
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549**

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2010

OR

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

For the transition period from _____ to _____

Commission file number 001-33559

BLACKROCK KELSO CAPITAL CORPORATION

(Exact Name of Registrant as Specified in Its Charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

40 East 52nd Street, New York, New York
(Address of Principal Executive Offices)

20-2725151
(I.R.S. Employer
Identification No.)

10022
(Zip Code)

Registrant's Telephone Number, Including Area Code: 212-810-5800

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, par value \$.001 per share	The NASDAQ Global Select Market

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT: None

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

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

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

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

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

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

Large Accelerated Filer Accelerated Filer Non-Accelerated Filer

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Securities Exchange Act of 1934). Yes No

The aggregate market value of the Registrant's common stock held by non-affiliates of the Registrant at June 30, 2010 (the last business day of the Registrant's most recently completed second quarter) was \$439,302,560 based upon the last sales price reported for such date on The NASDAQ Global Select Market. For purposes of this disclosure, shares of common stock beneficially owned by persons who own 5% or more of the outstanding shares of common stock and shares beneficially owned by executive officers and directors of the Registrant and members of their families have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily conclusive for other purposes. The Registrant has no non-voting common stock.

There were 72,780,636 shares of the Registrant's common stock outstanding at March 7, 2011.

Documents Incorporated by Reference: Portions of the Registrant's Proxy Statement relating to the Registrant's 2011 Annual Meeting of Stockholders to be filed not later than 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K are incorporated by reference into Part III of this Report.

[Table of Contents](#)

BLACKROCK KELSO CAPITAL CORPORATION
2010 FORM 10-K ANNUAL REPORT

TABLE OF CONTENTS

	PAGE
Part I	3
Item 1. Business	3
Item 1A. Risk Factors	17
Item 1B. Unresolved Staff Comments	33
Item 2. Properties	33
Item 3. Legal Proceedings	33
Item 4. [Reserved]	33
Part II	34
Item 5. Market For Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	34
Item 6. Selected Financial Data	37
Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations	38
Item 7A. Quantitative and Qualitative Disclosure About Market Risk	48
Item 8. Financial Statements and Supplementary Data	48
Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure	48
Item 9A. Controls and Procedures	48
Item 9B. Other Information	51
Part III	52
Item 10. Directors, Executive Officers and Corporate Governance	52
Item 11. Executive Compensation	52
Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholders Matters	52
Item 13. Certain Relationships and Related Transactions, and Director Independence	52
Item 14. Principal Accountant Fees and Services	52
Part IV	53
Item 15. Exhibits and Financial Statement Schedules	53
Signatures	

PART I

ITEM 1. BUSINESS

General

BlackRock Kelso Capital Corporation (“BlackRock Kelso,” the “Company” or the “Registrant,” which may also be referred to as “we,” “us” or “our”) provides middle-market companies with flexible financing solutions, including senior and junior secured, unsecured and subordinated debt securities and loans, and equity securities. Our strategy is to provide capital to meet our clients’ current and future needs across this spectrum, creating long-term partnerships with growing middle-market companies.

We are organized as an externally-managed, non-diversified closed-end management investment company. We have elected to be regulated as a business development company, or BDC, under the Investment Company Act of 1940, which we refer to as the 1940 Act. In addition, for tax purposes we intend to continue to qualify as a regulated investment company, or RIC, under the Internal Revenue Code of 1986, which we refer to as the Code.

Our investment objective is to generate both current income and capital appreciation through our debt and equity investments. We invest primarily in middle-market companies and target investments throughout the capital structure that we believe provide an attractive risk-adjusted return. The term “middle-market” refers to companies with annual revenues typically between \$50 million and \$1 billion. Our targeted investment typically ranges between \$10 million and \$50 million, although the investment sizes may be more or less than the targeted range and the size of our investments may grow with our capital availability. We generally seek to invest in companies that operate in a broad variety of industries and that generate positive cash flows.

Although most of our investments are in senior and junior secured, unsecured and subordinated loans to U.S. private and certain public middle-market companies, we invest throughout the capital structure, which may include common and preferred equity, options and warrants, credit derivatives, high-yield bonds, distressed debt and other structured securities. We may from time to time invest up to 30% of our assets opportunistically in other types of investments, including securities of other public companies and foreign securities.

The senior and junior secured loans in which we invest generally have stated terms of three to ten years and the subordinated debt investments we make generally have stated terms of up to ten years, but the expected average life of such senior and junior secured loans and subordinated debt is generally between three and seven years. However, we may invest in securities of any maturity or duration. The debt that we invest in typically is not initially rated by any rating agency, but we believe that if such investments were rated, they would be below investment grade (rated lower than “Baa3” by Moody’s Investors Service, lower than “BBB-” by Fitch Ratings or lower than “BBB-” by Standard & Poor’s). We may invest without limit in debt of any rating, as well as debt that has not been rated by any nationally recognized statistical rating organization.

We were incorporated on April 13, 2005, commenced operations with private funding on July 25, 2005, and completed our initial public offering on July 2, 2007. Since the commencement of our operations, the team of investment professionals of BlackRock Kelso Capital Advisors LLC (the “Advisor” or “BlackRock Kelso Capital Advisors”), including our senior management, has evaluated more than 1,800 investment opportunities and completed 117 investments, aggregating over \$2.2 billion in capital provided to middle-market companies through December 31, 2010.

During the year ended December 31, 2010, we invested approximately \$406.0 million across eight new and several existing portfolio companies. This compares to \$46.8 million across several existing portfolio companies for the year ended December 31, 2009. Sales, repayments and other exits of investment principal totaled \$395.3 million during the year ended December 31, 2010, versus \$128.2 million during the year ended December 31, 2009.

At December 31, 2010, our net portfolio consisted of 50 portfolio companies and was invested 50% in senior secured loans, 26% in unsecured or subordinated debt securities, 14% in equity investments, 10% in senior secured notes and less than 1% in cash and cash equivalents. This compares to our portfolio of 57 companies that was invested 59% in senior secured loans, 30% in unsecured or subordinated debt securities, 6% in senior secured notes, 5% in equity investments and less than 1% in cash and cash equivalents at December 31, 2009. Our average portfolio company investment at amortized cost was approximately \$19.7 million at December 31, 2010, versus \$18.5 million at December 31, 2009.

The weighted average yield of the debt and income producing equity securities in our portfolio at fair value was 12.4% at December 31, 2010 and 13.7% at December 31, 2009. The weighted average yields on our senior secured loans

[Table of Contents](#)

and other debt securities at fair value were 11.3% and 14.3%, respectively, at December 31, 2010, versus 11.6% and 17.2% at December 31, 2009. The weighted average yield of the debt and income producing equity securities in our portfolio at their current cost basis was 10.9% at December 31, 2010 and 11.2% at December 31, 2009. The weighted average yields on our senior secured loans and other debt securities at their current cost basis were 10.1% and 12.1%, respectively, at December 31, 2010, versus 9.4% and 14.2% at December 31, 2009.

BlackRock Kelso Capital Advisors

Our investment activities are managed by the Advisor. The Advisor is responsible for sourcing potential investments, conducting research on prospective investments, analyzing investment opportunities, structuring our investments, and monitoring our investments and portfolio companies on an ongoing basis. The Advisor is led by James R. Maher, Chairman and Chief Executive Officer of the Company and the Advisor, and Michael B. Lazar, Chief Operating Officer of the Company and the Advisor. They are supported by the Advisor's team of employees, including 13 investment professionals who have extensive experience in commercial lending, investment banking, accounting, corporate law and private equity investing.

The Advisor has an investment committee comprised of 12 members, including Messrs. Maher and Lazar, several senior executives of BlackRock, Inc. ("BlackRock") and several of the principals of Kelso & Company, L.P. (the "Kelso Principals"). The investment committee is responsible for approving our investments. We benefit from the extensive and varied relevant experience of the BlackRock executives and the Kelso Principals serving on the investment committee. Although the BlackRock executives and Kelso Principals who serve on the investment committee bring the benefit of expertise they have gained at BlackRock, Kelso & Company, L.P. ("Kelso") and elsewhere, neither of those organizations provides us with investment advice. Nevertheless, we benefit from the business and specific industry knowledge, transaction expertise and deal-sourcing capabilities of BlackRock. The Kelso Principals who serve on the investment committee bring the benefit of the expertise they gained at Kelso and elsewhere, including providing access to a broad network of contacts.

BlackRock is a leader in investment management, risk management and advisory services for institutional and retail clients worldwide. At December 31, 2010, BlackRock's assets under management were \$3.561 trillion. BlackRock offers products that span the risk spectrum to meet clients' needs, including active, enhanced and index strategies across markets and asset classes. Products are offered in a variety of structures including separate accounts, mutual funds, iShares® (exchange traded funds), and other pooled investment vehicles. BlackRock also offers risk management, advisory and enterprise investment system services to a broad base of institutional investors through BlackRock Solutions®.

The Kelso Principals have an average tenure of at least nineteen years at Kelso. Kelso is a leading private equity firm and since 1980 has raised over \$10 billion of committed private equity capital, investing primarily in middle-market companies across a broad range of industries and through different economic and interest rate environments. Kelso was organized in 1971 and has since made investments in over 110 companies with aggregate initial capitalization of over \$38 billion. The firm typically makes investments in companies where key managers make significant investments and works in partnership with management teams to create value for investors. Through our relationship with the Kelso Principals, we have access to these management teams who can provide unique insight into the industries in which they operate. Although the Kelso Principals who serve on the investment committee bring the benefit of the expertise they have gained at Kelso and elsewhere, Kelso as an organization does not participate in the activities of the Advisor or advise us.

Our executive officers and directors and the employees of the Advisor and members of its investment committee serve or may serve as investment advisors, officers, directors or principals of entities or investment funds that operate in the same or a related line of business as we do and/or investment funds managed by our affiliates. We note that any affiliated investment vehicle currently formed or formed in the future and managed by the Advisor or its affiliates may have overlapping investment objectives with our own and, accordingly, may invest in asset classes similar to those targeted by us. As a result, the Advisor and/or its affiliates may face conflicts in allocating investment opportunities between us and such other entities. Accordingly, we may not be given the opportunity to participate in certain investments made by investment funds managed by advisors affiliated with the Advisor. However, the Advisor and its affiliates will endeavor to allocate investment opportunities in a fair and equitable manner and consistent with applicable allocation procedures. In any such case, if the Advisor forms other affiliates in the future, we may co-invest on a concurrent basis with such other affiliates, subject to compliance with applicable regulations and regulatory guidance, as well as applicable allocation procedures. In certain circumstances, negotiated co-investments may be made only if we receive an order from the United States Securities and Exchange Commission, or the SEC, permitting us to do so.

[Table of Contents](#)

Administration

BlackRock, through its subsidiary, BlackRock Financial Management, Inc. (the “Administrator”), serves as our administrator and provides us with office space, equipment and office services. The Administrator oversees our financial records, assists in the preparation of reports to our stockholders and reports filed with the SEC, and generally monitors the payment of our expenses and the performance of administrative and professional services rendered to us by others.

Market opportunity

We believe there are abundant opportunities for investments in middle-market companies with attractive risk-adjusted returns for several reasons, including:

The current market environment may mean more favorable terms for investments in middle-market companies. We believe the tight supply of all forms of credit due to deleveraging by banks, hedge funds and structured investment vehicles, such as collateralized loan obligation (CLO) funds, will remain for years and that this situation provides a promising environment in which to originate investments in middle-market companies. We believe we are able to structure investments with lower leverage multiples, higher current returns, greater opportunity for equity appreciation, better prepayment protection, tighter deal structures and more meaningful financial covenants than were typical previously.

Middle-market companies have faced increasing difficulty in accessing the capital markets. While many middle-market companies were formerly able to raise funds by issuing high-yield bonds, we believe this approach to financing has become more difficult, as commercial and investment banks are capital-constrained.

There is a large pool of uninvested private equity capital likely to seek additional capital to support private investments. We believe there is a large pool of uninvested private equity capital available to middle-market companies. We expect that private equity firms will be active investors in middle-market companies and that these private equity firms will seek to supplement their equity investments with senior secured and junior loans and equity co-investments from other sources, such as us. Since our commencement of operations in July 2005, the Advisor has invested in transactions involving more than 70 private equity firms in 117 different portfolio companies. We believe that our extensive relationships with private equity firms and other deal sourcing contacts is a competitive advantage and a source for future investment opportunities.

Middle-market companies are increasingly seeking private sources for debt and equity capital. We believe that many middle-market companies prefer to execute transactions with private capital providers such as us, rather than execute high-yield bond or equity transactions in the public markets, which may necessitate increased financial and regulatory compliance and reporting obligations.

Consolidation among commercial banks has reduced the focus on middle-market business. We believe that many senior lenders have de-emphasized their service and product offerings to middle-market companies in favor of lending to large corporate clients, managing capital markets transactions and providing other non-credit services to their customers.

Competitive advantages

We believe we possess the following competitive advantages over many other capital providers to middle-market companies:

Demonstrated ability to deploy capital consistent with our investment policies. Since our inception, the Advisor has invested in excess of \$2.2 billion across 117 portfolio companies with 70 financial sponsors. We have a portfolio yield at fair value of approximately 12.4% at December 31, 2010. In 2010, we invested approximately \$406.0 million of gross assets across eight new and several existing portfolio companies.

