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

FORM 10-Q

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

For the quarterly period ended March 31, 2011

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
(State or other jurisdiction of
incorporation or organization)

20-5951150
(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)

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 No

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

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

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company)

Smaller reporting company

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

The number of outstanding shares of common stock of the registrant as of May 6, 2011 was 22,837,172.

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KOHLBERG CAPITAL CORPORATION

BALANCE SHEETS

	<u>As of</u> <u>March 31, 2011</u> <u>(unaudited)</u>	<u>As of</u> <u>December 31, 2010</u>
ASSETS		
Investments at fair value:		
Time deposits (cost: 2011 - \$168,132; 2010 - \$720,225)	\$ 168,132	\$ 720,225
Money market account (cost: 2011 - \$169,858; 2010 - \$210,311)	169,858	210,311
Debt securities (cost: 2011 - \$121,272,490; 2010 - \$126,545,510)	88,439,163	91,042,928
CLO fund securities managed by non-affiliates (cost: 2011 - \$15,692,113; 2010 - \$15,690,982)	6,261,000	4,921,000
CLO fund securities managed by affiliate (cost: 2011 - \$52,608,476; 2010 - \$52,589,217)	49,720,000	48,110,000
Equity securities (cost: 2011 - \$16,199,845; 2010 - \$13,483,227)	7,388,465	4,688,832
Asset manager affiliates (cost: 2011 - \$44,393,453; 2010 - \$44,532,329)	42,196,000	41,493,000
Total Investments at fair value	194,342,618	191,186,296
Cash	70,747,215	10,175,488
Restricted cash	—	67,023,170
Interest and dividends receivable	2,517,467	2,574,115
Receivable for open trades	—	7,681,536
Accounts Receivable	848,207	851,020
Other assets	2,562,267	331,061
	<u>271,017,774</u>	<u>279,822,686</u>
Total assets	<u>\$ 271,017,774</u>	<u>\$ 279,822,686</u>
LIABILITIES		
Borrowings	\$ —	\$ 86,746,582
Senior Convertible Notes	60,000,000	—
Payable for open trades	12,033,703	—
Accounts payable and accrued expenses	1,936,600	2,337,767
Dividend payable	—	3,812,670
	<u>73,970,303</u>	<u>92,897,019</u>
Total liabilities	<u>\$ 73,970,303</u>	<u>\$ 92,897,019</u>
STOCKHOLDERS' EQUITY		
Common stock, par value \$0.01 per share, 100,000,000 common shares authorized; 22,803,233 and 22,767,130 common shares issued and outstanding at March 31, 2011 and December 31, 2010, respectively.	\$ 224,692	\$ 224,274
Capital in excess of par value	283,310,777	282,794,025
Accumulated undistributed net investment income	5,826,266	818,664
Accumulated net realized losses	(36,152,515)	(34,325,792)
Net unrealized depreciation on investments	(56,161,749)	(62,585,504)
Total stockholders' equity	<u>\$ 197,047,471</u>	<u>\$ 186,925,667</u>
Total liabilities and stockholders' equity	<u>\$ 271,017,774</u>	<u>\$ 279,822,686</u>
NET ASSET VALUE PER COMMON SHARE	<u>\$ 8.64</u>	<u>\$ 8.21</u>

See accompanying notes to financial statements.

KOHLBERG CAPITAL CORPORATION

STATEMENTS OF OPERATIONS
(unaudited)

	Three Months Ended	
	March 31,	
	2011	2010
Investment Income:		
Interest from investments in debt securities	\$ 1,968,906	\$ 4,782,363
Interest from cash and time deposits	5,837	6,083
Dividends from investments in CLO fund securities managed by non-affiliates	521,151	348,874
Dividends from investments in CLO fund securities managed by affiliate	2,849,519	1,811,894
Capital structuring service fees	1,248	14,612
Other Income	2,000,000	—
Total investment income	<u>7,346,661</u>	<u>6,963,826</u>
Expenses:		
Interest and amortization of debt issuance costs	297,460	2,696,351
Compensation	841,442	787,691
Professional fees	769,965	508,518
Insurance	117,577	102,318
Administrative and other	312,615	290,454
Total expenses	<u>2,339,059</u>	<u>4,385,332</u>
Net Investment Income	5,007,602	2,578,494
Realized And Unrealized Gains (Losses) On Investments:		
Net realized gains (losses) from investment transactions	(1,826,723)	(2,272,141)
Net change in unrealized appreciation (depreciation) on:		
Debt securities	2,669,255	3,668,958
Equity securities	(16,985)	10,414
CLO fund securities managed by affiliate	1,590,741	2,050,333
CLO fund securities managed by non-affiliate	1,338,869	639,054
Affiliate asset manager investments	841,875	(5,080,203)
Net realized and unrealized appreciation (depreciation) on investments	<u>4,597,032</u>	<u>(983,585)</u>
Net Increase In Net Assets Resulting From Operations	\$ 9,604,634	\$ 1,594,909
Net Increase (Decrease) In Stockholders' Equity Resulting from Operations per Common Share:		
Basic:	\$ 0.42	\$ 0.07
Diluted:	\$ 0.40	\$ 0.07
Net Investment Income Per Common Share:		
Basic:	\$ 0.22	\$ 0.11
Diluted:	\$ 0.21	\$ 0.11
Weighted Average Shares of Common Stock Outstanding—Basic	22,791,242	22,445,457
Weighted Average Shares of Common Stock Outstanding—Diluted	23,987,407	22,445,457

See accompanying notes to financial statements.

KOHLBERG CAPITAL CORPORATION
STATEMENTS OF CHANGES IN NET ASSETS
(unaudited)

	Three Months Ended	
	March 31,	
	2011	2010
Operations:		
Net investment income	\$ 5,007,602	\$ 2,578,494
Net realized loss from investment transactions	(1,826,723)	(2,272,141)
Net change in unrealized appreciation (depreciation) on investments	6,423,755	1,288,556
Net increase in net assets resulting from operations	<u>9,604,634</u>	<u>1,594,909</u>
Capital transactions:		
Issuance of common stock for dividend reinvestment plan	294,904	499,779
Stock based compensation	222,266	220,397
Net increase in net assets resulting from capital transactions	<u>517,170</u>	<u>720,176</u>
Net assets at beginning of period	<u>186,925,667</u>	<u>213,895,723</u>
Net assets at end of period (including undistributed net investment income of \$5,826,266 in 2011 and accumulated distributions in excess of net investment income of \$3,904,874 in 2010)	<u>\$ 197,047,471</u>	<u>\$ 216,210,808</u>
Net asset value per common share	\$ 8.64	\$ 9.62
Common shares outstanding at end of period	22,803,233	22,475,339

See accompanying notes to financial statements.

KOHLBERG CAPITAL CORPORATION

STATEMENTS OF CASH FLOWS
(unaudited)

Three Months Ended
March 31,

	<u>2011</u>	<u>2010</u>
OPERATING ACTIVITIES:		
Net increase in stockholders' equity resulting from operations	\$ 9,604,634	\$ 1,594,909
Adjustments to reconcile net increase in stockholders' equity resulting from operations to net cash provided by operations:		
Net realized losses on investment transactions	1,826,723	2,272,141
Net change in unrealized appreciation on investments	(6,423,755)	(1,288,556)
Net accretion of discount on securities and loans	(45,127)	(142,555)
Amortization of debt issuance cost	22,908	206,174
Amortization of convertible notes offering cost	22,092	—
Purchases of investments	(8,063,534)	(23,681,703)
Capital contribution to affiliate asset manager	138,875	(2,557,431)
Payment-in-kind interest income	(185,431)	(187,842)
Proceeds from sale and redemption of investments	29,311,167	27,796,246
Stock based compensation expense	222,266	220,396
Changes in operating assets and liabilities:		
Decrease in interest and dividends receivable	56,648	135,478
Decrease in accounts receivable	2,814	—
(Increase) decrease in other assets	60,217	(130,012)
Decrease in due from affiliates	—	44,274
Decrease in accounts payable and accrued expenses	(401,167)	(837,085)
Net cash provided by operating activities	<u>26,149,330</u>	<u>3,444,434</u>
FINANCING ACTIVITIES:		
Dividends paid in cash	(3,517,767)	(3,912,450)
Cash paid on repayment of debt	(86,746,582)	(19,402,108)
Convertible notes offering costs	(2,336,424)	—
Issuance of Senior Convertible Notes	60,000,000	—
Decrease in restricted cash	67,023,170	16,221,971
Net cash provided by (used in) financing activities	<u>34,422,397</u>	<u>(7,092,587)</u>
CHANGE IN CASH	60,571,727	(3,648,153)
CASH, BEGINNING OF PERIOD	<u>10,175,488</u>	<u>4,140,408</u>
CASH, END OF PERIOD	<u>\$ 70,747,215</u>	<u>\$ 492,255</u>
Supplemental Information:		
Interest paid during the period	\$ 252,318	\$ 2,336,077
Non-cash dividends paid during the period under the dividend reinvestment plan	\$ 294,904	\$ 499,779

See accompanying notes to financial statements.

KOHLBERG CAPITAL CORPORATION
SCHEDULE OF INVESTMENTS
As of March 31, 2011
(unaudited)

Debt Securities Portfolio

Portfolio Company / Principal Business	Investment Interest Rate¹ / Maturity	Principal	Cost	Value²
Advanced Lighting Technologies, Inc. <i>Home and Office Furnishings, Housewares, and Durable Consumer Products</i>	Senior Secured Loan — Revolving Loan 3.2%, Due 6/13	\$ 1,000,000	\$ 996,357	\$ 921,230
Advanced Lighting Technologies, Inc. <i>Home and Office Furnishings, Housewares, and Durable Consumer Products</i>	Junior Secured Loan — Second Lien Term Loan Note 6.3%, Due 6/14	5,000,000	5,000,000	5,000,000
Alaska Communications Systems Holdings, Inc. <i>Telecommunications</i>	Senior Secured Loan — Term Loan 5.5%, Due 10/16	2,992,500	3,011,203	3,011,203
Avis Budget Car Rental, LLC <i>Personal Transportation</i>	Senior Secured Loan — Extended Term Loan 5.8%, Due 4/14	3,000,000	3,022,500	3,022,500
Bankruptcy Management Solutions, Inc. <i>Diversified/Conglomerate Service</i>	Junior Secured Loan — Loan (Second Lien) 8.3%, Due 8/15	1,225,250	1,217,438	91,894
Bankruptcy Management Solutions, Inc. <i>Diversified/Conglomerate Service</i>	Junior Secured Loan — Term Loan B 7.5%, Due 8/14	1,438,720	1,443,758	561,101
Bicent Power LLC <i>Utilities</i>	Junior Secured Loan — Advance (Second Lien) 4.3%, Due 12/14	4,000,000	4,000,000	1,960,800
Burger King Corporation <i>Personal, Food and Miscellaneous Services</i>	Senior Secured Loan — Tranche B Term Loan 4.5%, Due 10/16	2,992,500	2,992,500	2,992,500
Caribe Media Inc. (fka Caribe Information Investments Incorporated) <i>Printing and Publishing</i>	Senior Secured Loan — Term Loan 2.6%, Due 3/13	1,611,045	1,608,353	1,060,712
Charlie Acquisition Corp. ⁸ <i>Personal, Food and Miscellaneous Services</i>	Mezzanine Investment — Senior Subordinated Notes 17.5%, Due 6/13	14,261,996	10,744,496	250,000

