

PROSPECT CAPITAL CORP
Form 497
April 06, 2011

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**Filed Pursuant to Rule 497(c)
Registration No. 333-170724**

**PROSPECTUS SUPPLEMENT
(To Prospectus dated March 16, 2011)**

9,000,000 Shares

Common Stock

Prospect Capital Corporation is a financial services company that lends to and invests in middle market, privately-held companies. We are organized as an externally-managed, non-diversified closed-end management investment company that has elected to be treated as a business development company under the Investment Company Act of 1940. Prospect Capital Management LLC manages our investments and Prospect Administration LLC provides the administrative services necessary for us to operate.

The underwriter has agreed to purchase our common stock at a price of \$11.40 per share, which will result in \$102,400,000 of net proceeds, after deducting estimated offering expenses, to us, or \$117,790,000 assuming full exercise of the underwriter's option to purchase additional shares.

The underwriter has an option for a period of 30 days from the date of this prospectus supplement to purchase up to 1,350,000 additional shares of our common stock at \$11.40 per share.

The underwriter proposes to offer the shares of common stock from time to time for sale in negotiated transactions or otherwise, at market prices prevailing at the time of sale, at prices related to such prevailing market prices or at negotiated prices. See "Underwriting" beginning on page S-15 of this prospectus supplement for more information regarding this offering.

Our common stock is traded on the NASDAQ Global Select Market under the symbol "PSEC". The last reported closing sales price for our common stock on April 4, 2011 was \$12.15 per share and our most recently determined net asset value per share was \$10.25 as of December 31, 2010 (\$9.95 on an as adjusted basis solely to give effect to our distributions with record dates of January 31, 2011, February 28, 2011 and March 31, 2011 and our issuance of common stock on January 31, 2011, February 28, 2011 and March 31, 2011 in connection with our dividend reinvestment plan).

This prospectus supplement and the accompanying prospectus contain important information you should know before investing in our securities. Please read it before you invest and keep it for future reference. We file annual, quarterly and current reports, proxy statements and other information about us with the Securities and Exchange Commission, or the "SEC". This information is available free of charge by

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contacting us at 10 East 40th Street, 44th Floor, New York, NY 10016 or by telephone at (212) 448-0702. The SEC maintains a website at www.sec.gov where such information is available without charge upon written or oral request. Our internet website address is www.prospectstreet.com. Information contained on our website is not incorporated by reference into this prospectus supplement or the accompanying prospectus and you should not consider information contained on our website to be part of this prospectus supplement or the accompanying prospectus.

Investing in our common stock involves risks. See "Risk Factors" beginning on page S-6 of this prospectus supplement and on page 9 of the accompanying prospectus.

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

Goldman, Sachs & Co.

Prospectus Supplement dated April 4, 2011

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FORWARD-LOOKING STATEMENTS

Our annual report on Form 10-K for the year ended June 30, 2010, any of our quarterly reports on Form 10-Q or current reports on Form 8-K, or any other oral or written statements made in press releases or otherwise by or on behalf of Prospect Capital Corporation, including this prospectus supplement and the accompanying prospectus, may contain forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, or the "1934 Act", which involve substantial risks and uncertainties. Forward-looking statements predict or describe our future operations, business plans, business and investment strategies and portfolio management and the performance of our investments and our investment management business. These forward-looking statements are not historical facts, but rather are based on current expectations, estimates and projections about our industry, our beliefs, and our assumptions. Words such as "intends", "intend", "intended", "goal", "estimate", "estimates", "expects", "expect", "expected", "project", "projected", "projections", "plans", "seeks", "anticipates", "anticipated", "should", "could", "may", "will", "designed to", "foreseeable future", "believe", "believes" and "scheduled" and variations of these words and similar expressions are intended to identify forward-looking statements. Our actual results or outcomes may differ materially from those anticipated. Readers are cautioned not to place undue reliance on these forward looking statements, which speak only as of the date the statement was made. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. These statements are not guarantees of future performance and are subject to risks, uncertainties, and other factors, some of which are beyond our control and difficult to predict and could cause actual results to differ materially from those expressed or forecasted in the forward-looking statements, including without limitation:

our future operating results,

our business prospects and the prospects of our portfolio companies,

the impact of investments that we expect to make,

our contractual arrangements and relationships with third parties,

the dependence of our future success on the general economy and its impact on the industries in which we invest,

the ability of our portfolio companies to achieve their objectives,

difficulty in obtaining financing or raising capital, especially in the current credit and equity environment,

the level and volatility of prevailing interest rates and credit spreads, magnified by the current turmoil in the credit markets,

adverse developments in the availability of desirable loan and investment opportunities whether they are due to competition, regulation or otherwise,

a compression of the yield on our investments and the cost of our liabilities, as well as the level of leverage available to us,

our regulatory structure and tax treatment, including our ability to operate as a business development company and a regulated investment company,

the adequacy of our cash resources and working capital,

the timing of cash flows, if any, from the operations of our portfolio companies,

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

authoritative generally accepted accounting principles or policy changes from such standard-setting bodies as the Financial Accounting Standards Board, the Securities and Exchange Commission, Internal Revenue Service, the NASDAQ Global Select Market, and other authorities that we are subject to, as well as their counterparts in any foreign jurisdictions where we might do business, and

the risks, uncertainties and other factors we identify in "Risk Factors" and elsewhere in this prospectus supplement and the accompanying prospectus and in our filings with the SEC.

Although we believe that the assumptions on which these forward-looking statements are based are reasonable, any of those assumptions could prove to be inaccurate, and as a result, the forward-looking statements based on those assumptions also could be inaccurate. Important assumptions include our ability to originate new loans and investments, certain margins and levels of profitability and the availability of additional capital. In light of these and other uncertainties, the inclusion of a projection or forward-looking statement in this prospectus supplement and the accompanying prospectus, respectively, should not be regarded as a representation by us that our plans and objectives will be achieved. These risks and uncertainties include those described or identified in "Risk Factors" and elsewhere in this prospectus supplement and the accompanying prospectus, respectively. You should not place undue reliance on these forward-looking statements, which apply only as of the date of this prospectus supplement or the accompanying prospectus, as applicable. These forward-looking statements do not meet the safe harbor for forward-looking statements pursuant to Section 27A of the Securities Act of 1933, as amended, or the "1933 Act".

You should rely only on the information contained in this prospectus supplement and the accompanying prospectus. We have not, and the underwriter has not, authorized any other person to provide you with information that is different from that contained in this prospectus supplement or the accompanying prospectus. If anyone provides you with different or inconsistent information, you should not rely on it. We are not, and the underwriter is not, making an offer of these securities in any jurisdiction where the offer is not permitted. You should assume that the information appearing in this prospectus supplement and the accompanying prospectus is accurate only as of their respective dates. Our business, financial condition and results of operations may have changed since those dates. This prospectus supplement supersedes the accompanying prospectus to the extent it contains information that is different from or in addition to the information in that prospectus.

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PROSPECTUS SUMMARY

This summary highlights some information from this prospectus supplement and the accompanying prospectus, and it may not contain all of the information that is important to you. To understand the terms of the common stock offered hereby, you should read this prospectus supplement and the accompanying prospectus carefully. Together, these documents describe the specific terms of the shares of common stock we are offering. You should carefully read the sections titled "Risk Factors" in this prospectus supplement and in the accompanying prospectus and the documents identified in the section "Available Information".

The terms "we", "us", "our" and "Company", refer to Prospect Capital Corporation; "Prospect Capital Management", "Investment Advisor" and "PCM" refer to Prospect Capital Management LLC; and "Prospect Administration" and the "Administrator" refer to Prospect Administration LLC.

The Company

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

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

We seek to maximize total returns to our investors, including both current yield and equity upside, by applying rigorous credit analysis and asset-based and cash-flow based lending techniques to make and monitor our investments. Many of our investments to date have been in energy-related industries. We have made no investments to date in the real estate or mortgage industries, and we do not intend currently to focus on such investments.

We are currently pursuing multiple investment opportunities, including purchases of portfolios from private and public companies, as well as originations and secondary purchases of particular securities. There can be no assurance that we will successfully consummate any investment opportunity we are currently pursuing. Motivated sellers, including commercial finance companies, hedge funds, other business development companies, total return swap counterparties, banks, collateralized loan obligation funds, and other entities, are suffering from excess leverage, and we believe we are well positioned to capitalize as potential buyers of such assets at attractive prices. If any of these opportunities are consummated, there can be no assurance that investors will share our view of valuation or that any assets acquired will not be subject to future write downs, each of which could have an adverse effect on our stock price.

As of December 31, 2010, we held investments in 58 portfolio companies. The aggregate fair value as of December 31, 2010 of investments in these portfolio companies held on that date is approximately \$918 million. Our portfolio across all our long-term debt and certain equity investments had an annualized current yield of 14.1% as of December 31, 2010. The yield includes interest as well as dividends.

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Recent Developments

On March 18, 2011, we provided a \$60 million first-lien senior secured credit facility for Safe-Guard Products International, LLC ("Safe-Guard"), the leading third-party administrator of ancillary finance and insurance ("F&I") products and services for new, used, and leased motor vehicles.

On March 31, 2011, we provided a \$58.0 million first-lien senior secured credit facility to support the acquisition of a cargo handling company ("Cargo Company") by a leading private investment firm. The Cargo Company is a leading provider of outsourced cargo handling and warehousing solutions to global air cargo carriers at key international gateway airports in North America.

On March 31, 2011, we received \$7.7 million in settlement of our outstanding loans to KTPS Holdings, LLC, a discount from the amortized cost, and we recorded a realized loss of \$0.5 million on the settlement.

On March 31, 2011, we provided a net \$32 million in first-lien senior secured financing for the recapitalization of an existing Prospect portfolio company focused on the consumer credit information sector and controlled by an affiliate of H.I.G. Capital, LLC ("H.I.G."), a leading global private investment firm.

On March 31, 2011, we issued 76,253 shares of our common stock in connection with our dividend reinvestment plan.

On April 4, 2011, we updated our estimate of net investment income for the third fiscal quarter ended March 31, 2011 to \$0.25 to \$0.27 per share.

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The Offering

Common stock offered by us, excluding underwriter's over-allotment option	9,000,000 shares.
Common stock outstanding prior to this offering	88,358,811 shares.
Common stock outstanding after this offering, excluding the underwriter's over-allotment option	97,358,811 shares.
Use of proceeds	We expect to use the net proceeds from this offering initially to maintain balance sheet liquidity, involving repayment of debt under our credit facility, investments in high quality short-term debt instruments or a combination thereof, and thereafter to make long-term investments in accordance with our investment objective. See "Use of Proceeds" in this prospectus supplement.
The NASDAQ Global Select Market symbol	PSEC
Risk factors	See "Risk Factors" in this prospectus supplement and the accompanying prospectus and other information in this prospectus supplement and the accompanying prospectus for a discussion of factors you should carefully consider before you decide whether to make an investment in shares of our common stock.
Current distribution rate	<p>On February 9, 2011, we announced that our Board of Directors declared monthly distributions in the following amounts and with the following record and payment dates:</p> <p>\$0.101150 per share for February 2011 to holders of record on February 28, 2011 with a payment date of March 31, 2011;</p> <p>\$0.101175 per share for March 2011 to holders of record on March 31, 2011 with a payment date of April 29, 2011; and</p> <p>\$0.101200 per share for April 2011 to holders of record on April 29, 2011 with a payment date of May 31, 2011,</p> <p>representing an annualized distribution yield (based on the March 2011 distribution) of approximately 9.99% based on our April 4, 2011 closing stock price of \$12.15 per share. Such distributions are expected to be payable out of earnings. Our distribution levels are subject to change or discontinuance at any time in the discretion of our Board of Directors. Our future earnings and operating cash flow may not be sufficient to support a dividend.</p>

Table of Contents***Fees and Expenses***

The following tables are intended to assist you in understanding the costs and expenses that an investor in this offering will bear directly or indirectly. We caution you that some of the percentages indicated in the table below are estimates and may vary. In these tables, we assume that we have borrowed \$285 million under our credit facility, which is the maximum amount available under the credit facility. Except where the context suggests otherwise, whenever this prospectus contains a reference to fees or expenses paid by "you" or "us" or that "we" will pay fees or expenses, the Company will pay such fees and expenses out of our net assets and, consequently, you will indirectly bear such fees or expenses as an investor in the Company. However, you will not be required to deliver any money or otherwise bear personal liability or responsibility for such fees or expenses.

Stockholder transaction expenses:

Sales load (as a percentage of offering price)(1)	6.17%
Offering expenses borne by us (as a percentage of offering price)(2)	0.18%
Dividend reinvestment plan expenses(3)	None
Total stockholder transaction expenses (as a percentage of offering price)(4)	6.35%
Annual expenses (as a percentage of net assets attributable to common stock)(4):	
Management Fees(5)	3.40%
Incentive fees payable under Investment Advisory Agreement (20% of realized capital gains and 20% of pre-incentive fee net investment income)(6)	2.22%
Interest payments on the credit facility	1.34%
Interest payments on the 2010 Notes	1.04%(7)
Interest payments on the 2011 Notes	1.05%(8)
Acquired Fund Fees and Expenses	0.01%(9)
Other expenses	1.51%(10)
Total annual expenses	10.57%(6)(10)

Example

The following table demonstrates the projected dollar amount of cumulative expenses we would pay out of net assets and that you would indirectly bear over various periods with respect to a hypothetical investment in our common stock. In calculating the following expense amounts, we have assumed we would have borrowed all \$285 million available under our line of credit, that our annual operating expenses would remain at the levels set forth in the table above and that we would pay the costs shown in the table above.

	1 Year	3 Years	5 Years	10 Years
You would pay the following expenses on a \$1,000 investment, assuming a 5% annual return	\$ 131.91	\$ 263.94	\$ 389.97	\$ 680.54

While the example assumes, as required by the SEC, a 5% annual return, our performance will vary and may result in a return greater or less than 5%. The income incentive fee under our Investment Advisory Agreement with Prospect Capital Management is unlikely to be material assuming a 5% annual return and is not included in the example. If we achieve sufficient returns on our investments, including through the realization of capital gains, to trigger an incentive fee of a material amount, our distributions to our common stockholders and our expenses would likely be higher. In addition, while the example assumes reinvestment of all dividends and other distributions at net asset value, or NAV, participants in our dividend reinvestment plan will receive a number of shares of our common stock determined by dividing the total dollar amount of the distribution payable to a participant by the market price per share of our common stock at the close of trading on the valuation date for the distribution. See "Dividend Reinvestment Plan" for additional information regarding our dividend reinvestment plan.

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This example and the expenses in the table above should not be considered a representation of our future expenses. Actual expenses (including the cost of debt, if any, and other expenses) may be greater or less than those shown.

