Agreement, "the Company" shall mean both the Company as defined above and any such successor that assumes and agrees to perform this Agreement, by operation of law or otherwise.

(g) **Advice of Counsel.** EACH PARTY ACKNOWLEDGES THAT, IN EXECUTING THIS AGREEMENT, SUCH PARTY HAS HAD THE OPPORTUNITY TO SEEK THE ADVICE OF INDEPENDENT LEGAL COUNSEL, AND HAS READ AND UNDERSTOOD ALL OF THE TERMS AND PROVISIONS OF THIS AGREEMENT. THIS AGREEMENT SHALL NOT BE CONSTRUED AGAINST ANY PARTY BY REASON OF THE DRAFTING OR PREPARATION HEREOF.

[The remainder of this page has been left intentionally blank.]

IN WITNESS WHEREOF, the parties have executed this Agreement effective as of the Effective Date first set forth above.

KATONAH DEBT ADVISORS, L.L.C.

By: /s/ E.A. Kratzman

Name: E.A. Kratzman

Title: President

Accepted and agreed:

Signature: /s/ John M. Stack

Date: December 10, 2010

KATONAH
DEBT ADVISORS

August 13, 2009

Mr. Daniel Gilligan
401 East 88th Street, Apt. 16C
New York, NY 10128

Dear Dan:

This letter will confirm our offer to you of employment with Katonah Debt Advisors, L.L.C. ("KDA") (the "Company"), under the terms and conditions that follow. This letter supersedes the letter agreement dated February 23, 2006 between you and KDA in its entirety effective as of the date hereof.

1. Term, Position and Duties.

(a) You will be employed as a Director of Portfolio Administration. You will report to the Portfolio Manager or Managers of various funds managed by the Company and any of its affiliates.

(b) You agree to perform the duties of your position and such other duties as may reasonably be assigned to you from time to time including, but not limited to overseeing trade settlement, trustee reporting, and other documentation concerning loans, bonds, and other instruments purchased or held by various types of collateralized loan obligation ("CLO") funds, synthetic collateralized debt obligation ("CDO") funds, and other credit-based funds (collectively "Funds") as directed by the Portfolio Manager. You also agree that you will devote your full business time and your best efforts, business judgment, skill and knowledge exclusively to the advancement of the business and interests of the Company.

2. Compensation and Benefits. During your employment, as compensation for all services performed by you for the Company and its Affiliates, the Company will provide you the following pay and benefits:

(a) Base Salary. The Company will pay you a base salary at the rate of One Hundred Fifty Thousand Dollars ($150,000) per year, payable in accordance with the regular payroll practices of the Company and subject to increase from time to time by the Committee in its discretion.

(b) Bonus Compensation. During employment, you will be considered for a target annual minimum bonus of One Hundred and Twenty Five Thousand Dollars ($125,000) each calendar year. You will be considered for an increase in the annual bonus amount, solely at the discretion of the Committee, based on the future growth and performance of the Company. Bonus awards will be determined by the Committee against goals established annually by the Portfolio Manager after consultation with you. The bonus will be paid on or about January 31 of each succeeding calendar year.

(c) Vacation. You will be entitled to four (4) weeks paid vacation per calendar year.

(d) Participation in Employee Benefit Plans. You will be entitled to participate in all employee benefit plans from time to time in effect for employees of the Company generally, except to the extent such plans are duplicative of benefits otherwise provided you under this agreement. Your participation will be subject to the terms of the applicable plan documents and generally applicable Company policies.

3. Confidential Information and Restricted Activities.

(a) Confidential Information. During the course of your employment with the Company, you will learn of Confidential Information, as defined below, and you may develop Confidential Information on behalf of the Company. You agree that you will not use or disclose to any Person (except as required by applicable law or for the proper performance of your regular duties and responsibilities for the Company) any Confidential Information obtained by you incident to your employment or any other association with the Company or any of its Affiliates. You understand that this restriction shall continue to apply after your employment terminates, regardless of the reason for such termination.

(b) Protection of Documents. All documents, records and files, in any media of whatever kind and description, relating to the business, present or otherwise, of the Company or any of its Affiliates, and any copies, in whole or in part, thereof (the “Documents”), whether or not prepared by you shall be the sole and exclusive property of the Company. You agree to safeguard all Documents and to surrender to the Company, at the time your employment terminates or at such earlier time or times as the Committee or its designee may specify, all Documents then in your possession or control.