Proven transaction sourcing strategy. Since the Advisor’s inception of operations, it has sourced and reviewed more than 1,800 potential investments and has a proven process through which it has invested in excess of \$2.2 billion through December 31, 2010. The Advisor identifies potential investments through its dynamic transaction origination efforts. The origination efforts include calling on financial institutions such as investment banks, commercial banks, specialty finance companies and private equity firms; as well as on advisory firms, trade associations and the owners and managers of middle-market companies with whom its investment professionals and investment committee members have relationships. In addition to its investment professionals, senior members of the Advisor’s investment committee have relationships with a large and diverse group of financial intermediaries. We expect that our ability to leverage these relationships will continue to result in the referral of investment opportunities to us and provide us with a competitive advantage.

[Table of Contents](#)

Access to BlackRock and Kelso Principals' broad investing capabilities. Our Advisor's relationship with BlackRock and the Kelso Principals provides access to extensive expertise across asset classes. The Advisor's investment committee, which is comprised of individuals from BlackRock Kelso Capital Advisors, BlackRock and the Kelso Principals, and its team of dedicated investment professionals have had extensive experience in fixed-income, public equity and private equity investing. The Advisor has access to BlackRock's more than 130 investment professionals in traditional fixed income and alternative portfolios, including an over 30-person leveraged finance team. Collectively, members of the investment committee and the investment professionals of the Advisor have had experience investing in nearly every industry group in small, middle and large capitalization companies and at every level of the capital structure.

Highly experienced investment team. Our investment activities are carried out by BlackRock Kelso Capital Advisors and led by James R. Maher and Michael B. Lazar with guidance from the Advisor's investment committee. The investment committee is comprised of senior members of BlackRock and the Kelso Principals. Members of the investment committee and the Advisor's investment professionals have significant experience investing across market cycles and possess a broad range of transaction, financial, managerial and investment skills. Collectively, their involvement in our investment process provides us with substantial market insight and valuable access to investment opportunities. This insight and judgment enables us to achieve favorable risk-adjusted rates of return on the capital we deploy.

Disciplined investment process with focus on preservation of capital. In making investment decisions, the Advisor employs a disciplined and selective review process that focuses on, among other things, a thorough analysis of the underlying issuer's business and the performance drivers of that business, as well as an assessment of the legal and economic features of each particular investment. As part of its review process, the Advisor draws on the industry expertise of its investment professionals, as well as on that of the members of its investment committee and BlackRock's credit research analysts. Though each transaction involves a somewhat different approach, the Advisor undertakes a thorough due diligence analysis that leverages the capabilities of BlackRock and the Kelso Principals, including, for example, assessing business and industry prospects, conducting competitive analysis and meeting with management teams to get an insider's view of the business or industry. This enables the Advisor to consider the total return on investment when evaluating each prospective portfolio company, seeking to minimize the risk of capital loss without forgoing potential for capital appreciation.

Cost-effective and high quality infrastructure. We benefit from the existing infrastructure and administrative capabilities of BlackRock. BlackRock serves as our administrator and provides us with office space, equipment and office services. It oversees our financial records, assists in the preparation of reports to our stockholders and reports filed with the SEC, and generally monitors the payment of our expenses and the performance of administrative and professional services rendered to us by others. The BlackRock organization has over 20 years of experience managing closed-end investment products. Our relationship with BlackRock grants us access to BlackRock's fund administration platform which we believe provides higher quality service and lower cost than traditionally available in the industry.

Operating and regulatory structure

Our investment activities are managed by the Advisor and supervised by our Board of Directors, a majority of whom are independent of the Advisor, BlackRock, the Kelso Principals and their respective affiliates. The Advisor is registered under the Investment Advisers Act of 1940, or the Advisers Act. Under our investment management agreement, we have agreed to pay the Advisor an annual base management fee based on our total assets, as well as an incentive management fee based on our performance. The investment management agreement also provides that we will reimburse the Advisor for costs and expenses incurred by the Advisor for office space rental, office equipment and utilities allocable to the Advisor under that agreement, as well as any costs and expenses incurred by the Advisor relating to any non-investment advisory, administrative or operating services provided by the Advisor to us.

Also, while we may borrow funds to make investments, our ability to use debt is limited in certain significant respects. As a BDC and a RIC for tax purposes, we are dependent on our ability to raise capital through the issuance of our common stock. RICs generally must distribute substantially all of their earnings to stockholders as dividends in order to achieve pass-through tax treatment, which prevents us from using those earnings to support operations, which may include new investments (including investments into existing portfolio companies). Further, BDCs must maintain an asset coverage ratio (the ratio of total assets less total liabilities other than indebtedness to total indebtedness) of not less than 200% in order to incur debt or issue senior securities, meaning generally that for every dollar of debt incurred or senior securities issued, we must have two dollars of assets. Our existing debt arrangements also require that we maintain an asset coverage ratio of not less than 200%, among other things.

[Table of Contents](#)

Portfolio composition

We have built an investment portfolio that includes senior and junior secured, senior and junior unsecured and subordinated loans to U.S. private middle-market companies. We invest a range of \$10 million to \$50 million of capital, on average, per transaction, although the investment sizes may be more or less and are expected to grow with our capital availability. Although most of our investments are in senior and junior secured, senior and junior unsecured and subordinated loans to U.S. private and certain public middle-market companies, we invest throughout the capital structure of these companies in other securities, which may include common and preferred equity, options and warrants, credit derivatives, high-yield bonds, distressed debt and other structured securities. We generally seek to invest in companies that operate in a broad variety of industries and that generate positive cash flows. While our focus is to generate current income through these investments, we also seek capital appreciation.

At December 31, 2010, our net portfolio of 50 portfolio companies was invested 50% in senior secured loans, 26% in unsecured or subordinated debt securities, 14% in equity investments, 10% in senior secured notes and less than 1% in cash and cash equivalents.

The industry composition of our portfolio at December 31, 2010 and 2009 was as follows:

Industry	December 31,	
	2010	2009
Personal and Other Services	13.8%	9.4%
Business Services	11.8	12.6
Healthcare	10.6	10.0
Printing, Publishing and Media	8.5	3.2
Consumer Products	7.6	6.0
Manufacturing	7.1	7.6
Distribution	6.3	4.8
Electronics	6.1	8.5
Building and Real Estate	5.2	1.0
Financial Services	4.9	4.6
Automotive	4.5	—
Chemicals	4.4	4.4
Retail	4.0	4.6
Containers and Packaging	3.2	2.7
Beverage, Food and Tobacco	0.8	4.0
Entertainment and Leisure	0.8	2.6
Transportation	0.4	6.3
Metals	—	4.1
Utilities	—	3.6
Total	<u>100.0%</u>	<u>100.0%</u>

The geographic composition of our portfolio at fair value at December 31, 2010 was United States 94.7% and Canada 5.3%, and at December 31, 2009 was United States 93.7%, Canada 6.3% and United Kingdom and other less than 0.1%. The geographic composition is determined by the location of the corporate headquarters of the portfolio company.

We generally are not permitted to invest in any private company in which any of our affiliates holds an existing investment, except to the extent permitted by the 1940 Act. We may, however, co-invest on a concurrent basis with our affiliates, subject to compliance with applicable regulations and regulatory guidance, as well as applicable allocation procedures. We may invest, to the extent permitted by law, in the securities and instruments of other investment companies, including private funds.

Investment selection criteria

The Advisor chooses investments and constructs our portfolio based on the investment experience of its professionals and a detailed investment analysis for each investment opportunity. In analyzing each prospective portfolio company, the Advisor has identified several criteria it believes are important in identifying and investing in prospective portfolio companies. These criteria provide general guidelines for the Advisor's investment decisions on our behalf, although each prospective portfolio company may fail to meet one or more of these criteria. Generally, the Advisor seeks to utilize its access to information generated by its investment professionals and investment committee members to identify investment candidates and to structure investments quickly and effectively.

[Table of Contents](#)

Value Orientation/Positive Cash Flow. The Advisor's investment philosophy places a premium on fundamental analysis from an investor's perspective and has a distinct value orientation. The Advisor focuses on companies in which it can invest at relatively low multiples of operating cash flow and that are profitable at the time of investment on an operating cash flow basis. Typically, the Advisor does not invest in start-up companies or companies having speculative business plans.

Experienced Management. The Advisor generally requires that portfolio companies have an experienced management team. The Advisor also generally requires portfolio companies to have in place proper incentives to induce management to succeed and to act in concert with our interests as investors, which may include having significant equity interests.

Strong Competitive Position in Industry. The Advisor seeks to invest in companies that have strong market positions within their respective markets or market niches and are well positioned to capitalize on growth opportunities. The Advisor seeks companies that demonstrate significant competitive advantages versus their competitors, which it believes should help to protect their market position and profitability.

Exit Strategy. The Advisor seeks to invest in companies that it believes will provide a steady stream of cash flow to repay loans and/or build equity value. With respect to loans and debt securities, the Advisor expects that such internally generated cash flow, leading to the payment of interest on, and the repayment of the principal of, our investments will be a key means by which we exit these investments over time. In addition, the Advisor also seeks to invest in companies whose business models and expected future cash flows offer attractive exit possibilities. These companies include candidates for strategic acquisition by other industry participants and companies that may repay our investments through an initial public offering of common stock or another capital market transaction. With respect to our equity investments, the Advisor will look to exit such investments via repurchases by the portfolio company, public offerings and sales pursuant to merger and acquisition transactions.

Liquidation Value of Assets. The prospective liquidation value of the assets, if any, collateralizing loans in which we invest is an important factor in the Advisor's credit analysis. The Advisor emphasizes both tangible assets, such as accounts receivable, inventory, equipment and real estate, and intangible assets, such as intellectual property, customer lists, networks and databases.

Generally, the Advisor utilizes access to information generated by its investment professionals to identify investment candidates and to structure investments quickly and effectively. Furthermore, the Advisor seeks to identify those companies exhibiting superior fundamental risk-reward profiles and strong defensible business franchises while focusing on the relative value of the security in the company's capital structure.

Investment selection process

The Advisor selectively narrows prospective investment opportunities through a process designed to identify the most attractive opportunities. If the senior investment professionals responsible for the transaction and the Advisor's senior management determine that an investment opportunity merits pursuit, the Advisor engages in an intensive due diligence process. This process involves extensive research into the target company, its management, its industry, its growth prospects and its ability to withstand adverse conditions.

In conducting their due diligence, the Advisor's investment professionals use publicly available information as well as information from their extensive relationships with former and current management teams, consultants, competitors and investment bankers, among others. Though each transaction involves a somewhat different approach, the Advisor often undertakes the following due diligence steps. Initially, the investment team involved in the transaction may meet with management to get an insider's view of the business and probe for potential weaknesses in business prospects. They may also visit headquarters and company operations, meeting top- and middle-level executives. Independently from the company, the investment team may check management's backgrounds and references. With information provided by the company, the investment team performs a detailed review of historical financial performance and the quality of earnings. To assess both business prospects and standard practices, they may contact customers and vendors and conduct a competitive analysis, comparing the company to its main competitors on an operating, financial, market share and valuation basis. The investment team also researches the industry for historic growth trends and future prospects utilizing industry analysts at BlackRock, third party research, industry association literature and general news. Furthermore, they assess asset value and the ability of physical infrastructure and information systems to handle anticipated growth and investigate any legal risks and the viability of current financial and accounting systems. Attorneys and independent accountants as well as outside advisors, as appropriate, may conduct additional due diligence on behalf of the Advisor.

[Table of Contents](#)

After the Advisor has identified an investment opportunity and completed due diligence, the investment team involved in the transaction prepares a written investment analysis. Senior investment professionals involved in the transaction review the analysis, and if they are in favor of making the potential investment, present it first to Messrs. Maher and Lazar and then, if approved by Messrs. Maher and Lazar, to the Advisor's investment committee. The investment committee is comprised of Messrs. Maher and Lazar and several senior executives of BlackRock and several of the Kelso Principals. Investment committee members have an average of over 20 years of investment experience in the fixed income and private equity markets. Each investment opportunity requires the consensus of the investment committee in order to be approved, except that investments of less than approximately 3% of our net assets may be made without the prior approval of the investment committee if approved by Messrs. Maher and Lazar and two other members of the investment committee, one of whom must be an individual from BlackRock and the other a Kelso Principal. In addition, follow-on investments in existing portfolio companies generally do not require investment committee approval beyond that obtained when the initial investment in the company was made. Temporary investments, such as those in cash equivalents, U.S. Government securities and other high quality debt investments that mature in one year or less, do not require approval by the investment committee.

Investment structure

Once the Advisor determines that a prospective portfolio company is a suitable investment, it works with the management of that company, any intermediaries and other capital providers, including senior and junior debt security investors and equity capital providers, to structure an investment quickly and effectively.

We invest in portfolio companies primarily in the form of senior and junior secured loans and unsecured and subordinated loans. The senior and junior secured loans generally have terms of three to ten years. We obtain security interests in the assets of our portfolio companies that serve as collateral in support of the repayment of the senior and junior secured loans. The collateral may take the form of first or second priority liens on the assets of a portfolio company.

The Advisor structures unsecured and subordinated debt securities and loans to have relatively high floating or fixed interest rates that provide us with current investment income. These debt securities and loans generally have terms of up to ten years. Such unsecured and subordinated debt securities and loans may have interest-only payments in the early years, with amortization of principal deferred to the later years of the loan. Also, some of these loans will be collateralized by a subordinate lien on some or all of the assets of the company.

In some cases, our debt investments may provide for a portion of the interest payable to be payment-in-kind, or PIK, interest. To the extent interest is PIK, it will be payable through the increase of the principal amount of the loan by the amount of the interest due on the then-outstanding principal amount of the loan. We must recognize PIK interest, a non-cash source of income, as taxable income, increasing the amounts we are required to distribute to stockholders to qualify for the federal income tax benefits applicable to RICs.