- (1) The sales load (underwriting discounts and commissions) with respect to our common stock sold in this offering, which is a one time fee, is the only sales load paid in connection with this offering. For the purpose of calculating sales load, we assume the underwriter will sell to the public at a stock price of \$12.15, our closing stock price on April 4, 2011.
- (2) The offering expenses of this offering are estimated to be approximately \$200,000.
- (3) The expenses of the dividend reinvestment plan are included in "other expenses".
- (4) The related prospectus supplement will disclose the offering price and the total stockholder transaction expenses as a percentage of the offering price.
- (5) Our base management fee is 2% of our gross assets (which include any amount borrowed, i.e., total assets without deduction for any liabilities). Although no plans are in place to borrow the full amount under our line of credit, assuming that we borrowed \$285 million, the 2% management fee of gross assets equals approximately 3.40% of net assets. See "Business Management Services Investment Advisory Agreement" in the accompanying prospectus and footnote 6 below.
- (6) Based on an annualized level of incentive fee paid during our second fiscal quarter ended December 31, 2010, all of which consisted of an income incentive fee. For a more detailed discussion of the calculation of the two-part incentive fee, see "Management Services Investment Advisory Agreement" in the accompanying prospectus.
- (7) On December 21, 2010, the Company issued \$150 million in aggregate principal amount of 6.25% Convertible Senior Notes due 2015, which we refer to as the 2010 Notes. See "Business General" and "Risk Factors Risks Related to our Business" in the accompanying prospectus for more detail on the 2010 Notes.
- (8) On February 18, 2011, the Company issued \$172.5 million in aggregate principal amount of 5.5% Convertible Senior Notes due 2016, which we refer to as the 2011 Notes. See "Business General" and "Risk Factors Risks Related to our Business" in the accompanying prospectus for more detail on the 2011 Notes. The 2011 Notes and the 2010 Notes are referred to collectively as the Notes.
- (9) The Company's stockholders indirectly bear the expenses of underlying investment companies in which the Company invests. This amount includes the fees and expenses of investment companies in which the Company is invested in as of December 31, 2010. When applicable, fees and expenses are based on historic fees and expenses for the investment companies and for those investment companies with little or no operating history, fees and expenses are based on expected fees and expenses stated in the investment companies' prospectus or other similar communication without giving effect to any performance. Future fees and expenses for certain investment companies may be substantially higher or lower because certain fees and expenses are based on the performance of the investment companies, which may fluctuate over time. The amount of the Company's average net assets used in calculating this percentage was based on net assets of approximately \$903 million as of December 31, 2010.
- (10) "Other expenses" are based on estimated amounts for the current fiscal year. The amount shown above represents annualized expenses during our three months ended December 31, 2010 representing all of our estimated recurring operating expenses (except fees and expenses reported in other items of this table) that are deducted from our operating income and reflected as expenses in our Statement of Operations. The estimate of our overhead expenses, including payments under an administration agreement with Prospect Administration, or the Administration Agreement, based on our projected allocable portion of overhead and other expenses incurred by Prospect Administration in performing its obligations under the Administration Agreement. "Other expenses" does not include non-recurring expenses. See "Business Management Services Administration Agreement" in the accompanying prospectus.

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RISK FACTORS

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

Recent developments may increase the risks associated with our business and an investment in us.

The U.S. financial markets have been experiencing a high level of volatility, disruption and distress, which was exacerbated by the failure of several major financial institutions in the last few months of 2008. Despite actions of the United States federal government, these events contributed to worsening general economic conditions that materially and adversely impacted the broader financial and credit markets and reduced the availability of debt and equity capital for the market as a whole and financial services firms in particular. Similar conditions have occurred in the financial markets and economies of numerous other countries. While these conditions appear to be improving, they could continue for a prolonged period of time or worsen in the future both in the U.S. and globally. These conditions have raised the level of many of the risks described in this prospectus supplement and in the accompanying prospectus and could have an adverse effect on our portfolio companies as well as on our business, financial condition, results of operations, dividend payments, credit facility, access to capital, valuation of our assets, including our NAV, and our stock price.

Our most recent NAV was calculated on December 31, 2010 and our NAV when calculated effective March 31, 2011 may be higher or lower.

Our most recently estimated NAV per share is \$9.95 on an as adjusted basis solely to give effect to our distributions with record dates of January 31, 2011, February 28, 2011 and March 31, 2011 and our issuance of common stock on January 31, 2011, February 28, 2011 and March 31, 2011 in connection with our dividend reinvestment plan versus \$10.25 determined by us as of December 31, 2010. NAV per share as of March 31, 2011, may be higher or lower than \$9.95 based on potential changes in valuations and earnings for the quarter then ended. Our Board of Directors has not yet determined the fair value of portfolio investments at any date subsequent to December 31, 2010. Our Board of Directors determines the fair value of our portfolio investments on a quarterly basis in connection with the preparation of quarterly financial statements and based on input from an independent valuation firm, our Investment Advisor and the audit committee of our Board of Directors.

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

We have obtained approval from our stockholders for us to be able to sell an unlimited number of shares of our common stock at any level of discount from NAV per share in certain circumstances during the one-year period ending on December 11, 2011 as described in the accompanying prospectus. The issuance or sale by us of shares of our common stock at a discount to net asset value poses a risk of dilution to our stockholders. In particular, stockholders who do not purchase additional shares of common stock at or below the discounted price in

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proportion to their current ownership will experience an immediate decrease in NAV per share (as well as in the aggregate NAV of their shares of common stock if they do not participate at all). These stockholders will also experience a disproportionately greater decrease in their participation in our earnings and assets and their voting power than the increase we experience in our assets, potential earning power and voting interests from such issuance or sale. In addition, such sales may adversely affect the price at which our common stock trades. For additional information about recent sales below NAV per share, see "Recent Sales of Common Stock Below Net Asset Value" in this prospectus supplement and for additional information and hypothetical examples of these risks, see "Sales of Common Stock Below Net Asset Value" in the accompanying prospectus.

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SUPPLEMENT TO MATERIAL U.S. FEDERAL INCOME TAXATION CONSIDERATIONS

The following summary of certain U.S. federal income tax considerations supplements the discussion set forth under the heading "Material U.S. Federal Income Tax Considerations Taxation Of Non-U.S. Stockholders" in the accompanying prospectus and is subject to the qualifications and assumptions set forth therein.

For our taxable years beginning before January 1, 2012, properly designated distributions to Non-U.S. Stockholders are generally exempt from U.S. federal withholding tax where they (i) are paid in respect of our "qualified net interest income" (generally, our U.S.-source interest income, other than certain contingent interest and interest from obligations of a corporation or partnership in which we are at least a 10% shareholder, reduced by expenses that are allocable to such income) or (ii) are paid in respect of our "qualified short-term capital gains" (generally, the excess of our net short-term capital gain over our long-term capital loss for such taxable year). Depending on the circumstances, however, we may designate all, some or none of our potentially eligible distributions as such qualified net interest income or as qualified short-term capital gains, and/or treat such distributions, in whole or in part, as ineligible for this exemption from withholding. In order to qualify for this exemption from withholding, a Non-U.S. Stockholder will need to comply with applicable certification requirements relating to its non-U.S. status (including, in general, furnishing an IRS Form W-8BEN or substitute Form). In the case of our shares held through an intermediary, the intermediary may withhold even if we designate the payment as qualified net interest income or qualified short-term capital gain. Non-U.S. Stockholders should contact their intermediaries with respect to the application of these rules to their accounts. There can be no assurance as to what portion of our distributions will qualify for favorable treatment as qualified net interest income or qualified short-term capital gains.

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USE OF PROCEEDS

The net proceeds from the sale of 9,000,000 shares of our common stock in this offering will be \$102,400,000 (or \$117,790,000 if the over-allotment is exercised in full) after deducting offering expenses of approximately \$200,000 payable by us.

We expect to use the net proceeds from this offering initially to maintain balance sheet liquidity, involving repayment of debt under our credit facility, investments in high quality short-term debt instruments or a combination thereof, and thereafter to make long-term investments in accordance with our investment objective. We anticipate that substantially all of the net proceeds from this offering will be used for the above purposes within six months, depending on the availability of appropriate investment opportunities consistent with our investment objective and market conditions.

As of April 4, 2011, we had \$22.5 million outstanding under our credit facility and, based on the assets currently pledged as collateral on the facility, an additional approximately \$204.7 million was available to us for borrowing under our credit facility. Interest on borrowings under the credit facility is one-month LIBOR plus 325 basis points, subject to a minimum Libor floor of 100 basis points. Additionally, the lenders charge a fee on the unused portion of the credit facility equal to either 75 basis points if at least half of the credit facility is used or 100 basis points otherwise.

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The following table sets forth our capitalization as of December 31, 2010:

on an actual basis;

on an as adjusted basis giving effect to our distributions with record dates of January 31, 2011, February 28, 2011 and March 31, 2011 and our issuance of 84,155, 83,021 and 76,253 shares of our common stock in connection with our dividend reinvestment plan on January 31, 2011, February 28, 2011 and March 31, 2011, respectively, and the sale of the \$172.5 million of 5.50% Senior Convertible Notes due 2016 and borrowings on our credit facility; and

on an as further adjusted basis giving effect to the transactions noted above and the assumed sale of 9,000,000 shares of our common stock at a price of \$12.15 per share (the last reported sale price per share of our common stock on the NASDAQ Global Select Market on April 4, 2011) less commissions and expenses.

This table should be read in conjunction with "Use of Proceeds" and our "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our financial statements and notes thereto included in this prospectus supplement and the accompanying prospectus. The adjusted information is illustrative only; our capitalization following the completion of this offering is subject to adjustment based on the actual public offering price of our common stock and the actual number of shares of common stock we sell in this offering, both of which will be determined at pricing.

	As of December 31, 2010		
	As Adjusted for		As Further
	Actual	Stock Issuances and Borrowings After December 31, 2010	Adjusted for this Offering(2)
	(In thousands, except shares and per share data)		
	(Unaudited)		
Long-term debt, including current maturities:			
Borrowings under senior credit facility(1)	\$	\$	22,500
2010 Notes	150,000	150,000	150,000
2011 Notes	N/A	172,500	172,500
Amount owed to affiliates	10,104	10,104	10,104
Total long-term debt	160,104	355,104	355,104
Stockholders' equity:			
Common stock, par value \$0.001 per share (200,000,000 common shares authorized; 88,115,382 shares outstanding actual, 88,358,811 shares outstanding as adjusted for stock issuances in connection with our dividend reinvestment plan and 97,358,811 shares outstanding as further adjusted for this offering)	88	88	97
Paid-in capital in excess of par value	988,897	964,996	1,067,387
Distributions in excess of net investment income	(18,369)	(18,369)	(18,369)

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Accumulated realized losses on investments	(99,579)	(99,579)	(99,579)
Net unrealized appreciation on investments	32,153	32,153	32,153
Total stockholders' equity	903,190	879,289	981,689
Total capitalization	\$1,063,294	\$ 1,234,393	\$ 1,336,793

-
- (1) As of December 31, 2010, we had no borrowings outstanding under our recently completed extended credit facility. As of April 4, 2011, we had \$22.5 million of borrowings under our credit facility, representing a \$22.5 million increase in borrowing subsequent to December 31, 2010.
- (2) The As Further Adjusted for this Offering calculations exclude any exercise of the underwriter's over-allotment option.

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Table of Contents**RECENT SALES OF COMMON STOCK BELOW NET ASSET VALUE**

At our 2008, 2009 and 2010 annual meeting of stockholders, our stockholders approved our ability to sell an unlimited number of shares of our common stock at any level of discount to NAV per share during the twelve-month period following such approval. Accordingly, we may make offerings of our common stock without any limitation on the total amount of dilution to stockholders. See "Sales of Common Stock Below Net Asset Value" in this prospectus supplement and in the accompanying prospectus. Pursuant to this authority and the approval of our Board of Directors, we have made the following offerings:

Date of Offering	Price Per Share to Investors	Shares Issued	Estimated Net Asset Value per Share (1)	Percentage Dilution
March 18, 2009	\$8.20	1,500,000	\$14.43	2.20%
April 22, 2009	\$7.75	3,680,000	\$14.15	5.05%
May 19, 2009	\$8.25	7,762,500	\$13.44	7.59%
July 7, 2009	\$9.00	5,175,000	\$12.40	3.37%
August 20, 2009	\$8.50	3,449,686	\$11.57	1.78%
September 24, 2009	\$9.00	2,807,111	\$11.36	1.20%
June 21, 2010 to June 25, 2010(2)	\$10.01-\$10.67	1,072,500	\$10.39-10.40	0.06%
June 28, 2010 to July 16, 2010(3)	\$9.47-\$10.04	2,748,600	\$10.31-10.34	0.29%
July 19, 2010 to August 19, 2010(4)	\$9.28-\$10.04	3,814,528	\$10.26-10.36	0.39%
September 7, 2010 to September 23, 2010(5)	\$9.47-\$9.98	2,185,472	\$10.22-10.25	0.18%
September 24, 2010 to September 27, 2010(6)	\$9.74-\$9.92	302,400	\$10.25-10.26	0.02%
September 28, 2010 to October 29, 2010(7)	\$9.65-\$10.09	4,929,556	\$10.13-10.27	0.32%
November 11, 2010 to December 10, 2010(8)	\$9.70-\$10.54	4,513,920	\$10.18-10.28	0.22%

- (1) The data for sales of shares below NAV pursuant to our previous equity distribution agreements are an estimate based on the last reported NAV adjusted and capital events occurring during the period since the last calculated NAV. All amounts presented are approximations based on the best available data at the time of issuance. Overall, the dilution from the issuance of shares below NAV in connection with the at-the-market program is estimated to be less than 1.5%.
- (2) Dates of offering represent the sales dates of the stock. The settlement dates are three business days later or June 24, 2010 to June 30, 2010.
- (3) Dates of offering represent the sales dates of the stock. The settlement dates are three business days later or July 1, 2010 to July 21, 2010.
- (4) Dates of offering represent the sales dates of the stock. The settlement dates are three business days later or July 22, 2010 to August 24, 2010.
- (5) Dates of offering represent the sales dates of the stock. The settlement dates are three business days later or September 10, 2010 to September 28, 2010.
- (6)

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Dates of offering represent the sales dates of the stock. The settlement dates are three business days later or September 29, 2010 to September 30, 2010.

(7)

Dates of offering represent the sales dates of the stock. The settlement dates are three business days later or October 1, 2010 to November 3, 2010.

(8)

Dates of offering represent the sales dates of the stock. The settlement dates are three business days later or November 16, 2010 to December 15, 2010.

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DISTRIBUTIONS AND PRICE RANGE OF COMMON STOCK

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

In order to maintain RIC tax treatment, we must distribute at least 90% of our ordinary income and realized net short-term capital gains in excess of realized net long-term capital losses, if any, out of the assets legally available for distribution. In order to avoid certain excise taxes imposed on RICs, we are required to distribute with respect to each calendar year by January 31 of the following year an amount at least equal to the sum of

98% of our ordinary income for the calendar year,

98.2% of our capital gains in excess of capital losses for the one-year period ending on October 31 of the calendar year, and

any ordinary income and net capital gains for preceding years that were not distributed during such years.

In December 2008, our Board of Directors elected to retain excess profits generated in the quarter ended September 30, 2008 and pay a 4% excise tax on such retained earnings. We paid \$533,000 for the excise tax with the filing of our tax return in March 2009. No such election was made in December 2009.

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

We maintain an "opt out" dividend reinvestment plan for our common stockholders. As a result, if we declare a dividend, then stockholders' cash dividends will be automatically reinvested in additional shares of our common stock, unless they specifically "opt out" of the dividend reinvestment plan so as to receive cash dividends. Stockholders who receive distributions in the form of stock are subject to the same U.S. Federal, state and local tax consequences as are stockholders who elect to receive their distributions in cash. See "Dividend Reinvestment Plan" in the accompanying prospectus. The tax consequences of distributions to stockholders are described in the accompanying prospectus under the label "Material U.S. Federal Income Tax Considerations". To the extent prudent and practicable, we intend to declare and pay dividends on a monthly basis.

With respect to the distributions paid to stockholders, income from origination, structuring, closing, commitment and other upfront fees associated with investments in portfolio companies were treated as taxable income and accordingly, distributed to stockholders. During the fiscal year ended June 30, 2009, we recorded total dividends of approximately \$56.1 million. For the fiscal year ended June 30, 2010, we recorded total distributions of approximately \$81.5 million. On June 18, 2010, we announced a change in dividend policy from quarterly to monthly dividends. For the first,

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second and third quarters of the fiscal year ending June 30, 2011, we recorded total distributions of approximately \$75.5 million.

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

Our common stock is quoted on the NASDAQ Global Select Market under the symbol "PSEC". The following table sets forth, for the periods indicated, our NAV per share of common stock and the high and low closing prices per share of our common stock as reported on the NASDAQ Global Select Market. Our common stock historically trades at prices both above and below its NAV per share. There can be no assurance, however, that such premium or discount, as applicable, to NAV per share will be maintained. Common stock of business development companies, like that of closed-end investment companies, frequently trades at a discount to current NAV per share. In the past, our common stock has traded at a discount to our NAV per share. The risk that our common stock may continue to trade at a discount to our NAV per share is separate and distinct from the risk that our NAV per share may decline.