(c) Non-Competition. You acknowledge that in your employment with the Company you will have access to Confidential Information which, if disclosed, would assist in competition against the Company and its Affiliates and that you will also generate goodwill for the Company and its Affiliates in the course of your employment. Therefore, you agree that the following restrictions on your activities during and after your employment are necessary to protect the goodwill, Confidential Information and other legitimate interests of the Company and its Affiliates:

(i) While you are employed by the Company and for six (6) months after your employment terminates (in the aggregate, the "Non-Competition Period"), you agree that you will not, without the prior written consent of the Company, directly or indirectly, own, manage, operate, join, control, finance, or participate in the ownership, marketing, management, operation, control, fundraising or financing of, or be connected as an officer, director, employee, partner, principal, agent, representative, consultant, or otherwise use or permit your name to be used in connection with any business or enterprise engaged in the United States in the business of structuring CDO or CLO securitization vehicles, analyzing and acquiring loans and other assets to be held by CDO or CLO vehicles, arranging for the issuance of debt and preferred securities by CDO or CLO vehicles, acting as collateral managers for such securitizations, or performing similar functions.

(ii) You agree that during the Non-Competition Period, you will not, directly or through any other Person, (i) hire any employee of the Company or any of its Affiliates or seek to persuade any employee of the Company or any of its Affiliates to discontinue employment, (ii) solicit or encourage any customer or investor of the Company or any of its Affiliates or independent contractor providing services to the Company or any of its Affiliates to terminate or diminish its relationship with them or (iii) seek to persuade any customer or investor or prospective customer or investor of the Company or any of its Affiliates to conduct with anyone else any business or activity that such customer or investor or prospective customer or investor conducts or could conduct with the Company or any of its Affiliates.

(d) In signing this agreement, you give the Company assurance that you have carefully read and considered all the terms and conditions of this agreement, including the restraints imposed on you under this Section 3. You agree without reservation that these restraints are necessary for the reasonable and proper protection of the Company and its Affiliates and that each and every one of the restraints is reasonable in respect to subject matter, length of time and geographic area. You further agree that, were you to breach any of the covenants contained in this Section 3, the damage to the Company and its Affiliates would be irreparable. You therefore agree that the Company, in addition to any other remedies available to it, shall be entitled to preliminary and permanent injunctive relief against any breach or threatened breach by you of any of those covenants, without having to post bond. You and the Company further agree that, in the event that any provision of this Section 3 is determined by any court of competent jurisdiction to be unenforceable by reason of its being extended over too great a time, too large a geographic area or too great a range of activities, that provision shall be deemed to be modified to permit its enforcement to the maximum extent permitted by law. It is also agreed that each of the Company's Affiliates shall have the right to enforce all of your obligations to that Affiliate under this agreement, including without limitation pursuant to this Section 3.

4. Termination of Employment. Your employment under this agreement may be terminated at any time pursuant to this Section 4.

(a) The Company may terminate your employment for cause upon notice to you setting forth in reasonable detail the nature of the cause. The following shall constitute cause for termination: (i) your repeated material failure to perform (other than by reason of disability), or gross negligence in the performance of, your duties and responsibilities to the Company or any of its Affiliates which failure is not cured within thirty (30) days after written notice of such failure or negligence is delivered to you; (ii) your material breach of this agreement or any other agreement between you and the Company or any of its Affiliates which breach is not cured within thirty (30) days after written notice of such breach is delivered to you; or (iii) commission by you of a felony involving moral turpitude or fraud with respect to the Company or any of its Affiliates. The Company also may terminate your employment at any time without cause upon notice to you.

(b) This agreement shall automatically terminate in the event of your death during employment, and you shall be entitled to the severance payments set forth under 5 (a) below. In the event of your death, any amounts owed to you under this agreement will be paid to the beneficiary designated in writing by you or, if no beneficiary has been so designated by you, to your estate. In the event you become disabled during employment and, as a result, are unable to continue to perform substantially all of your duties and responsibilities under this agreement, the Company will continue to pay you your base salary and to provide you benefits in accordance with Section 2(a) above, to the extent permitted by plan terms, for up to twelve (12) weeks of disability during any period of three hundred and sixty-five (365) consecutive calendar days. If you are unable to return to work after twelve (12) weeks of disability, the Company may terminate your employment, upon written notice to you, and you shall be entitled to the severance payments set forth under 5(a) below. If any question shall arise as to whether you are disabled to the extent that you are unable to perform substantially all of your duties and responsibilities for the Company and its Affiliates, you shall, at the Company's request, submit to a medical examination by a physician selected by the Company to whom you or your guardian, if any, has no reasonable objection to determine whether you are so disabled and such determination shall for the purposes of this agreement be conclusive of the issue. If such a question arises and you fail to submit to the requested medical examination, the Company's determination of the issue shall be binding on you.