In the case of the senior secured and junior loans, the Advisor tailors the terms of the investment to the facts and circumstances of the transaction and the prospective portfolio company, negotiating a structure that aims to protect our rights and manage our risk while creating incentives for the portfolio company to achieve its business plan and improve its profitability. For example, in addition to seeking a senior position in the capital structure of our portfolio companies, the Advisor seeks to limit the downside potential of our investments. The Advisor may accomplish this through requiring a total return on our investment (including both interest and potential equity appreciation) that compensates us for credit risk or through incorporating call protection into the investment structure. The Advisor may also negotiate covenants in connection with our investments that protect the preservation of our capital. Such restrictions may include affirmative and negative covenants, default penalties, lien protection, change of control provisions and board rights, including either observation or participation rights.

In general, our debt investments include financial covenants and terms that require the portfolio company to reduce leverage over time, thereby enhancing its credit quality. These methods may include, among others: maintenance leverage covenants requiring a decreasing ratio of debt to cash flow; maintenance cash flow covenants requiring an increasing ratio of cash flow to interest expense and possibly other cash expenses such as capital expenditures, cash taxes and mandatory principal payments; and debt incurrence prohibitions, limiting a company's ability to relevel its balance sheet. In addition, limitations on asset sales and capital expenditures prevent a company from changing the nature of its business or capitalization without our consent.

Structurally, subordinated loans usually rank junior in priority of payment to senior debt, such as senior bank debt, and are often unsecured. As such, other creditors may rank senior to us in the event of an insolvency. However, subordinated loans rank senior to common and preferred equity in a borrower's capital structure. Due to their higher risk

[Table of Contents](#)

profile and often less restrictive covenants as compared to senior loans, subordinated loans generally earn higher interest yields than senior secured loans. We believe that subordinated loans offer an attractive alternative investment opportunity. In many cases investors in subordinated loans receive opportunities to invest directly in the equity securities of borrowers, and from time to time also may receive warrants to purchase equity securities.

Our debt investments may include equity features, such as warrants or options to buy a minority interest in the portfolio company. Warrants we receive with our debt may require only a nominal cost to exercise, and thus, as a portfolio company appreciates in value, we may achieve additional investment return from this equity interest. We generally seek to structure the warrants to provide provisions protecting our rights as a minority-interest holder, and we generally seek to structure puts or rights to sell such securities back to the company upon the occurrence of specified events.

Our equity investments may consist of preferred equity that pays dividends on a current basis or preferred equity that does not pay current dividends. Preferred equity generally has a preference over common equity as to distributions on liquidations and dividends. In some cases, we may acquire common equity. Our equity investments frequently are not control-oriented investments, and in many cases, we acquire equity securities as part of a group of private equity investors in which we are not the lead investor. Our preferred and common equity investments typically are made in conjunction with loans to these companies.

Ongoing relationship with portfolio companies

The Advisor monitors our portfolio companies on an ongoing basis. The Advisor monitors the financial trends of each portfolio company to determine if it is meeting its business plans and to assess the appropriate course of action for each company.

The Advisor has several methods of evaluating and monitoring the performance and fair values of our investments, which may include the following and other methods:

- assessment of success of the portfolio company in adhering to its business plan and compliance with covenants;
- periodic and regular contact with portfolio company management and, if appropriate, the financial or strategic sponsor, to discuss financial position, requirements and accomplishments;
- comparisons to other companies in the industry;
- attendance at and participation in board meetings;
- review of interim and annual financial statements and financial projections for portfolio companies; and
- retention of third-party valuation firms to assist in determination of fair value.

Managerial assistance

As a BDC, we offer, and must provide upon request, managerial assistance to our portfolio companies. This assistance could involve, among other things, participating in board and management meetings, consulting with and advising officers of portfolio companies and providing other organizational and financial guidance or exercising strategic or managerial influence over such companies. We may receive fees for these services. The Advisor will provide managerial assistance on our behalf to those portfolio companies that request this assistance. Employees of the Advisor have experience providing managerial assistance to private operating companies like our portfolio companies, and such assistance has tended to be related to board representation and to strategic and financing transactions. The Advisor generally will not receive any direct compensation from our portfolio companies for providing managerial assistance although it may do so from time to time.

Investment rating system

The Advisor employs a grading system for our entire portfolio. The Advisor grades all loans on a scale of 1 to 4. This system is intended to reflect the performance of the borrower's business, the collateral coverage of the loans and other factors considered relevant. Generally, the Advisor assigns only one loan grade to each portfolio company for all loan investments in that portfolio company; however, the Advisor will assign multiple ratings when appropriate for different investments in one portfolio company. The following is a description of the conditions associated with each investment rating:

Grade 1: Investments in portfolio companies whose performance is substantially within the Advisor's expectations and whose risk factors are neutral to favorable to those at the time of the original investment.

Table of Contents

Grade 2: Investments in portfolio companies whose performance is below the Advisor's expectations and that require closer monitoring; however, no loss of investment return (interest and/or dividends) or principal is expected.

Grade 3: Investments in portfolio companies whose performance is below the Advisor's expectations and for which risk has increased materially since origination. Some loss of investment return is expected, but no loss of principal is expected. Companies graded 3 generally will be out of compliance with debt covenants and will be unlikely to make debt repayments on their original schedule.

Grade 4: Investments in portfolio companies whose performance is materially below the Advisor's expectations where business trends have deteriorated and risk factors have increased substantially since the original investment. Investments graded 4 are those for which some loss of principal is expected.

The Advisor monitors and, when appropriate, changes the investment ratings assigned to each investment in our portfolio. In connection with our valuation process, the Advisor and Board of Directors review these investment ratings on a quarterly basis. Our average investment rating was 1.32 at December 31, 2010 and 1.46 at December 31, 2009. The following is a distribution of the investment ratings of our portfolio companies at December 31, 2010 and December 31, 2009:

	<u>December 31, 2010</u>	<u>December 31, 2009</u>
Grade 1	\$ 649,170,919	\$ 553,361,682
Grade 2	212,416,256	224,552,728
Grade 3	9,631,767	51,207,962
Grade 4	18,259,678	21,528,959
Total investments including unearned income	889,478,620	850,651,331
Unearned income	(9,392,954)	(3,909,286)
Total investments	<u>\$ 880,085,666</u>	<u>\$ 846,742,045</u>

The investment rating process begins with each portfolio company or investment being initially evaluated by the transaction team, led by a senior investment professional who is responsible for the portfolio company relationship. This evaluation generally is completed no less frequently than quarterly. At the Advisor's weekly investment professionals' meeting, the transaction team presents an update on the activities of any company rated below Grade 1. Each quarter, all investment professionals attend a separate investment rating meeting. At these quarterly meetings, the transaction team responsible for each portfolio investment reviews each portfolio company and suggests a rating for each investment for discussion among the investment professionals. At the conclusion of discussion, and subject to the approval of the Advisor's chief executive officer and chief operating officer, the Advisor's chief financial officer records the internal investment ratings for review by the Board of Directors quarterly.

The investment committee

The Advisor's investment committee is responsible for approving our investments. The members of the investment committee are:

<u>Committee Member</u>	<u>Affiliation</u>	<u>Title at Affiliated Entity</u>
James R. Maher	BlackRock Kelso Capital Advisors LLC	Chairman and Chief Executive Officer
Michael B. Lazar	BlackRock Kelso Capital Advisors LLC	Chief Operating Officer
Laurence D. Fink	BlackRock, Inc.	Chairman and Chief Executive Officer
Robert S. Kapito	BlackRock, Inc.	President
Richard S. Davis	BlackRock, Inc.	Managing Director and Chief Operating Officer of Boston Office
Sacha M. Bacro	BlackRock, Inc.	Managing Director and Head of Capital Markets
James Keenan	BlackRock, Inc.	Managing Director and Head of Leveraged Finance
Leland T. Hart	BlackRock, Inc.	Managing Director, Leveraged Finance
Frank T. Nickell	Kelso & Company, L.P.	President and Chief Executive Officer
Michael B. Goldberg	Kelso & Company, L.P.	Managing Director

Table of Contents

<u>Committee Member</u>	<u>Affiliation</u>	<u>Title at Affiliated Entity</u>
Frank J. Loverro	Kelso & Company, L.P.	Managing Director
George E. Matelich	Kelso & Company, L.P.	Managing Director

Investment management agreement

We have entered into an investment management agreement, which we refer to as the management agreement, with the Advisor, under which the Advisor, subject to the overall supervision of our Board of Directors, manages our day-to-day operations and provides us with investment advisory services. For providing these services, the Advisor receives a base management fee from us at an annual rate of 2.0% of our total assets, including any assets acquired with the proceeds of leverage, payable quarterly in arrears.

On June 22, 2008, the owners of the Advisor amended its limited liability operating agreement to reduce the voting power of certain of its owners, which may have been deemed to cause an “assignment,” as defined in the 1940 Act, of our previous management agreement and such an assignment results in termination of the agreement under the 1940 Act. Pursuant to the approval of our Board of Directors at an in-person meeting on March 5, 2008 and of our stockholders at our Annual Meeting of Stockholders on April 24, 2008, we entered into a new management agreement, the terms of which are identical to the previous management agreement, except for the date of the agreement and the expiration of its initial term. The date of the new agreement is June 22, 2008 and its initial term expired on June 22, 2010. In 2010, our Board of Directors approved the continuation of the management agreement for another one-year term, to expire on June 22, 2011.

For the years ended December 31, 2010, 2009 and 2008, the Advisor earned \$16,877,854, \$18,498,189 and \$22,716,602, respectively, in base management fees under the management agreement.

The management agreement provides that the Advisor or its affiliates may be entitled to an incentive management fee, which we refer to as the Incentive Fee, under certain circumstances. The determination of the Incentive Fee, as described in more detail below, will result in the Advisor or its affiliates receiving no Incentive Fee payments if returns to our stockholders do not meet an 8.0% annualized rate of return during the applicable fee measurement period and will result in the Advisor or its affiliates receiving less than the full amount of the Incentive Fee percentage until returns to our stockholders exceed an approximate 13.3% annualized rate of return during such period. Annualized rate of return in this context is computed by reference to our net asset value and does not take into account changes in the market price of our common stock.

The Advisor will be entitled to receive the Incentive Fee from us if our performance exceeds a “hurdle rate” during different measurement periods: the transition period; trailing four quarters’ periods (which applies only to the portion of the Incentive Fee based on income); and annual periods (which applies only to the portion of the Incentive Fee based on capital gains).

- The “transition period” began on July 1, 2007 and ended on June 30, 2008.
- The initial “trailing four quarters’ period” ended on September 30, 2008. In other words, beginning for the quarterly period ended on September 30, 2008 and for each calendar quarter thereafter, the income portion of the Incentive Fee payable for the quarter was determined by reference to such calendar quarter and the three preceding calendar quarters.
- The term “annual period” means the period beginning on July 1 of each calendar year and ending on June 30 of the next calendar year.

The hurdle rate for each quarterly portion of a measurement period is 2.0% multiplied by our net asset values at the beginning of each calendar quarter during the measurement period, calculated after giving effect to any distribution that occurred during the measurement period. A portion of the Incentive Fee is based on our income and a portion is based on capital gains. Each portion of the Incentive Fee is described below.

Quarterly Incentive Fee Based on Income. For each of the first two measurement periods referred to above (the transition period and each trailing four quarters’ period), we pay the Advisor an Incentive Fee based on the amount by which (A) aggregate distributions and amounts distributable out of taxable net income (excluding any capital gain and loss) during the period less the amount, if any, by which net unrealized capital depreciation exceeds net realized capital gains during the period exceeds (B) the hurdle rate for the period. The amount of the excess of (A) over (B) described in this paragraph for each period is referred to as the excess income amount.

[Table of Contents](#)

The portion of the Incentive Fee based on income for each period will equal 50% of the period's excess income amount, until the cumulative Incentive Fee payments for the period equal 20% of the period's income amount distributed or distributable to stockholders as described in clause (A) of the preceding paragraph. Thereafter, the portion of the Incentive Fee based on income for the period equals 20% of the period's remaining excess income amount.

Annual Incentive Fee Based on Capital Gains. The portion of the Incentive Fee based on capital gains is calculated on an annual basis. For each annual period, we pay the Advisor an Incentive Fee based on the amount by which (A) net realized capital gains, if any, to the extent they exceed gross unrealized capital depreciation, if any, occurring during the period exceeds (B) the amount, if any, by which the period's hurdle rate exceeds the amount of income used in the determination of the Incentive Fee based on income for the period. The amount of the excess of (A) over (B) described in this paragraph is referred to as the excess gain amount.

The portion of the Incentive Fee based on capital gains for each period will equal 50% of the period's excess gain amount, until such payments equal 20% of the period's capital gain amount distributed or distributable to our stockholders. Thereafter, the portion of the Incentive Fee based on capital gains for the period equals an amount such that the portion of the Incentive Fee payments to the Advisor based on capital gains for the period equals 20% of the period's remaining excess gain amount. The result of this formula is that, if the portion of the Incentive Fee based on income for the period exceeds the period's hurdle, then the portion of the Incentive Fee based on capital gains will be capped at 20% of the capital gain amount.

In calculating whether the portion of the Incentive Fee based on capital gains is payable with respect to any period, we account for our assets on a security-by-security basis. In addition, we use the "period-to-period" method pursuant to which the portion of the Incentive Fee based on capital gains for any period is based on realized capital gains for the period reduced by realized capital losses and gross unrealized capital depreciation for the period. Based on current interpretations of Section 205(b)(3) of the Investment Advisers Act of 1940 by the SEC and its staff, the calculation of unrealized depreciation for each portfolio security over a period is based on the fair value of the security at the end of the period compared to the fair value at the beginning of the period. Incentive Fees earned in any of the periods described above are not subject to modification or repayment based upon performance in a subsequent period.