	Stock Price			Premium (Discount) of High to NAV	Premium (Discount) of Low to NAV	Dividend Declared
	NAV(1)	High(2)	Low(2)			
Twelve Months Ending June 30, 2008						
First quarter	\$ 15.08	\$ 18.68	\$ 14.16	23.9%	(6.1)%	\$ 0.3925
Second quarter	14.58	17.17	11.22	17.8%	(23.0)%	0.395
Third quarter	14.15	16.00	13.55	13.1%	(4.2)%	0.400
Fourth quarter	14.55	16.12	13.18	10.8%	(9.4)%	0.40125
Twelve Months Ending June 30, 2009						
First quarter	\$ 14.63	\$ 14.24	\$ 11.12	(2.7)%	(24.0)%	\$ 0.4025
Second quarter	14.43	13.08	6.29	(9.4)%	(56.4)%	0.40375
Third quarter	14.19	12.89	6.38	(9.2)%	(55.0)%	0.405
Fourth quarter	12.40	10.48	7.95	(15.5)%	(35.9)%	0.40625
Twelve Months Ending June 30, 2010						
First quarter	\$ 11.11	\$ 10.99	\$ 8.82	(1.1)%	(20.6)%	\$ 0.4075
Second quarter	10.10	12.31	9.93	21.9%	(1.7)%	0.40875
Third quarter	10.12	13.20	10.45	30.4%	3.3%	0.410
Fourth quarter	10.30	12.20	9.65	18.4%	(6.3)%	0.10
Twelve Months Ending June 30, 2011						
First quarter	\$ 10.24	\$ 10.00	\$ 9.18	(2.3)%	(10.4)%	\$ 0.301375(5)
Second quarter	10.25	10.86	9.69	6.0%	(5.5)%	0.302625(5)
Third quarter	(3)(4)	12.33	10.72	(4)	(4)	(5)
Fourth quarter (to April 4, 2011)	(3)(4)	12.18	12.15	(4)	(4)	(5)

(1)

Net asset value per share is determined as of the last day in the relevant quarter and therefore may not reflect the net asset value per share on the date of the high or low sales price. The NAVs shown are based on outstanding shares of our common stock at the end of each period.

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- (2) The High/Low Stock Price is calculated as of the closing price on a given day in the applicable quarter.
- (3) Our most recently estimated NAV per share is \$9.95 on an as adjusted basis solely to give effect to our distributions with record dates of January 31, 2011, February 28, 2011 and March 31, 2011 and our issuance of common stock on January 31, 2011, February 28, 2011 and March 31, 2011 in connection with our dividend reinvestment plan versus \$10.25 determined by us as of December 31, 2010. NAV per share as of March 31, 2011, may be higher or lower than \$9.95 based on potential changes in valuations and earnings for the quarter then ended.
- (4) NAV has not yet been finally determined for any day after December 31, 2010.
- (5) In June 2010, we changed our distribution policy from a quarterly payment to a monthly payment.

In August 2010, we announced the declaration of two monthly distributions as follows:

\$0.100625 per share for September 2010 to holders of record on September 30, 2010 with a payment date of October 29, 2010; and

\$0.100750 per share for October 2010 to holders of record on October 24, 2010 with a payment date of November 30, 2010.

In November 2010, we announced the declaration of three additional monthly distributions as follows:

\$0.100875 per share for November 2010 to holders of record on November 30, 2010 with a payment date of December 31, 2010;

\$0.101000 per share for December 2010 to holders of record on December 31, 2010 with a payment date of January 31, 2011; and

\$0.101125 per share for January 2011 to holders of record on January 31, 2011 with a payment date of February 28, 2011.

In February 2011, we announced the declaration of three additional monthly distributions as follows:

\$0.101150 per share for February 2011 to holders of record on February 28, 2011 with a payment date of March 31, 2011;

\$0.101175 per share for March 2011 to holders of record on March 31, 2011 with a payment date of April 29, 2011; and

\$0.101200 per share for April 2011 to holders of record on April 29, 2011 with a payment date of May 31, 2011.

On April 4, 2011, the last reported sales price of our common stock was \$12.15 per share.

As of April 1, 2011, we had approximately 69 stockholders of record.

The below table sets forth each class of our outstanding securities as of April 4, 2011.

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Title of Class	Amount Authorized	Amount Held by Registrant or for its Account	Amount Outstanding
Common Stock	200,000,000	0	88,358,811

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UNDERWRITING

Under the terms and subject to the conditions contained in an underwriting agreement dated April 4, 2011, the Company has agreed to sell to Goldman, Sachs & Co., the sole underwriter, and Goldman, Sachs & Co. has agreed to purchase, 9,000,000 shares of common stock at a price of \$11.40 per share.

The underwriter has an option to buy up to 1,350,000 additional shares of common stock from the Company representing 15% of the aggregate offering amount at a price of \$11.40 per share. The underwriter has 30 days from the date of this prospectus supplement to exercise its option to purchase additional shares.

The underwriter proposes to offer the shares of common stock for sale from time to time in one or more transactions (which may include block transactions), in negotiated transactions or otherwise, or a combination of those methods of sale, at market prices prevailing at the time of sale, at prices related to prevailing market prices or at negotiated prices. The underwriter may do so by selling the shares of common stock to or through broker/dealers, who may receive compensation in the form of underwriting discounts, concessions or commissions from the underwriter and/or the purchasers of the shares of common stock for whom they may act as agents. In connection with the sale of the shares of common stock, the underwriter may be deemed to have received compensation in the form of underwriting discounts, and the underwriter may also receive commissions from the purchasers of the shares of common stock for whom they may act as agents. The underwriter and any broker/dealers that participate with the underwriter in the distribution of the shares of common stock may be deemed to be underwriters, and any discounts or commissions received by them and any profit on the resale of the shares of common stock by them may be deemed to be underwriting discounts or commissions.

The underwriting agreement provides that the underwriter is obligated to purchase all the shares of common stock if any are purchased, other than those covered by the option to purchase additional shares described above.

We estimate that the expenses for this offering payable by us will be approximately \$200,000.

We and each of our directors and executive officers have agreed, without the prior written consent of the underwriter not to, during the period ending 45 days following the date of the underwriting agreement, (i) offer, sell, contract to sell, pledge, grant any option to purchase, make any short sale or otherwise transfer or dispose of, directly or indirectly, or file with the Commission a registration statement relating to, any securities of the Company that are substantially similar to the common stock offered hereby, including but not limited to any options or warrants to purchase shares of common stock or any securities that are convertible into or exchangeable for, or that represent the right to receive, common stock or any such substantially similar securities, or publicly disclose the intention to make any offer, sale, pledge, disposition or filing or (ii) enter into any swap or other agreement that transfers, in whole or in part, any of the economic consequences of ownership of the common stock or any such other securities, whether any such transaction described in clause (i) or (ii) above is to be settled by delivery of common stock or such other securities, in cash or otherwise (other than shares of common stock to be sold hereunder or pursuant to employee stock option plans existing on, or upon the conversion or exchange of convertible or exchangeable securities outstanding as of, the date of the underwriting agreement).

We have agreed to indemnify the underwriter against certain liabilities, including liabilities under the Securities Act, and to contribute to payments that the underwriter may be required to make in that respect.

In connection with this offering, the underwriter may engage in stabilizing transactions, which involves making bids for, purchasing and selling shares of our common stock in the open market

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for the purpose of preventing or retarding a decline in the market price of our common stock while this offering is in progress. These stabilizing transactions may include making short sales of our common stock, which involves the sale by the underwriter of a greater number of shares of our common stock than they are required to purchase in this offering, and purchasing shares of our common stock on the open market to cover positions created by short sales. Short sales may be "covered" shorts, which are short positions in an amount not greater than the underwriter's option to purchase additional shares referred to above, or may be "naked" shorts, which are short positions in excess of that amount. The underwriter may close out any covered short position either by exercising its option to purchase additional shares, in whole or in part, or by purchasing shares in the open market. In making this determination, the underwriter will consider, among other things, the price of shares available for purchase in the open market compared to the price at which the underwriter may purchase shares through their option to purchase additional shares. A naked short position is more likely to be created if the underwriter is concerned that there may be downward pressure on the price of our common stock in the open market that could adversely affect investors who purchase in this offering. To the extent that the underwriter creates a naked short position, it will purchase shares in the open market to cover the position.

The underwriter has advised us that, pursuant to Regulation M of the Securities Act, it may also engage in other activities that stabilize, maintain or otherwise affect the price of our common stock. These activities may have the effect of raising or maintaining the market price of our common stock or preventing or retarding a decline in the market price of our common stock, and, as a result, the price of our common stock may be higher than the price that otherwise might exist in the open market. If the underwriter commences these activities, it may discontinue them at any time. The underwriter may carry out these transactions on the NASDAQ Global Select Market, in the over-the-counter market or otherwise.

Notice to Prospective Investors in the European Economic Area

In relation to each member state of the European Economic Area which has implemented the Prospectus Directive (each, a "Relevant Member State"), including each Relevant Member State that has implemented the 2010 PD Amending Directive with regard to persons to whom an offer of securities is addressed and the denomination per unit of the offer of securities (each, an "Early Implementing Member State"), with effect from and including the date on which the Prospectus Directive is implemented in that Relevant Member State (the "Relevant Implementation Date"), no offer of shares will be made to the public in that Relevant Member State (other than offers (the "Permitted Public Offers") where a prospectus will be published in relation to the shares that has been approved by the competent authority in a Relevant Member State or, where appropriate, approved in another Relevant Member State and notified to the competent authority in that Relevant Member State, all in accordance with the Prospectus Directive), except that with effect from and including that Relevant Implementation Date, offers of shares may be made to the public in that Relevant Member State at any time:

(1) to "qualified investors" as defined in the Prospectus Directive, including:

(a) in the case of Relevant Member States other than Early Implementing Member States), legal entities which are authorized or regulated to operate in the financial markets or, if not so authorized or regulated, whose corporate purpose is solely to invest in securities, or any legal entity which has two or more of (i) an average of at least 250 employees during the last financial year; (ii) a total balance sheet of more than €43.0 million and (iii) an annual turnover of more than €50.0 million as shown in its last annual or consolidated accounts; or

(b) (in the case of Early Implementing Member States), persons or entities that are described in points (1) to (4) of Section I of Annex II to Directive 2004/39/EC, and those who

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are treated on request as professional clients in accordance with Annex II to Directive 2004/39/EC, or recognized as eligible counterparties in accordance with Article 24 of Directive 2004/39/EC unless they have requested that they be treated as non-professional clients; or

(2) to fewer than 100 (or, in the case of Early Implementing Member States, 150) natural or legal persons (other than "qualified investors" as defined in the Prospectus Directive), as permitted in the Prospectus Directive, subject to obtaining the prior consent of the representatives for any such offer; or

(3) in any other circumstances falling within Article 3(2) of the Prospectus Directive, provided that no such offer of shares shall result in a requirement for the publication of a prospectus pursuant to Article 3 of the Prospectus Directive or of a supplement to a prospectus pursuant to Article 16 of the Prospectus Directive.

Each person in a Relevant Member State (other than a Relevant Member State where there is a Permitted Public Offer) who initially acquires any shares or to whom any offer is made will be deemed to have represented, acknowledged and agreed that (A) it is a "qualified investor", and (B) in the case of any shares acquired by it as a financial intermediary, as that term is used in Article 3(2) of the Prospectus Directive, (x) the shares acquired by it in the offering have not been acquired on behalf of, nor have they been acquired with a view to their offer or resale to, persons in any Relevant Member State other than "qualified investors" as defined in the Prospectus Directive, or in circumstances in which the prior consent of the Subscribers has been given to the offer or resale, or (y) where shares have been acquired by it on behalf of persons in any Relevant Member State other than "qualified investors" as defined in the Prospectus Directive, the offer of those shares to it is not treated under the Prospectus Directive as having been made to such persons.

For the purpose of the above provisions, the expression "an offer to the public" in relation to any shares in any Relevant Member State means the communication in any form and by any means of sufficient information on the terms of the offer of any shares to be offered so as to enable an investor to decide to purchase any shares, as the same may be varied in the Relevant Member State by any measure implementing the Prospectus Directive in the Relevant Member State and the expression "Prospectus Directive" means Directive 2003/71 EC (including the 2010 PD Amending Directive, in the case of Early Implementing Member States) and includes any relevant implementing measure in each Relevant Member State and the expression "2010 PD Amending Directive" means Directive 2010/73/EU.

Notice to Prospective Investors in Switzerland

The shares being sold by the Company in this offering may not be publicly offered in Switzerland and will not be listed on the SIX Swiss Exchange ("SIX") or on any other stock exchange or regulated trading facility in Switzerland. This document has been prepared without regard to the disclosure standards for issuance prospectuses under art. 652a or art. 1156 of the Swiss Code of Obligations or the disclosure standards for listing prospectuses under art. 27 ff. of the SIX Listing Rules or the listing rules of any other stock exchange or regulated trading facility in Switzerland. Neither this document nor any other offering or marketing material relating to the offering or the shares being sold in the offering may be publicly distributed or otherwise made publicly available in Switzerland.

Neither this document nor any other offering or marketing material relating to the offering, the Company or the shares being sold in the offering have been or will be filed with or approved by any Swiss regulatory authority. In particular, this document will not be filed with, and the offering will not be supervised by, the Swiss Financial Market Supervisory Authority FINMA (FINMA), and the offering has not been and will not be authorized under the Swiss Federal Act on Collective Investment Schemes ("CISA"). The investor protection afforded to acquirers of interests in collective

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investment schemes under the CISA does not extend to acquirers of the shares being sold in the offering.

Notice to Prospective Investors in the Dubai International Financial Centre

This document relates to an exempt offer in accordance with the Offered Securities Rules of the Dubai Financial Services Authority. This document is intended for distribution only to persons of a type specified in those rules. It must not be delivered to, or relied on by, any other person. The Dubai Financial Services Authority has no responsibility for reviewing or verifying any documents in connection with exempt offers. The Dubai Financial Services Authority has not approved this document nor taken steps to verify the information set out in it, and has no responsibility for it. The shares which are the subject of the offering contemplated by this prospectus may be illiquid and/or subject to restrictions on their resale. Prospective purchasers of the shares offered should conduct their own due diligence on the shares. If you do not understand the contents of this document you should consult an authorized financial adviser.

Notice to Prospective Investors in Hong Kong

The shares may not be offered or sold by means of any document other than (1) in circumstances which do not constitute an offer to the public within the meaning of the Companies Ordinance (Cap.32, Laws of Hong Kong), or (2) to "professional investors" within the meaning of the Securities and Futures Ordinance (Cap.571, Laws of Hong Kong) and any rules made thereunder, or (3) in other circumstances which do not result in the document being a "prospectus" within the meaning of the Companies Ordinance (Cap.32, Laws of Hong Kong), and no advertisement, invitation or document relating to the shares may be issued or may be in the possession of any person for the purpose of issue (in each case whether in Hong Kong or elsewhere), which is directed at, or the contents of which are likely to be accessed or read by, the public in Hong Kong (except if permitted to do so under the laws of Hong Kong) other than with respect to shares which are or are intended to be disposed of only to persons outside Hong Kong or only to "professional investors" within the meaning of the Securities and Futures Ordinance (Cap. 571, Laws of Hong Kong) and any rules made thereunder.

Notice to Prospective Investors in Singapore

This prospectus has not been registered as a prospectus with the Monetary Authority of Singapore. Accordingly, this prospectus and any other document or material in connection with the offer or sale, or invitation for subscription or purchase, of the shares may not be circulated or distributed, nor may the shares be offered or sold, or be made the subject of an invitation for subscription or purchase, whether directly or indirectly, to persons in Singapore other than (1) to an institutional investor under Section 274 of the Securities and Futures Act, Chapter 289 of Singapore (the "SFA"), (2) to a relevant person, or any person pursuant to Section 275(1A), and in accordance with the conditions, specified in Section 275 of the SFA or (3) otherwise pursuant to, and in accordance with the conditions of, any other applicable provision of the SFA.