Portfolio Company / Principal Business	Investment Interest Rate¹ / Maturity	Principal	Cost	Value²
CoActive Technologies LLC (fka CoActive Technologies, Inc.) <i>Machinery (Non-Agriculture, Non-Construction, Non-Electronic)</i>	Junior Secured Loan — Term Loan (Second Lien) 7.1%, Due 1/15	\$ 2,000,000	\$ 1,979,047	\$ 1,465,400
Del Monte Foods Company <i>Beverage, Food and Tobacco</i>	Senior Secured Loan — Initial Term Loan 4.5%, Due 3/18	3,000,000	3,007,500	3,007,500
eInstruction Corporation <i>Healthcare, Education and Childcare</i>	Junior Secured Loan — Term Loan (Second Lien) 14.0%, Due 7/14	10,000,000	10,000,000	10,000,000
Freescale Semiconductor, Inc. <i>Electronics</i>	Senior Subordinated Bond — 10.125% - 12/2016 10.1%, Due 12/16	3,000,000	3,005,883	3,213,750
Ginn LA Conduit Lender, Inc. ⁸ <i>Buildings and Real Estate</i> ⁴	Senior Secured Loan — First Lien Tranche A Credit-Linked Deposit 7.8%, Due 6/11	1,257,143	1,224,101	102,665
Ginn LA Conduit Lender, Inc. ⁸ <i>Buildings and Real Estate</i> ⁴	Senior Secured Loan — First Lien Tranche B Term Loan 7.8%, Due 6/11	2,694,857	2,624,028	220,076
Ginn LA Conduit Lender, Inc. ⁸ <i>Buildings and Real Estate</i> 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) <i>Insurance</i>	Junior Secured Loan — Loan (Second Lien) 5.7%, Due 10/14	5,000,000	4,897,522	3,962,000
Hunter Fan Company <i>Home and Office Furnishings, Housewares, and Durable Consumer Products</i>	Junior Secured Loan — Loan (Second Lien) 7.0%, Due 10/14	3,000,000	3,000,000	2,932,800
International Architectural Products, Inc. ⁸ <i>Mining, Steel, Iron and Non-Precious Metals</i>	Senior Secured Loan — Term Loan 12.0%, Due 5/15	971,409	944,845	926,238
Intrapac Corporation/Corona Holdco <i>Containers, Packaging and Glass</i>	Junior Secured Loan — Term Loans (Second Lien) 7.8%, Due 5/13	3,000,000	3,008,678	3,000,000
Jones Stephens Corp. <i>Buildings and Real Estate</i> ⁴	Senior Secured Loan — Term Loan 7.0%, Due 9/15	5,006,338	5,006,338	5,006,338

Portfolio Company / Principal Business	Investment Interest Rate¹ / Maturity	Principal	Cost	Value²
KIK Custom Products Inc. <i>Personal and Non Durable Consumer Products (Mfg. Only)</i>	Junior Secured Loan — Loan (Second Lien) 5.2%, Due 12/14	\$ 5,000,000	\$ 5,000,000	\$ 3,407,500
LBREP/L-Suncal Master I LLC ⁸ <i>Buildings and Real Estate⁴</i>	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 ⁸ <i>Buildings and Real Estate⁴</i>	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 ⁸ <i>Buildings and Real Estate⁴</i>	Junior Secured Loan — Term Loan (Second Lien) 9.5%, Due 1/11	2,000,000	1,920,211	7,600
Legacy Cabinets, Inc. <i>Home and Office Furnishings, Housewares, and Durable Consumer Products</i>	Senior Secured Loan — Term Loan 7.3%, Due 5/14	470,521	463,380	70,578
MCCI Group Holdings, LLC <i>Healthcare, Education and Childcare</i>	Junior Secured Loan — Term Loan (Second Lien) 7.6%, Due 6/13	1,000,000	1,000,000	1,000,000
Pegasus Solutions, Inc. <i>Leisure, Amusement, Motion Pictures, Entertainment</i>	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. ⁶ <i>Leisure, Amusement, Motion Pictures, Entertainment</i>	Preferred Stock — Preferred Stock 14.0%, Due 4/14	400,000	400,000	373,560
Resco Products, Inc. <i>Mining, Steel, Iron and Non-Precious Metals</i>	Junior Secured Loan — Term Loan (Second Lien) 20.0%, Due 6/14	2,119,641	2,119,641	2,119,641
Resco Products, Inc. <i>Mining, Steel, Iron and Non-Precious Metals</i>	Junior Secured Loan — Term Loan (Second Lien) 20.0%, Due 6/14	7,337,327	7,231,905	7,337,327
Specialized Technology Resources, Inc. <i>Diversified/Conglomerate Service</i>	Junior Secured Loan — Loan (Second Lien) 7.2%, Due 12/14	7,500,000	7,500,000	7,500,000
TUI University, LLC <i>Healthcare, Education and Childcare</i>	Senior Secured Loan — Term Loan (First Lien) 3.5%, Due 10/14	3,119,818	3,039,459	2,877,097

Portfolio Company / Principal Business	Investment Interest Rate¹ / Maturity	Principal	Cost	Value²
Walker Group Holdings LLC <i>Cargo Transport</i>	Junior Secured Loan — Term Loan B 13.3%, Due 12/13	\$ 416,737	\$ 416,737	\$ 416,737
Walker Group Holdings LLC <i>Cargo Transport</i>	Junior Secured Loan — Term Loan B 12.3%, Due 12/13	3,957,614	3,957,614	3,957,614
Wesco Aircraft Hardware Corp. <i>Aerospace and Defense</i>	Junior Secured Loan — Loan (Second Lien) Retired 04/07/2011 6.0%, Due 3/14	1,720,000	1,682,398	1,720,000
Wesco Aircraft Hardware Corp. <i>Aerospace and Defense</i>	Junior Secured Loan — Loan (Second Lien) Retired 04/07/2011 6.0%, Due 3/14	3,554,283	3,568,118	3,554,283
Total Investment in Debt Securities (45% of net asset value at fair value)		\$ 125,570,182	\$ 121,272,490	\$ 88,439,163

Equity Portfolio

Portfolio Company / Principal Business	Investment	Percentage Interest/Shares	Cost	Value²
Aerostructures Holdings L.P. ⁶ <i>Aerospace and Defense</i>	Partnership Interests	1.2%	\$ 1,000,000	\$ 66,800
Aerostructures Holdings L.P. ⁶ <i>Aerospace and Defense</i>	Series A Preferred Interests	1.2%	250,961	250,961
Bankruptcy Management Solutions, Inc. ⁶ <i>Diversified/Conglomerate Service</i>	Common Stock	1.2%	218,592	12,394
Bankruptcy Management Solutions, Inc. ⁶ <i>Diversified/Conglomerate Service</i>	Warrants	0.1%	-	-
Coastal Concrete Holding II, LLC ⁶ <i>Buildings and Real Estate⁴</i>	Class A Units	10.8%	8,625,626	250,143
eInstruction Acquisition, LLC ⁶ <i>Healthcare, Education and Childcare</i>	Membership Units	1.1%	1,079,617	1,040,642

Portfolio Company / Principal Business	Investment	Percentage Interest/Shares	Cost	Value²
FP WRCA Coinvestment Fund VII, Ltd. ^{3, 6} <i>Machinery (Non-Agriculture, Non-Construction, Non-Electronic)</i>	Class A Shares	1,500	\$ 1,500,000	\$ 2,535,000
International Architectural Products, Inc. ⁶ <i>Mining, Steel, Iron and Non-Precious Metals</i>	Common	2.5%	292,851	187,512
Legacy Cabinets, Inc. ⁶ <i>Home and Office Furnishings, Housewares, and Durable Consumer Products</i>	Equity	4.0%	115,580	1,006
Perseus Holding Corp. ⁶ <i>Leisure, Amusement, Motion Pictures, Entertainment</i>	Common	0.2%	400,000	370,040
Plumbing Holdings Corporation ⁶ <i>Buildings and Real Estate⁴</i>	Common	7.8%	-	-
Plumbing Holdings Corporation ⁶ <i>Buildings and Real Estate⁴</i>	Preferred Stock	9.0%	2,716,618	2,673,967
Total Investment in Equity Securities (4% of net asset value at fair value)			\$ 16,199,845	\$ 7,388,465

CLO Fund Securities

CLO Equity Investments

Portfolio Company	Investment	Percentage Interest	Cost	Value²
Grant Grove CLO, Ltd. ^{3, 10}	Subordinated Securities	22.2%	\$ 4,722,113	\$ 3,550,000
Katonah III, Ltd. ^{3, 10}	Preferred Shares	23.1%	4,500,000	820,000
Katonah IV, Ltd. ^{3, 10}	Preferred Shares	17.1%	3,150,000	1,890,000
Katonah V, Ltd. ^{3, 10, 11}	Preferred Shares	26.7%	3,320,000	1,000
Katonah VII CLO Ltd. ^{3, 7, 10}	Subordinated Securities	16.4%	4,500,000	2,470,000
Katonah VIII CLO Ltd. ^{3, 7, 10}	Subordinated Securities	10.3%	3,400,000	2,190,000
Katonah IX CLO Ltd. ^{3, 7, 10}	Preferred Shares	6.9%	2,000,000	1,400,000
Katonah X CLO Ltd. ^{3, 7, 10}	Subordinated Securities	33.3%	11,617,246	9,480,000
Katonah 2007-I CLO Ltd. ^{3, 7, 10}	Preferred Shares	100.0%	29,998,944	26,070,000
Total Investment in CLO Equity Securities			\$ 67,208,303	\$ 47,871,000

CLO Rated-Note Investment

Portfolio Company	Investment	Percentage Interest	Cost	Value²
Katonah 2007-I CLO Ltd. ^{3, 7, 10}	Class B-2L Notes Par Value of \$10,500,000 5.3%, Due 4/22	5.3%	\$ 1,092,286	\$ 8,110,000
Total Investment in CLO Rated-Note			\$ 1,092,286	\$ 8,110,000

Total Investment in CLO Fund Securities (28% of net asset value at fair value)			\$ 68,300,589	\$ 55,981,000
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Asset Manager Affiliate

Portfolio Company / Principal Business	Investment	Percentage Interest	Cost	Value²
Katonah Debt Advisors	Asset Management Company	100.0%	\$ 44,393,453	\$ 42,196,000
Total Investment in Asset Manager Affiliate (21% of net asset value at fair value)			\$ 44,393,453	\$ 42,196,000

Time Deposits and Money Market Account

Time Deposits and Money Market Account	Investment	Yield	Par / Cost	Value²
JP Morgan Asset Account	Time Deposit	0.0%	\$ 168,132	\$ 168,132
JP Morgan Business Money Market Account ⁹	Money Market Account	0.2%	169,858	169,858
Total Investment in Time Deposit and Money Market Accounts (0% of net asset value at fair value)			\$ 337,990	\$ 337,990

Total Investments⁵ (99% of net asset value at fair value)			\$ 250,504,367	\$ 194,342,618
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See accompanying notes to financial statements.