For the years ended December 31, 2010, 2009 and 2008, the Advisor earned \$15,108,049, \$16,818,602 and zero, respectively, in Incentive Fees from the Company.

Expenses

All investment professionals and staff of the Advisor, when and to the extent engaged in providing investment advisory and management services, and the compensation and routine overhead expenses of such personnel allocable to such services, will be provided and paid for by the Advisor. We will bear all other costs and expenses of our operations and transactions, including those relating to:

- our organization;
- calculating our net asset value (including the cost and expenses of any independent valuation firms);
- expenses incurred by the Advisor payable to third parties in monitoring our investments and performing due diligence on prospective portfolio companies;
- interest payable on debt, if any, incurred to finance our investments;
- the costs of future offerings of common shares and other securities, if any;
- the base management fee and any incentive management fee;
- dividends and distributions on our preferred shares, if any, and common shares;
- administration fees payable under the administration agreement;
- fees payable to third parties relating to, or associated with, making investments;
- transfer agent and custodial fees;
- registration fees;
- listing fees;
- taxes;
- independent director fees and expenses;
- costs of preparing and filing reports or other documents with the SEC;

Table of Contents

- the costs of any reports, proxy statements or other notices to our stockholders, including printing costs;
- our fidelity bond;
- directors and officers/errors and omissions liability insurance, and any other insurance premiums;
- indemnification payments;
- direct costs and expenses of administration, including audit and legal costs; and
- all other expenses reasonably incurred by us or the Administrator in connection with administering our business, such as the allocable portion of overhead under the administration agreement, including rent and other allocable portions of the cost of certain of our officers and their respective staffs.

We will reimburse the Advisor for costs and expenses incurred by the Advisor for office space rental, office equipment and utilities allocable to the Advisor under the management agreement, as well as any costs and expenses incurred by the Advisor relating to any non-investment advisory, administrative or operating services provided by the Advisor to us. For the years ended December 31, 2010, 2009 and 2008, we incurred \$1,622,957, \$1,466,563 and \$1,027,135, respectively, for such investment advisor expenses under the management agreement.

From time to time, the Advisor may pay amounts owed by us to third party providers of goods or services. We will subsequently reimburse the Advisor for such amounts paid on our behalf. Reimbursements to the Advisor for the years ended December 31, 2010, 2009 and 2008 were \$3,240,732, \$1,978,629 and \$1,691,420, respectively.

Indemnification

The management agreement provides that in the absence of willful misfeasance, bad faith, gross negligence or reckless disregard of its obligations thereunder, the Advisor is not liable to us or any of our stockholders for any act or omission by it or its employees in the supervision or management of our investment activities or for any loss sustained by us or our stockholders, and provides for indemnification by us of its members, directors, officers, employees, agents and control persons for liabilities incurred by it in connection with their services to us, subject to certain limitations and conditions.

Board and stockholder approval of the management agreement

The management agreement was originally approved by our Board of Directors at an in-person meeting of the Board of Directors held on April 14, 2005, including a majority of the directors who are not parties to the agreement or interested persons (as such term is defined in the 1940 Act) of any such party. In addition, the management agreement was approved by our sole stockholder on July 21, 2005. On June 22, 2008, the owners of the Advisor amended its limited liability operating agreement to reduce the voting power of certain of its owners, which may have been deemed to cause an "assignment," as defined in the 1940 Act, of our previous management agreement and such an assignment results in termination of the agreement under the 1940 Act. Pursuant to the approval of our Board of Directors at an in-person meeting on March 5, 2008 and of our stockholders at our Annual Meeting of Stockholders on April 24, 2008, we entered into a new management agreement, the terms of which are identical to the previous management agreement, except for the date of the agreement and the expiration of its initial term. A discussion regarding the basis for the Board's approval of the management agreement is available in our Proxy Statement for our 2008 Annual Meeting of Stockholders. The date of the new agreement is June 22, 2008 and its initial term expired on June 22, 2010. In 2010, our Board of Directors approved the continuation of the management agreement for another one-year term, to expire on June 22, 2011.

Duration and termination

The management agreement will continue in effect until June 22, 2011, and if not sooner terminated, will continue in effect for successive periods of twelve months thereafter, provided that each continuance is specifically approved at least annually by both (1) the vote of a majority of our Board of Directors or the vote of a majority of our outstanding voting securities and (2) the vote of a majority of the Board of Directors who are not parties to the management agreement or interested persons (as such term is defined in the 1940 Act) of any such party, cast in person at a meeting called for the purpose of voting on such approval. We may terminate the management agreement as a whole at any time, without the payment of any penalty, upon the vote of a majority of our Board of Directors or a majority of our outstanding voting securities or by the Advisor, on 60 days' written notice by either party to the other which can be waived by the non-terminating party. The management agreement will terminate automatically in the event of its assignment.

[Table of Contents](#)

Organization of the Advisor

The Advisor is organized as a Delaware limited liability company. The Advisor is registered as an investment advisor with the SEC under the Advisers Act. Its principal executive offices are located at 40 East 52nd Street, New York, New York. James R. Maher and Michael B. Lazar, the managing members of the Advisor, are the control persons of the Advisor.

Administration agreement

We have entered into an administration agreement with the Administrator, a subsidiary of BlackRock, under which the Administrator provides administrative services to us. In payment for these services, facilities and personnel, we reimburse the Administrator for our allocable portion of overhead and other expenses incurred by the Administrator in performing its obligations under the administration agreement, including rent and our allocable portion of the cost of certain of our officers and their respective staffs.

For the years ended December 31, 2010, 2009 and 2008, we incurred \$587,469, \$642,993 and \$847,387, respectively, for administrative services expenses payable to the Administrator under the administration agreement.

License agreements

We have entered into a license agreement with BlackRock and the Advisor pursuant to which BlackRock has agreed to grant to the Advisor, and the Advisor has agreed to grant to us, a non-exclusive, royalty-free license to use the name "BlackRock." In addition, we have entered into a license agreement with Michael B. Lazar, our Chief Operating Officer, and the Advisor pursuant to which Mr. Lazar has agreed to grant to the Advisor, and the Advisor has agreed to grant to us, a non-exclusive, royalty-free license to use the name "Kelso." Mr. Lazar obtained this limited right to license the name "Kelso" under an agreement with Kelso.

Competition

A number of entities compete with us to make the types of investments that we make. We compete with other BDCs, public and private funds, commercial and investment banks, CLO funds, commercial financing companies, insurance companies, high yield investors and, to the extent they provide an alternative form of financing, private equity funds. 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. 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 competitors may have higher risk tolerances or different risk assessments, which could allow them to consider a wider variety of investments and establish more relationships than us. Furthermore, many of our competitors are not subject to the regulatory restrictions that the 1940 Act imposes on us as a BDC or the restrictions that the Code imposes on us as a RIC.

Leverage

We maintain a multi-currency \$375 million senior secured credit facility with a group of lenders, under which we had approximately \$170 million of indebtedness outstanding at December 31, 2010. Availability under the facility, which we refer to as our Credit Facility, consists of \$275 million in revolving loan commitments and \$100 million in term loan commitments. The term loan commitments have been fully drawn and may not be reborrowed once repaid. The Credit Facility has an "accordion" feature that allows the Company, under certain circumstances, to increase the size of the Credit Facility by up to an additional \$275 million of revolving loan commitments and \$250 million of term loan commitments. The Credit Facility has a stated maturity date of December 6, 2013 and the interest rate applicable to borrowings thereunder is generally LIBOR plus an applicable spread of either 3.00% or 3.25% for revolving loans, based on a pricing grid depending on the Company's credit rating, and LIBOR plus 3.00% for term loans. The Credit Facility contains customary affirmative and negative covenants, including the maintenance of a minimum stockholders' equity, the maintenance of a ratio of not less than 200% of total assets (less total liabilities other than indebtedness) to total indebtedness, and restrictions on certain payments and issuance of debt. In addition, borrowings under the Credit Facility (and the incurrence of certain other permitted debt) are subject to compliance with a borrowing base that applies different advance rates to different types of assets in the Company's portfolio. At December 31, 2010, we were in compliance with all financial and operational covenants required by the Credit Facility.

[Table of Contents](#)

On January 18, 2011, we closed a private placement issuance of \$158 million in aggregate principal amount of five-year, senior secured notes with a fixed interest rate of 6.50% and a maturity date of January 18, 2016 and \$17 million in aggregate principal amount of seven-year, senior secured notes with a fixed interest rate of 6.60% and a maturity date of January 18, 2018 (collectively, the “Senior Secured Notes”). The Senior Secured Notes were sold to certain institutional accredited investors pursuant to an exemption from registration under the Securities Act of 1933, as amended. Interest on the Senior Secured Notes is due semi-annually on January 18 and July 18, commencing on July 18, 2011. The proceeds from the issuance of the Senior Secured Notes were used to fund new portfolio investments, reduce outstanding borrowings under the Credit Facility and for general corporate purposes.

Staffing

Services necessary for our business are provided by individuals who are employees of the Advisor or the Administrator and its affiliates, pursuant to the terms of the management agreement and the administration agreement. Each of our executive officers is an employee of the Advisor or the Administrator and its affiliates. Our executive officers are also executive officers of the Advisor. Our day-to-day investment operations are managed by the Advisor. The Advisor currently has 15 investment professionals who focus on origination and transaction development and monitoring of our investments. We reimburse the Advisor for costs and expenses incurred by the Advisor for office space rental, office equipment and utilities allocable to the Advisor under the management agreement, as well as any costs and expenses incurred by the Advisor relating to any non-investment advisory, administrative or operating services provided by the Advisor to us. In addition, we reimburse the Administrator for our allocable portion of expenses it incurs in performing its obligations under the administration agreement, including rent and our allocable portion of the cost of certain of our officers and their respective staffs.

Regulation

We are a BDC under the 1940 Act. The 1940 Act contains prohibitions and restrictions relating to transactions between BDCs and their affiliates (including any investment advisors or sub-advisors), principal underwriters and affiliates of those affiliates or underwriters and requires that a majority of the directors be persons other than “interested persons,” as that term is defined in the 1940 Act. In addition, the 1940 Act provides that we may not change the nature of our business so as to cease to be, or to withdraw our election as, a BDC unless that change is approved by a majority of our outstanding voting securities.

We may invest up to 100% of our assets in securities acquired directly from issuers in privately negotiated transactions. With respect to such securities, we may, for the purpose of public resale, be deemed an “underwriter” as that term is defined in the Securities Act of 1933, or the Securities Act. We may purchase or otherwise receive warrants to purchase the common stock of our portfolio companies in connection with acquisition financing or other investment. Similarly, in connection with an acquisition, we may acquire rights to require the issuers of acquired securities or their affiliates to repurchase them under certain circumstances. We also do not intend to acquire securities issued by any investment company that exceed the limits imposed by the 1940 Act. Under these limits, except for registered money market funds we generally cannot acquire more than 3% of the voting stock of any investment company, invest more than 5% of the value of our total assets in the securities of one investment company or invest more than 10% of the value of our total assets in the securities of investment companies in the aggregate. With regard to that portion of our portfolio invested in securities issued by investment companies, it should be noted that such investments might subject our stockholders to additional expenses. None of these are fundamental policies and they may be changed without stockholder approval.

Sarbanes-Oxley Act of 2002

The Sarbanes-Oxley Act of 2002 imposes a wide variety of regulatory requirements on publicly-held companies and their insiders. We have adopted procedures to comply with the Sarbanes-Oxley Act and the regulations promulgated thereunder. The Sarbanes-Oxley Act requires us to review our policies and procedures to determine whether we comply with the Sarbanes-Oxley Act and such regulations. We will continue to monitor our compliance with all regulations that are adopted under the Sarbanes-Oxley Act and will take actions necessary to ensure that we are in compliance therewith.

The NASDAQ Global Select Market corporate governance regulations

The NASDAQ Global Select Market has adopted corporate governance regulations with which listed companies must comply. We believe we are in compliance with such corporate governance listing standards. We will continue to monitor our compliance with all future listing standards and will take actions necessary to ensure that we are in compliance therewith.

[Table of Contents](#)

Privacy principles

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

Generally, we do not receive any nonpublic personal information relating to our stockholders, although certain nonpublic personal information of our stockholders may become available to us. We do not disclose any nonpublic personal information about our stockholders or former stockholders to anyone, except as permitted by law or as is necessary in order to service stockholder accounts (for example, to a transfer agent or third party administrator).

We restrict access to nonpublic personal information about our stockholders to our investment advisor's employees with a legitimate business need for the information. We maintain physical, electronic and procedural safeguards designed to protect the nonpublic personal information of our stockholders.

Available information

Our internet address is www.blackrockkelso.com. We make available free of charge on our website our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC. Information contained on our website is not incorporated by reference into this annual report on Form 10-K and you should not consider information contained on our website to be part of this annual report on Form 10-K.

ITEM 1A. RISK FACTORS

You should carefully consider these risk factors, together with all of the other information included in this Annual Report on Form 10-K, including our financial statements and the related notes thereto, before making a decision to purchase our common stock. The risks set out below are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results. If any of the following events occur, our business, financial condition and results of operations could be materially adversely affected. In such case, our net asset value and the trading price of our common stock could decline, and you may lose all or part of your investment in the Company.

Risks Related to Our Business

We may be unable to achieve our investment objective if we are unable to manage our investments effectively.