Where the shares are subscribed or purchased under Section 275 by a relevant person which is: (1) a corporation (which is not an accredited investor) the sole business of which is to hold investments and the entire share capital of which is owned by one or more individuals, each of whom is an accredited investor; or (2) a trust (where the trustee is not an accredited investor) whose sole purpose is to hold investments and each beneficiary is an accredited investor, shares, debentures and units of shares and debentures of that corporation or the beneficiaries' rights and interest in that trust shall not be transferable for 6 months after that corporation or that trust has acquired the shares under Section 275 except: (a) to an institutional investor under Section 274 of the SFA or to a relevant person, or any person pursuant to Section 275(1A), and in accordance

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with the conditions, specified in Section 275 of the SFA; (b) where no consideration is given for the transfer; or (c) by operation of law.

Notice to Prospective Investors in Japan

The securities have not been and will not be registered under the Financial Instruments and Exchange Law of Japan (the Financial Instruments and Exchange Law) and each underwriter has agreed that it will not offer or sell any securities, directly or indirectly, in Japan or to, or for the benefit of, any resident of Japan (which term as used herein means any person resident in Japan, including any corporation or other entity organized under the laws of Japan), or to others for re-offering or resale, directly or indirectly, in Japan or to a resident of Japan, except pursuant to an exemption from the registration requirements of, and otherwise in compliance with, the Financial Instruments and Exchange Law and any other applicable laws, regulations and ministerial guidelines of Japan.

The underwriter and its affiliates are full service financial institutions engaged in various activities, which may include securities trading, commercial and investment banking, financial advisory, investment management, investment research, principal investment, hedging, financing and brokerage activities. The underwriter and certain of its affiliates have, from time to time, performed, and may in the future perform, various financial advisory and investment banking services for us, for which they received or will receive customary fees and expenses.

In the ordinary course of their various business activities, the underwriter and its affiliates may make or hold a broad array of investments and actively trade debt and equity securities (or related derivative securities) and financial instruments (including bank loans) for their own account and for the accounts of their customers, and such investment and securities activities may involve securities and/or instruments issued by us. The underwriter and its affiliates may also make investment recommendations and/or publish or express independent research views in respect of such securities or instruments and may at any time hold, or recommend to clients that they acquire, long and/or short positions in such securities and instruments.

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LEGAL MATTERS

Certain legal matters regarding the common stock offered hereby have been passed upon for the Company by Skadden, Arps, Slate, Meagher & Flom LLP, New York, New York, and Venable LLP as special Maryland counsel. Certain legal matters will be passed upon for the underwriter by Troutman Sanders LLP. Troutman Sanders LLP will rely as to certain matters of Maryland law upon Venable LLP.

INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

BDO USA, LLP (formerly BDO Seidman, LLP) is the independent registered public accounting firm for the Company.

AVAILABLE INFORMATION

We have filed with the SEC a registration statement on Form N-2, together with all amendments and related exhibits, under the 1933 Act, with respect to our common stock offered by this prospectus supplement. The registration statement contains additional information about us and the common stock being registered by this prospectus supplement. We file with or submit to the SEC annual, quarterly and current periodic reports, proxy statements and other information meeting the informational requirements of the 1934 Act. This information and the information specifically regarding how we voted proxies relating to portfolio securities for the period ended June 30, 2010, are available free of charge by contacting us at 10 East 40th Street, 44th floor, New York, NY 10016 or by telephone at toll-free (888) 748-0702. You may inspect and copy these reports, proxy statements and other information, as well as the registration statement and related exhibits and schedules, at the Public Reference Room of the SEC at 100 F Street NE, Washington, D.C. 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at (202) 551-8090. The SEC maintains an Internet site that contains reports, proxy and information statements and other information filed electronically by us with the SEC which are available on the SEC's Internet site at <http://www.sec.gov>. Copies of these reports, proxy and information statements and other information may be obtained, after paying a duplicating fee, by electronic request at the following E-mail address: publicinfo@sec.gov, or by writing the SEC's Public Reference Section, Washington, D.C. 20549-0102.

No dealer, salesperson or other individual has been authorized to give any information or to make any representation other than those contained in this prospectus supplement and, if given or made, such information or representations must not be relied upon as having been authorized by us or the underwriter. This prospectus supplement does not constitute an offer to sell or a solicitation of an offer to buy any securities in any jurisdiction in which such an offer or solicitation is not authorized or in which the person making such offer or solicitation is not qualified to do so, or to any person to whom it is unlawful to make such offer or solicitation. Neither the delivery of this prospectus supplement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in our affairs or that information contained herein is correct as of any time subsequent to the date hereof.

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\$750,000,000

PROSPECT CAPITAL CORPORATION

Common Stock Preferred Stock Debt Securities Warrants

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

We may offer shares of common stock, or warrants, options or rights to acquire shares of common stock, at a discount to net asset value per share in certain circumstances. Sales of common stock at prices below net asset value per share dilute the interests of existing stockholders, have the effect of reducing our net asset value per share and may reduce our market price per share.

Our Securities may be offered directly to one or more purchasers, or through agents designated from time to time by us, or to or through underwriters or dealers. The prospectus supplement relating to the offering will identify any agents or underwriters involved in the sale of our Securities, and will disclose any applicable purchase price, fee, commission or discount arrangement between us and our agents or underwriters or among our underwriters or the basis upon which such amount may be calculated. See "Plan of Distribution." We may not sell any of our Securities through agents, underwriters or dealers without delivery of the prospectus and a prospectus supplement describing the method and terms of the offering of such Securities. Our common stock is traded on The NASDAQ Global Select Market under the symbol "PSEC." As of March 11, 2011, the last reported sales price for our common stock was \$11.81.

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

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

Investing in our Securities involves a heightened risk of total loss of investment and is subject to risks. Before buying any Securities, you should read the discussion of the material risks of investing in our Securities in "Risk Factors" beginning on page 9 of this prospectus.

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

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

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

The date of this Prospectus is March 16, 2011

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ABOUT THIS PROSPECTUS

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

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PROSPECTUS SUMMARY

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

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

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

The Company

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

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

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

The Investment Adviser

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

The Offering

We may offer, from time to time, in one or more offerings or series, together or separately, up to \$750,000,000 of our Securities, which we expect to use initially to maintain balance sheet liquidity,

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involving repayment of debt under our credit facility, investment in high quality short-term debt instruments or a combination thereof, and thereafter to make long-term investments in accordance with our investment objectives.

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

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

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

Use of proceeds

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

Distributions

In June 2010, our Board of Directors approved a change in dividend policy from quarterly distributions to monthly distributions. Since that time, we have paid monthly distributions to the holders of our common stock and generally intend to continue to do so. The amount of the monthly distributions is determined by our Board of Directors and is based on our estimate of our investment company taxable income and net short-term capital gains. Certain amounts of the monthly distributions may from time to time be paid out of our capital rather than from earnings for the month as a result of our deliberate planning or accounting reclassifications. Distributions in excess of our current or accumulated earnings

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or profits constitute a return of capital and will reduce the stockholder's adjusted tax basis in such stockholder's common stock. After the adjusted basis is reduced to zero, these distributions will constitute capital gains to such stockholders. Certain additional amounts may be deemed as distributed to stockholders for income tax purposes. Other types of Securities will likely pay distributions in accordance with their terms. See "Price Range of Common Stock," "Distributions" and "Material U.S. Federal Income Tax Considerations."

Taxation

We have qualified and elected to be treated for U.S. Federal income tax purposes as a regulated investment company, or a RIC, under Subchapter M of the Internal Revenue Code of 1986, or the Code. As a RIC, we generally do not have to pay corporate-level U.S. Federal income taxes on any ordinary income or capital gains that we distribute to our stockholders as dividends. To maintain our qualification as a RIC and obtain RIC tax treatment, we must maintain specified source-of-income and asset diversification requirements and distribute annually at least 90% of our ordinary income and realized net short-term capital gains in excess of realized net long-term capital losses, if any. See "Distributions" and "Material U.S. Federal Income Tax Considerations."

Dividend reinvestment plan

We have a dividend reinvestment plan for our stockholders. This is an "opt out" dividend reinvestment plan. As a result, when we declare a dividend, the dividends are automatically reinvested in additional shares of our common stock, unless a stockholder specifically "opts out" of the dividend reinvestment plan so as to receive cash dividends. Stockholders who receive distributions in the form of stock are subject to the same U.S. Federal, state and local tax consequences as stockholders who elect to receive their distributions in cash. See "Dividend Reinvestment Plan."

The NASDAQ Global Select Market Symbol

PSEC

Anti-takeover provisions

Our charter and bylaws, as well as certain statutory and regulatory requirements, contain provisions that may have the effect of discouraging a third party from making an acquisition proposal for us. These anti-takeover provisions may inhibit a change in control in circumstances that could give the holders of our common stock the opportunity to realize a premium over the market price of our common stock. See "Description Of Our Capital Stock."

Management arrangements

Prospect Capital Management serves as our investment adviser. Prospect Administration serves as our administrator. For a description of Prospect Capital Management, Prospect Administration and our contractual arrangements with these companies, see "Business Management Services Investment Advisory Agreement," and "Business Management Services Administration Agreement."

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Risk factors

Investment in our Securities involves certain risks relating to our structure and investment objective that should be considered by prospective purchasers of our Securities. In addition, while we continue to broaden our portfolio, investment in our Securities involves certain risks relating to investing in the energy sector, including, but not limited to, risks associated with commodity pricing, regulation, production, demand, depletion and expiration, weather, and valuation. We are also subject to numerous investment and other risks not associated with the energy sector. We have a limited operating history upon which you can evaluate our business. In addition, as a business development company, our portfolio primarily includes securities issued by privately-held companies. These investments generally involve a high degree of business and financial risk, and are less liquid than public securities. We are required to mark the carrying value of our investments to fair value on a quarterly basis, and economic events, market conditions and events affecting individual portfolio companies can result in quarter-to-quarter mark-downs and mark-ups of the value of individual investments that collectively can materially affect our net asset value, or NAV. Also, our determinations of fair value of privately-held securities may differ materially from the values that would exist if there was a ready market for these investments. A large number of entities compete for the same kind of investment opportunities as we do. Moreover, our business requires a substantial amount of capital to operate and to grow and we seek additional capital from external sources. In addition, the failure to qualify as a RIC eligible for pass-through tax treatment under the Code on income distributed to stockholders could have a materially adverse effect on the total return, if any, obtainable from an investment in our Securities. See "Risk Factors" and the other information included in this prospectus for a discussion of factors you should carefully consider before deciding to invest in our Securities.

Plan of distribution

We may offer, from time to time, up to \$750,000,000 of our common stock, preferred stock, debt securities or warrants representing rights to purchase shares of our common stock, preferred stock or debt securities on the terms to be determined at the time of the offering. Securities may be offered at prices and on terms described in one or more supplements to this prospectus directly to one or more purchasers, through agents designated from time to time by us, or to or through underwriters or dealers. The supplement to this prospectus relating to the offering will identify any agents or underwriters involved in the sale of our Securities, and will set forth any applicable purchase price, fee and commission or discount arrangement or the basis upon which such amount may be calculated. We may not sell Securities pursuant to this prospectus without delivering a prospectus supplement describing the method and terms of the offering of such Securities. For more information, see "Plan of Distribution."

Table of Contents**Fees and Expenses**

The following tables are intended to assist you in understanding the costs and expenses that an investor in this offering will bear directly or indirectly. We caution you that some of the percentages indicated in the table below are estimates and may vary. In these tables, we assume that we have borrowed \$285 million under our credit facility, which is the maximum amount available under the credit facility. Except where the context suggests otherwise, whenever this prospectus contains a reference to fees or expenses paid by "you" or "us" or that "we" will pay fees or expenses, the Company will pay such fees and expenses out of our net assets and, consequently, you will indirectly bear such fees or expenses as an investor in the Company. However, you will not be required to deliver any money or otherwise bear personal liability or responsibility for such fees or expenses.

Stockholder transaction expenses:

Sales load (as a percentage of offering price)(1)	5.00%
Offering expenses borne by us (as a percentage of offering price)(2)	0.50%
Dividend reinvestment plan expenses(3)	None
Total stockholder transaction expenses (as a percentage of offering price)(4)	5.50%

Annual expenses (as a percentage of net assets attributable to common stock)(4):

Management Fees(5)	3.35%
Incentive fees payable under Investment Advisory Agreement (20% of realized capital gains and 20% of pre-incentive fee net investment income)(6)	2.22%
Interest payments on the credit facility	1.34%
Interest payments on the 2010 Notes	1.04%(7)
Interest payments on the 2011 Notes	0.91%(8)
Acquired Fund Fees and Expenses	0.01%(9)
Other expenses	1.51%(10)
Total annual expenses	10.38%(6)(10)

Example

The following table demonstrates the projected dollar amount of cumulative expenses we would pay out of net assets and that you would indirectly bear over various periods with respect to a hypothetical investment in our common stock. In calculating the following expense amounts, we have assumed we would have borrowed all \$285 million available under our line of credit, that our annual operating expenses would remain at the levels set forth in the table above and that we would pay the costs shown in the table above.

	1 Year	3 Years	5 Years	10 Years
You would pay the following expenses on a \$1,000 investment, assuming a 5% annual return	\$ 123.51	\$ 255.94	\$ 382.47	\$ 674.73

While the example assumes, as required by the SEC, a 5% annual return, our performance will vary and may result in a return greater or less than 5%. The income incentive fee under our Investment Advisory Agreement with Prospect Capital Management is unlikely to be material assuming a 5% annual return and is not included in the example. If we achieve sufficient returns on our investments, including through the realization of capital gains, to trigger an incentive fee of a material amount, our distributions to our common stockholders and our expenses would likely be higher. In addition, while the example assumes reinvestment of all dividends and other distributions at NAV, participants in our dividend reinvestment plan will receive a number of shares of our common stock determined by dividing the total dollar amount of the distribution payable to a participant by the market price per share of our common stock at the close of trading on the valuation date for the distribution. See "Dividend Reinvestment Plan" for additional information regarding our dividend reinvestment plan.

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This example and the expenses in the table above should not be considered a representation of our future expenses. Actual expenses (including the cost of debt, if any, and other expenses) may be greater or less than those shown.

- (1) In the event that the Securities to which this prospectus relates are sold to or through underwriters, a corresponding prospectus supplement will disclose the estimated applicable sales load.
- (2) The related prospectus supplement will disclose the estimated amount of offering expenses, the offering price and the estimated offering expenses borne by us as a percentage of the offering price.
- (3) The expenses of the dividend reinvestment plan are included in "other expenses."
- (4) The related prospectus supplement will disclose the offering price and the total stockholder transaction expenses as a percentage of the offering price.
- (5) Our base management fee is 2% of our gross assets (which include any amount borrowed, i.e., total assets without deduction for any liabilities). Although no plans are in place to borrow the full amount under our line of credit, assuming that we borrowed \$285 million, the 2% management fee of gross assets equals approximately 3.35% of net assets. See "Business Management Services Investment Advisory Agreement" and footnote 6 below.
- (6) Based on an annualized level of incentive fee paid during our second fiscal quarter ended December 31, 2010, all of which consisted of an income incentive fee. For a more detailed discussion of the calculation of the two-part incentive fee, see "Management Services Investment Advisory Agreement" in this prospectus.
- (7) On December 21, 2010, the Company issued \$150 million in aggregate principal amount of 6.25% Convertible Senior Notes due 2015, which we refer to as the 2010 Notes. See "Business General" and "Risk Factors Risks Related to our Business" for more detail on the 2010 Notes.
- (8) On February 18, 2011, the Company issued \$150 million in aggregate principal amount of 5.5% Convertible Senior Notes due 2016, which we refer to as the 2011 Notes. See "Business General" and "Risk Factors Risks Related to our Business" for more detail on the 2011 Notes. The 2011 Notes and the 2010 Notes are referred to collectively as the Notes.
- (9) The Company's stockholders indirectly bear the expenses of underlying investment companies in which the Company invests. This amount includes the fees and expenses of investment companies in which the Company is invested in as of December 31, 2010. When applicable, fees and expenses are based on historic fees and expenses for the investment companies and for those investment companies with little or no operating history, fees and expenses are based on expected fees and expenses stated in the investment companies' prospectus or other similar communication without giving effect to any performance. Future fees and expenses for certain investment companies may be substantially higher or lower because certain fees and expenses are based on the performance of the investment companies, which may fluctuate over time. The amount of the Company's average net assets used in calculating this percentage was based on net assets of approximately \$903 million as of December 31, 2010.
- (10) "Other expenses" are based on estimated amounts for the current fiscal year. The amount shown above represents annualized expenses during our three months ended December 31, 2010 representing all of our estimated recurring operating expenses (except fees and expenses reported in other items of this table) that are deducted from our operating income and reflected as expenses in our Statement of Operations. The estimate of our overhead expenses, including payments under an administration agreement with Prospect Administration, or the Administration Agreement, based on our projected allocable portion of overhead and other expenses incurred by Prospect Administration in performing its obligations under the Administration Agreement. "Other expenses" does not include non-recurring expenses. See "Business Management Services Administration Agreement."