- 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 March 31, 2011.
- 2 Reflects the fair market value of all existing investments as of March 31, 2011, 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 March 31, 2011, 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 \$251 million. The aggregate gross unrealized appreciation is
approximately \$8 million and the aggregate gross unrealized depreciation is approximately \$65 million.
- 6 Non-income producing.
- 7 An affiliate CLO Fund managed by Katonah Debt Advisors, L.L.C. or its affiliate.
- 8 Loan or debt security is on non-accrual status and therefore is considered non-income producing.
- 9 Money market account holding restricted cash for employee flexible spending accounts.
- 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 March 31, 2011, this CLO Fund Security was not providing a dividend distribution.

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

Debt Securities Portfolio

Portfolio Company / Principal Business	Investment Interest Rate¹ / Maturity	Principal	Cost	Value²
Advanced Lighting Technologies, Inc. <i>Home and Office Furnishings, Housewares, and Durable Consumer Products</i>	Senior Secured Loan — Revolving Loan 3.7%, Due 6/13	\$ 1,080,000	\$ 1,075,943	\$ 979,452
Advanced Lighting Technologies, Inc. ⁶ <i>Home and Office Furnishings, Housewares, and Durable Consumer Products</i>	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 <i>Personal, Food and Miscellaneous Services</i>	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 <i>Diversified/Conglomerate Service</i>	Junior Secured Loan — Second Lien Facility 8.3%, Due 8/15	1,217,438	1,217,438	95,368
Bankruptcy Management Solutions, Inc. ⁶ <i>Diversified/Conglomerate Service</i>	Senior Secured Loan — Term Loan B 7.5%, Due 8/14	1,438,720	1,448,006	719,360
Bicent Power LLC ⁶ <i>Utilities</i>	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 <i>Mining, Steel, Iron and Non-Precious Metals</i>	Senior Secured Loan — Term Loan 12.0%, Due 6/13	3,982,143	3,982,143	4,002,054
Caribe Information Investments Incorporated ⁶ <i>Printing and Publishing</i>	Senior Secured Loan — Term Loan 2.5%, Due 3/13	1,611,045	1,608,021	1,273,692
Charlie Acquisition Corp. ⁹ <i>Personal, Food and Miscellaneous Services</i>	Mezzanine Investment — Senior Subordinated Notes 17.5%, Due 6/13	14,261,996	10,744,496	250,000

Portfolio Company / Principal Business	Investment Interest Rate¹ / Maturity	Principal	Cost	Value²
CoActive Technologies LLC (fka CoActive Technologies, Inc.) ⁶ <i>Machinery (Non-Agriculture, Non-Construction, Non-Electronic)</i>	Junior Secured Loan — Term Loan (Second Lien) 7.1%, Due 1/15	\$ 2,000,000	\$ 1,977,696	\$ 1,464,600
eInstruction Corporation ⁶ <i>Healthcare, Education and Childcare</i>	Junior Secured Loan — Term Loan (Second Lien) 7.8%, Due 7/14	10,000,000	10,000,000	10,000,000
Freescale Semiconductor, Inc. <i>Electronics</i>	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 <i>Buildings and Real Estate</i> 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 <i>Buildings and Real Estate</i> 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 <i>Buildings and Real Estate</i> 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 <i>Insurance</i>	Junior Secured Loan — Loan (Second Lien) 5.8%, Due 10/14	5,000,000	4,890,322	4,049,000
Hunter Fan Company ⁶ <i>Home and Office Furnishings, Housewares, and Durable Consumer Products</i>	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} <i>Mining, Steel, Iron and Non-Precious Metals</i>	Senior Secured Loan — Term Loan 12.0%, Due 5/15	967,622	948,809	929,498
Intracpac Corporation/Corona Holdco ⁶ <i>Containers, Packaging and Glass</i>	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} <i>Buildings and Real Estate</i> ⁴	Senior Secured Loan — Term Loan (2006) 7.8%, Due 9/12	9,541,180	9,527,522	6,364,921

Portfolio Company / Principal Business	Investment Interest Rate¹ / Maturity	Principal	Cost	Value²
KIK Custom Products Inc. ⁶ <i>Personal and Non Durable Consumer Products (Mfg. Only)</i>	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 <i>Buildings and Real Estate⁴</i>	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} <i>Buildings and Real Estate⁴</i>	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} <i>Buildings and Real Estate⁴</i>	Junior Secured Loan — Term Loan (Second Lien) 9.5%, Due 1/11	2,000,000	1,920,211	7,600
Legacy Cabinets, Inc. ⁶ <i>Home and Office Furnishings, Housewares, and Durable Consumer Products</i>	Senior Secured Loan — Term Loan 7.3%, Due 5/14	463,380	463,380	92,676
MCCI Group Holdings, LLC ⁶ <i>Healthcare, Education and Childcare</i>	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 <i>Leisure, Amusement, Motion Pictures, Entertainment</i>	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 <i>Leisure, Amusement, Motion Pictures, Entertainment</i>	Preferred Stock — Preferred Stock 14.0%, Due 1/00	400,000	400,000	356,960
QA Direct Holdings, LLC ⁶ <i>Printing and Publishing</i>	Senior Secured Loan — Term Loan 8.3%, Due 8/14	4,396,024	4,372,508	4,396,024
Resco Products, Inc. <i>Mining, Steel, Iron and Non-Precious Metals</i>	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 <i>Mining, Steel, Iron and Non-Precious Metals</i>	Junior Secured Loan — Term Loan (Second Lien) 20.0%, Due 6/14	7,193,458	7,079,981	7,193,458

Portfolio Company / Principal Business	Investment Interest Rate¹ / Maturity	Principal	Cost	Value²
Specialized Technology Resources, Inc. ⁶ <i>Diversified/Conglomerate Service</i>	Junior Secured Loan — Loan (Second Lien) 7.3%, Due 12/14	\$ 7,500,000	\$ 7,500,000	\$ 7,500,000
TUI University, LLC ⁶ <i>Healthcare, Education and Childcare</i>	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 <i>Cargo Transport</i>	Junior Secured Loan — Term Loan B 13.3%, Due 12/13	470,643	470,643	470,643
Walker Group Holdings LLC ⁶ <i>Cargo Transport</i>	Junior Secured Loan — Term Loan B 13.3%, Due 12/13	4,469,539	4,469,539	4,469,539
Wesco Aircraft Hardware Corp. <i>Aerospace and Defense</i>	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 <i>Aerospace and Defense</i>	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	Value²
Aerostructures Holdings L.P. ⁷ <i>Aerospace and Defense</i>	Partnership Interests	1.2%	\$ 1,000,000	\$ 88,600
Aerostructures Holdings L.P. ⁷ <i>Aerospace and Defense</i>	Series A Preferred Interests	1.2%	250,961	250,961
Bankruptcy Management Solutions, Inc. ^{6, 7} <i>Diversified/Conglomerate Service</i>	Warrants	0.1%	-	-
Coastal Concrete Holding II, LLC ⁷ <i>Buildings and Real Estate⁴</i>	Class A Units	10.8%	8,625,626	250,143

Portfolio Company / Principal Business	Investment	Percentage Interest/Shares	Cost	Value²
eInstruction Acquisition, LLC ⁷ <i>Healthcare, Education and Childcare</i>	Membership Units	1.1%	\$ 1,079,617	\$ 1,079,724
FP WRCA Coinvestment Fund VII, Ltd. ^{3, 7} <i>Machinery (Non-Agriculture, Non-Construction, Non-Electronic)</i>	Class A Shares	1,500	1,500,000	2,400,000
International Architectural Products, Inc. ^{6, 7} <i>Mining, Steel, Iron and Non-Precious Metals</i>	Common	2.5%	292,851	227,223
Legacy Cabinets, Inc. ^{6, 7} <i>Home and Office Furnishings, Housewares, and Durable Consumer Products</i>	Equity	4.0%	115,580	49,422
Perseus Holding Corp. ⁷ <i>Leisure, Amusement, Motion Pictures, Entertainment</i>	Common	0.2%	400,000	312,200
Bankruptcy Management Solutions, Inc. ^{6, 7} <i>Diversified/Conglomerate Service</i>	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	Value²
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}	Preferred Shares	6.9%	2,000,000	1,300,000
Katonah X CLO Ltd. ^{3, 8, 12}	Subordinated Securities	33.3%	11,612,676	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			\$ 67,191,617	\$ 45,021,000

CLO Rated-Note Investment

<u>Portfolio Company</u>	<u>Investment</u>	<u>Percentage Interest</u>	<u>Cost</u>	<u>Value²</u>
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)			\$ 68,280,199	\$ 53,031,000
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Asset Manager Affiliate

<u>Portfolio Company / Principal Business</u>	<u>Investment</u>	<u>Percentage Interest</u>	<u>Cost</u>	<u>Value²</u>
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

<u>Time Deposits and Money Market Account</u>	<u>Investment</u>	<u>Yield</u>	<u>Par / Cost</u>	<u>Value²</u>
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
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Total Investments⁵ (102% of net asset value at fair value)			\$ 253,771,801	\$ 191,186,296
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See accompanying notes to financial statements.

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.

KOHLBERG CAPITAL CORPORATION
FINANCIAL HIGHLIGHTS
(unaudited)
(\$ per share)

	Three Months Ended	
	March 31,	
	2011	2010
Per Share Data:		
Net asset value, at beginning of period	\$ 8.21	\$ 9.56
Net income (loss)		
Net investment income ¹	0.22	0.11
Net realized losses ¹	(0.08)	(0.10)
Net change in unrealized appreciation/depreciation on investments ¹	0.27	0.02
Net income	0.41	0.03
Net decrease in net assets resulting from distributions		
Net increase in net assets relating to stock-based transactions		
Issuance of common stock under dividend reinvestment plan	0.01	0.02
Stock based compensation expense	0.01	0.01
Net increase in net assets relating to stock-based transactions	0.02	0.03
Net asset value, end of period	\$ 8.64	\$ 9.62
Total net asset value return ²	5.2%	6.5%
Ratio/Supplemental Data:		
Per share market value at beginning of period	\$ 6.97	\$ 3.64
Per share market value at end of period	\$ 8.26	\$ 5.66
Total market return ³	18.5%	55.5%
Shares outstanding at end of period	22,803,233	22,475,339
Net assets at end of period	\$ 197,047,471	\$ 216,210,807
Portfolio turnover rate ⁴	2.6%	0.9%
Average debt outstanding	\$ 35,561,620	\$ 203,292,118
Asset coverage ratio	428%	209%
Ratio of net investment income to average net assets ⁵	9.8%	4.8%
Ratio of total expenses to average net assets ⁵	4.6%	8.2%
Ratio of interest expense to average net assets ⁵	0.6%	5.0%
Ratio of non-interest expenses to average net assets ⁵	4.0%	3.1%

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 (not annualized) equals the change in the ending market price over the beginning of period price per share plus dividends, divided by the beginning price.

⁴ Not annualized

⁵ Annualized

See accompanying notes to financial statements.

KOHLBERG CAPITAL CORPORATION

NOTES TO FINANCIAL STATEMENTS (unaudited)

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 IPO, 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 March 31, 2011, Katonah Debt Advisors had approximately \$1.9 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

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 unaudited 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”) for interim financial information. Accordingly, they do not include all of the information and footnotes required for annual financial statements. The unaudited interim financial statements and notes thereto should be read in conjunction with the financial statements and notes thereto in the Company’s Form 10-K for the year ended December 31, 2010, as filed with the Securities and Exchange Commission (the “Commission” or the “SEC”).

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 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.

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.