Our ability to achieve our investment objective depends on our ability to manage our business, which depends, in turn, on the ability of the Advisor to identify, invest in and monitor companies that meet our investment criteria. Accomplishing this result is largely a function of the Advisor's investment process and, in conjunction with the Administrator, its ability to provide competent, attentive and efficient services to us. Our executive officers and many of the members of the Advisor's investment committee have substantial responsibilities to other clients in addition to their activities and responsibilities on our behalf. The investment professionals dedicated to us may also be required to provide managerial assistance to our portfolio companies. These demands on their time may distract them or slow our rate of investment. Any failure to manage our business effectively could have a material adverse effect on our business, financial condition and results of operations.

Our investment advisor and its management have limited experience operating under the constraints imposed on us as a BDC or a RIC.

The 1940 Act and the Code impose numerous constraints on the operations of BDCs and RICs. For example, under the 1940 Act, BDCs are required to invest at least 70% of their total assets primarily in securities of private or thinly traded U.S. public companies, cash, cash equivalents, U.S. Government securities and other high quality debt investments that mature in one year or less. Moreover, qualification for taxation as a RIC under subchapter M of the Code requires satisfaction of source-of-income and diversification requirements and our ability to avoid corporate-level taxes on our income and gains depends on our satisfaction of distribution requirements. The failure to comply with these provisions in a timely manner could prevent us from qualifying as a BDC or RIC or could force us to pay unexpected taxes and penalties, which could be material. These constraints, among others, may hinder the Advisor's ability to take advantage of attractive investment opportunities and to achieve our investment objective. The Advisor's experience operating under these constraints is limited to the period since our inception.

We operate in a highly competitive market for investment opportunities.

A number of entities compete with us to make the types of investments that we make. We compete with other BDCs, public and private funds, commercial and investment banks, CLO funds, commercial financing companies, insurance companies, high yield investors, hedge funds and, to the extent they provide an alternative form of financing, private equity funds. Many of our competitors are substantially larger and have considerably greater financial, technical and marketing resources than we do. 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 relationships than us. Furthermore, many of our competitors are not subject to the regulatory restrictions that the 1940 Act imposes on us as a BDC and that the Code imposes on us as a RIC. We cannot assure you that the competitive pressures we face will not have a material adverse effect on our business, financial condition and results of operations. Also, as a result of this competition, we may not be able to pursue attractive investment opportunities from time to time.

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

We depend on the members of senior management of the Advisor, particularly its Chairman and Chief Executive Officer, James R. Maher, and its Chief Operating Officer, Michael B. Lazar, as well as other key personnel for the identification, final selection, structuring, closing and monitoring of our investments. These employees of the Advisor have critical industry experience and relationships that we rely on to implement our business plan. Our future success depends on the continued service of our Advisor's senior management team. The departure of any of the members of our Advisor's senior management or a significant number of the members of its investment team could have a material adverse effect on our ability to achieve our investment objective. As a result, we may not be able to operate our business as we expect, and our ability to compete could be harmed, which could cause our operating results to suffer. In addition, we can offer no assurance that BlackRock Kelso Capital Advisors will remain our investment advisor, that BlackRock Financial Management, Inc. will remain our administrator or that we will continue to have access to BlackRock's investment professionals or the Kelso Principals.

Our investment adviser has the right to resign on 60 days' notice, and we may not be able to find a suitable replacement within that time, resulting in a disruption in our operations that could adversely affect our business, financial condition and results of operations.

Our investment adviser has the right, under our investment management agreement, to resign at any time upon not less than 60 days' written notice, whether we have found a replacement or not. If our investment adviser resigns, we may not be able to find a new investment adviser or hire internal management with similar expertise and ability to provide the same or equivalent services on acceptable terms within 60 days, or at all. If we are unable to do so quickly, our operations are likely to experience a disruption, our financial condition, business and results of operations as well as our ability to pay distributions are likely to be adversely affected and the market price of our shares may decline. In addition, the coordination of our internal management and investment activities is likely to suffer if we are unable to identify and reach an agreement with a single institution or group of executives having the expertise possessed by our investment adviser and its affiliates. Even if we are able to retain comparable management, whether internal or external, the integration of such management and their lack of familiarity with our investment objective may result in additional costs and time delays that may adversely affect our business, financial condition and results of operations.

Capital markets have experienced 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 had, and may in the future have, a negative impact on our business and operations.

The global capital markets have experienced a period of disruption as evidenced by a lack of liquidity in the debt capital markets, write-offs in the financial services sector, the re-pricing of credit risk 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 have 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 indicators suggest improvement in the capital markets, these conditions could deteriorate in the future. During such market disruptions, we may have difficulty raising debt or equity capital especially as a result of regulatory constraints.

Market conditions 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

[Table of Contents](#)

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. In addition, significant changes in the capital markets, including the disruption and volatility, have 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 and results of operations.

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. Decreases in the market values or fair values of our investments are recorded as unrealized depreciation, which reduces our net asset value. 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.

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

The agreements governing our Credit Facility and Senior Secured Notes require 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 all applicable covenants for our outstanding borrowings. 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 debt arrangements. Failure to comply with these covenants would result in a default under these arrangements which, if we were unable to obtain a waiver from the lenders thereunder, could result in an acceleration of repayments on our debt and thereby have a material adverse impact on our business, financial condition and results of operations.

Substantially all of our assets are subject to security interests under our borrowings and if we default on our obligations, we may suffer adverse consequences, including the lenders foreclosing on our assets.

As of December 31, 2010, substantially all of our assets were pledged as collateral under our Credit Facility. If we default on our obligations, the lenders may have the right to foreclose upon and sell, or otherwise transfer, the collateral subject to their security interests. In such event, we may be forced to sell our investments to raise funds to repay our outstanding borrowings in order to avoid foreclosure and these forced sales may be at times and at prices we would not consider advantageous. Moreover, such deleveraging of our company could significantly impair our ability to effectively operate our business in the manner in which we have historically operated. As a result, we could be forced to curtail or cease new investment activities and lower or eliminate the dividends that we pay to our stockholders.

In addition, if the lenders exercise their right to sell the assets pledged under our borrowings, such sales may be completed at distressed sale prices, thereby diminishing or potentially eliminating the amount of cash available to us after repayment of the amounts outstanding.

Our Credit Facility matures in December 2013 and any inability to renew, extend or replace our Credit Facility could adversely impact our liquidity and ability to find new investments or maintain distributions to our stockholders.

We maintain a multi-currency \$375 million senior secured credit facility with a group of lenders, under which we had approximately \$170 million of indebtedness outstanding at December 31, 2010. Availability under our Credit Facility consists of \$275 million in revolving loan commitments and \$100 million in term loan commitments. The Credit Facility has a stated maturity date of December 6, 2013. There can be no assurance that we will be able to renew, extend or replace the Credit Facility upon its maturity on terms that are favorable to us, if at all. Our ability to renew, extend or replace the Credit Facility will be constrained by then-current economic conditions affecting the credit markets. In the event that we are not able to renew, extend or replace the Credit Facility at the time of its maturity, this could have a

[Table of Contents](#)

material adverse effect on our liquidity and ability to fund new investments, our ability to make distributions to our stockholders and our ability to qualify as a RIC.

If we incur additional debt, it could increase the risk of investing in our common stock.

We have indebtedness outstanding pursuant to our Credit Facility and expect, in the future, to borrow additional amounts under our Credit Facility and may increase the size of our Credit Facility. In January 2011, we closed a private placement of \$175 million of our Senior Secured Notes. Lenders under our Credit Facility and Senior Secured Notes have fixed dollar claims on our assets that are superior to the claims of our common stockholders or any preferred stockholders, and we have granted a security interest in our assets in connection with our borrowings. In the case of a liquidation event, those lenders would receive proceeds before our stockholders. In addition, borrowings, also known as leverage, magnify the potential for gain or loss on amounts invested and, therefore, increase the risks associated with investing in our common stock. Leverage is generally considered a speculative investment technique. If the value of our assets increases, then leveraging would cause the net asset value attributable to our common stock to increase more than it otherwise would have had we not leveraged. Conversely, if the value of our assets decreases, leveraging would cause the net asset value attributable to our common stock to decline more than it otherwise would have had we not leveraged. Similarly, any increase in our revenue in excess of interest expense on our borrowed funds would cause our net income to increase more than it would without the leverage. Any decrease in our revenue would cause our net income to decline more than it would have had we not borrowed funds and could negatively affect our ability to make distributions on our common stock. Our ability to service any debt that we incur depends largely on our financial performance and is subject to prevailing economic conditions and competitive pressures.

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

Illustration. The following table illustrates the effect of leverage on returns from an investment in our common stock assuming various annual returns, net of expenses. The calculations in the table below are hypothetical and actual returns may be higher or lower than those appearing below. The calculation is based on our level of borrowing at December 31, 2010, which represented borrowings equal to 19% of our total assets. On such date, we also had \$916 million in total assets; an average cost of funds of 3.48%; \$170 million in debt outstanding; and \$698 million of total net assets. In order to compute the “Corresponding Return to Common Stockholders,” the “Assumed Return on Portfolio (Net of Expenses Other than Interest)” is multiplied by the total value of our assets at December 31, 2010 to obtain an assumed return to us. From this amount, the interest expense calculated by multiplying the interest rate of 3.48% by the \$170 million debt is subtracted to determine the return available to stockholders. The return available to stockholders is then divided by the total value of our net assets at December 31, 2010 to determine the “Corresponding Return to Common Stockholders.” Actual interest payments may be different.

<u>Assumed Return on Portfolio (Net of Expenses Other than Interest)⁽¹⁾</u>	<u>-10%</u>	<u>-5%</u>	<u>0%</u>	<u>5%</u>	<u>10%</u>
Corresponding Return to Common Stockholders	-14.0%	-7.4%	-0.8%	5.7%	12.3%

- (1) The assumed portfolio return in the table is based on SEC regulations and is not a prediction of, and does not represent, our projected or actual performance. The table also assumes that we will maintain a constant level of leverage. The amount of leverage that we use will vary from time to time.

Our use of borrowed funds to make investments exposes us to risks typically associated with leverage.

We borrow money and may issue additional debt securities or preferred stock to leverage our capital structure. As a result:

- shares of our common stock are exposed to incremental risk of loss; therefore, a decrease in the value of our investments would have a greater negative impact on the value of our common shares than if we did not use leverage;
- adverse changes in interest rates could reduce or eliminate the incremental income we make with the proceeds of any leverage;
- our ability to pay dividends on our common stock will be restricted if our asset coverage ratio is not at least 200% and any amounts used to service indebtedness or preferred stock may not be available for such dividends;

[Table of Contents](#)

- such securities are governed by an indenture or other instrument containing covenants restricting our operating flexibility;
- we, and indirectly our stockholders, bear the cost of issuing and paying interest or dividends on such securities; and
- any convertible or exchangeable securities that we issue may have rights, preferences and privileges more favorable than those of our common stock.

There is a risk that we may not make distributions and consequently will be subject to corporate-level income tax.

We intend to make distributions on a quarterly basis to our stockholders out of assets legally available for distribution. We may not be able to achieve operating results that will allow us to make distributions at a specific level or to increase the amount of these distributions from time to time. In addition, due to the asset coverage test applicable to us as a BDC, we may be limited in our ability to make distributions. Also, restrictions and provisions in our existing and any future debt arrangements may limit our ability to make distributions. If we do not distribute a certain percentage of our income annually, we could fail to qualify for tax treatment as a RIC, and we would be subject to corporate-level federal income tax. We cannot assure you that you will receive distributions at a particular level or at all.

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

In accordance with U.S. generally accepted accounting principles, or GAAP, and tax regulations, we include in income certain amounts that we have not yet received in cash, such as payment-in-kind, or PIK, interest, which represents contractual interest added to the loan balance and due at the end of the loan term. In addition to the cash yields received on our loans, in some instances, certain loans may also include any of the following: origination, structuring, closing, commitment and other upfront fees, end of term payments, exit fees, balloon payment fees or prepayment fees. The increases in loan balances as a result of contracted payment-in-kind arrangements are included in income for the period in which such PIK interest was received, which is often in advance of receiving cash payment. We also may be required to include in income certain other amounts that we will not receive in cash. Any warrants that we receive in connection with our debt investments are generally valued as part of the negotiation process with the particular portfolio company. As a result, a portion of the aggregate purchase price for the debt investments and warrants are allocated to the warrants that we receive. This will generally result in “original issue discount” for tax purposes, which we must recognize as ordinary income, increasing the amounts we are required to distribute to qualify for the federal income tax benefits applicable to RICs. Because such original issue discount income would not be accompanied by cash, we would need to obtain cash from other sources to satisfy such distribution requirements. If we are unable to obtain cash from other sources to satisfy such distribution requirements, we may fail to qualify for favorable tax treatment as a RIC and, thus, could become subject to a corporate-level income tax on all of our income. Other features of the debt instruments that we hold may also cause such instruments to generate original issue discount, resulting in a dividend distribution requirement in excess of current cash received. Since in certain cases we may recognize income before or without receiving cash representing such income, we may have difficulty meeting the requirement to distribute at least 90% of our net ordinary income and realized net short-term capital gains in excess of realized net long-term capital losses, if any. If we are unable to meet these distribution requirements, we will not qualify for favorable tax treatment as a RIC or, even if such distribution requirements are satisfied, we may be subject to tax on the amount that is undistributed. Accordingly, we may have to sell some of our assets, raise additional debt or equity capital or reduce new investment originations to meet these distribution requirements and avoid tax.