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SELECTED CONDENSED FINANCIAL DATA

You should read the condensed consolidated financial information below with the Consolidated Financial Statements and notes thereto included in this offering memorandum. Financial information below for the years ended June 30, 2010, 2009, 2008, 2007 and 2006 has been derived from the financial statements that were audited by our independent registered public accounting firm. The selected consolidated financial data at and for the three and six months ended December 31, 2010 and 2009 have been derived from unaudited financial data, but in the opinion of our management, reflects all adjustments (consisting only of normal recurring adjustments) that are necessary to present fairly the results for such interim periods. Interim results at and for the three and six months ended December 31, 2010 are not necessarily indicative of the results that may be expected for the year ending June 30, 2011. Certain reclassifications have been made to the prior period financial information to conform to the current period presentation. See "Management's Discussion and Analysis of Financial Condition and Results of Operations" starting on page 31 for more information.

	For the Three Months Ended December 31,		For the Six Months Ended December 31,		For the Year Ended June 30,				
	2010	2009	2010	2009	2010	2009	2008	2007	2006
(In thousands except data relating to shares, per share and number of portfolio companies)									
Performance Data:									
Interest income	\$ 27,362	\$ 18,539	\$ 56,283	\$ 33,374	\$ 86,518	\$ 62,926	\$ 59,033	\$ 30,084	\$ 13,268
Dividend income	3,371	4,170	5,565	10,388	15,366	22,793	12,033	6,153	3,601
Other income	2,567	9,092	6,664	9,556	12,675	14,762	8,336	4,444	
Total investment income	33,300	31,801	68,512	53,318	114,559	100,481	79,402	40,681	16,869
Interest and debt expenses	2,261	1,995	4,522	3,369	(8,382)	(6,161)	(6,318)	(1,903)	(642)
Investment advisory expense	9,672	7,992	19,197	14,281	(30,727)	(26,705)	(20,199)	(11,226)	(3,868)
Other expenses	2,287	2,556	4,718	4,092	(8,260)	(8,452)	(7,772)	(4,421)	(3,801)
Total operating expenses	14,220	12,543	28,437	21,742	(47,369)	(41,318)	(34,289)	(17,550)	(8,311)
Net investment income	19,080	19,258	40,075	31,576	67,190	59,163	45,113	23,131	8,558
Realized and unrealized gains (losses)	12,860	(33,778)	17,445	(52,474)	(47,565)	(24,059)	(17,522)	(6,403)	4,338
Net increase (decrease) in net assets from operations	\$ 31,940	\$ (14,520)	\$ 57,520	\$ (20,898)	\$ 19,625	\$ 35,104	\$ 27,591	\$ 16,728	\$ 12,896
Per Share Data:									
Net increase (decrease) in net assets from operations(1)	\$ 0.38	\$ (0.25)	\$ 0.73	\$ (0.39)	\$ 0.33	\$ 1.11	\$ 1.17	\$ 1.06	\$ 1.83
Distributions declared per share	\$ 0.30	\$ 0.41	\$ 0.60	\$ 0.82	\$ (1.33)	\$ (1.62)	\$ (1.59)	\$ (1.54)	\$ (1.12)
Average weighted shares outstanding for the period	84,091,152	57,613,489	79,134,173	53,709,197	59,429,222	31,559,905	23,626,642	15,724,095	7,056,846
Assets and Liabilities Data:									
Investments	\$ 918,221	\$ 648,135	\$ 918,221	\$ 648,135	\$ 748,483	\$ 547,168	\$ 497,530	\$ 328,222	\$ 133,969
Other assets	157,874	40,945	157,874	40,945	84,212	119,857	44,248	48,280	4,511

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Total assets	1,076,095	689,080	1,076,095	689,080	832,695	667,025	541,778	376,502	138,480
Amount drawn on credit facility		10,000		10,000	100,300	124,800	91,167		28,500
2010 Notes	150,000		150,000						
Amount owed to related parties	10,104	7,997	10,104	7,997	9,300	6,713	6,641	4,838	745
Other liabilities	12,801	31,273	12,801	31,273	11,671	2,916	14,347	71,616	965
Total liabilities	172,905	49,270	172,905	49,270	121,271	134,429	112,155	76,454	30,210
Net assets	903,190	639,810	\$ 903,190	\$ 639,810	\$ 711,424	\$ 532,596	\$ 429,623	\$ 300,048	\$ 108,270

Investment Activity Data:

No. of portfolio companies at period end	58	55	58	55	58	30	29(2)	24(2)	15
Acquisitions	\$ 140,933	\$ 210,438(4)	\$ 281,884	\$ 216,504(4)	\$ 364,788(4)	\$ 98,305	\$ 311,947	\$ 167,255	\$ 83,625
Sales, repayments, and other disposals	\$ 62,915	\$ 45,494	\$ 131,063	\$ 69,735	\$ 136,221	\$ 27,007	\$ 127,212	\$ 38,407	\$ 9,954
Weighted-Average Yield at end of period(3)	14.1%	15.6%	14.1%	15.6%	14.2%	13.7%	15.5%	17.1%	17.0%

- (1) Per share data is based on average weighted shares for the period.
- (2) Includes a net profits interest in Charlevoix Energy Trading LLC, or Charlevoix, remaining after loan was paid.
- (3) Includes dividends from certain equity investments.
- (4) Includes \$207.1 million of acquired portfolio investments from Patriot Acquisition.

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RISK FACTORS

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

Risks Relating To Our Business

We may suffer credit losses.

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

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

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

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

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

We operate in a highly competitive market for investment opportunities.

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

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

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

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

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

In addition, decreases in the market values or fair values of our investments are recorded as unrealized depreciation. Unprecedented declines in prices and liquidity in the corporate debt markets experienced during the recent financial crises resulted in significant net unrealized depreciation in our portfolio in the past. The effect of all of these factors on our portfolio reduced our NAV by increasing net unrealized depreciation in our portfolio. Depending on market conditions, we could incur substantial realized losses and may continue to suffer additional unrealized losses in future periods, which could have a material adverse impact on our business, financial condition and results of operations.

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

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

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

A likelihood of greater volatility in the net asset value and market price of our common stock;

Diminished operating flexibility as a result of asset coverage or investment portfolio composition requirements required by lenders or investors that are more stringent than those imposed by the 1940 Act;

The possibility that investments will have to be liquidated at less than full value or at inopportune times to comply with debt covenants or to pay interest or dividends on the leverage;

Increased operating expenses due to the cost of leverage, including issuance and servicing costs;

Convertible or exchangeable securities issued in the future may have rights, preferences and privileges more favorable than those of our common stock;

Subordination to lenders' superior claims on our assets as a result of which lenders will be able to receive proceeds available in the case of our liquidation before any proceeds will be distributed to our stockholders;

Making it more difficult for us to meet our payment and other obligations under the Notes and our other outstanding debt;

The occurrence of an event of default if we fail to comply with the financial and/or other restrictive covenants contained in our debt agreements, including the credit agreement and each indenture governing the Notes, which event of default could result in all or some of our debt becoming immediately due and payable;

Reduced availability of our cash flow to fund investments, acquisitions and other general corporate purposes, and limiting our ability to obtain additional financing for these purposes;

The risk of increased sensitivity to interest rate increases on our indebtedness with variable interest rates, including borrowings under our amended senior credit facility; and

Reduced flexibility in planning for, or reacting to, and increasing our vulnerability to, changes in our business, the industry in which we operate and the general economy.

For example, the amount we may borrow under our revolving credit facility is determined, in part, by the fair value of our investments. If the fair value of our investments declines, we may be forced to sell investments at a loss to maintain compliance with our borrowing limits.

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Other debt facilities we may enter into in the future may contain similar provisions. Any such forced sales would reduce our NAV and also make it difficult for the net asset value to recover. Our Investment Adviser and our Board of Directors in their best judgment nevertheless may determine to use leverage if they expect that the benefits to our stockholders of maintaining the leveraged position will outweigh the risks.

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

Illustration. The following table illustrates the effect of leverage on returns from an investment in our common stock assuming various annual returns, net of interest expense. The calculations in the table below are hypothetical and actual returns may be higher or lower than those appearing below. The calculation assumes (i) \$1.2 billion in total assets, (ii) an average cost of funds of 5.88%, (iii) \$300 million in debt outstanding and (iv) \$900 million of shareholders' equity.

Assumed Return on Our Portfolio (net of expenses)	(10)%	(5)%	0%	5%	10%
Corresponding Return to Stockholder	(11.38)%	(4.71)%	1.96%	8.63%	15.29%

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

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

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

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

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

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

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have had we not borrowed. Such a decline could negatively affect our ability to make common stock dividend payments. Leverage is generally considered a speculative investment technique.

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

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

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

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

restrictions on the level of indebtedness that we are permitted to incur in relation to the value of our assets;

restrictions on our ability to incur liens; and

maintenance of a minimum level of stockholders' equity.

As of December 31, 2010, we were in compliance with these covenants. However, our continued compliance with these covenants depends on many factors, some of which are beyond our control. Accordingly, there are no assurances that we will continue to comply with the covenants in our credit facility. Failure to comply with these covenants would result in a default under this facility which, if we were unable to obtain a waiver from the lenders thereunder, could result in an acceleration of repayments under the facility and thereby have a material adverse impact on our business, financial condition and results of operations.

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

The revolving period for our credit facility with a syndicate of lenders is currently scheduled to terminate on June 13, 2012. If the credit facility is not renewed or extended by the participant banks by June 13, 2012, we will not be able to make further borrowings under the facility after such date and the outstanding principal balance on that date will be due and payable on June 13, 2013. At March 11, 2011 we had no outstanding borrowings under our credit facility. Interest on borrowings under the credit facility is one-month LIBOR plus 325 basis points, subject to a minimum LIBOR floor of 100 basis points. Additionally, the lenders charge a fee on the unused portion of the credit facility equal to either 75 basis points if at least half of the credit facility is used or 100 basis points otherwise. If we are unable to extend our facility or find a new source of borrowing on acceptable terms, we will be required to pay down the amounts outstanding under the facility during the one-year term-out period through one or more of the following: (1) principal collections on our securities pledged under the facility, (2) at our option, interest collections on our securities pledged under the facility and cash collections on our securities not pledged under the facility, or (3) possible liquidation of some or all of our loans and other assets, any of which could have a material adverse effect on our results of operations and financial position and may force us to decrease or stop paying certain expenses and making distributions until the facility is repaid. In addition,

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

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

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

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

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

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

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

We may experience fluctuations in our quarterly results.

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

Our most recent NAV was calculated as of December 31, 2010 and our NAV when calculated as of March 31, 2011 may be higher or lower.

Our most recently estimated NAV per share is \$10.05 on an as adjusted basis solely to give effect to our distributions with record dates of January 31, 2011 and February 28, 2011 and our issuance of common stock on January 31, 2011 and February 28, 2011 in connection with our dividend reinvestment plan versus \$10.25 determined by us as of December 31, 2010. NAV per share as of March 31, 2011, may be higher or

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lower than \$10.05 based on potential changes in valuations and earnings for the quarter then ended. Our Board of Directors has not yet determined the fair value of portfolio investments at any date subsequent to December 31, 2010. Our Board of Directors determines the fair value of our portfolio investments on a quarterly basis in connection with the preparation of quarterly financial statements and based on input from an independent valuation firm, our Investment Adviser and the audit committee of our Board of Directors.

Potential conflicts of interest could impact our investment returns.

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

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

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

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

We have entered into a royalty-free license agreement with Prospect Capital Management. Under this agreement, Prospect Capital Management agrees to grant us a non-exclusive license to use the name

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

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

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

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

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

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

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

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

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

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

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

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

Risks Relating To Our Operation As A Business Development Company

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

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

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

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

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

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

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

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

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

For U.S. federal income tax purposes, we include in income certain amounts that we have not yet received in cash, such as original issue discount or payment-in-kind interest, which represents contractual interest added to the loan balance and due at the end of the loan term. Such original issue discount, which could be significant relative to our overall investment activities, or increases in loan balances as a result of payment-in-kind arrangements, are included in our taxable income before we receive any corresponding cash payments. We also may be required to include in taxable income certain other amounts that we do not receive in cash. While we focus primarily on investments that will generate a current cash return, our investment portfolio currently includes, and we may continue to invest in, securities that do not pay some or all of their return in periodic current cash distributions.

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

Since in some cases we may recognize taxable income before or without receiving cash representing such income, we may have difficulty distributing at least 90% of our ordinary income and realized net short-term capital gains in excess of realized net long-term capital losses, if any, as required to maintain RIC tax treatment. Accordingly, we may have to sell some of our investments at times we would not

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consider advantageous, raise additional debt or equity capital or reduce new investment originations to meet these distribution requirements. If we are not able to obtain cash from other sources, we may fail to qualify for RIC treatment and thus become subject to corporate-level income tax. See "Regulation Senior Securities" and "Material U.S. Federal Income Tax Considerations".

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

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

As a BDC regulated under provisions of the 1940 Act, we are not generally able to issue and sell our common stock at a price below the current net asset value per share. If our common stock trades at a discount to net asset value, this restriction could adversely affect our ability to raise capital. We may, however, sell our common stock, or warrants, options or rights to acquire our common stock, at a price below the current net asset value of our common stock in certain circumstances, including if (i)(1) the holders of a majority of our shares (or, if less, at least 67% of a quorum consisting of a majority of our shares) and a similar majority of the holders of our shares who are not affiliated persons of us approve the sale of our common stock at a price that is less than the current net asset value, and (2) a majority of our Directors who have no financial interest in the transaction and a majority of our independent Directors (a) determine that such sale is in our and our stockholders' best interests and (b) in consultation with any underwriter or underwriters of the offering, make a good faith determination as of a time either immediately prior to the first solicitation by us or on our behalf of firm commitments to purchase such shares, or immediately prior to the issuance of such shares, that the price at which such shares are to be sold is not less than a price which closely approximates the market value of such shares, less any distributing commission or discount or if (ii) a majority of the number of the beneficial holders of our common stock entitled to vote at our annual meeting, without regard to whether a majority of such shares are voted in favor of the proposal, approve the sale of our common stock at a price that is less than the current net asset value per share. At our 2010 annual meeting of stockholders held on December 10, 2010, we obtained the first method of approval from our shareholders to sell an unlimited number of shares of common stock at any discount to net asset value per share for a period of twelve months, expiring on December 10, 2011. We will not sell shares of common stock under a prospectus supplement to the registration statement (the "current registration statement") if the cumulative dilution to our NAV per share from offerings under the current registration statement exceeds 15%. See "If we sell common stock at a discount to our net asset value per share, stockholders who do not participate in such sale will experience immediate dilution in an amount that may be material" discussed below.

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

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

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Securitization of our assets subjects us to various risks.

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

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

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

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

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

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assets are qualifying assets and the leverage incurred by such SPE may or may not be treated as borrowings by us for purposes of the requirement that we not issue senior securities in an amount in excess of our net assets.