In 2010, the Company engaged Valuation Research Corporation ("VRC"), an independent valuation firm, to provide a third-party review of 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 I or Level II 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.
- 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 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 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 at December 31, 2010 consisted mostly of cash held in an operating account pursuant to the Company's secured credit facility agreement with its lender. As the Company paid off its secured credit facility as of January 31, 2011, no such restricted cash balances were needed.

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 March 31, 2011, four issuers representing 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 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. In January 31, 2011, the Company fully repaid its outstanding secured credit borrowing facility which had a balance of \$86.7 million as of December 31, 2010 and, at repayment, all related debt issuance costs were fully amortized. During March 2011, the Company issued \$60 million of convertible senior notes and incurred debt issuance costs of approximately \$2.3 million which will be amortized over a five-year period. At March 31, 2011, there was an unamortized debt issuance cost of approximately \$2.3 million included in other assets in the accompanying balance sheet. Amortization expense for the three months ended March 31, 2011 and 2010 was approximately \$45,000 and \$206,000, 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 quarter. The adoption of this disclosure-only guidance is included in Note 4 “— Portfolio Investments” and did not have a material impact on the Company’s financial results.

3. EARNINGS PER SHARE

The following information sets forth the computation of basic and diluted net increase in stockholders’ equity per share for the three months ended March 31, 2011 and 2010:

	Three Months Ended March 31,	
	2011	2010
Net increase in net assets from operations	\$ 9,604,634	\$ 1,594,909
Net increase in net assets allocated to unvested share awards	(141,105)	(21,469)
Add: Interest on Senior Convertible Notes	232,335	—
Net increase in net assets available to common stockholders	<u>9,695,864</u>	<u>1,573,440</u>
Weighted average number of common shares outstanding for basic shares computation	22,791,242	22,445,457
Effect of dilutive securities - stock options	10,910	—
Effect of dilutive Senior Convertible Notes	<u>1,185,255</u>	—
Weighted average number of common and common stock equivalent shares outstanding for diluted shares computation	<u>23,987,407</u>	<u>22,445,457</u>
Net increase (decrease) in net assets per basic common shares:		
Net increase in net assets from operations	0.42	0.07
Net increase in net assets allocated to unvested share awards	(0.01)	(0.00)

Share-based awards that contain nonforfeitable rights to dividends or dividend equivalents, whether paid or unpaid, are participating securities and included in the computation of both basic and diluted earnings per share. Grants of restricted stock awards to our employees and directors are considered participating securities when there are earnings in the period and the earnings per share calculations include outstanding unvested restricted stock awards in the basic weighted average shares outstanding calculation.

Options to purchase 20,000 and 40,000 shares were not included in the computation of diluted earnings per share for the periods ended March 31, 2011 and 2010, respectively, because the effect would be antidilutive as the exercise prices exceeded the average market price of the common shares.

The Company's Senior Convertible Notes are included in the computation of the diluted net increase or decrease in net assets resulting from operations per share in accordance with ASC 261-10-45-40-b by application of the "if-converted method." Under the if-converted method, interest charges applicable to the convertible debt for the period are added to the reported net increase or decrease in net assets resulting from operations and the full amount of shares (pro-rata if not outstanding for the full period) that would be issued are added to weighted average basic shares. Convertible debt is considered anti-dilutive only when its interest per share upon conversion exceeds the basic net increase or decrease in net assets resulting from operations per share.

The as-if converted method of computing the dilutive effects on convertible debt assumes a conversion even if the contracted conversion price exceeds the market value of the shares. The Company's Senior Convertible Debt has a conversion price of \$8.44 per share which was above the Company's net asset value per share at the time of issuance. Upon conversion, the Company would issue the full amount of common stock upon conversion and retire the full amount of debt outstanding.

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 industries in which it currently has little or no investment if it is presented with attractive opportunities.

The following table shows the Company's portfolio by security type at March 31, 2011 and December 31, 2010:

Security Type	March 31, 2011 (unaudited)			December 31, 2010		
	Cost	Fair Value	% ¹	Cost	Fair Value	% ¹
Time Deposits	\$ 168,132	\$ 168,132	-%	\$ 720,225	\$ 720,225	-%
Money Market Account	169,858	169,858	-	210,311	210,311	-
Senior Secured Loan	31,815,722	23,276,764	12	34,183,551	22,001,256	12
Junior Secured Loan	73,991,930	60,010,630	31	76,896,867	63,944,003	34
Mezzanine Investment	10,744,496	250,000	-	10,744,496	250,000	-
Senior Subordinated Bond	4,320,342	4,528,209	2	4,320,596	4,490,709	3
CLO Fund Securities	68,300,589	55,981,000	28	68,280,200	53,031,000	28
Equity Securities	16,199,845	7,388,465	4	13,232,266	4,437,871	3
Preferred	400,000	373,560	-	650,961	607,921	-
Affiliate Asset Managers	44,393,453	42,196,000	22	44,532,329	41,493,000	22
Total	\$ 250,504,367	\$ 194,342,618	99%	\$ 253,771,802	\$ 191,186,296	102%

¹ Calculated as a percentage of net asset value.

The industry unaudited concentrations, based on the fair value of the Company's investment portfolio as of March 31, 2011 and December 31, 2010, were as follows:

Industry Classification	March 31, 2011 (unaudited)			December 31, 2010		
	Cost	Fair Value	% ¹	Cost	Fair Value	% ¹
Aerospace and Defense	\$ 6,501,477	\$ 5,592,044	3%	\$ 6,499,518	\$ 5,613,844	3%
Asset Management Companies ²	44,393,453	42,196,000	22	44,532,329	41,493,000	22
Beverage, Food and Tobacco	3,007,500	3,007,500	1	-	-	-
Buildings and Real Estate ³	31,040,943	8,334,849	4	32,845,509	6,923,964	4
Cargo Transport	4,374,351	4,374,351	2	4,940,182	4,940,182	3
CLO Fund Securities	68,300,589	55,981,000	28	68,280,200	53,031,000	28
Containers, Packaging and Glass	3,008,678	3,000,000	2	3,009,682	3,000,000	2
Diversified/Conglomerate Service	10,379,788	8,165,389	4	10,384,036	8,345,287	4
Electronics	3,005,883	3,213,750	2	3,006,137	3,176,250	2
Healthcare, Education and Childcare	15,119,076	14,917,739	8	15,113,551	15,037,936	8
Home and Office Furnishings, Housewares, and Durable Consumer Products	9,575,317	8,925,614	5	9,654,903	8,804,450	5
Insurance	4,897,522	3,962,000	2	4,890,322	4,049,000	2
Leisure, Amusement, Motion Pictures, Entertainment	2,114,458	2,058,059	1	2,114,458	1,983,619	1
Machinery (Non-Agriculture, Non-Construction, Non-Electronic)	3,479,047	4,000,400	2	3,477,696	3,864,600	2
Mining, Steel, Iron and Non-Precious Metals	10,589,242	10,570,718	5	14,381,863	14,430,312	8
Personal and Non Durable Consumer Products (Mfg. Only)	5,000,000	3,407,500	2	5,000,000	3,435,000	2
Personal, Food and Miscellaneous Services	13,736,996	3,242,500	2	14,730,350	4,090,000	2
Personal Transportation	3,022,500	3,022,500	1	-	-	-
Printing and Publishing	1,608,354	1,060,712	1	5,980,529	5,669,716	3
Telecommunications	3,011,203	3,011,203	1	-	-	-
Time Deposit and Money Market Accounts	337,990	337,990	-	930,537	930,536	-
Utilities	4,000,000	1,960,800	1	4,000,000	2,367,600	1
Total	\$ 250,504,367	\$ 194,342,618	99%	\$ 253,771,802	\$ 191,186,296	102%

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 March 31, 2011 and December 31, 2010, 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.

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 March 31, 2011 and December 31, 2010, approximately 22% and 20% of the Company's total assets were foreign assets (including the Company's investments in CLO Funds, which are typically domiciled outside the U.S.) At March 31, 2011, no foreign assets were in U.S. dollar denominated over-night time Eurodollar deposits which revert to cash each business morning.

At March 31, 2011 and December 31, 2010, the Company's ten largest portfolio companies represented approximately 64% and 65%, 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 16% and 22% of the total fair value of the Company's investments at March 31, 2011 and December 31, 2010, respectively. Excluding Katonah Debt Advisors and CLO Fund securities, the Company's ten largest portfolio companies represented approximately 27% and 30% of the total fair value of the Company's investments at March 31, 2011 and December 31, 2010, 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.

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 March 31, 2011 and December 31, 2010, the Company had approximately \$48 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 March 31, 2011 was approximately \$67 million and aggregate unrealized depreciation on the CLO Fund securities totaled approximately \$19 million. 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.

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 March 31, 2011 were approximately \$8 million, \$1 million, and \$7 million, respectively. At December 31, 2010, the fair value, cost basis, and aggregate unrealized appreciation of the Katonah 2007-1 B-2L investment were \$8 million, \$1 million, and \$7 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.

All CLO Funds managed by Katonah Debt Advisors are currently making quarterly dividend distributions to the Company and are paying all senior and subordinate management fees to Katonah Debt Advisors. With the exception of the Katonah V, Ltd. CLO Fund, all third-party managed CLO Funds held as investments are making quarterly dividend distributions to the Company.

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.

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.

The following table summarizes the fair value of investments by the above *Fair Value Measurements and Disclosures* fair value hierarchy levels as of March 31, 2011 (unaudited) and December 31, 2010, respectively:

As of March, 31 2011 (unaudited)				
	Level I	Level II	Level III	Total
Time deposit and money market account	\$ —	\$ 337,990	\$ —	\$ 337,990
Debt securities	—	—	88,439,163	88,439,163
CLO fund securities	—	—	55,981,000	55,981,000
Equity securities	—	—	7,388,465	7,388,465
Asset manager affiliate	—	—	42,196,000	42,196,000

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 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 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 2010, the Company engaged VRC, an independent valuation firm, to provide a third-party review of 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.

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

	Three Months Ended March 31, 2011 (unaudited)				
	Debt Securities	CLO Fund Securities	Equity Securities	Asset Manager Affiliates	Total
Balance, December 31, 2010	\$ 91,042,928	\$ 53,031,000	\$ 4,688,832	\$ 41,493,000	\$ 190,255,760
Transfers in/out of Level III	—	—	—	—	—
Net accretion of discount	24,736	20,390	—	—	45,126
Purchases	17,424,281	—	2,858,387	—	20,282,668
Sales	(20,895,314)	—	(141,769)	(138,875)	(21,175,958)
Total loss realized and unrealized included in earnings	842,532	2,929,610	(16,985)	841,875	4,597,032
Balance, March 31, 2011	<u>\$ 88,439,163</u>	<u>\$ 55,981,000</u>	<u>\$ 7,388,465</u>	<u>\$ 42,196,000</u>	<u>\$ 194,004,628</u>
Changes in unrealized gains (losses) included in earnings related to investments still held at reporting date	<u>\$ 2,669,255</u>	<u>\$ 2,929,610</u>	<u>\$ (16,985)</u>	<u>\$ 841,875</u>	<u>\$ 6,423,755</u>

	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 in/out of Level III	—	—	—	—	—
Net accretion of discount	381,677	85,149	—	—	466,826
Purchases	9,981,426	—	1,927,366	3,780,817	15,689,609
Sales	(208,820,374)	—	—	—	(208,820,374)
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	<u>\$ 91,042,928</u>	<u>\$ 53,031,000</u>	<u>\$ 4,688,832</u>	<u>\$ 41,493,000</u>	<u>\$ 190,255,760</u>
Changes in unrealized gains (losses) included in earnings related to investments still held at reporting date	<u>\$ 9,196,912</u>	<u>\$ 3,974,851</u>	<u>\$ (1,142,038)</u>	<u>\$ (20,352,537)</u>	<u>\$ (8,322,812)</u>

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 March 31, 2011, Katonah Debt Advisors had approximately \$1.9 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 its operating expenses. The annual management fees Katonah Debt Advisors receives have two components - a senior management fee and a subordinated management fee. Currently, all CLO Funds managed by Katonah Debt Advisors are paying both their senior and subordinated management fees on a current basis.