(c) You may terminate your employment hereunder for “Good Reason” by providing written notice to the Company of the condition giving rise to the Good Reason no later than thirty (30) days following the occurrence of the condition; by giving the Company thirty (30) days to remedy the condition; and, if the Company fails to remedy the condition, by terminating your employment within ten (10) days following the expiration of such thirty (30) day period. For purposes of this letter agreement, the term “Good Reason” means, without your consent, the occurrence of one or more of the following events: (i) material diminution in the nature or scope of your responsibilities, duties or authority as contemplated by this letter agreement; (ii) failure by the Company to pay the minimum Bonus Compensation set forth in 2(b) above in any year under this letter agreement if you have achieved the annual financial target referenced therein; or (iii) your being required to relocate to a principal place of employment outside of the New York metropolitan area. For purposes of this paragraph 4(c) a change in reporting relationships resulting from a Change in Control will constitute Good Reason. In addition, a termination of your employment by you for any reason during the 90-day period immediately following a Change in Control shall be deemed to be a termination for Good Reason for all purposes of this letter agreement.

5. Severance Payments and Other Matters Related to Termination.

(a) In the event of termination of your employment by the Company without cause, the Company will continue to pay you your base salary ("severance payments") and will continue to contribute to the premium cost of your health insurance on the same terms and conditions as it contributes for active employees provided that you make a timely election under the federal law known as "COBRA". The Company may, in its sole discretion, elect to cease the continuation of base salary and contributions toward health insurance premiums at any point after you have received six (6) months of base salary continuation and health insurance contributions (or one (1) year if you are terminated by the Company within ninety (90) days of the completion of a Change in Control) provided that it also releases you from your remaining obligation under Section 3(c)(i) above. The Company will also pay you on the date of termination any base salary earned but not paid through the date of termination and pay for any vacation time accrued but not used to that date. In addition, the Company will pay you any bonus compensation and profit sharing payment to which you are entitled in accordance with Sections 2(b) and 2(d) above, prorated to the date of termination and payable at the time such monies are payable to Company executives generally. Any obligation of the Company to provide you severance payments or other payments or benefits under this Section 5(a) is conditioned, however, upon your signing and not revoking a release of claims in the form provided by the Company (the "Employee Release"), which shall be delivered to you not later than ten (10) business days following the date of termination and you shall be required to execute the Employee Release and return it to the Company, if at all, not later than the date determined by the Company to be the last day of the period it must provide to you by law to consider the Employee Release. All severance payments will be in the form of salary continuation, payable in accordance with the normal payroll practices of the Company, and will begin at the Company's next regular payroll period following the effective date of the Employee Release, but shall be retroactive to the date of termination. Notwithstanding anything else contained in this agreement, no bonus or severance payments or other payments or benefits will be due and payable under any provision of this Section 5(a) until the next regular Company payday following the effective date of the Employee Release.

(b) In the event of termination of your employment by the Company for cause or by you for any reason, the Company will pay you any base salary earned but not paid through the date of termination and pay for any vacation time accrued but not used to that date. The Company shall have no obligation to you for any bonus or other incentive compensation, benefits continuation or severance payments.

(c) In the event of termination of your employment by death, or by disability, the Company will pay you any base salary earned but not paid through the date of termination, pay for any vacation time accrued but not used to that date, and any bonus or other incentive compensation to which you are entitled in accordance with Sections 2(b) and 2(c) above, prorated to the date of termination and payable at the time such bonuses are payable to Company executives generally. The Company shall have no obligation to you for any severance payments or benefits continuation.

(d) Except for any rights you may have under Section 5(a) above or under the federal law known as "COBRA" to continue participation in the Company's group health and dental plans at your cost, benefits shall terminate in accordance with the terms of the applicable benefit plans based on the date of termination of your employment, without regard to any continuation of base salary or other payment to you following termination. Your Option and/or Restricted Stock Agreement will govern your exercise, if any, of your option following termination of employment.