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

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

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

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

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

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

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

Common stock of BDCs, like that of closed-end investment companies, frequently trades at a discount to current net asset value, which could adversely affect the ability to raise capital. In the past, our common

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stock has traded at a discount to our net asset value. The risk that our common stock may continue to trade at a discount to our net asset value is separate and distinct from the risk that our net asset value per share may decline.

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

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

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

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

Risks Relating To Our Investments

We may not realize gains or income from our investments.

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

While we continue to broaden our portfolio, we continue to be invested in a number of companies in the energy and energy related industries. A consequence of this lack of diversification is that the aggregate returns we realize may be significantly and adversely affected if a small number of such investments perform poorly or if we need to write down the value of any one investment. Beyond our income tax diversification requirements, we do not have fixed guidelines for diversification, and our investments are

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concentrated in relatively few portfolio companies. In addition, to date we have concentrated on making investments in the energy industry. While we expect to be less focused on the energy and energy related industries in the future, we anticipate that we will continue to have large holdings in the energy and energy related industries. As a result, a downturn in the energy industry could materially and adversely affect us.

The energy industry is subject to many risks.

While we continue to broaden our portfolio, a large portion of our portfolio is concentrated in the energy and energy related industries. Our definition of energy, as used in the context of the energy industry, is broad, and different sectors in the energy industry may be subject to variable risks and economic pressures. As a result, it is difficult to anticipate the impact of changing economic and political conditions on our portfolio companies and, as a result, our financial results. The revenues, income (or losses) and valuations of energy companies can fluctuate suddenly and dramatically due to any one or more of the following factors:

Commodity Pricing Risk. Energy companies in general are directly affected by energy commodity prices, such as the market prices of crude oil, natural gas and wholesale electricity, especially for those that own the underlying energy commodity. In addition, the volatility of commodity prices can affect other energy companies due to the impact of prices on the volume of commodities transported, processed, stored or distributed and on the cost of fuel for power generation companies. The volatility of commodity prices can also affect energy companies' ability to access the capital markets in light of market perception that their performance may be directly tied to commodity prices. Historically, energy commodity prices have been cyclical and exhibited significant volatility. Although we generally prefer risk controls, including appropriate commodity and other hedges, by certain of our portfolio companies, if available, some of our portfolio companies may not engage in hedging transactions to minimize their exposure to commodity price risk. For those companies that engage in such hedging transactions, they remain subject to market risks, including market liquidity and counterparty creditworthiness. In addition, such companies may also still have exposure to market prices if such companies do not produce volumes or other contractual obligations in accordance with such hedging contracts.

Regulatory Risk. The profitability of energy companies could be adversely affected by changes in the regulatory environment. The businesses of energy companies are heavily regulated by federal, state and local governments in diverse ways, such as the way in which energy assets are constructed, maintained and operated and the prices energy companies may charge for their products and services. Such regulation can change over time in scope and intensity. For example, a particular by-product of an energy process may be declared hazardous by a regulatory agency, which can unexpectedly increase production costs. Moreover, many state and federal environmental laws provide for civil penalties as well as regulatory remediation, thus adding to the potential liability an energy company may face. In addition, the deregulation of energy markets and the unresolved regulatory issues related to some power markets such as California create uncertainty in the regulatory environment as rules and regulations may be adopted on a transitional basis. We cannot assure you that the deregulation of energy markets will continue and if it continues, whether its impact on energy companies' profitability will be positive.

Production Risk. The profitability of energy companies may be materially impacted by the volume of crude oil, natural gas or other energy commodities available for transporting, processing, storing, distributing or power generation. A significant decrease in the production of natural gas, crude oil, coal or other energy commodities, due to the decline of production from existing facilities, import supply disruption, depressed commodity prices, political events, OPEC actions or otherwise, could reduce revenue and operating income or increase operating costs of energy companies and, therefore, their ability to pay debt or dividends.

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Demand Risk. A sustained decline in demand for crude oil, natural gas, refined petroleum products and electricity could materially affect revenues and cash flows of energy companies. Factors that could lead to a decrease in market demand include a recession or other adverse economic conditions, an increase in the market price of the underlying commodity, higher taxes or other regulatory actions that increase costs, or a shift in consumer demand for such products.

Depletion and Exploration Risk. A portion of any one energy company's assets may be dedicated to natural gas, crude oil and/or coal reserves and other commodities that naturally deplete over time. Depletion could have a materially adverse impact on such company's ability to maintain its revenue. Further, estimates of energy reserves may not be accurate and, even if accurate, reserves may not be fully utilized at reasonable costs. Exploration of energy resources, especially of oil and gas, is inherently risky and requires large amounts of capital.

Weather Risk. Unseasonable extreme weather patterns could result in significant volatility in demand for energy and power. In addition, hurricanes, storms, tornados, floods, rain, and other significant weather events could disrupt supply and other operations at our portfolio companies as well as customers or suppliers to such companies. This volatility may create fluctuations in earnings of energy companies.

Operational Risk. Energy companies are subject to various operational risks, such as failed drilling or well development, unscheduled outages, underestimated cost projections, unanticipated operation and maintenance expenses, failure to obtain the necessary permits to operate and failure of third-party contractors (for example, energy producers and shippers) to perform their contractual obligations. In addition, energy companies employ a variety of means of increasing cash flow, including increasing utilization of existing facilities, expanding operations through new construction, expanding operations through acquisitions, or securing additional long-term contracts. Thus, some energy companies may be subject to construction risk, acquisition risk or other risk factors arising from their specific business strategies.

Competition Risk. The progress in deregulating energy markets has created more competition in the energy industry. This competition is reflected in risks associated with marketing and selling energy in the evolving energy market and a competitor's development of a lower-cost energy or power source, or of a lower cost means of operations, and other risks arising from competition.

Valuation Risk. Since mid-2001, excess power generation capacity in certain regions of the United States has caused substantial decreases in the market capitalization of many energy companies. While such prices have recovered to some extent, we can offer no assurance that such decreases in market capitalization will not recur, or that any future decreases in energy company valuations will be insubstantial or temporary in nature.

Terrorism Risk. Since the September 11th attacks, the United States government has issued public warnings indicating that energy assets, specifically those related to pipeline infrastructure, production facilities and transmission and distribution facilities, might be specific targets of terrorist activity. The continued threat of terrorism and related military activity will likely increase volatility for prices of natural gas and oil and could affect the market for products and services of energy companies. In addition, any future terrorist attack or armed conflict in the United States or elsewhere may undermine economic conditions in the United States in general.

Financing Risk. Some of our portfolio companies rely on the capital markets to raise money to pay their existing obligations. Their ability to access the capital markets on attractive terms or at all may be affected by any of the risks associated with energy companies described above, by general economic and market conditions or by other factors. This may in turn affect their ability to satisfy their obligations with us.

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Climate Change. There may be evidence of global climate change. Climate change creates physical and financial risk and some of our portfolio companies may be adversely affected by climate change. For example, customers of energy companies needs vary with weather conditions, primarily temperature and humidity. To the extent weather conditions are affected by climate change, energy use could increase or decrease depending on the duration and magnitude of any changes. Increased energy use due to weather changes may require additional investments by our portfolio companies in more pipelines and other infrastructure to serve increased demand. A decrease in energy use due to weather changes may affect our portfolio companies financial condition, through decreased revenues. Extreme weather conditions in general require more system backup, adding to costs, and can contribute to increased system stresses, including service interruptions. Energy companies could also be affected by the potential for lawsuits against or taxes or other regulatory costs imposed on greenhouse gas emitters, based on links drawn between greenhouse gas emissions and climate change.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

We make both debt and minority equity investments in portfolio companies. As a result, we are subject to the risk that a portfolio company may make business decisions with which we disagree, and the

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management of such company, as representatives of the holders of their common equity, may take risks or otherwise act in ways that do not serve our interests. As a result, a portfolio company may make decisions that could decrease the value of our portfolio holdings.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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Risks Relating To Our Securities

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

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

The market price of our securities may fluctuate significantly.

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

significant volatility in the market price and trading volume of securities of business development companies or other companies in the energy industry, which are not necessarily related to the operating performance of these companies;

changes in regulatory policies or tax guidelines, particularly with respect to RICs or business development companies;

loss of RIC qualification;

changes in earnings or variations in operating results;

changes in the value of our portfolio of investments;

any shortfall in revenue or net income or any increase in losses from levels expected by investors or securities analysts;

departure of one or more of Prospect Capital Management's key personnel;

operating performance of companies comparable to us;

changes in prevailing interest rates;

litigation matters;

general economic trends and other external factors; and

loss of a major funding source.

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

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

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

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

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

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

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

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

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

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

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

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

The Maryland Control Share Acquisition Act, which provides that "control shares" of a Maryland corporation (defined as shares of common stock which, when aggregated with other shares of common stock controlled by the stockholder, entitles the stockholder to exercise one of three increasing ranges of voting power in electing directors, as described more fully below) acquired in a "control share acquisition" (defined as the direct or indirect acquisition of ownership or control of "control shares") have no voting rights except to the extent approved by stockholders by the affirmative vote of at least two-thirds of all the votes entitled to be cast on the matter, excluding all interested shares of common stock.

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

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

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

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

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

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

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

Note on Forward Looking Statements

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

our future operating results;

our business prospects and the prospects of our portfolio companies;

the impact of investments that we expect to make;

our contractual arrangements and relationships with third parties;

the dependence of our future success on the general economy and its impact on the industries in which we invest;

the ability of our portfolio companies to achieve their objectives;

our expected financings and investments;

the adequacy of our cash resources and working capital; and

the timing of cash flows, if any, from the operations of our portfolio companies.

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

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

General

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

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

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

The aggregate value of our portfolio investments was \$918,221 and \$748,483 as of December 31, 2010 and June 30, 2010, respectively. During the six months ended December 31, 2010, our net cost of investments increased by \$157,309, or 21.6%, primarily as a result of our investment in ten new and seven follow-on investments of \$275,867, while we received full repayment on eight investments, sold three investments and received several partial prepayments and revolver paydowns of \$135,553. Several new investments that we anticipated closing prior to December 31, 2010 were delayed by the borrowers when the expiring tax breaks were extended. The closing of these loans has increased the level of activity during the current quarter ending March 31, 2011 as detailed in the *Recent Developments*, which follows.

Compared to the end of last fiscal year (ended June 30, 2010), net assets increased by \$191,766 or 27.0% during the six months ended December 31, 2010, from \$711,424 to \$903,190. This increase resulted from the issuance of new shares of our common stock (less offering costs) in the amount of \$177,718, dividend reinvestments of \$5,280, and another \$57,520 from operations. These increases, in turn, were offset by \$48,752 in dividend distributions to our stockholders. The \$57,520 increase in net assets resulting from operations is net of the following: net investment income of \$40,075, net realized gain on investments of \$5,016, and an increase in net assets due to changes in net unrealized appreciation of investments of \$12,429.

Market Conditions

While the economy continues to show signs of recovery from the deteriorating credit markets of 2008 and 2009, there is still a level of uncertainty and volatility in the capital markets. The growth and improvement in the capital markets that began during the second half of 2009 carried over into the first half of 2010. While encouraged by the signs of improvement, we operate in a challenging environment that is still recovering from a recession and financial services industry negatively affected by the deterioration of credit quality in subprime residential mortgages that spread rapidly to other credit markets. Market liquidity and credit quality conditions continue to remain weaker today than three years ago.

We believe that Prospect is well positioned to navigate through these adverse market conditions. As a business development company, we are limited to a maximum 1 to 1 debt to equity ratio. On December 21, 2010, we issued \$150,000 of 6.25% Senior Convertible Notes due December 15, 2015, or the 2010 Notes, to further enhance our liquidity position and to demonstrate our access to the unsecured term debt market (See Note 6 to our consolidated financial statements.). The 2010 Notes are general unsecured obligations, rank equally in right of payment with our existing and future senior unsecured debt, and will rank senior in right of payment to any potential subordinated debt, should any be issued in the future. The 2010 Notes have no restrictions related to the type and security of assets in which Prospect might invest.

As of December 31, 2010, we had no outstanding borrowings on the credit facility and \$150,000 outstanding on our 2010 Notes. We also had \$242,890 available under our credit facility for additional borrowing. Further, as we make additional investments that are eligible to be pledged under the credit facility, we will generate additional credit facility availability. The revolving period for our credit facility continues until June 13, 2012, with an amortization running to June 13, 2013. During the amortization period only principal payments received on the pledged assets are required to be used for amortization.

We also continue to generate liquidity through public and private stock offerings. On July 7, 2009, we completed a public stock offering for 5,175,000 shares of our common stock at \$9.00 per share, raising

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\$46,575 of gross proceeds. On August 20, 2009 and September 24, 2009, we issued 3,449,686 shares and 2,807,111 shares, respectively, of our common stock at \$8.50 and \$9.00 per share, respectively, in private stock offerings, raising \$29,322, and \$25,264 of gross proceeds, respectively. Concurrent with the sale of these shares, we entered into a registration rights agreement in which we granted the purchasers certain registration rights with respect to the shares. Under the terms and conditions of the registration rights agreement, we filed with the SEC a post-effective amendment to the registration statement on Form N-2 on November 6, 2009. Such amendment was declared effective by the SEC on November 9, 2009.

On March 4, 2010, our Registration Statement on Form N-2 was declared effective by the SEC. Under this Shelf Registration Statement, we can issue up to \$257,676 of additional equity securities as of December 31, 2010.

On March 17, 2010, we established an at-the-market program through which we sold shares of our common stock. An at-the-market offering is a registered offering by a publicly traded issuer of its listed equity securities selling shares directly into the market at market prices. We engaged two broker-dealers to act as agents and sell our common stock directly into the market over a period of time. We paid a 2% commission to the broker-dealer on shares sold. Through this program we issued 8,000,000 shares of our common stock at an average price of \$10.90 per share, raising \$87,177 of gross proceeds, from March 23, 2010 through July 21, 2010.

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

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

On November 10, 2010, we established a fourth at-the-market program, through which we may sell, from time to time and at our discretion, 9,750,000 shares of our common stock. We engaged four broker-dealers to act as potential agents and sell our common stock directly into the market over a period of time. We pay a 2% commission to the broker-dealer on shares sold. Through this program we issued 4,513,920 shares of our common stock at an average price of \$10.00 per share, raising \$45,147 of gross proceeds, from November 16, 2010 through December 15, 2010.

Our Board of Directors, pursuant to the Maryland General Corporation Law, executed Articles of Amendment to increase the number of shares authorized for issuance from 100,000,000 to 200,000,000 in the aggregate. The amendment became effective August 31, 2010.

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

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Second Quarter Highlights

Investment Transactions

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

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

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

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

On November 29, 2010, we made a senior subordinated debt investment of \$14,000 in Royal Adhesives & Sealants LLC ("Royal"), a leading producer of proprietary, high-performance adhesives and sealants. The unsecured note bears interest in cash at the greater of 12.0% or LIBOR plus 8.5%, with a LIBOR ceiling of 4.5%, plus 2.0% PIK and has a final maturity on November 29, 2016. On December 13, 2010, we made a follow-on secured debt investment of \$11,000 in Royal.

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

On December 3, 2010, we exercised our warrants in Miller and received 2,013,814 shares of Miller common stock. On December 27, 2010, we sold 1,397,510 of these shares at \$3.95 net proceeds per share, realizing a gain of \$5,415.

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

On December 23, 2010, we made a second lien secured debt investment of \$15,300 in Jordan Healthcare Holdings, Inc. ("Jordan"), a leading provider of home healthcare services in Texas. The second lien note bears interest in cash at the greater of 12.0% or LIBOR plus 10.0% plus 2.5% PIK and has a final maturity on June 23, 2016.

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

Equity Issuance

On October 29, 2010, November 30, 2010 and December 31, 2010, we issued shares of our common stock in connection with the dividend reinvestment plan of 92,999, 87,941 and 89,603, respectively.