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

We have elected to be taxed for federal income tax purposes as a RIC under Subchapter M of the Code. If we can meet certain requirements, including source of income, asset diversification and distribution requirements, and if we continue to qualify as a BDC, we will continue to qualify to be a RIC under the Code and will not have to pay corporate-level taxes on income we distribute to our stockholders as dividends, allowing us to substantially reduce or eliminate our corporate-level tax liability. As a BDC, we are generally required to meet a coverage ratio of total assets to total senior securities, which includes all of our borrowings and any preferred stock we may issue in the future, of at least 200%. This requirement limits the amount that we may borrow. Because we will continue to need capital to grow our investment portfolio, this limitation may prevent us from incurring debt and require us to raise additional equity at a time when it may be disadvantageous to do so. We cannot assure you that debt and equity financing will be available to us on favorable terms, if at all, and debt financings may be restricted by the terms of any of our outstanding borrowings. In

[Table of Contents](#)

addition, as a BDC, we are generally not permitted to issue equity securities priced below net asset value without stockholder approval. If additional funds are not available to us, we could be forced to curtail or cease new lending and investment activities, and our net asset value and profitability could decline.

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

Decreases in the market values or fair values of our investments will be recorded as unrealized depreciation. Any unrealized losses in our investment portfolio could be an indication of a portfolio company's inability to meet its repayment obligations to us with respect to the affected investments. This could result in realized losses in the future and ultimately in reductions of our income available for distribution in future periods.

Our investment advisor and its affiliates, officers and employees have certain conflicts of interest.

The Advisor, its officers and employees and members of its investment committee serve or may serve as investment advisors, officers, directors or principals of entities or investment funds that operate in the same or a related line of business as us and/or of investment funds managed by our affiliates. Accordingly, these individuals may have obligations to investors in those entities or funds, the fulfillment of which might not be in our best interests or the best interests of our stockholders. In addition, we note that any affiliated investment vehicle currently formed or formed in the future and managed by the Advisor or its affiliates may have overlapping investment objectives with our own and, accordingly, may invest in asset classes similar to those targeted by us. As a result, the Advisor and/or its affiliates may face conflicts in allocating investment opportunities between us and such other entities. Although the Advisor and its affiliates will endeavor to allocate investment opportunities in a fair and equitable manner and consistent with applicable allocation procedures, it is possible that, in the future, we may not be given the opportunity to participate in investments made by investment funds managed by the Advisor or its affiliates. In any such case, if the Advisor forms other affiliates in the future, we may co-invest on a concurrent basis with such other affiliates, subject to compliance with applicable regulations and regulatory guidance, as well as applicable allocation procedures. In certain circumstances, negotiated co-investments may be made only if we receive an order from the SEC permitting us to do so. There can be no assurance when any such order would be obtained or that one will be obtained at all.

Our base management fee may induce our investment advisor to incur leverage.

Our base management fee is calculated on the basis of our total assets, including assets acquired with the proceeds of leverage. This may encourage the Advisor to use leverage to increase the aggregate amount of and the return on our investments, even when it may not be appropriate to do so, and to refrain from delevering when it would otherwise be appropriate to do so. Under certain circumstances, the use of increased leverage may increase the likelihood of default, which would impair the value of our common stock. Given the subjective nature of the investment decisions made by our investment adviser on our behalf, we will not be able to monitor this conflict of interest.

Our incentive fee structure and the formula for calculating the incentive fee may incentivize our investment advisor to pursue speculative investments.

The incentive fee payable by us to the Advisor may create an incentive for the Advisor to pursue investments on our behalf that are riskier or more speculative than would otherwise be the case in the absence of such compensation arrangement. The incentive fee payable to the Advisor is calculated based on a percentage of distributions on our common stock. The incentive fee payable by us to the Advisor also may induce the Advisor to invest on our behalf in instruments that have a deferred interest feature, even if such deferred payments would not provide cash necessary to enable us to pay current distributions to our stockholders. Under these investments, we would accrue interest over the life of the investment but would not receive the cash income from the investment until the end of the term, if at all. Our net investment income used to calculate the income portion of our incentive fee, however, will include accrued interest. Thus, a portion of this incentive fee would be based on income that we have not yet received in cash and may never receive in cash if the portfolio company is unable to satisfy such interest payment obligation to us. The foregoing risks could be increased because the Advisor is not obligated to reimburse us for any incentive fee received even if we subsequently incur losses or never receive in cash income that was previously accrued.

We may not replicate the success of BlackRock or Kelso.

We are not managed by either BlackRock or Kelso. Our investment strategies differ from those of BlackRock, the Kelso Principals or their respective affiliates. We can provide no assurance that we will replicate the historical or future performance of BlackRock's or Kelso's investments and our investment returns may be substantially lower than the returns achieved by those firms. As a BDC, we are subject to certain investment restrictions that do not apply to

[Table of Contents](#)

BlackRock or Kelso. In addition, recent market conditions and the current stage of the economic cycle present significant challenges to us that have not been present in the past. Accordingly, we can offer no assurance that the Advisor will be able to continue to implement our investment objective with the same degree of success as it has in the past or that shares of our common stock will trade at or above the current level.

Substantially all of our portfolio investments are recorded at fair value as determined in good faith by or under the direction of our Board of Directors and, as a result, there is uncertainty regarding the value of our portfolio investments.

There is not a readily available market value for substantially all of the investments in our portfolio. We value these investments quarterly at fair value as determined in good faith under the direction of our Board of Directors using a consistently applied valuation process in accordance with a documented valuation policy that has been reviewed and approved by our Board of Directors. Our Board of Directors utilizes the services of one or more independent valuation firms to aid it in determining the fair value of these investments. Due to the inherent uncertainty and subjectivity of determining the fair value of investments that do not have a readily available market value, the fair value of our investments may differ significantly from the values that would have been used had a readily available market value existed for such investments and may differ materially from the amounts we realize on any dispositions of such investments. In addition, the impact of changes in the market environment and other events on the fair values of our investments that have no readily available market values may differ from the impact of such changes on the readily available market values for our other investments. Our net asset value could be adversely affected if our determinations regarding the fair value of our investments were materially higher than the values that we ultimately realize upon the disposal of such investments.

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.

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

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

We may experience fluctuations in our periodic results.

We could experience fluctuations in our periodic results due to a number of factors, some of which are beyond our control, including our ability to make investments in companies that meet our investment criteria, the interest rates payable on the debt investments we make, the default rate on such investments, the level of our expenses (including the interest rates payable on our borrowings and the dividend rates on any preferred stock we may issue), 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 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.

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

General interest rate fluctuations may have a substantial negative impact on our investments, the value of our common stock and our rate of return on invested capital. A reduction in the interest rates on new investments relative to interest rates on current investments could also have an adverse impact on our net interest income. An increase in interest rates could decrease the value of any investments we hold which earn fixed interest rates, including subordinated loans, senior and junior secured and unsecured debt securities and loans and high-yield bonds, and also could increase our interest expense, thereby decreasing our net income. Also, an increase in interest rates available to investors could make

investment in our common stock less attractive if we are not able to increase our dividend rate, which could reduce the value of our common stock.

Risks Related to Our Investments

Our investments are risky and highly speculative, and we could lose all or part of our investment.

Investing in private middle-market companies involves a high degree of risk and our financial results may be affected adversely if one or more of our significant portfolio investments defaults on its loans or fails to perform as we expect. We invest primarily in middle-market companies in the form of senior and junior secured and unsecured debt securities and loans, each of which may include an equity component, and by making direct preferred, common and other equity investments in such companies.

Investing in private middle-market companies involves a number of significant risks, including:

- these companies may have limited financial resources and may be unable to meet their obligations under their debt securities that we hold, which may be accompanied by a deterioration in the value of any collateral and a reduction in the likelihood of us realizing any guarantees we may have obtained in connection with our investment;
- these companies typically 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;
- these companies 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 material adverse impact on our portfolio company and, in turn, on us;
- these companies generally have less predictable operating results, may from time to time be parties to litigation, may be engaged in rapidly changing businesses with products subject to a substantial risk of obsolescence, and may require substantial additional capital to support their operations, finance expansion or maintain their competitive position; and
- these companies may have difficulty accessing the capital markets to meet future capital needs, which may limit their ability to grow or to repay their outstanding indebtedness upon maturity.

In addition, in the course of providing significant managerial assistance to certain of our portfolio companies, certain of our officers and directors may serve as directors on the boards of such companies. To the extent that litigation arises out of our investments in these companies, our officers and directors may be named as defendants in such litigation, which could result in an expenditure of funds (through our indemnification of such officers and directors) and the diversion of management time and resources.

An investment strategy focused primarily on privately held companies presents certain challenges, including the lack of available information about these companies.

We invest primarily in privately held companies. Generally, little public information exists about these companies, including typically a lack of audited financial statements and ratings by third parties. We must therefore rely on the ability of our investment adviser to obtain adequate information to evaluate the potential risks of investing in these companies. These companies and their financial information may not be subject to the Sarbanes-Oxley Act of 2002 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 investments. These factors could affect our investment returns.

Our investments in lower credit quality obligations are risky and highly speculative, and we could lose all or part of our investment.

Most of our debt investments are likely to be in lower grade obligations. The lower grade investments in which we invest may be rated below investment grade by one or more nationally-recognized statistical rating agencies at the time of investment or may be unrated but determined by the Advisor to be of comparable quality. Debt securities rated below investment grade are commonly referred to as "junk bonds" and are considered speculative with respect to the issuer's capacity to pay interest and repay principal. The debt that we invest in typically is not initially rated by any rating agency, but we believe that if such investments were rated, they would be below investment grade (rated lower than "Baa3" by Moody's Investors Service, lower than "BBB-" by Fitch Ratings or lower than "BBB-" by Standard & Poor's). We may

[Table of Contents](#)

invest without limit in debt of any rating, as well as debt that has not been rated by any nationally recognized statistical rating organization.

Investment in lower grade investments involves a substantial risk of loss. Lower grade securities or comparable unrated securities are considered predominantly speculative with respect to the issuer's ability to pay interest and principal and are susceptible to default or decline in market value due to adverse economic and business developments. The market values for lower grade debt tend to be very volatile and are less liquid than investment grade securities. For these reasons, your investment in our company is subject to the following specific risks: increased price sensitivity to a deteriorating economic environment; greater risk of loss due to default or declining credit quality; adverse company specific events are more likely to render the issuer unable to make interest and/or principal payments; and if a negative perception of the lower grade debt market develops, the price and liquidity of lower grade securities may be depressed. This negative perception could last for a significant period of time.

Our investments in distressed debt obligations may not produce income and may require us to bear large expenses in order to protect and recover our investment.

At times, distressed debt obligations may not produce income and may require us to bear certain extraordinary expenses (including legal, accounting, valuation and transaction expenses) in order to protect and recover our investment. Therefore, to the extent we invest in distressed debt, our ability to achieve current income for our stockholders may be diminished. We also will be subject to significant uncertainty as to when and in what manner and for what value the distressed debt we invest in will eventually be satisfied (e.g., through liquidation of the obligor's assets, an exchange offer or plan of reorganization involving the distressed debt securities or a payment of some amount in satisfaction of the obligation). In addition, even if an exchange offer is made or plan of reorganization is adopted with respect to distressed debt we hold, there can be no assurance that the securities or other assets received by us in connection with such exchange offer or plan of reorganization will not have a lower value or income potential than may have been anticipated when the investment was made. Moreover, any securities received by us upon completion of an exchange offer or plan of reorganization may be restricted as to resale. As a result of our participation in negotiations with respect to any exchange offer or plan of reorganization with respect to an issuer of distressed debt, we may be restricted from disposing of such securities.

If we invest in preferred stock, we may incur additional risks.

To the extent we invest in preferred securities, we may incur particular risks, including

- Preferred securities may include provisions that permit the issuer, at its discretion, to defer distributions for a stated period without any adverse consequences to the issuer. If we own a preferred security that is deferring its distributions, we may be required to report income for tax purposes before we receive such distributions. Preferred securities are subordinated to bonds and other debt instruments in a company's capital structure in terms of priority to corporate income and liquidation payments, and therefore will be subject to greater credit risk than more senior debt instruments; and
- Generally, preferred security holders have no voting rights with respect to the issuing company unless preferred dividends have been in arrears for a specified number of periods, at which time the preferred security holders may elect a number of directors to the issuer's board. Generally, once all the arrearages have been paid, the preferred security holders no longer have voting rights.

Our equity investments may decline in value.

The equity securities in which we invest may not appreciate or may decline in value. We may thus not be able to realize gains from our equity securities, and any gains that we do realize on the disposition of any equity securities may not be sufficient to offset any other losses we experience. As a result, the equity securities in which we invest may decline in value, which may negatively impact our ability to pay distributions and cause you to lose all or part of your investment.

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

We may enter into hedging transactions, which could expose us to risks associated with such transactions. We may utilize instruments such as forward contracts and interest rate swaps, caps, collars and floors to seek to hedge against fluctuations in the relative values of our portfolio positions and amounts due under our debt arrangements from changes in market interest rates. Use of these hedging instruments may include counterparty credit risk. Utilizing such hedging instruments does not eliminate the possibility of fluctuations in the values of such positions and amounts due under our debt arrangements or prevent losses if the values of such positions decline. However, such hedging can establish other

[Table of Contents](#)

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 underlying portfolio positions should increase. Moreover, it may not be possible to hedge against an 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 will depend on our ability to correctly predict movements and interest rates. Therefore, while we may enter into such transactions to seek to reduce interest rate risks, unanticipated changes in interest rates may result in poorer overall investment performance than if we had not engaged in any such hedging transactions. In addition, 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 or debt arrangements being hedged. Any such imperfect correlation may prevent us from achieving the intended hedge and expose us to risk of loss. See also “— Changes in interest rates may affect our cost of capital and net investment income.”