(e) Provisions of this agreement shall survive any termination if so provided in this agreement or if necessary or desirable to accomplish the purposes of other surviving provisions, including without limitation your obligations under Section 3 of this agreement. The obligation of the Company to make payments to you under this Section 5 is expressly conditioned upon your continued full performance of obligations under Section 3 hereof. Upon termination by either you or the Company, all rights, duties and obligations of you and the Company to each other shall cease, except as otherwise expressly provided in this agreement.

6. Definitions. For purposes of this agreement, the following definitions apply:

"Affiliates" means all persons and entities directly or indirectly controlling, controlled by or under common control with the Company, where control may be by management authority, equity interest or otherwise.

"Change in Control" means:

(i) The acquisition by any person, entity or "group", within the meaning of Section 13(d)(3) or 14(d)(2) of the Exchange Act, (excluding, for this purpose, the Company or its Affiliates) of beneficial ownership of 33% or more of either the then outstanding shares of the Company's common stock or the combined voting power of the Corporation's then outstanding voting securities entitled to vote generally in the election of directors.

(ii) Individuals who, as of the date hereof, constitute the Board (the "Incumbent Board") cease for any reason to constitute at least a majority of the Board, provided that any person who first becomes a director subsequent to the date hereof whose recommendation, election or nomination for election by the Company's stockholders was approved by a vote of at least a majority of the directors then comprising the Incumbent Board (other than an election or nomination of an individual whose initial assumption of office is in connection with an actual or threatened election contest relating to the election of the directors of the Company as described in Rule 14a-11 of Regulation 14A promulgated under the Exchange Act) shall be, for the purposes of this Agreement, considered as though such person were a member of the Incumbent Board; or

(iii) Approval by the stockholders of the Company of a reorganization share exchange, merger or consolidation with respect to which, in any such case, the persons who were the stockholders of the Company immediately prior to such reorganization, share exchange, merger or consolidation do not, immediately thereafter, own more than 50% of the combined voting power entitled to vote in the election of directors of the reorganized, merged or consolidated company; or

(iv) Liquidation or dissolution of the Company or a sale of all or substantially all of the assets of the Company.

"Confidential Information" means any and all information of the Company and its Affiliates that is not generally available to the public. Confidential Information also includes any information received by the Company or any of its Affiliates from any Person with any understanding, express or implied, that it will not be disclosed. Confidential Information does not include information that enters the public domain, other than through your breach of your obligations under this agreement.

"Person" means an individual, a corporation, a limited liability company, an association, a partnership, an estate, a trust or any other entity or organization, other than the Company or any of its Affiliates.

7. Conflicting Agreements. You hereby represent and warrant that your signing of this agreement and the performance of your obligations under it will not breach or be in conflict with any other agreement to which you are a party or are bound and that you are not now subject to any covenants against competition or similar covenants or any court order that could affect the performance of your obligations under this agreement. You agree that you will not disclose to or use on behalf of the Company any proprietary information of a third party without that party's consent.

8. Withholding. All payments made by the Company under this agreement shall be reduced by any tax or other amounts required to be withheld by the Company under applicable law.

9. Assignment. Neither you nor the Company may make any assignment of this agreement or any interest in it, by operation of law or otherwise, without the prior written consent of the other; provided, however, that the Company may assign its rights and obligations under this agreement without your consent to one of its Affiliates or to any Person with whom the Company shall hereafter affect a reorganization, consolidate with, or merge into or to whom it transfers all or substantially all of its properties or assets. This Agreement shall inure to the benefit of and be binding upon you and the Company, and each of our respective successors, executors, administrators, heirs and permitted assigns.

10. Severability. If any portion or provision of this agreement shall to any extent be declared illegal or unenforceable by a court of competent jurisdiction, then the remainder of this agreement, or the application of such portion or provision in circumstances other than those as to which it is so declared illegal or unenforceable, shall not be affected thereby, and each portion and provision of this agreement shall be valid and enforceable to the fullest extent permitted by law.

11. Miscellaneous. This agreement sets forth the entire agreement between you and the Company and replaces all prior and contemporaneous communications, agreements and understandings, written or oral, with respect to the terms and conditions of your employment. This agreement may not be modified or amended, and no breach shall be deemed to be waived, unless agreed to in writing by you and an expressly authorized representative of the Committee. The headings and captions in this agreement are for convenience only and in no way define or describe the scope or content of any provision of this Agreement. This agreement may be executed in two or more counterparts, each of which shall be an original and all of which together shall constitute one and the same instrument. This is a Delaware contract and shall be governed and construed in accordance with the laws of the State of Delaware, without regard to the conflict of laws principles thereof.