During the period from October 1, 2010 to November 3, 2010, we issued 4,929,556 shares of our common stock at an average price of \$9.86 per share, and raised \$48,611 of gross proceeds, under our at-the-market program. Net proceeds were \$47,639 after 2% commission to the broker-dealer on shares sold.

On November 10, 2010, we established a new at-the-market program through which we may sell 9,750,000 shares of our common stock. Through this program we issued 4,513,920 shares of our common stock at an average price of \$10.00 per share, raising \$45,147 of gross proceeds, from November 16, 2010 to December 15, 2010. Net proceeds were \$44,244 after 2% commission to the broker-dealer on shares sold.

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Dividend

On November 8, 2010, we announced the declaration of monthly dividends in the following amounts and with the following dates:

\$0.100875 per share for November 2010 to holders of record on November 30, 2010 with a payment date of December 31, 2010;

\$0.101000 per share for December 2010 to holders of record on December 31, 2010 with a payment date of January 31, 2011;

\$0.101125 per share for January 2011 to holders of record on January 31, 2011 with a payment date of February 28, 2011.

Credit Facility

On November 1, 2010, we announced an increase in commitments to our credit facility of \$20,000. As of December 31, 2010, the lenders have extended commitments of \$285,000 under the credit facility. Our credit facility includes an accordion feature which allows the facility to be increased to up to \$300,000 of commitments in the aggregate to the extent additional or existing lenders commit to increase the commitments. We will seek to add additional lenders in order to reach the maximum size; although no assurance can be given we will be able to do so.

2010 Notes

On December 21, 2010, we issued \$150,000 in aggregate principal amount of 6.25% Senior Convertible Notes due 2015. The 2010 Notes mature on December 15, 2015, unless previously converted in accordance with their terms. The 2010 Notes are general unsecured obligations, rank equally in right of payment with our existing and future senior unsecured debt, and rank senior in right of payment to any potential subordinated debt, should any be issued in the future. The 2010 Notes are convertible into shares of Common Stock at an initial conversion rate and conversion rate at December 31, 2010 of 88.0902 shares of Common Stock per \$1,000 principal amount of 2010 Notes, which is equivalent to a conversion price of approximately \$11.352 per share of Common Stock, subject to adjustment in certain circumstances. At March 11, 2011, the 2010 Notes are convertible into 88.0904 shares of Common Stock, as adjusted for dividends paid in excess of \$0.101125 per month after the closing. The holders of the 2010 Notes may also put back the 2010 Notes to the Company under certain circumstances. The net proceeds from the offering of the 2010 Notes were approximately \$145,200, which will be used initially to maintain balance sheet liquidity, including repayment of debt under the Company's credit facility, investments in high quality short-term debt instruments or a combination thereof, and thereafter to make long-term investments in accordance with the Company's investment objective. We have analyzed the features of the 2010 Notes to determine if bifurcation was necessary and have determined that it is not material.

Recent Developments

On January 6, 2011, we made a senior secured term loan investment of \$30,000 to support the acquisition of Progressive Logistics Services, LLC by a middle market private equity firm.

On January 10, 2011, we made a senior secured debt investment of \$19,000 to support the acquisition of Endeavor House by Pinnacle Treatment Centers, Inc.

On January 10, 2011, we sold 616,304 shares of Miller Petroleum, Inc. ("Miller") common stock realizing \$4.23 of net proceeds per share, realizing a gain of \$2,561 on the sale.

On January 13, 2011, we amended our revolving credit facility. The amendment increases the accordion feature limit from \$300,000 to \$400,000 of commitments, of which \$285,000 of commitments are currently in place. Other changes in the amendment increase our borrowing base with the investments

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currently pledged to the facility by reducing some concentration limits and allow us to pledge new assets to the facility on an expedited basis.

On January 21, 2011, we provided senior secured credit facilities of \$28,200 to support the acquisition of Stauber Performance Ingredients, by ICV Partners. Through February 14, 2011, we have funded \$26,450 of the commitment.

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

On January 31, 2011, we issued 84,155 shares of our common stock in connection with the dividend reinvestment plan.

On January 31, 2011, we made a senior secured term investment of \$7,500 to support the recapitalization of Empire Today, LLC, which is the second largest independent provider of carpet and hard surface flooring to consumers in the residential replacement flooring industry.

On February 3, 2011, we made a senior secured debt investment of \$22,000 to support the recapitalization of a pharmacy services company by a leading private equity firm. Through February 14, 2011, we have funded \$20,500 of the commitment.

On February 4, 2011, we made a secured second-lien debt investment of \$45,000 to support the refinancing of Clearwater Seafoods Limited Partnership, a leading premium seafood company based in Nova Scotia, Canada.

On February 8, 2011, we announced the declaration of monthly dividends in the following amounts and with the following dates:

\$0.101150 per share for February 2011 to holders of record on February 28, 2011 with a payment date of March 31, 2011;

\$0.101175 per share for March 2011 to holders of record on March 31, 2011 with a payment date of April 29, 2011;

\$0.101200 per share for April 2011 to holders of record on April 29, 2011 with a payment date of May 31, 2011.

On February 9, 2011, we made a net follow-on investment of \$2,967 in The Copernicus Group, Inc. that increased our total investment to \$22,500.

On February 18, 2011, we issued \$172,500 in aggregate principal amount of 5.50% Senior Convertible Notes due 2016. The 2011 Notes mature on August 15, 2016, unless previously converted in accordance with their terms. The 2011 Notes are general unsecured obligations, rank equally in right of payment with our existing, including the 2010 Notes and future senior unsecured debt, and rank senior in right of payment to any potential subordinated debt, should any be issued in the future. The 2011 Notes are convertible into shares of Common Stock at an initial conversion rate and conversion rate at March 11, 2011 of 78.3699 shares of Common Stock per \$1,000 principal amount of 2011 Notes, which is equivalent to a conversion price of approximately \$12.76 per share of Common Stock, subject to adjustment in certain circumstances. The holders of the 2011 Notes may also put back the 2011 Notes to the Company under certain circumstances. The net proceeds from the offering of the 2011 Notes were approximately \$166,925, which will be used initially to maintain balance sheet liquidity, including repayment of debt under the Company's credit facility, investments in high quality short-term debt instruments or a combination thereof, and thereafter to make long-term investments in accordance with the Company's investment objective. We have analyzed the features of the 2011 Notes to determine if bifurcation was necessary and have determined that it is not material.

On March 2, 2011, we made a senior secured first-lien debt investment of \$12,500 to support the acquisition of a sporting goods manufacturer. The company is a market leader in the bowhunting equipment industry.

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On March 4, 2011, we made a \$27,000 secured second-lien term loan to Arrowhead General Insurance Agency, Inc. After the financing we received a repayment of the loan that was previously outstanding.

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

Critical Accounting Policies and Estimates

Our discussion and analysis of our financial condition and results of operations are based upon our financial statements, which have been prepared in accordance with GAAP. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Changes in the economic environment, financial markets and any other parameters used in determining such estimates could cause actual results to differ materially. In addition to the discussion below, our critical accounting policies are further described in the notes to the financial statements.

Basis of Consolidation

Under the 1940 Act rules, the regulations pursuant to Article 6 of Regulation S-X, and the American Institute of Certified Public Accountants' Audit and Accounting Guide for Investment Companies, we are precluded from consolidating any entity other than another investment company or an operating company which provides substantially all of its services and benefits to us. Our December 31, 2010 and June 30, 2010 financial statements include our accounts and the accounts of Prospect Capital Funding, LLC, our only wholly-owned, closely-managed subsidiary, which is also an investment company. All intercompany balances and transactions have been eliminated in consolidation.

Investment Classification

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

Investments are recognized when we assume an obligation to acquire a financial instrument and assume the risks for gains or losses related to that instrument. Investments are derecognized when we assume an obligation to sell a financial instrument and forego the risks for gains or losses related to that instrument. Specifically, we record all security transactions on a trade date basis. Investments in other, non-security financial instruments are recorded on the basis of subscription date or redemption date, as applicable. Amounts for investments recognized or derecognized but not yet settled are reported as Receivables for investments sold and Payables for investments purchased, respectively, in the Consolidated Statements of Assets and Liabilities.

Investment Valuation

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

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

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

- 1) Each portfolio company or investment is reviewed by our investment professionals with the independent valuation firm engaged by our Board of Directors;
- 2) the independent valuation firm conducts independent appraisals and makes their own independent assessment;
- 3) the audit committee of our Board of Directors reviews and discusses the preliminary valuation by our Investment Adviser within the valuation range presented by the independent valuation firm; and
- 4) the Board of Directors discusses the valuations and determines the fair value of each investment in our portfolio in good faith based on the input of our Investment Adviser, the independent valuation firm and the audit committee.

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

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

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

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

Level 3: Unobservable inputs for the asset or liability.

In all cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has been determined 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 considers factors specific to each investment.

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

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

In April 2009, the FASB issued ASC 820-10-65, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly* ("ASC 820-10-65"). This update provides further clarification for ASC 820 in markets that are not active and provides additional guidance for determining when the volume of trading level of activity for an asset or liability has significantly decreased and for identifying circumstances that indicate a transaction is not orderly. ASC 820-10-65 is effective for interim and annual reporting periods ending after June 15,

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2009. The adoption of ASC 820-10-65 for the three and six months ended December 31, 2010 and 2009, did not have any effect on our net asset value, financial position or results of operations as there was no change to the fair value measurement principles set forth in ASC 820.

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

Federal and State Income Taxes

We have elected to be treated as a regulated investment company and intend to continue to comply with the requirements of the Code, applicable to regulated investment companies. We are required to distribute at least 90% of our investment company taxable income and intend to distribute (or retain through a deemed distribution) all of our investment company taxable income and net capital gain to stockholders; therefore, we have made no provision for income taxes. The character of income and gains that we will distribute is determined in accordance with income tax regulations that may differ from GAAP. Book and tax basis differences relating to stockholder dividends and distributions and other permanent book and tax differences are reclassified to paid-in capital.

If we do not distribute (or are not deemed to have distributed) at least 98% of our annual taxable income in the calendar year earned, we will generally be required to pay an excise tax equal to 4% of the amount by which 98% of our annual taxable income exceeds the distributions from such taxable income for the year. To the extent that we determine that our estimated current year annual taxable income will be in excess of estimated current year dividend distributions from such taxable income, we accrue excise taxes, if any, on estimated excess taxable income as taxable income is earned using an annual effective excise tax rate. The annual effective excise tax rate is determined by dividing the estimated annual excise tax by the estimated annual taxable income.

We adopted FASB ASC 740, *Income Taxes* ("ASC 740"). 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 our tax returns to determine whether the tax positions are "more-likely-than-not" of being sustained by the applicable tax authority. Tax positions not deemed to meet the more-likely-than-not threshold are recorded as a tax benefit or expense in the current year. Adoption of ASC 740 was applied to all open tax years as of July 1, 2007. The adoption of ASC 740 did not have an effect on our net asset value, financial condition or results of operations as there was no liability for unrecognized tax benefits and no change to our beginning net asset value. As of December 31, 2010 and for the three and six months then ended, we did not have a liability for any unrecognized tax benefits. 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 on-going analysis of tax laws, regulations and interpretations thereof.

Revenue Recognition

Realized gains or losses on the sale of investments are calculated using the specific identification method. Interest income, adjusted for amortization of premium and accretion of discount, is recorded on an accrual basis. Origination, closing and/or commitment fees associated with investments in portfolio companies are accreted into interest income over the respective terms of the applicable loans. Upon the prepayment of a loan or debt security, any prepayment penalties and unamortized loan origination, closing and commitment fees are recorded as interest income.

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Loans are placed on non-accrual status when there is reasonable doubt that principal or interest will not be collected in accordance with the terms of the investment. Accrued interest is generally reversed when a loan is placed on non-accrual status. Interest payments received on non-accrual loans may be recognized as income or applied to principal depending upon management's judgment. Non-accrual loans are restored to accrual status when past due principal and interest is paid and in management's judgment, are likely to remain current. As of December 31, 2010, approximately 2.3% of our net assets are in non-accrual status.

Dividend income is recorded on the ex-dividend date.

Structuring fees and similar fees are recognized as income as earned, usually when paid. Structuring fees, excess deal deposits, net profits interests and overriding royalty interests are included in other income.

Dividends and Distributions

Dividends and distributions to common stockholders are recorded on the ex-dividend date. The amount, if any, to be paid as a monthly dividend or distribution is approved by our Board of Directors quarterly and is generally based upon our management's estimate of our earnings for the quarter. Net realized capital gains, if any, are distributed at least annually.

Financing Costs

We record origination expenses related to our credit facility and the 2010 Notes as deferred financing costs. These expenses are deferred and amortized as part of interest expense using the straight-line method for our revolving credit facility and the effective interest method for our 2010 Notes, over the respective stated life.

We record registration expenses related to shelf filings as prepaid assets. These expenses consist principally of SEC registration fees, legal fees and accounting fees incurred. These prepaid assets will be charged to capital upon the receipt of an equity offering proceeds or charged to expense if no offering completed.

2010 Notes

We have recorded the 2010 Notes (See Note 6 to our consolidated financial statements.) at their contractual amounts. The 2010 Notes were analyzed for any features that would require its accounting to be bifurcated and they were determined to be immaterial.

Guarantees and Indemnification Agreements

We follow FASB ASC 460, *Guarantees* ("ASC 460"). ASC 460 elaborates on the disclosure requirements of a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. It also requires a guarantor to recognize, at the inception of a guarantee, for those guarantees that are covered by ASC 460, the fair value of the obligation undertaken in issuing certain guarantees. ASC 460 did not have a material effect on the financial statements.

Per Share Information

Net increase or decrease in net assets resulting from operations per common share are calculated using the weighted average number of common shares outstanding for the period presented. In accordance with ASC 946, *Financial Services - Investment Companies*, convertible securities are not considered in the calculation of net assets per share.

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Recent Accounting Pronouncements

In June 2009, the FASB issued ASC 860, *Accounting for Transfers of Financial Assets – an amendment to FAS 140* ("ASC 860"). ASC 860 improves the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets: the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor's continuing involvement, if any, in transferred financial assets. ASC 860 is effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. The adoption of this standard had no effect on our results of operation or our financial position.

In June 2009, the FASB issued ASC 810, *Consolidation* ("ASC 810"). ASC 810 is intended to (1) address the effects on certain provisions of FASB Interpretation No. 46 (revised December 2003), Consolidation of Variable Interest Entities, as a result of the elimination of the qualifying special-purpose entity concept in ASC 860, and (2) constituent concerns about the application of certain key provisions of Interpretation 46(R), including those in which the accounting and disclosures under the Interpretation do not always provided timely and useful information about an enterprise's involvement in a variable interest entity. ASC 810 is effective as of the beginning of our first annual reporting period that begins after November 15, 2009. The adoption of this standard had no effect on our results of operation or our financial position.

In January 2010, the FASB issued Accounting Standards Update 2010-06, *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements* ("ASC 2010-06"). ASU 2010-06 amends ASC 820-10 and clarifies and provides additional disclosure requirements related to recurring and non-recurring fair value measurements and employers' disclosures about postretirement benefit plan assets. ASU 2010-06 is effective December 15, 2009, except for the disclosure about purchase, sales, issuances and settlements in the roll forward of activity in level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010 and for interim periods within those fiscal years. We do not believe that the adoption of the amended guidance in ASC 820-10 will have a significant effect on our financial statements.

In February 2010, the FASB issued Accounting Standards Update 2010-10, *Consolidation (Topic 810) – Amendments for Certain Investments Funds* ("ASU 2010-10"), which defers the application of the consolidation guidance in ASC 810 for certain investments funds. The disclosure requirements continue to apply to all entities. ASU 2010-10 is effective as of the beginning of the first annual period that begins after November 15, 2009 and for interim periods within that first annual period. The adoption of this standard had no effect on our results of operation or our financial position.

In August 2010, the FASB issued Accounting Standards Update 2010-21, *Accounting for Technical Amendments to Various SEC Rules and Schedules* ("ASU 2010-21"). This Accounting Standards Update various SEC paragraphs pursuant to the issuance of Release No. 33-9026: Technical Amendments to Rules, Forms, Schedules and Codification of Financial Reporting Policies. The adoption of this standard had no effect on our results of operation or our financial position.