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.

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. On February 4, 2011, Katonah Debt Advisors entered into 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.

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 three months ended March 31, 2011, Katonah Debt Advisors had approximately \$450,000 of pre-tax net income before net capital losses and made no distributions to the Company. For the three months ended March 31, 2010, Katonah Debt Advisors earned approximately \$650,000 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. It is anticipated that Katonah Debt Advisors will make a dividend distribution(s) to the Company during 2011.

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 three months ended March 31, 2011, Katonah Debt Advisors had an increase in fair value of approximately \$703,000.

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 March 31, 2011 and December 31, 2010 there were no intercompany balances with our affiliates.

6. BORROWINGS

The Company's debt obligations consist of the following:

	<u>As of</u> <u>March 31, 2011</u>	<u>As of</u> <u>December 31, 2010</u>
Senior Convertible Notes, due March 15, 2016	60,000,000	-
Secured credit facility, due February 28, 2011 ⁽¹⁾	-	86,746,582

(1) February 28, 2011 was the maturity date as established by a Forbearance and Settlement Agreement dated September 20, 2010. This borrowing was fully repaid on January 31, 2011.

Secured Credit Facility

At December 31, 2010, the Company had a secured credit facility with an outstanding balance of \$86,746,582. On January 31, 2011, this secured credit facility was fully repaid.

In connection with the above noted 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 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.

On January 31, 2011, the Company repaid in full the outstanding balance under this facility in advance of the scheduled forbearance date of February 28, 2011, resulting in no outstanding balance thereafter. As a result, 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.

Senior Convertible Notes

On March 16, 2011, the Company issued \$55 million in aggregate principal amount of unsecured 8.75% convertible senior notes due 2016 ("Convertible Senior Notes"). On March 23, 2011, pursuant to an over-allotment option, the Company issued an additional \$5 million of such Convertible Senior Notes for a total of \$60 million in aggregate principal amount. The net proceeds for the Convertible Senior Notes, following underwriting expenses, were approximately \$57.7 million. Interest on the Convertible Senior Notes is paid semi-annually in arrears on March 15 and September 15, at a rate of 8.75%, commencing September 15, 2011. The Notes mature on March 15, 2016 unless converted earlier. The Convertible Senior Notes are senior unsecured obligations of the Company.

The Convertible Senior Notes are convertible into shares of Company's common stock based on an initial conversion rate of 118.5255 shares of common stock per \$1,000 principal amount of Convertible Senior Notes, which is equivalent to an initial conversion price of approximately \$8.44 per share of common stock. The conversion rate will be subject to adjustment upon certain events.

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

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

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

In connection with the issuance of the Convertible Senior Notes, the Company incurred approximately \$2.3 million of debt offering costs which are being amortized over the term of the facility on a straight-line basis, which approximates the effective yield method, of which approximately \$2.3 million remains to be amortized.

The Convertible Senior Notes have been analyzed for any features that would require its accounting to be bifurcated and, as a result, they are recorded as a liability at their contractual amounts.

For the period from March 11, 2011 (the date of issuance of the notes) to March 31, 2011, the Company recorded approximately \$230,000 of interest costs and amortization of financing costs as interest expense.

Fair Value of Convertible Senior Notes. The Company carries the Convertible Senior Notes at cost. The Convertible Senior Notes were issued in a private placement and there is no active trading of these notes. The fair value of the Company's outstanding Convertible Senior Notes was approximately \$62.5 Million at March 31, 2011. The fair value was determined based on the average of indicative bid and offer pricing for the Convertible Senior Notes.

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 2011). 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 incur a US federal excise tax for the calendar year 2011.

The following reconciles net increase in net assets resulting from operations to taxable income for the three months ended March 31, 2011:

	Three Months Ended March 31, 2011 (unaudited)
Net increase in net assets resulting from operations	\$ 9,604,634
Net change in unrealized (appreciation) depreciation from investments	(6,423,755)
Excess capital losses over capital gains	1,826,723
Income not on GAAP books currently taxable	20,932
Income not currently taxable	(42,394)
Expenses not currently deductible	179,472
Expenses not on GAAP books currently deductible	(3,978)
Taxable income before deductions for distributions	<u>\$ 5,161,634</u>
Taxable income before deductions for distributions per weighted average shares for the period	<u>\$ 0.23</u>

For the quarter ended March 31, 2011, the Company declared a dividend on March 21, 2011 of \$0.17 per share for a total of approximately \$4 million. The record date was April 8, 2011 and the dividend was distributed on April 29, 2011.

Taxable income differs from net decrease in net assets 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.

At March 31, 2011, the Company had a net capital loss carryforward of \$35 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. The Company recognizes the tax benefits of uncertain tax positions only where the position is "more likely than not" to be sustained assuming examination by tax authorities. Management has analyzed the Company's tax positions, and has concluded that no liability for unrecognized tax benefits should be recorded related to uncertain tax positions taken on returns filed for open tax years (the last three fiscal years) or expected to be taken in the Company's current year tax return. The Company identifies its major tax jurisdictions as U.S. Federal and New York State, and the Company is not aware of any tax positions for which it is reasonably possible that the total amounts of unrecognized tax benefits will change materially in the next 12 months. 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 March 31, 2011 and December 31, 2010, 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 March 31, 2011 and \$1 million had been funded as of December 31, 2010.

The Company and certain directors and officers were 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. On March 21, 2011, the three putative class actions were consolidated. A consolidated complaint has not yet been filed. The Company believes that the above-mentioned suit is without merit and will defend it 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 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

During the quarter ended March 31, 2011 and the year ended December 31, 2010, the Company issued 41,771 and 301,663 shares, respectively, of common stock under its dividend reinvestment plan. For the three months ended March 31, 2011, no shares of restricted stock were issued or converted to common stock and 2,334 shares of restricted stock were forfeited. 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 March 31, 2011 and December 31, 2010 was 22,803,233 and 22,767,130, respectively.

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.

Information with respect to options granted, exercised and forfeited under the Plan for the period January 1, 2010 through March 31, 2011 is as follows:

	Shares	Weighted Average Exercise Price per Share	Weighted Average Contractual Remaining Term (years)	Aggregate Intrinsic Value ¹
Options outstanding at January 1, 2010	40,000	\$ 11.97		
Granted	20,000	\$ 4.93		
Exercised	—	\$ —		
Forfeited	—	\$ —		
Options outstanding at December 31, 2010	60,000	\$ 7.24		
Granted	—	\$ —		
Exercised	—	\$ —		
Forfeited	—	\$ —		
Outstanding at March 31, 2011	60,000	\$ 7.24	8.2	\$ 135,200
Total vested at March 31, 2011	50,000	\$ 7.73	8.0	

¹ Represents the difference between the market value of shares of the Company upon exercise of the options at March 31, 2011 and the cost for the option holders to exercise the options.

The Company uses a Binary Option Pricing Model (American, call option) as its valuation model to establish the expected value of all stock option grants. For the three months ended March 31, 2011 and March 31, 2010, the Company recognized non-cash compensation expense related to stock options of approximately \$4,000 and \$2,000, respectively. At March 31, 2011, the Company had approximately \$4,000 of remaining compensation cost related to unvested stock-based awards expected to be recognized by the Company over a weighted average period of 0.25 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.

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 March 31, 2011, 190,000 of such shares were vested and converted to common shares, and 45,332 of such shares had yet to vest. The remaining 23,668 shares have been forfeited.

During the three months ended March 31, 2011, no shares of restricted stock were vested and converted to common shares. As of March 31, 2011, after giving effect to these option cancellations and restricted stock awards, there were options to purchase 60,000 shares of common stock outstanding and there were 333,990 shares of restricted stock outstanding. Information with respect to restricted stock granted, exercised and forfeited under the Plan for the period January 1, 2010 through March 31, 2011 is as follows:

	Unvested Restricted Shares	Weighted Average Exercise Price per Share
Unvested shares outstanding at December 31, 2009	302,139	\$ 9.63
Granted	103,519	\$ 4.83
Vested	(64,667)	\$ 10.39
Forfeited	(4,667)	\$ —
Unvested shares outstanding at December 31, 2010	336,324	\$ 8.01
Granted	—	\$ —
Vested	—	\$ —
Forfeited	(2,334)	\$ 10.39
Outstanding at March 31, 2011	<u>333,990</u>	\$ 7.99
Total unvested shares at March 31, 2011	333,990	\$ 7.99

For the three months ended March 31, 2011, non-cash compensation expense related to restricted stock was approximately \$219,000; of this amount approximately \$178,000 was expensed at the Company and approximately \$41,000 was a reimbursable expense allocated to Katonah Debt Advisors. For the three months ended March 31, 2010, non-cash compensation expense related to restricted stock was approximately \$218,000; of this amount approximately \$148,000 was expensed at the Company and approximately \$70,000 was a reimbursable expense allocated to Katonah Debt Advisors. Dividends are paid on all outstanding shares of restricted stock, whether or not vested. In general, shares of unvested restricted stock are forfeited upon the recipient's termination of employment. As of March 31, 2011, there was approximately \$1 million of total unrecognized compensation cost related to unvested share-based awards. That cost is expected to be recognized over a weighted average period of 2 years.

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 three months ended March 31, 2011 and 2010 the Company made contributions to the 401K Plan of approximately \$7,000 and \$14,000, respectively.

The Company has also adopted a deferred compensation plan (“Pension Plan”) effective January 1, 2007. Employees are eligible for the Pension 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 Pension Plan. On behalf of the employee, the Company may contribute to the Pension 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 Pension Plan after five years of service. For the three months ended March 31, 2011, the Company made a \$30,000 contribution to the Pension Plan and no contribution to the Pension Plan for the three months ended March 31, 2010.

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

In this Quarterly Report on Form 10-Q, “Kohlberg Capital,” “Company,” “we,” “us,” and “our” refer to Kohlberg Capital Corporation, its subsidiaries and its wholly-owned portfolio company, Katonah Debt Advisors, L.L.C. (collectively with its affiliates, “Katonah Debt Advisors”), and related companies, unless the context otherwise requires.

The information contained in this section should be read in conjunction with our financial statements and notes thereto appearing elsewhere in this Quarterly Report. In addition, some of the statements in this report constitute 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 Quarterly Report, as well as in future oral and written statements by management of Kohlberg Capital, 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,” “believes,” “estimates,” “predicts,” “potential” or “continue” or the negative of these terms or other similar words. Important assumptions include our ability to originate new investments, achieve certain margins and levels of profitability, the availability of funds under our credit facility, 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 Quarterly 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 Quarterly 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;
- 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.