12. Notices. Any notices provided for in this agreement shall be in writing and shall be effective when delivered in person or deposited in the United States mail, postage prepaid, and addressed to you at your last known address on the books of the Company or, in the case of the Company, to it at its principal place of business, attention of the Committee, or to such other address as either party may specify by notice to the other actually received.

If the foregoing is acceptable to you, please sign this letter in the space provided and return it to me at your earliest convenience. We will provide a countersigned copy for your records.

Sincerely yours,

/s/ E.A. Kratzman

E.A. Kratzman
President and Portfolio Manager

Accepted and agreed:

/s/ Daniel Gilligan

Daniel Gilligan

August 13, 2009

Date

cc: Michael Wirth

Exhibit 21.1

List of Subsidiaries[1]

	Jurisdiction
Katonah Debt Advisors, L.L.C.[2]	Delaware
Kohlberg Capital Funding LLC I	Delaware
Katonah Management Holdings LLC[2]	Delaware
Katonah X Management LLC[2][3]	Delaware
Katonah 2007-I Management LLC[2][3]	Delaware
Katonah 2008-II Management LLC[2][3]	Delaware
Katonah Scott's Cove Management LLC[2][3]	Delaware
KPKSI Management Holdings LLC[2]	Delaware
KPKSI Holdings LLC[2][4]	Delaware

(1) Excludes a 35% interest in PKSIL LLC.
(2) Represents a wholly-owned portfolio company that is not consolidated for financial reporting purposes.
(3) A wholly-owned subsidiary of Katonah Management Holdings LLC.
(4) A wholly-owned subsidiary of KPKSI Management Holdings LLC.

Exhibit 23.1

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We have issued our reports dated March 4, 2011, with respect to the financial statements and internal control over financial reporting, included in the Annual Report of Kohlberg Capital Corporation on Form 10-K for the year ended December 31, 2010. We hereby consent to the incorporation by reference of said reports in the Registration Statements of Kohlberg Capital Corporation on Forms S-8 (File No. 333-152364, effective July 16, 2008 and File No. 333-151995, effective June 27, 2008).

/s/ GRANT THORNTON LLP

New York, New York
March 4, 2011

Exhibit 31.1

CERTIFICATION PURSUANT TO
RULE 13a-14(a) and 15d-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934,
AS AMENDED

I, Dayl W. Pearson, certify that:

1. I have reviewed this annual report on Form 10-K of Kohlberg Capital Corporation (the “registrant”);

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant’s other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s Board of Directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: March 4, 2011	By: /s/ Dayl W. Pearson
	Dayl W. Pearson
	President and Chief Executive Officer
	(Principal Executive Officer)

Exhibit 31.2

**CERTIFICATION PURSUANT TO
RULE 13a-14(a) and 15d-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934,
AS AMENDED**

I, Michael I. Wirth, certify that:

1. I have reviewed this annual report on Form 10-K of Kohlberg Capital Corporation (the "registrant");

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's Board of Directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 4, 2011	By: /s/ MICHAEL I. WIRTH
	Michael I. Wirth **Chief Financial Officer and** **Chief Compliance Officer** **(Principal Financial Officer)**

Exhibit 32.1

CERTIFICATION PURSUANT TO
SECTION 1350, CHAPTER 63 OF TITLE 18, UNITED STATES CODE,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the accompanying Annual Report of Kohlberg Capital Corporation (the “Company”) on Form 10-K for the year ended December 31, 2010 (the “Report”), I, Dayl W. Pearson, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 4, 2011

By: /s/ DAYL W. PEARSON

Dayl W. Pearson
President and Chief Executive Officer
(Principal Executive Officer)

Exhibit 32.2

CERTIFICATION PURSUANT TO
SECTION 1350, CHAPTER 63 OF TITLE 18, UNITED STATES CODE,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the accompanying Quarterly Report of Kohlberg Capital Corporation (the "Company") on Form 10-K for the year ended December 31, 2010 (the "Report"), I, Michael I. Wirth, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 4, 2011

By: /s/ MICHAEL I. WIRTH

Michael I. Wirth
Chief Financial Officer and
Chief Compliance Officer
(Principal Financial Officer)