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

Many of our portfolio companies may be susceptible to economic slowdowns or recessions and may be unable to repay our loans during these periods. Therefore, our non-performing assets may increase and the value of our portfolio may decrease during these periods as we are required to record the values of our investments. 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.

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

Our portfolio companies usually will have, or may be permitted to incur, other debt that ranks equally with, or senior to, debt securities in which we invest. By their terms, such debt instruments may provide that the holders are entitled to receive payment of interest or principal on or before the dates on which we are entitled to receive payments. Also, in the event of insolvency, liquidation, dissolution, reorganization or bankruptcy of a portfolio company, holders of debt instruments ranking senior to our investment in that portfolio company would typically be entitled to receive payment in full before we receive any distribution in respect of our investment. After repaying such senior creditors, the portfolio company may not have any remaining assets to use for repaying its obligations to us. In the case of debt ranking equally with debt securities in which we invest, we would have to share on an equal basis any distributions with other creditors holding such debt in the event of an insolvency, liquidation, dissolution, reorganization or bankruptcy of the relevant portfolio company. In addition, we may not be in a position to control any portfolio company by investing in its debt securities. As a result, we are subject to the risk that a portfolio company in which we invest may make business decisions with which we disagree, and the management of such company, as representatives of the holders of their common equity, may take risks or otherwise act in ways that do not serve our interests as debt investors.

Because we generally do not hold controlling equity interests in our portfolio companies, we may not be in a position to exercise control over our portfolio companies or to prevent decisions by management of our portfolio companies that could decrease the value of our investments.

We generally do not hold controlling equity positions in our portfolio companies. As a result, we are subject to the risk that a portfolio company may make business decisions with which we disagree, and that the management and/or stockholders of a portfolio company may take risks or otherwise act in ways that are adverse to our interests. Due to the lack of liquidity of the debt and equity investments that we typically hold in our portfolio companies, we may not be able to dispose of our investments in the event we disagree with the actions of a portfolio company and may therefore suffer a decrease in the value of our investments.

Concentration of our assets in an issuer, industry or sector may present more risks than if we were more broadly diversified over numerous issuers, industries and sectors of the economy.

We are classified as a non-diversified investment company within the meaning of the 1940 Act, which means that we are not limited by the 1940 Act with respect to the proportion of our assets that we may invest in securities of a single issuer. To the extent that we assume large positions in the securities of a small number of issuers, our net asset value may fluctuate to a greater extent than that of a diversified investment company as a result of changes in the financial condition

[Table of Contents](#)

or the market's assessment of the issuer. We may also be more susceptible to any single economic or regulatory occurrence than a diversified investment company.

In addition, we may, from time to time, invest a substantial portion of our assets in the securities of issuers in any single industry or sector of the economy or in only a few issuers. We cannot predict the industries or sectors in which our investment strategy may cause us to concentrate and cannot predict the level of our diversification among issuers to ensure that we satisfy diversification requirements for qualification as a RIC for U.S. federal income tax purposes. A downturn in an industry or sector in which we are concentrated would have a larger impact on us than on a company that does not concentrate in an industry or sector. Furthermore, the Advisor has not made and does not intend to make any determination as to the allocation of assets among different classes of securities. At any point in time we may be highly concentrated in a single type of asset, such as junior unsecured loans or distressed debt. Consequently, events which affect a particular asset class disproportionately could have an equally disproportionate effect on us.

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: (i) increase or maintain in whole or in part our equity ownership percentage; (ii) exercise warrants, options or convertible securities that were acquired in the original or any subsequent financing; or (iii) attempt to preserve or enhance the value of our investments. We may elect not to make follow-on investments or otherwise lack sufficient funds to make those investments. We will 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 maintain or 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, either because we prefer other opportunities or because we are subject to BDC requirements that would prevent such follow-on investments or the desire to maintain our RIC status.

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

Our investment strategy contemplates that a portion of our investments may be in securities of foreign companies. Investing in foreign companies may expose us to additional risks not typically associated with investing in U.S. companies. These risks include changes in exchange control regulations, political and social instability, expropriation, imposition of foreign taxes (potentially at confiscatory levels), less liquid markets and less available information than is generally the case in the U.S., 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.

Although most of our investments are denominated in U.S. dollars, our investments that are denominated in a foreign currency are subject to the risk that the value of a particular currency may 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 employ hedging techniques to minimize these risks, but we can offer no assurance that we will, in fact, hedge currency risk or, that if we do, such strategies will be effective.

Our investments in the healthcare sector face considerable uncertainties including substantial regulatory challenges.

Our investments in the healthcare sector are subject to substantial risks. The laws and rules governing the business of healthcare companies and interpretations of those laws and rules are subject to frequent change. Broad latitude is given to the agencies administering those regulations. Existing or future laws and rules could force our portfolio companies engaged in healthcare to change how they do business, restrict revenue, increase costs, change reserve levels, change business practices and increase liability in federal and state courts. Healthcare companies often must obtain and maintain regulatory approvals to market many of their products, change prices for certain regulated products and to consummate some of their acquisitions and divestitures. Delays in obtaining or failure to obtain or maintain these approvals could reduce revenue or increase costs. Policy changes on the local, state and federal level, such as the expansion of the government's role in the health care arena and alternative assessments and tax increases specific to the healthcare industry or healthcare products as part of federal health care reform initiatives, could fundamentally change the dynamics of the healthcare industry.

Risks Related to Our Operations as a BDC

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 certain of our affiliates without the prior approval of our independent directors and, in some cases, of the SEC. Any person that owns, directly or indirectly, 5% or more of our outstanding voting securities will be our affiliate for purposes of the 1940 Act and we are generally prohibited from buying or selling any security (other than our securities) from or to such affiliate, absent the prior approval of our independent directors. The 1940 Act also prohibits certain “joint” transactions with certain of our affiliates, which could include investments in the same portfolio company (whether at the same or different times), without prior approval of our independent directors and, in some cases, of the SEC. We are prohibited from buying or selling any security from or to any person who owns more than 25% of our voting securities or certain of that person’s affiliates, or entering into prohibited joint transactions with such persons, absent the prior approval of the SEC through an exemptive order (other than in certain limited situations pursuant to current regulatory guidance). The analysis of whether a particular transaction constitutes a joint transaction requires a review of the relevant facts and circumstances then existing. Similar restrictions limit our ability to transact business with our officers or directors or their affiliates.

We have applied for an exemptive order from the SEC that would permit us and certain of our affiliates, including investment funds managed by our affiliates, to co-invest. Any such order will be subject to certain terms and conditions and there can be no assurance that such order will be granted by the SEC. Accordingly, we cannot assure you that we or our affiliates, including investment funds managed by our affiliates, will be permitted to co-invest, other than in the limited circumstances currently permitted by regulatory guidance or in the absence of a joint transaction.

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

Our business requires a substantial amount of capital. We may acquire additional capital from the issuance of senior securities or other indebtedness, the issuance of additional shares of our common stock or from securitization transactions. However, we may not be able to raise additional capital in the future on favorable terms or at all. We may issue debt securities or preferred securities, which we refer to collectively as “senior securities,” and we may borrow money from banks or other financial institutions, up to the maximum amount permitted by the 1940 Act. The 1940 Act permits us to issue senior securities or incur indebtedness only in amounts such that our asset coverage, as defined in the 1940 Act, equals at least 200% after such issuance or incurrence. Our ability to pay dividends or issue additional senior securities would be restricted if our asset coverage ratio were not at least 200%. If the value of our assets declines, we may be unable to satisfy this test. If that happens, we may be required to liquidate a portion of our investments and repay a portion of our indebtedness at a time when such sales may be disadvantageous.

- *Senior Securities.* As a result of issuing senior securities, we would also be exposed to typical risks associated with leverage, including an increased risk of loss. If we issue preferred securities they would rank “senior” to common stock in our capital structure, preferred stockholders would have separate voting rights and may have rights, preferences or privileges more favorable than those of our common stock. Furthermore, the issuance of preferred securities could have the effect of delaying, deferring or preventing a transaction or a change of control that might involve a premium price for our common stockholders or otherwise be in the best interests of our common stockholders.
- *Additional Common Stock.* Our Board of Directors may decide to issue common stock to finance our operations rather than issuing debt or other senior securities. As a BDC, we are generally not able to issue our common stock at a price below net asset value, or issue securities convertible into common stock, without first obtaining the required approvals from our stockholders and our independent directors. We may also make rights offerings to our stockholders. If we raise additional funds by issuing more common stock or senior securities convertible into, or exchangeable for, our common stock, the percentage ownership of our common stockholders at that time would decrease, and our common stockholders may experience dilution.
- *Securitization.* In addition to issuing securities to raise capital as described above, we anticipate that in the future we may securitize our loans to generate cash for funding new investments. To securitize loans, we may create a wholly-owned subsidiary, contribute a pool of loans to the subsidiary and have the subsidiary issue primarily investment grade debt securities to purchasers who we would expect would be willing to accept a substantially lower interest rate than the loans earn. We would retain all or a portion of the equity in the securitized pool of loans. Our retained equity would be exposed to any losses on the portfolio of loans before any of the debt securities would be exposed to such losses. An inability to successfully securitize our loan portfolio could limit our ability to grow our business and fully execute our business strategy and adversely

affect our earnings, if any. Moreover, the successful securitization of our loan portfolio might expose us to losses as the residual loans in which we do not sell interests will tend to be those that are riskier and more apt to generate losses.

Stockholders will likely incur dilution if we sell or otherwise issue shares of our common stock at prices below the then current net asset value per share of our common stock.

At a special meeting of stockholders held on February 8, 2010, subject to certain Board of Director determinations, 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. Such stockholder approval expired on the twelve-month anniversary of approval, or February 8, 2011. If we obtain future stockholder approval, we may issue shares of our common stock at a price below its then current net asset value per share, subject to the determination by our Board of Directors that such issuance and sale is in our and our stockholders' best interests.

In addition, we may also issue shares in certain limited circumstances under our dividend reinvestment plan and under interpretive advice issued by the Internal Revenue Service. Any sale or other issuance of shares of our common stock at a price below net asset value per share would result in an immediate dilution to the net asset value per share. This dilution would occur as a result of a proportionately greater decrease in a stockholder's interest in our earnings and assets and voting interest in us than the increase in our assets resulting from such issuance. Because the number of shares of common stock that could be so issued and the timing of any issuance is not currently known, the actual dilutive effect cannot be predicted.

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

We are subject to changing rules and regulations of federal and state governments, as well as the stock exchange on which our common stock is listed. These entities, including the Public Company Accounting Oversight Board, the SEC and The NASDAQ Global Select Market, have issued a significant number of new and increasingly complex requirements and regulations over the course of the last several years and continue to develop additional regulations. In particular, changes in the laws or regulations or the interpretations of the laws and regulations that govern BDCs, RICs or non-depository commercial lenders could significantly affect our operations and our cost of doing business. We are subject to federal, state and local laws and regulations and are subject to judicial and administrative decisions that affect our operations, including our loan originations, maximum interest rates, fees and other charges, disclosures to portfolio companies, the terms of secured transactions, collection and foreclosure procedures and other trade practices. If these laws, regulations or decisions change, or if we expand our business into jurisdictions that have adopted more stringent requirements than those in which we currently conduct business, we may have to incur significant expenses in order to comply, or we might have to restrict our operations. In addition, if we do not comply with applicable laws, regulations and decisions, we may lose licenses needed for the conduct of our business and be subject to civil fines and criminal penalties, any of which could have a material adverse effect upon our business, financial condition and results of operations.

The impact of recent financial reform legislation on us is uncertain.

In light of current conditions in the U.S. and global financial markets and the U.S. and global economy, legislators, the presidential administration and regulators have increased their focus on the regulation of the financial services industry. The Dodd-Frank Wall Street Reform and Consumer Protection Act became effective on July 21, 2010, although many provisions of the Dodd-Frank Reform Act have delayed effectiveness or will not become effective until the relevant federal agencies issue new rules to implement the Dodd-Frank Reform Act. Nevertheless, the Dodd-Frank Reform Act may have a material adverse impact on the financial services industry as a whole and on our business, financial condition and results of operations. Accordingly, we cannot predict the effect the Dodd-Frank Reform Act or its implementing regulations will have on our business, financial condition and results of operations.

Any failure on our part to maintain our status as a BDC would reduce our operating flexibility.

The 1940 Act imposes numerous constraints on the operations of BDCs. Any failure to comply with the requirements imposed on BDCs by the 1940 Act could cause the SEC to bring an enforcement action against us and/or expose us to claims of private litigants. In addition, upon approval of a majority of our stockholders, we may elect to withdraw our status as a BDC. If we decide to withdraw our election, or if we otherwise fail to qualify, or maintain our qualification, as a BDC, we may be subject to the substantially greater regulation under the 1940 Act as a closed-end

[Table of Contents](#)

investment company. Compliance with such regulations would significantly decrease our operating flexibility, and could significantly increase our costs of doing business.

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

As a BDC, we may not acquire any assets other than “qualifying assets” unless, at the time of and after giving effect to such acquisition, at least 70% of our total assets are qualifying assets. We believe that most of the investments that we may acquire in the future will constitute qualifying assets. However, we may be precluded from investing in what we believe are attractive investments if such investments are not qualifying assets for purposes of the 1940 Act. If we do not invest a sufficient portion of our assets in qualifying assets, we could be found to be in violation of the 1940 Act provisions applicable to BDCs, which would have a material adverse effect on our business, financial condition and results of operations. Similarly, these rules could prevent us from making follow-on investments in existing portfolio companies (which could result in the dilution of our position) or could require us to dispose of investments at inappropriate times in order to come into compliance with the 1940 Act. Because most of our investments will be in private companies, and therefore will be relatively illiquid, any such dispositions could be made at disadvantageous prices and could result in substantial losses.