There are a number of important risks and uncertainties that could cause our actual results to differ materially from those indicated by such forward-looking statements. For a discussion of factors that could cause our actual results to differ from forward-looking statements contained in this Quarterly Report, please see the discussion in Part II, “Item 1A. Risk Factors” below and in Part I, “Item 1A. Risk Factors” in our Annual Report on Form 10-K for the fiscal year ended December 31, 2010. You should not place undue reliance on these forward-looking statements. The forward-looking statements made in this Quarterly 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 Quarterly Report.

GENERAL

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, manages 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., LLC (“Kohlberg & Co.”), a leading private equity firm focused on middle market investing. As of March 31, 2011, Katonah Debt Advisors had approximately \$1.9 billion of assets under management.

Our investment objective is to generate current income and capital appreciation from our investments. We also expect to continue 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”), 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. Pursuant to these elections, we generally will not have to pay corporate-level taxes on any income that we distribute to our stockholders.

Our common stock is traded on The NASDAQ Global Select Market under the symbol “KCAP.” The net asset value (“NAV”) per share of our common stock as of March 31, 2011 was \$8.64. On March 31, 2011, the last reported sale price of a share of our common stock on The NASDAQ Global Select Market was \$8.26.

KEY QUANTITATIVE AND QUALITATIVE FINANCIAL MEASURES AND INDICATORS

Net Asset Value

Our NAV per share was \$8.64 and \$8.21 as of March 31, 2011 and December 31, 2010, respectively. As we must report our assets at fair value for each reporting period, NAV also represents the amount of stockholder’s equity per share for the reporting period. Our NAV is comprised mostly of investment assets less debt and other liabilities:

	March 31, 2011 (unaudited)		December 31, 2010	
	Fair Value ¹	Per Share ¹	Fair Value ¹	Per Share ¹
Investments at fair value:				
Investments in time deposits	\$ 168,132	\$ 0.01	\$ 720,225	\$ 0.03
Investments in money market accounts	169,858	0.01	210,311	0.01
Investments in debt securities	88,439,163	3.88	91,042,928	4.00
Investments in CLO Fund securities	55,981,000	2.45	53,031,000	2.33
Investments in equity securities	7,388,465	0.32	4,688,832	0.21
Investments in asset manager affiliates	42,196,000	1.85	41,493,000	1.82
Cash	70,747,215	3.10	10,175,488	0.45
Restricted Cash	—	-	67,023,170	2.93
Other assets	5,927,941	0.26	11,437,732	0.50
Total Assets	\$ 271,017,774	\$ 11.88	\$ 279,822,686	\$ 12.28
Borrowings	\$ —	\$ -	\$ 86,746,582	\$ 3.81
Other liabilities	13,970,303	0.61	6,150,437	0.27
Senior Convertible Notes	60,000,000	2.63	—	—
Total Liabilities	\$ 73,970,303	\$ 3.24	\$ 92,897,019	\$ 4.08
NET ASSET VALUE	\$ 197,047,471	\$ 8.64	\$ 186,925,667	\$ 8.21

¹ Our balance sheet at fair value and resultant NAV 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 in that our shares may trade based on a percentage of NAV and individual investors may weight certain balance sheet items differently in performing an analysis of the Company.

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 March 31, 2011, we had approximately \$60 million of outstanding borrowings and our asset coverage ratio of total assets to total borrowings was 428%, 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.

At December 31, 2010, we had approximately \$87 million of outstanding indebtedness through a secured credit facility. On January 31, 2011, we repaid in full the outstanding balance under this facility. As a result, approximately \$73 million of collateral previously securing the facility was released to us and we also received a \$2 million cash settlement from the lenders to settle litigation previously initiated by us against the lenders. In order to pay off this facility, we utilized proceeds received from the paydown, amortization or sale of portfolio loan investments totaling approximately \$133 million together with available cash.

On March 16, 2011, we issued \$55 million in aggregate principal amount of unsecured 8.75% convertible senior notes due 2016 (“Convertible Senior Notes”). On March 23, 2011, pursuant to an over-allotment option, we issued an additional \$5 million of such Convertible Senior Notes for a total of \$60 million in aggregate principal amount. The net proceeds for the Convertible Senior Notes, following underwriting expenses, were approximately \$57.7 million. Interest on the Convertible Senior Notes is paid semi-annually in arrears on March 15 and September 15, at a rate of 8.75%, commencing September 15, 2011. The Notes mature on March 15, 2016 unless converted earlier. The Convertible Senior Notes are senior unsecured obligations of the Company.

The Convertible Senior Notes are convertible into shares of Company’s common stock based on an initial conversion rate of 118.5255 shares of common stock per \$1,000 principal amount of Convertible Senior Notes, which is equivalent to an initial conversion price of approximately \$8.44 per share of common stock. The conversion rate will be subject to adjustment upon certain events.

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. As a result, we may seek to enter into new agreements with other lenders or into other financing arrangements as market conditions permit.

Investment Portfolio Summary Attributes as of and for the Three Months ended March 31, 2011

Our investment portfolio generates net investment income which is generally used to pay principal and interest on our borrowings under the Facility and to fund our dividend. 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 \$7 million, which comprises approximately 4% 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 three months ended March 31, 2011:

Debt Securities

- represent approximately 32% of total assets;
- 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 (26% and 68% of debt securities, respectively);
- spread across 19 different industries and 28 different entities;
- average balance per investment of approximately \$3 million;
- all but four issuers (representing less than 1% of total investments at fair value) are current on their debt service obligations; and
- weighted average interest rate of 8.7% on income producing debt investments.

CLO Fund Securities (as of the last monthly trustee report prior to March 31, 2011 unless otherwise specified)

- represent approximately 21% of total assets at March 31, 2011;
- 86% of CLO Fund Securities represent investments in subordinated securities or equity securities issued by CLO Funds and 14% 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 16% of total assets;
- represents our 100% ownership of the equity interest of a profitable CLO Fund manager focused on corporate credit investing;
- has approximately \$1.9 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 three months ended March 31, 2011, Katonah Debt Advisors had pre-tax net income before net capital losses of approximately \$450,000; and
- for the three months ended March 31, 2011, Katonah Debt Advisors made no distributions to the Company in the form of a dividend which is recognized as current earnings to the Company.

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 may 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 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 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 three months ended March 31, 2011, the Company's investments had a net change in unrealized appreciation of approximately \$6.4 million; during three months ended March 31, 2010, the Company's investments had a net change in unrealized appreciation of approximately \$1 million.

The net change in unrealized appreciation for the three months ended March 31, 2011 is primarily due to (i) an approximate \$2.7 million net increase in the market value of certain loans as a result of credit considerations and current market conditions; (ii) an approximate \$2.9 million increase in the net value of CLO Fund securities; and (iii) an approximate \$703,000 increase in the value of Katonah Debt Advisors (an approximate \$800,000 increase in unrealized appreciation offset by an approximate \$100,000 decrease in the cost basis of Katonah Debt Advisors).

Net Change in Stockholders' Equity Resulting From Operations

The net change in stockholders' equity resulting from operations for the three months ended March 31, 2011 and 2010 was an increase of approximately \$10 million and an increase of \$2 million, respectively, or an increase of \$0.42 and \$0.07 per share, respectively.

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 three months ended March 31, 2011, net investment income and realized gains was approximately \$3 million, or \$0.22 per share. For the three months ended March 31, 2010, net investment income and realized gains was approximately \$306,000, or \$0.11, per share.

Dividends

For the three months ended March 31, 2011, we declared a \$0.17 dividend per share. As a result, there was a dividend distribution of approximately \$4 million for the first quarter declaration, which was booked in the second quarter. 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% of our ordinary net taxable income for the calendar year;
- 98% 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 since the most recent completed calendar year, 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, if any, plus a portion of any prior year undistributed amounts of net investment income distributed in subsequent years:

	Dividend	Declaration Date	Record Date	Pay Date
2011:				
First quarter	\$ 0.17	3/21/2011	4/8/2011	4/29/2011
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	<u>\$ 0.68</u>			

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 three months ended March 31, 2011, Katonah Debt Advisors had approximately \$450,000 of pre-tax net income before net capital losses and made no distributions to us. For the three months ended March 31, 2010, Katonah Debt Advisors earned approximately \$650,000 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.

INVESTMENT PORTFOLIO

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. We intend to grow our portfolio of assets by raising additional capital, including through the prudent use of leverage available to us. 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.

The following table shows the Company's portfolio by security type at March 31, 2011 and December 31, 2010:

Security Type	March 31, 2011 (unaudited)			December 31, 2010		
	Cost	Fair Value	% ¹	Cost	Fair Value	% ¹
Time Deposits	\$ 168,132	\$ 168,132	-%	\$ 720,225	\$ 720,225	-%
Money Market Account	169,858	169,858	-	210,311	210,311	-
Senior Secured Loan	31,815,722	23,276,764	12	34,183,551	22,001,256	12
Junior Secured Loan	73,991,930	60,010,630	31	76,896,867	63,944,003	34
Mezzanine Investment	10,744,496	250,000	-	10,744,496	250,000	-
Senior Subordinated Bond	4,320,342	4,528,209	2	4,320,596	4,490,709	3
CLO Fund Securities	68,300,589	55,981,000	28	68,280,200	53,031,000	28
Equity Securities	16,199,845	7,388,465	4	13,232,266	4,437,871	3
Preferred	400,000	373,560	-	650,961	607,921	-
Affiliate Asset Managers	44,393,453	42,196,000	22	44,532,329	41,493,000	22
Total	\$ 250,504,367	\$ 194,342,618	99%	\$ 253,771,802	\$ 191,186,296	102%

¹ Calculated as a percentage of net asset 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.

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 March 31, 2011 and March 31, 2010, our investments in income producing loans and debt securities, excluding CLO Fund securities, had a weighted average interest rate of approximately 8.7% and 6.4%, respectively.

The investment portfolio (excluding the Company's investment in asset manager affiliates and CLO Funds) at March 31, 2011 was spread across 19 different industries and 28 different entities with an average balance per entity of approximately \$3 million. As of March 31, 2011, all but four of our portfolio companies (representing less than 1% of total investments at fair value) were current on their debt service obligations. Our portfolio, including the CLO Funds in which it invests, 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 U.S., which investments are generally not anticipated to be in excess of 10% of our investment portfolio at the time such investments are made. At March 31, 2011, approximately 22% of our total assets were foreign assets (including our investments in CLO Funds, which are typically domiciled outside the U.S.). 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 U.S. Securities and Exchange Commission (the "Commission" or 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 March 31, 2011, our ten largest portfolio companies represented approximately 64% of the total fair value of our investments. Our largest investment, Katonah Debt Advisors which is our wholly-owned portfolio company, represented 16% of the total fair value of our investments. Excluding Katonah Debt Advisors and CLO Fund securities, our ten largest portfolio companies represent approximately 27% of the total fair value of our investments.