In August 2010, the FASB issued Accounting Standards Update 2010-22, *Accounting for Various Topics – Technical Corrections to SEC Paragraphs* ("ASU 2010-22"). ASU 2010-22 amends various SEC paragraphs based on external comments received and the issuance of Staff Accounting Bulletin ("SAB") 112, which amends or rescinds portions of certain SAB topics. The adoption of this standard had no effect on our results of operation or our financial position.

In December 2010, the FASB issued Accounting Standards Update 2010-29, *Business Combinations (Topic 805) – Disclosure of Supplementary Pro Forma Information for Business Combinations (a consensus of the FASM Emerging Issues Task Force* ("ASU 2010-29"). ASU 2010-29 addresses diversity in practice

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about the interpretation of pro forma revenue and earnings disclosure requirements for business combinations. The amended guidance in ASU 2010-29 specifies that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination that occurred during the current year had occurred as of the beginning of the comparable prior reporting period only. This standard also expands the supplemental pro forma disclosures under ASC 805 to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. The amendments in ASU 2010-29 are effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010, with early adoption permitted. Our management does not believe that the adoption of the amended guidance in ASU 2010-29 will have a significant effect on our financial statements

Patriot Acquisition

On December 2, 2009, we acquired the outstanding shares of Patriot Capital Funding, Inc. ("Patriot") common stock for \$201,083. Under the terms of the merger agreement, Patriot common shareholders received 0.363992 shares of our common stock for each share of Patriot common stock, resulting in 8,444,068 shares of common stock being issued by us. In connection with the transaction, we repaid all the outstanding borrowings of Patriot, in compliance with the merger agreement.

On December 2, 2009, Patriot made a final dividend equal to its undistributed net ordinary income and capital gains of \$0.38 per share. In accordance with a recent IRS revenue procedure, the dividend was paid 10% in cash and 90% in newly issued shares of Patriot's common stock. The exchange ratio was adjusted to give effect to the final income distribution.

The merger has been accounted for as an acquisition of Patriot by Prospect Capital Corporation ("Prospect") in accordance with acquisition method of accounting as detailed in Accounting Standards Codification ("ASC" or "Codification") 805, *Business Combinations* ("ASC 805"). The fair value of the consideration paid was allocated to the assets acquired and liabilities assumed based on their fair values as the date of acquisition. As described in more detail in ASC 805, goodwill, if any, would have been recognized as of the acquisition date, if the consideration transferred exceeded the fair value of identifiable net assets acquired. As of the acquisition date, the fair value of the identifiable net assets acquired exceeded the fair value of the consideration transferred, and we recognized the excess as a gain. A preliminary gain of \$5,714 was recorded by Prospect in the quarter ended December 31, 2009 related to the acquisition of Patriot, which was revised in the fourth quarter of Fiscal 2010, to \$7,708, when we settled severance accruals related to certain members of Patriot's top management, and finalized during the first quarter of Fiscal 2011, to \$8,632, when we settled the remaining severance accruals related to the last two members of Patriot's top management. Under ASC 805, the adjustments to our preliminary estimates were reflected in the three months ended December 31, 2009 (See Note 13 to our consolidated financial statements.). The acquisition of Patriot was negotiated in July 2009 with the purchase agreement being signed on August 3, 2009. Between July 2009 and December 2, 2009, our valuation of certain of the investments acquired from Patriot increased due to market improvement, which resulted in the recognition of the gain at closing.

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The purchase price has been allocated to the assets acquired and the liabilities assumed based on their estimated fair values as summarized in the following table:

Cash (to repay Patriot debt)	\$ 107,313
Cash (to fund purchase of restricted stock from former Patriot employees)	970
Common stock issued(1)	92,800
Total purchase price	201,083
Assets acquired:	
Investments(2)	207,126
Cash and cash equivalents	1,697
Other assets	3,859
Assets acquired	212,682
Other liabilities assumed	(2,967)
Net assets acquired	209,715
Gain on Patriot acquisition(3)	\$ 8,632

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- (1) The value of the shares of common stock exchanged with the Patriot common shareholders was based upon the closing price of our common stock on December 2, 2009, the price immediately prior to the closing of the transaction.
- (2) The fair value of Patriot's investments was determined by the Board of Directors in conjunction with an independent valuation agent. This valuation resulted in a purchase price which was \$98,150 below the amortized cost of such investments. For those assets which are performing, Prospect will record the accretion to par value in interest income over the remaining term of the investment.
- (3) The gain has been determined after the final payments of certain liabilities have been settled.

During the three and six months ended December 31, 2010, we recognized \$1,305 and \$5,353 of interest income due to purchase discount accretion from the assets acquired from Patriot, respectively. Included in the \$5,353 for the six months ended December 31, 2010, is \$1,116 of accelerated accretion resulting from the repayment of Impact Products, LLC ("Impact"). We also recapitalized our debt investment in Northwestern Management Services, LLC ("Northwestern"), which precipitated the acceleration of \$1,612 of original purchase discount. There was no accelerated accretion recorded during the quarter ended December 31, 2010. As of December 31, 2010, \$25,777 of purchase discount from the Patriot acquisition remains to be accreted.

During the period from the acquisition of Patriot on December 2, 2009 to December 31, 2009, we recognized \$7,495 of interest income from the assets acquired from Patriot. Included in this amount is \$4,560 resulting from the acceleration of purchase discounts from the early repayments of three loans, three revolving lines of credit and the sale of one investment position.

Investment Holdings

As of December 31, 2010, we continue to pursue our investment strategy. Despite our name change to "Prospect Capital Corporation" and the termination of our policy to invest at least 80% of our net assets in energy companies in May 2007, we currently have a concentration of investments in companies in the energy and energy related industries. Some of the companies in which we invest have relatively short or no operating histories. These companies are and will be subject to all of the business risk and uncertainties associated with any new business enterprise, including the risk that these companies may not reach their investment objective or the value of our investment in them may decline substantially or fall to zero.

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During the six months ended December 31, 2010, we have originated \$281,884 of new investments. Our origination efforts recently have focused primarily on secured lending, including a higher percentage of first lien loans than in recent prior fiscal quarters, though we also continue to close selected junior debt and equity investments. In addition to targeting investments senior in corporate capital structures with our new originations, we have also increased our origination business mix of third party private equity sponsor owned companies, which tend to have more third party equity capital supporting our debt investments than non sponsor transactions. As a result of these credit risk management initiatives, as well as a decrease in the dividends received from Gas Solutions Holdings, Inc. ("GSHI"), our portfolio's annualized current yield decreased from 15.7% to 14.1% across all long-term debt and certain equity investments as of December 31, 2009 and December 31, 2010, respectively. The decrease in dividends from GSHI is primarily the result of GSHI distributing dividends in excess of their current earnings in 2009, as GSHI had accumulated excess earnings and profits available for distribution. GSHI remains profitable and has increased its EBITDA in 2010 in comparison with 2009. We anticipate that GSHI may be able to increase its dividends in the future as the result of organic growth and add-on acquisitions. We expect Prospect's current asset yield may decline modestly over the next few quarters as we increase the size of the portfolio while reducing credit risk. Monetization of other equity positions that we hold is not included in this yield calculation. In each of our portfolio companies, we hold equity positions, ranging from minority interests to majority stakes, which we expect over time to contribute to our investment returns. Some of these equity positions include features such as contractual minimum internal rates of returns, preferred distributions, flip structures and other features expected to generate additional investment returns, as well as contractual protections and preferences over junior equity, in addition to the yield and security offered by our cash flow and collateral debt protections.

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

As of December 31, 2010, we own controlling interests in AIRMALL USA, Inc. ("AIRMALL"), Ajax Rolled Ring & Machine, Inc. ("Ajax"), AWCNC, LLC, Borga, Inc., C&J Cladding, LLC ("C&J"), Change Clean Energy Holdings, Inc. ("CCEHI"), Fischbein, LLC ("Fischbein"), Freedom Marine Services LLC, GSHI, Integrated Contract Services, Inc. ("ICS"), Iron Horse Coiled Tubing, Inc. ("Iron Horse"), Manx Energy, Inc. ("Manx"), NRG, Nupla Corporation, R-V Industries ("R-V"), Inc. and Yatesville Coal Holdings, Inc. ("Yatesville"). We also own an affiliated interest in Biotronic NeuroNetwork ("Biotronic"), Boxercraft Incorporated, KTPS Holdings, LLC ("KTPS"), Smart, LLC, and Sport Helmets Holdings, LLC.

The following is a summary of our investment portfolio by level of control:

Level of Control	December 31, 2010				June 30, 2010			
	Cost	Percent of Portfolio	Fair Value	Percent of Portfolio	Cost	Percent of Portfolio	Fair Value	Percent of Portfolio
Control	\$ 235,729	23.2%	\$ 264,228	25.2%	\$ 185,720	23.3%	\$ 195,958	24.0%
Affiliate	65,815	6.5%	74,709	7.1%	65,082	8.2%	73,740	9.0%
Non-control/Non-affiliate	584,524	57.3%	579,284	55.1%	477,957	59.9%	478,785	58.6%
Money Market Funds	132,194	13.0%	132,194	12.6%	68,871	8.6%	68,871	8.4%
Total Portfolio	\$ 1,018,262	100.0%	\$ 1,050,415	100.0%	\$ 797,630	100.0%	\$ 817,354	100.0%

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The following is our investment portfolio presented by type of investment at December 31, 2010 and June 30, 2010, respectively:

Type of Investment	December 31, 2010				June 30, 2010			
	Cost	Percent of Portfolio	Fair Value	Percent of Portfolio	Cost	Percent of Portfolio	Fair Value	Percent of Portfolio
Money Market Funds	\$ 132,194	13.0%	\$ 132,194	12.6%	\$ 68,871	8.6%	\$ 68,871	8.4%
Revolving Line of Credit	3,721	0.4%	3,841	0.4%	4,754	0.6%	5,017	0.6%
Senior Secured Debt	434,276	42.6%	406,756	38.7%	313,755	39.4%	287,470	35.2%
Subordinated Secured Debt	338,413	33.2%	316,485	30.1%	333,453	41.8%	313,511	38.4%
Subordinated Unsecured Debt	54,413	5.3%	54,840	5.2%	30,209	3.8%	30,895	3.8%
Preferred Stock	27,468	2.7%	18,258	1.7%	16,969	2.1%	5,872	0.7%
Common Stock	19,003	1.9%	81,497	7.8%	20,243	2.5%	77,131	9.4%
Membership Interests	5,921	0.6%	23,933	2.3%	6,964	0.9%	17,730	2.2%
Overriding Royalty Interests		%	2,250	0.2%		%	2,768	0.3%
Net Profit Interests		%	191	%		%	1,020	0.1%
Warrants	2,853	0.3%	10,170	1.0%	2,412	0.3%	7,069	0.9%
Total Portfolio	\$ 1,018,262	100.0%	\$ 1,050,415	100.0%	\$ 797,630	100.0%	\$ 817,354	100.0%

The following is our investment portfolio presented by geographic location of the investment at December 31, 2010 and June 30, 2010, respectively:

Geographic Location	December 31, 2010				June 30, 2010			
	Cost	Percent of Portfolio	Fair Value	Percent of Portfolio	Cost	Percent of Portfolio	Fair Value	Percent of Portfolio
Canada	\$ 18,387	1.8%	\$ 18,993	1.8%	\$ 21,002	2.6%	\$ 12,054	1.5%
Ireland	14,905	1.5%	15,000	1.4%	14,903	1.9%	15,000	1.8%
Netherlands		%		%	1,397	0.2%	1,233	0.2%
Midwest US	212,829	20.9%	208,736	19.9%	170,869	21.5%	167,571	20.5%
Northeast US	115,449	11.3%	118,932	11.3%	61,813	7.7%	62,727	7.7%
Southeast US	161,124	15.8%	146,218	13.9%	193,420	24.2%	171,144	20.9%
Southwest US	189,368	18.6%	238,197	22.7%	179,641	22.6%	235,945	28.9%
Western US	174,006	17.1%	172,145	16.4%	85,714	10.7%	82,809	10.1%
Money Market Funds	132,194	13.0%	132,194	12.6%	68,871	8.6%	68,871	8.4%
Total Portfolio	\$ 1,018,262	100.0%	\$ 1,050,415	100.0%	\$ 797,630	100.0%	\$ 817,354	100.0%

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The following is our investment portfolio presented by industry sector of the investment at December 31, 2010 and June 30, 2010, respectively:

Industry	December 31, 2010				June 30, 2010			
	Cost	Percent of Portfolio	Fair Value	Percent of Portfolio	Cost	Percent of Portfolio	Fair Value	Percent of Portfolio
Aerospace and Defense	\$ 56	%	34	%	\$ 56	%	38	%
Automobile	17,454	1.8%	17,767	1.7%	19,017	2.4%	18,615	2.3%
Biomass Power	2,540	0.2%		%	2,383	0.3%		%
Business Services	12,148	1.2%	12,358	1.2%	12,060	1.5%	12,132	1.5%
Chemicals	25,026	2.5%	25,026	2.4%	1,397	0.2%	1,233	0.2%
Consumer Services	35,820	3.5%	35,820	3.4%		%		%
Contracting	16,712	1.7%	1,370	0.1%	16,652	2.1%	4,542	0.6%
Durable Consumer Products	52,332	5.1%	52,587	5.0%	20,000	2.5%	20,000	2.4%
Ecological	141	%	325	%	141	%	340	%
Electronics	24,265	2.4%	24,721	2.4%	25,777	3.2%	25,629	3.1%
Financial Services		%		%	25,814	3.2%	25,592	3.1%
Food Products	62,076	6.1%	70,463	6.7%	53,681	6.7%	60,882	7.4%
Gas Gathering and Processing	42,003	4.1%	97,596	9.3%	37,503	4.7%	93,096	11.4%
Healthcare	101,230	9.9%	109,722	10.4%	89,026	11.2%	93,593	11.5%
Home and Office Furnishings, Housewares and Durable	2,057	0.2%	5,370	0.5%	14,112	1.8%	17,232	2.1%
Insurance	6,076	0.6%	6,506	0.6%	5,811	0.7%	5,952	0.7%
Machinery	12,997	1.4%	22,148	2.1%	15,625	2.0%	17,776	2.2%
Manufacturing	72,381	7.1%	63,640	6.1%	74,961	9.4%	64,784	7.9%
Metal Services and Minerals	13,348	1.3%	28,659	2.7%	19,252	2.4%	33,620	4.1%
Mining, Steel, Iron and Non-Precious Metals and Coal Production	1,435	0.1%		%	1,130	0.1%	808	0.1%
Oil and Gas Production	123,868	12.2%	87,382	8.3%	122,034	15.3%	96,988	11.9%
Oilfield Fabrication	26,326	2.6%	26,326	2.5%	30,429	3.8%	30,429	3.7%
Personal and Nondurable Consumer Products	15,234	1.5%	21,010	2.0%	14,387	1.8%	20,049	2.5%
Pharmaceuticals		%		%	11,955	1.5%	12,000	1.5%
Printing and Publishing	5,255	0.5%	5,385	0.5%	5,222	0.7%	5,284	0.6%
Property Management	52,420	5.1%	55,796	5.3%		%		%
Production Services	18,387	1.8%	18,993	1.8%	21,002	2.6%	12,054	1.5%
Retail	14,669	1.5%	1,452	0.1%	14,669	1.8%	2,148	0.3%
Shipping Vessels	10,367	1.0%	3,649	0.4%	10,040	1.3%	3,583	0.4%
Software & Computer Services	37,885	3.7%	38,000	3.6%	14,903	1.9%	15,000	1.8%
Specialty Minerals	30,000	2.9%	33,253	3.2%	15,814	2.1%	18,463	2.3%
Technical Services	11,401	1.1%	11,500	1.1%	11,387	1.4%	11,615	1.4%
Textiles and Leather								