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 March 31, 2011, we had approximately \$56 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 March 31, 2011 and December 31, 2010 are as follows:

CLO Fund Securities	Investment	% ¹	March 31, 2011 (unaudited)		December 31, 2010	
			Cost	Fair Value	Cost	Fair Value
Grant Grove CLO, Ltd.	Subordinated Securities	22.2%	\$ 4,722,113	\$ 3,550,000	\$ 4,720,982	\$ 3,150,000
Katonah III, Ltd.	Preferred Shares	23.1	4,500,000	820,000	4,500,000	470,000
Katonah IV, Ltd.	Preferred Shares	17.1	3,150,000	1,890,000	3,150,000	1,300,000
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	2,470,000	4,500,000	2,090,000
Katonah VIII CLO Ltd. ²	Subordinated Securities	10.3	3,400,000	2,190,000	3,400,000	1,690,000
Katonah IX CLO Ltd. ²	Preferred Shares	6.9	2,000,000	1,400,000	2,000,000	1,300,000
Katonah X CLO Ltd. ²	Subordinated Securities	33.3	11,617,246	9,480,000	11,612,676	8,820,000
Katonah 2007-1 CLO Ltd. ²	Preferred Shares	100.0	29,998,944	26,070,000	29,987,959	26,200,000
Katonah 2007-1 CLO Ltd. ²	Class B-2L Notes	100.0	1,092,286	8,110,000	1,088,582	8,010,000
Total			\$ 68,300,589	\$ 55,981,000	\$ 68,280,199	\$ 53,031,000

¹ Represents percentage of class held.

² An affiliate CLO Fund managed by Katonah Debt Advisors.

³ As of March 31, 2011, 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 unaudited table below summarizes certain attributes of each CLO Fund as per their most recent trustee reports as of March 31, 2011:

CLO Fund Securities¹	Number of Securities	Number of Issuers	Number of Industries	Average Security Position Size	Average Issuer Position Size
Grant Grove CLO, Ltd.	279	220	33	\$ 1,007,755	\$ 1,278,016
Katonah III, Ltd.	187	110	29	1,661,372	2,824,333
Katonah IV, Ltd.	153	96	26	896,993	1,429,582
Katonah V, Ltd.	213	128	28	476,991	793,743
Katonah VII CLO Ltd.	240	183	32	1,318,551	1,729,247
Katonah VIII CLO Ltd.	262	198	32	1,355,977	1,794,273
Katonah IX CLO Ltd.	271	203	31	1,457,100	1,945,193
Katonah X CLO Ltd.	270	201	31	1,712,963	2,300,995
Katonah 2007-1 CLO Ltd.	238	185	31	1,228,992	1,581,081

¹ All data from most recent Trustee reports as of March 31, 2011.

In May 2009, we purchased the class B-2L notes of the Katonah 2007-1 CLO investment managed by Katonah Debt Advisors (“Katonah 2007-1 B-2L”). We 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 March 31, 2011 were approximately \$8 million, \$1 million, and \$7 million, respectively, and at December 31, 2010, the fair value, cost basis, and aggregate unrealized appreciation of the Katonah 2007-1 B-2L investment were \$8 million, \$1 million, and \$7 million, respectively. Both the B-2L notes and preferred shares of Katonah 2007-1 are owned 100% by us and Katonah 2007-1 is current in the payment of all quarterly distributions in respect of the B-2L notes and the preferred shares.

All CLO Funds managed by Katonah Debt Advisors are currently making quarterly dividend distributions to us and are paying all senior and subordinate management fees to Katonah Debt Advisors. With the exception of the Katonah V, Ltd. CLO Fund, all third-party managed CLO Funds held as investments are making quarterly dividend distributions to us.

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 March 31, 2011, Katonah Debt Advisors had approximately \$1.9 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 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.

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.

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 three months ended March 31, 2011 and for the year ended December 31, 2010 was as follows:

	<u>Debt Securities</u>	<u>CLO Fund Securities</u>	<u>Equity Securities</u>	<u>Affiliate Asset Managers</u>	<u>Total Portfolio</u>
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)
Decrease in fair value	9,196,912	3,974,850	(1,142,038)	(20,352,537)	(8,322,813)
Fair Value at December 31, 2010	91,042,928	53,031,000	4,688,832	41,493,000	190,255,758
Year to Date 2011 Activity:					
Purchases / originations / draws	17,424,281	—	2,858,387	—	20,282,668
Pay-downs / pay-offs / sales	(20,895,314)	—	(141,769)	(138,875)	(21,175,958)
Net accretion of discount	24,736	20,390	—	—	45,126
Net realized losses	(1,826,723)	—	—	—	(1,826,723)
Increase (decrease) in fair value	2,669,255	2,929,610	(16,985)	841,875	6,423,755
Fair Value at March 31, 2011	\$ 88,439,163	\$ 55,981,000	\$ 7,388,465	\$ 42,196,000	\$ 194,004,628

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 three months ended March 31, 2011 and 2010.

Investment Income

Investment income for the three months ended March 31, 2011 and 2010 was approximately \$7 million and \$7 million, respectively. Of these amounts, approximately \$2 million and \$5 million was attributable to interest income on our loan and bond investments, respectively. The decrease in interest income on our loan and bond portfolio is primarily due to reduced loan and bond investment balances as a result of the sale, prepayment and amortization of such investments since March 31, 2010. Rather than reinvest such proceeds, such proceeds were used primarily to fully repay, on January 31, 2011, the outstanding balance of our secured credit facility which had a balance of \$199 million at March 31, 2010. For the three months ended March 31, 2011 and 2010, approximately \$3 million and \$2 million of investment income is attributable to dividends earned on CLO equity investments, respectively. The increase in income attributable to dividends earned on CLO equity investments is due to the enhanced financial performance of such investments and their resultant distributions to us. At March 31, 2010, approximately 19% of our total CLO Fund securities at fair value made no distributions to us as compared to nearly 100% of total CLO Fund securities making distributions to us as of March 31, 2011.

For the three months ended March 31, 2011, we received a \$2 million cash settlement to settle litigation previously initiated by us against the lenders related to our secured credit facility which we fully repaid on January 31, 2011. Upon receipt, this settlement was recognized as other income during the three months ended March 31, 2011.

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 March 31, 2011, our investment in Katonah Debt Advisors was approximately \$42 million. For the three months ended March 31, 2011 and 2010, Katonah Debt Advisors had pre-tax net income before net capital losses of approximately \$450,000 and \$650,000, respectively. For the three months ended March 31, 2011 and 2010, Katonah Debt Advisors made no distributions of net income.

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

Total expenses for the three months ended March 31, 2011 and 2010 were approximately \$2 million and \$4 million, respectively. Interest expense and amortization on debt issuance costs for the period, which includes facility and program fees on the unused loan balance, were approximately \$297,000 and \$3 million, respectively, on average debt outstanding of \$36 million and \$203 million, respectively. Approximately \$841,000 and \$788,000, respectively, of expenses were attributable to employment compensation, including salaries, bonuses and stock option expense for the three months ended March 31, 2011 and 2010. For the three months ended March 31, 2011, other expenses included approximately \$1 million for professional fees, insurance, administrative and other. For the three months ended March 31, 2010, other expenses included approximately \$901,000 for professional fees, insurance, administrative and other. For the three months ended March 31, 2011 and 2010, administrative and other costs (including occupancy expense, insurance, technology and other office expenses) totaled approximately \$313,000 and \$290,000, respectively.

Interest and compensation expense are generally expected to be our largest expenses each period. Interest expense is dependent on the average outstanding principal balance on our borrowings and the related 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 generally paid annually.

Professional fee expenses for the three months ended March 31, 2011 are higher by approximately \$260,000 relative to the same prior year period primarily due to fees paid to a third party advisor for strategic analysis of debt and equity alternatives as well as increased accounting fees related to our recent issuance of Convertible Senior Notes. Such increase was offset, in part, by reduced legal fees.

Net Unrealized Appreciation on Investments

During the three months ended March 31, 2011 and 2010, our total investments had a change in net unrealized appreciation of approximately \$6.4 million, and a change in net unrealized appreciation of approximately \$1 million, respectively. For the three months ended March 31, 2011, Katonah Debt Advisors had a change in unrealized appreciation of approximately \$842,000 and our middle market portfolio of debt securities, equity securities and CLO Fund securities had a change in net unrealized appreciation of approximately \$4 million. For the three months ended March 31, 2010, Katonah Debt Advisors had a change in unrealized depreciation of \$5 million offset by a change in unrealized appreciation of approximately \$6 million on debt securities, equity securities and CLO Fund securities in our investment portfolio.

Net Increase (Decrease) in Stockholders' Equity Resulting From Operations

The net increase in stockholders' equity resulting from operations for the three months ended March 31, 2011 was approximately \$10 million, or an increase of \$0.42 per share. The net increase in stockholders' equity resulting from operations for the three months ended March 31, 2010 was approximately \$2 million, or \$0.07 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, if available), we also have the ability 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 March 31, 2011 and December 31, 2010 the fair value of investments and cash were as follows:

Security Type	Investments at Fair Value	
	March 31, 2011	December 31, 2010
Cash	\$ 70,747,215	\$ 10,175,488
Time Deposits	168,132	720,225
Money Market Accounts	169,858	210,311
Senior Secured Loan	23,276,764	22,001,256
Junior Secured Loan	60,010,630	63,944,003
Mezzanine Investment	250,000	250,000
Senior Subordinated Bond	4,528,209	4,490,709
CLO Fund Securities	55,981,000	53,031,000
Equity Securities	7,388,465	4,688,832
Preferred	373,560	—
Affiliate Asset Managers	42,196,000	41,493,000
Total	\$ 265,089,833	\$ 201,004,824

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 March 31, 2011, we had approximately \$60 million of outstanding borrowings and our asset coverage ratio of total assets to total borrowings was 428%, 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.

At December 31, 2010, we had approximately \$87 million of outstanding indebtedness through a secured credit facility. On January 31, 2011, we repaid in full the outstanding balance under this facility. On March 16, 2011, we issued \$55 million in aggregate principal amount of unsecured 8.75% convertible senior notes due 2016 (“Convertible Senior Notes”). On March 23, 2011, pursuant to an over-allotment option, we issued an additional \$5 million of such Convertible Senior Notes for a total of \$60 million in aggregate principal amount.

As of March 31, 2011, we had total outstanding indebtedness of \$60 million at a fixed rate of interest of 8.75%. As of March 31, 2011, we had cash and time deposits of approximately \$71 million which will fund future investments and operational needs.

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. As a result, we may seek to enter into new agreements 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 preferred securities or debt guaranteed by the Small Business Administration. 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.

COMMITMENTS AND 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 our 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 both March 31, 2011 and December 31, 2010, 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 had been funded as of March 31, 2011 and \$1 million had been funded as of December 31, 2010. As of March 31, 2011 and December 31, 2010, we had committed to make no investments in delayed draw senior secured loans.

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 unaudited 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”) for interim financial information. Accordingly, they do not include all of the information and footnotes required for annual financial statements. The unaudited interim financial statements and notes thereto should be read in conjunction with the financial statements and notes thereto in the Company’s Form 10-K for the fiscal year ended December 31, 2010, as filed with the Commission.

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 March 31, 2011, four issuers representing 1% of our total investments at fair value were on non-accrual status. As of December 31, 2010, five issuers representing 4% 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

We record dividend income from our 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 we have 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 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.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

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 March 31, 2011, approximately 84% 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 March 31, 2011, we had \$60 million of borrowings outstanding at a fixed rate of 8.75%.

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 or lowering interest rates, our current cost of debt would remain the same at 8.75% given that our debt is at a fixed rate. We would expect that an increase in the base rate index for our floating rate investment assets would increase our net investment income and that a decrease in the base rate index for such assets would decrease our net investment income (in either case, such increase/decrease may be limited by interest rate floors/minimums for certain investment assets).

We have analyzed the potential impact of changes in interest rates on interest income net of interest expense. Assuming that our balance sheet at March 31, 2011 were to remain constant and no actions were taken to alter the existing interest rate sensitivity, a hypothetical increase of a 1% change in interest rates would correspondingly increase net interest income proportionately by approximately \$2 million over a one-year period. Conversely, a hypothetical decrease of a 1% change in interest rates would correspondingly decrease net interest income proportionately by approximately \$629,000 over a one-year period.

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 March 31, 2011.

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.

In 2010, we engaged VRC, an independent valuation firm, to provide a third-party review of 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 4 Controls and Procedures

Evaluation of Disclosure Controls and Procedures

As required by Rule 13a-15 under the Exchange Act, management has evaluated, with the participation of our Chief Executive Officer and Chief Financial Officer, the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Disclosure controls and procedures refer to controls and other procedures designed to ensure that information required to be disclosed in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding our required disclosure. In designing and evaluating our disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management was required to apply its judgment in evaluating and implementing possible controls and procedures.

The Company's management, under the supervision and with the participation of various members of management, including our Chief Executive Officer ("CEO") and our Chief Financial Officer ("CFO"), has evaluated the effectiveness of the design and operation of our 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, our CEO and CFO have concluded that our current disclosure controls and procedures are effective as of the end of the period covered by this report.

Changes in Internal Control Over Financial Reporting

Changes in Internal Control Over Financial Reporting

During the quarter ended March 31, 2011, the Company had no changes in its internal control over financial reporting.

PART II. Other Information

Item 1. Legal Proceedings

Class Actions against the Company and Certain Directors and Officers

The Company and certain directors and officers were 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. On March 21, 2011, the three putative class actions were consolidated. A consolidated complaint has not yet been filed. The Company believes that the above-mentioned suit is without merit and will defend it 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 scheduled the testimony of some and taken the testimony of other current and former Company employees. 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 1A. Risk Factors

Investing in our common stock involves a high degree of risk. Our Annual Report on Form 10-K for the year ended December 31, 2010 contains important risk factors that could cause our actual results to differ materially from our historical experience or our present expectations and projections. If any such risks (or any risks we face) occur, our business, financial condition and results of our operations could be materially adversely affected. In such case, the NAV and trading price of our common stock could decline, and you may lose all or part of your investment. Other than described below, there have been no material changes from the risk factors previously disclosed in Part I, "Item 1A. Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2010, which should be read together with the other risk factors and information disclosed elsewhere in this Quarterly Report on Form 10-Q and our other reports filed with the SEC.

The following disclosure replaces and supplements the risk factors titled "We may be exposed to additional risks associated with leverage" and "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" included in our Annual Report on Form 10-K for the year ended December 31, 2010:

We borrow money, which magnifies the potential for gain or loss on amounts invested and may increase the risk of investing with us.

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. We have issued senior securities, and in the future may borrow from, or issue additional senior securities (such as preferred or convertible securities or the senior debt securities) to, banks and other lenders and investors, including debt guaranteed by the Small Business Administration (“SBA”). 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. Lenders and holders of such senior securities have fixed dollar claims on our consolidated assets that are superior to the claims of our common stockholders or any preferred stockholders. Leverage is generally considered a speculative investment technique. If the value of our consolidated assets increases, then leveraging would cause the NAV per share of our common stock to increase more sharply than it would have had we not incurred leverage. Conversely, if the value of our consolidated assets decreases, leveraging would cause net asset value to decline more sharply than it otherwise would have had we not incurred leverage. Similarly, any increase in our consolidated income in excess of consolidated interest payable on our outstanding indebtedness would cause our net income to increase more than it would have had we not incurred leverage, while any decrease in our consolidated income would cause net income to decline more sharply than it would have had we not incurred leverage. Such a decline could negatively affect our ability to make common stock dividend payments. There can be no assurance that our leveraging strategy will be successful.

As of March 31, 2011, we had \$60 million in aggregate principal amount of our 8.75% convertible senior notes due 2016 outstanding. We may incur additional indebtedness in the future, although there can be no assurance that we will be successful in doing so. Our ability to service our debt depends largely on our financial performance and is subject to prevailing economic conditions and competitive pressures. The amount of leverage that we employ at any particular time will depend on our management’s and our Board of Directors’ assessment of market and other factors at the time of any proposed borrowing.

Our convertible senior notes impose, and additional debt we may incur in the future will likely impose, financial and operating covenants that restrict our business activities, including limitations that could hinder our ability to finance additional loans and investments or to make the distributions required to maintain our status as a RIC. A failure to add new debt facilities or issue additional debt securities or other evidences of indebtedness in lieu of or in addition to existing indebtedness could have a material adverse effect on our business, financial condition or results of operations.

The following table illustrates the effect on return to a holder of our common stock of the leverage created by our use of borrowing at the convertible senior notes interest rate of 8.75% as of March 31, 2011, together with (a) total value of our net assets of \$197.2 million as of March 31, 2011, (b) \$60 million of principal indebtedness outstanding as of March 31, 2011 and (c) hypothetical annual returns on our portfolio of minus 15% to plus 15%.

Assumed Return on Portfolio (Net of Expenses)(1)	-15%	-10%	-5%	0%	5%	10%	15%
Corresponding Return to Common Stockholders(2)	-23%	-16%	-10%	-3%	4%	11%	18%

(1) The assumed portfolio return is required by SEC rules and is not a prediction of, and does not represent, our projected or actual performance. The table also assumes that we will maintain a constant level of leverage. The amount of leverage that we use will vary from time to time. Actual returns may be greater or smaller than those appearing in the table.

(2) In order to compute the “Corresponding Return to Common Stockholders,” the “Assumed Return on Portfolio” is multiplied by the total value of our assets of \$197.2 million at March 31, 2011 to obtain an assumed return to us. From this amount, the interest expense (calculated by multiplying the convertible senior notes interest rate of 8.75% as of March 31, 2011 by the \$60 million of principal indebtedness outstanding as of March 31, 2011) is subtracted to determine the return available to stockholders. The return available to stockholders is then divided by the total value of our net assets as of March 31, 2011 to determine the “Corresponding Return to Common Stockholders.”

Our indebtedness could adversely affect our financial health and our ability to respond to changes in our business.

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. As of March 31, 2011, our asset coverage ratio was 428%. The amount of leverage that we employ in the future 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. As a result of the level of our leverage:

- there is a likelihood of greater volatility of NAV and market price of our common stock than without leverage;
- our exposure to risk of loss is greater if we incur debt or issue senior securities to finance investments because a decrease in the value of our investments has a greater negative impact on our returns and, therefore, the value of our common stock than if we did not use leverage;
- the decrease in our asset coverage ratio resulting from increased leverage and the covenants contained in documents governing our indebtedness (which may impose asset coverage or investment portfolio composition requirements that are more stringent than those imposed by the 1940 Act) limit our flexibility in planning for, or reacting to, changes in our business and industry, as a result of which we could be required to liquidate investments at an inopportune time;
- we are required to dedicate a portion of our cash flow to interest payments, limiting the availability of cash for dividends and other purposes; and
- our ability to obtain additional financing in the future may be impaired.

If we have to sell assets at a loss to redeem or pay interest on our outstanding indebtedness or for other reasons, our NAV will be reduced and may not fully recover. We cannot be sure that our leverage will not have a material adverse effect on us. In addition, we cannot be sure that additional financing will be available when required or, if available, will be on terms satisfactory to us. Further, even if we are able to obtain additional financing, we may be required to use some or all of the proceeds thereof to repay our outstanding indebtedness.

Our stockholders may experience dilution upon the conversion of our convertible senior notes.

Our 8.75% convertible senior notes due 2016 are convertible into shares of our common stock at any time prior to the end of business on the business day preceding the maturity date. Upon conversion, we will satisfy our conversion obligation by issuing shares of our common stock to the converting holder and, under certain limited circumstances, may elect to deliver cash in lieu of shares otherwise deliverable upon conversion to comply with certain listing standards of The NASDAQ Global Select Market. The current conversion price of the convertible senior is approximately 118.5255 shares of our common stock per \$1,000 principal amount of the convertible senior notes, equivalent to a conversion price of approximately \$8.437 per share of our common stock. Our stockholders will experience dilution in their ownership percentage of common stock upon our issuance of common stock on any conversion of the convertible senior notes and any dividends paid on our common stock will also be paid on shares issued on any conversion.

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

On March 16, 2011, the Company issued \$55 million in aggregate principal amount of unsecured 8.75% convertible senior notes due 2016 (“Convertible Senior Notes”). On March 23, 2011, pursuant to an over-allotment option, the Company issued an additional \$5 million of such Convertible Senior Notes for a total of \$60 million in aggregate principal amount. Kohlberg Capital offered and sold the Convertible Senior Notes to JMP Securities LLC, as initial purchaser, in reliance on the exemption from registration provided by Section 4(2) of the Securities Act of 1933, as amended (the “Securities Act”), for resale by the initial purchaser to qualified institutional buyers (as defined in the Securities Act) pursuant to the exemption from registration provided by Rule 144A under the Securities Act.

Item 3. *Defaults Upon Senior Securities*

None.

Item 4. *[Removed and Reserved]*

None.

Item 5. *Other Information*

None.

Item 6. Exhibits

Exhibit Number	Description of Document
4.1	Indenture dated as of March 16, 2011, by and between Kohlberg Capital Corporation and U.S. Bank National Association, as trustee (incorporated by reference to Exhibit 4.1 of the Current Report on Form 8-K, as filed on March 16, 2011 (File No. 814-00735)).
4.2	Form of 8.75% Convertible Senior Note Due 2016 (included as part of Exhibit 4.1).
31.1*	Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certification of Chief Executive Officer Pursuant to 18 U. S. C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2*	Certification of Chief Financial Officer Pursuant to 18 U. S. C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

* Submitted herewith.

SIGNATURES

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

KOHLBERG CAPITAL CORPORATION

Date: May 6, 2011

By

/s/ Dayl W. Pearson

Dayl W. Pearson
President and Chief Executive Officer
(Principal Executive Officer)

Date: May 6, 2011

By

/s/ Michael I. Wirth

Michael I. Wirth
Chief Financial Officer, Chief Compliance Officer, Secretary and
Treasurer
(Principal Financial and Accounting Officer)

* * * * *

Exhibit Index

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32.2*	Certification of Chief Financial Officer Pursuant to 18 U. S. C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

* Submitted herewith.

**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 Quarterly Report on Form 10-Q for the quarter ended March 31, 2011 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 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 fiscal 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: May 6, 2011

By: _____ / S / MICHAEL I. WIRTH

Michael I. Wirth
Chief Financial Officer and Chief Compliance Officer
(Principal 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**

In connection with the accompanying Quarterly Report of Kohlberg Capital Corporation (the "Company") on Form 10-Q for the quarter ended March 31, 2011 (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: May 6, 2011

By:

/ S / DAYL W. PEARSON

Dayl W. Pearson
President and Chief Executive Officer
(Principal 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**

In connection with the accompanying Quarterly Report of Kohlberg Capital Corporation (the "Company") on Form 10-Q for the quarter ended March 31, 2011 (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: May 6, 2011

By:

/ S / MICHAEL I. WIRTH

Michael I. Wirth
Chief Financial Officer and Chief Compliance Officer
(Principal Financial Officer)