Loss of status as a RIC would reduce our net asset value and distributable income.

We currently qualify as a RIC under the Code and intend to continue to qualify each year as a RIC. As a RIC we do not have to pay federal income taxes on our income (including realized gains) that is distributed to our stockholders, provided that we satisfy certain distribution requirements. Accordingly, we are not permitted under accounting rules to establish reserves for taxes on our unrealized capital gains. If we fail to qualify for RIC status in any year, to the extent that we had unrealized gains, we would have to establish reserves for taxes, which would reduce our net asset value. In addition, if we, as a RIC, were to decide to make a deemed distribution of net realized capital gains and retain the net realized capital gains, we would have to establish appropriate reserves for taxes that we would have to pay on behalf of stockholders. It is possible that establishing reserves for taxes could have a material adverse effect on the value of our common stock.

We will be subject to corporate-level income tax if we are unable to maintain our qualification as a RIC under Subchapter M of the Code or do not satisfy the annual distribution requirement.

To maintain RIC status and be relieved of federal taxes on income and gains distributed to our stockholders, we must meet the following annual distribution, income source and asset diversification requirements.

- The annual distribution requirement for a RIC will be satisfied if we distribute to our stockholders on an annual basis at least 90% of our net ordinary income and realized net short-term capital gains in excess of realized net long-term capital losses, if any. Because we may use debt financing, we are subject to an asset coverage ratio requirement under the 1940 Act and we may be subject to certain financial covenants under our debt arrangements that could, under certain circumstances, restrict us from making distributions necessary to satisfy the distribution requirement. If we are unable to obtain cash from other sources, we could fail to qualify for RIC tax treatment and thus become subject to corporate-level income tax.
- The income source requirement will be satisfied if we obtain at least 90% of our income for each year from dividends, interest, gains from the sale of stock or securities or similar sources.
- The asset diversification requirement will be satisfied if we meet certain asset diversification requirements at the end of each quarter of our taxable year. To satisfy this requirement, at least 50% of the value of our assets must consist of cash, cash equivalents, U.S. government securities, securities of other RICs, and other acceptable securities; and no more than 25% of the value of our assets can be invested in the securities, other than U.S. government securities or securities of other RICs, of one issuer, of two or more issuers that are controlled, as determined under applicable Code rules, by us and that are engaged in the same or similar or related trades or businesses or of certain “qualified publicly traded partnerships.” Failure to meet these requirements 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 will be in private companies, and therefore will be relatively illiquid, any such dispositions could be made at disadvantageous prices and could result in substantial losses.

If we fail to qualify for or maintain RIC status for any reason and are subject to corporate-level income tax, the resulting corporate-level taxes could substantially reduce our net assets, the amount of income available for distribution and the amount of our distributions. Such a failure would have a material adverse effect on us and our stockholders.

Risks Relating to an Investment in Our Common Stock

Our shares of common stock have traded at a discount from net asset value and may do so again in the future, which could limit our ability to raise additional equity capital.

Shares of closed-end investment companies, including business development companies, may trade at a market discount from net asset value. This characteristic of closed-end investment companies and business development companies is separate and distinct from the risk that our net asset value per share may decline. In the past, the stocks of BDCs as an industry, including shares of our common stock, have traded below net asset value and at historic lows as a result of concerns over liquidity, leverage restrictions and distribution requirements. When our common stock is trading below its net asset value per share, we will generally not be able to issue additional shares of our common stock at its market price without first obtaining approval for such issuance from our stockholders and our independent directors.

Investing in our common stock may involve an above average degree of risk.

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

The price of our common stock may fluctuate significantly.

As with any company, the price of our common stock will fluctuate with market conditions and other factors. The market price and liquidity of the market for our common stock may from time to time be affected by a number of factors, which include, but are not limited to, the following:

- volatility in the market price and trading volume of common stocks of BDCs or other financial services companies, which are not necessarily related to the operating performance of these companies;
- investors' general perception of our company, the economy and general market conditions;
- our quarterly results of operations;
- our origination activity, including the pace of, and competition for, new investment opportunities;
- the financial performance of the specific industries in which we invest on a recurring basis, including without limitation, our investments in the business services and healthcare industries;
- announcements of strategic developments, acquisitions and other material events by us or our competitors;
- changes in regulatory policies or tax guidelines, particularly with respect to RICs or BDCs;
- loss of RIC status;
- 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 key personnel from the Advisor;
- operating performance of companies comparable to us;
- general economic trends and other external factors, including price and volume fluctuations in the overall stock market; and
- loss of a major funding source.

Our principal stockholders have substantial ownership in us, and this concentration of ownership could limit your ability to influence the outcome of key transactions, including a change of control.

As a result of their substantial ownership in us, our principal stockholders may be able to exert influence over our management and policies. This concentration of ownership may have the effect of delaying, preventing or deterring a change of control of our company, depriving our stockholders of an opportunity to receive a premium for their common stock as part of a sale of our company, and ultimately affecting the market price of our common stock.

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

The shares of our common stock beneficially owned by our principal stockholders are generally available for resale, subject to the provisions of Rule 144 promulgated under the Securities Act. Sales of substantial amounts of our common stock, or the availability of such common stock for sale, could adversely affect the prevailing market prices for our common stock. 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.

There is a risk that investors in our equity securities may not receive dividends or that our dividends may not grow over time.

We intend to make distributions on a quarterly basis to our stockholders out of assets legally available for distribution. There can be no assurance that we will achieve investment results that will allow us to make a specified level of cash distributions or year-to-year increases in cash distributions. If we declare a dividend and if more stockholders opt to receive cash distributions rather than participate in our dividend reinvestment plan, we may be forced to sell some of our investments in order to make cash dividend payments. In addition, due to the asset coverage test applicable to us as a BDC, we may be limited in our ability to make distributions. Further, if we invest a greater amount of assets in equity securities that do not pay current dividends, it could reduce the amount available for distribution.

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, and which may adversely affect the market price of our common stock.

We may distribute taxable dividends that are payable in part in our stock. Under a recently issued IRS revenue procedure, up to 90% of any such taxable dividend for taxable years ending prior to 2012 could be payable in our stock. The IRS has also issued (and where Revenue Procedure 2009-15 or 2010-12 is not currently applicable, the IRS continues to issue) private letter rulings on cash/stock dividends paid by regulated investment companies and real estate investment trusts using a 20% cash standard (instead of the 10% cash standard of Revenue Procedures 2009-15 and 2010-12) if certain requirements are satisfied. Taxable stockholders receiving such dividends will 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, 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.

If we issue preferred stock, the net asset value and market value of our common stock may become more volatile.

We cannot assure that the issuance of preferred stock would result in a higher yield or return to the holders of our common stock. The issuance of preferred stock would likely cause the net asset value and market value of our common stock to become more volatile. If the dividend rate on the preferred stock were to approach the net rate of return on our investment portfolio, the benefit of leverage to the holders of our common stock would be reduced. If the dividend rate on the preferred stock were to exceed the net rate of return on our portfolio, the leverage would result in a lower rate of return to the holders of common stock than if we had not issued preferred stock. Any decline in the net asset value of our investment would be borne entirely by the holders of our common stock. Therefore, if the market value of our portfolio were to decline, the leverage would result in a greater decrease in net asset value to the holders of our common stock than if we were not leveraged through the issuance of preferred stock. This greater net asset value decrease would also tend to cause a greater decline in the market price for our common stock. We might be in danger of failing to maintain the required asset coverage of the preferred stock or of losing our ratings on the preferred stock or, in an extreme case, our current investment income might not be sufficient to meet the dividend requirements on the preferred stock. In order to counteract such an event, we might need to liquidate investments in order to fund a redemption of some or all of the preferred stock. In addition, we would pay (and the holders of our common stock would bear) all costs and expenses relating to the issuance and ongoing maintenance of the preferred stock, including higher incentive fees if our total return exceeds the dividend rate on the preferred stock. Holders of preferred stock may have different interests than holders of common stock and may at times have disproportionate influence over our affairs.

[Table of Contents](#)

Holders of any preferred stock we might issue would have the right to elect members of our Board of Directors and class voting rights on certain matters.

Holders of any preferred stock we might issue, voting separately as a single class, would have the right to elect two members of our Board of Directors at all times and in the event dividends become two full years in arrears would have the right to elect a majority of the directors until such arrearage is completely eliminated. In addition, preferred stockholders have class voting rights on certain matters, including changes in fundamental investment restrictions and conversion to open-end status, and accordingly can veto any changes. Restrictions imposed on the declarations and payment of dividends or other distributions to the holders of our common stock and preferred stock, both by the 1940 Act and by requirements imposed by rating agencies, might impair our ability to maintain our qualification as a RIC for federal income tax purposes. While we would intend to redeem our preferred stock to the extent necessary to enable us to distribute our income as required to maintain our qualification as a RIC, there can be no assurance that such actions could be effected in time to meet the tax requirements.

Certain provisions of the Delaware General Corporation Law and our certificate of incorporation and bylaws could deter takeover attempts and have an adverse impact on the price of our common stock.

The Delaware General Corporation Law, our amended certificate of incorporation and our amended and restated bylaws 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. We have also adopted measures that may make it difficult for a third party to obtain control of us, including provisions of our amended certificate of incorporation and amended and restated bylaws dividing our Board of Directors in three classes serving staggered three-year terms, requiring the affirmative vote of the holders of 75% of the then outstanding shares of our capital stock entitled to vote to remove a director for cause, and, subject to the rights of any holders of preferred stock, filling any vacancy on our Board of Directors only by a vote of a majority of the directors then in office. The classification of our Board of Directors and the limitations on removal of directors and filling of vacancies could have the effect of making it more difficult for a third party to acquire us, or of discouraging a third party from acquiring us. Our certificate of incorporation and bylaws also provide that special meetings of the stockholders may only be called by our Board of Directors, Chairman, Chief Executive Officer or Secretary. These provisions, as well as other provisions of amended certificate of incorporation and amended and restated bylaws, may delay, defer or prevent a transaction or a change in control that might otherwise be in the best interests of our stockholders.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

We do not own any real estate or other physical properties materially important to our operation. Our administrative and principal executive offices are located at 40 East 52nd Street, New York, NY 10022. We believe that our office facilities are suitable and adequate for our business as it is contemplated to be conducted.

ITEM 3. LEGAL PROCEEDINGS

From time to time, we and the Advisor may be a party to certain legal proceedings incidental to the normal course of our business, including the enforcement of our rights under contracts with our portfolio companies. While we cannot predict the outcome of these legal proceedings with certainty, we do not expect that these proceedings will have a material effect on our financial statements.

ITEM 4. [RESERVED]

PART II

ITEM 5. MARKET FOR REGISTRANT’S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Price range of common stock

Our common stock is quoted on The NASDAQ Global Select Market under the symbol “BKCC”. The following table lists the high and low closing sales price for our common stock, the closing sales price as a percentage of NAV, and quarterly dividends per share for the years ended December 31, 2010 and 2009.

	Closing Sales Price			Premium/ Discount of High Sales Price to NAV (2)	Premium/ Discount of Low Sales Price to NAV (2)	Declared Dividends
	NAV(1)	High	Low			
Year Ended December 31, 2010						
First Quarter	\$ 9.77	\$10.10	\$ 8.52	103%	87%	\$ 0.32
Second Quarter	\$ 9.83	\$11.58	\$ 9.70	118%	99%	\$ 0.32
Third Quarter	\$ 9.76	\$11.97	\$ 9.58	123%	98%	\$ 0.32
Fourth Quarter	\$ 9.62	\$12.69	\$10.95	132%	114%	\$ 0.32
Year Ended December 31, 2009						
First Quarter	\$ 9.04	\$10.98	\$ 2.41	121%	27%	\$ 0.16
Second Quarter	\$ 9.24	\$ 7.00	\$ 4.24	76%	46%	\$ 0.16
Third Quarter	\$ 9.59	\$ 8.91	\$ 5.79	93%	60%	\$ 0.16
Fourth Quarter	\$ 9.55	\$ 8.79	\$ 7.23	92%	76%	\$ 0.32

- (1) NAV per share is determined as of the last day in the relevant quarter and therefore may not reflect the NAV per share on the date of the high and low sales prices. The NAVs shown are based on outstanding shares at the end of the relevant quarter.
- (2) Calculated as of the respective high or low closing sales price divided by NAV.

Holders

At February 28, 2011, there were approximately 356 holders of record of our common stock. Such number of stockholders includes institutional or omnibus accounts that hold common stock for multiple underlying investors.

Dividends

Our quarterly dividends, if any, are determined by our Board of Directors. Dividends are declared considering our estimate of annual taxable income available for distribution to stockholders and the amount of taxable income carried over from the prior year for distribution in the current year. We cannot assure stockholders that they will receive any dividends and distributions or dividends and distributions at a particular level. Dividends declared by the Company since July 25, 2005 (inception of operations) have been as follows:

Dividend Amount Per Share Outstanding	Record Date	Payment Date
\$ 0.20	December 31, 2005	January 31, 2006
\$ 0.20	March 15, 2006	March 31, 2006
\$ 0.23	June 15, 2006	June 30, 2006
\$ 0.30	September 15, 2006	September 29, 2006
\$ 0.42	December 31, 2006	January 31, 2007
\$ 0.42	March 15, 2007	March 30, 2007
\$ 0.42	May 15, 2007	May 31, 2007
\$ 0.42	September 14, 2007	September 28, 2007
\$ 0.43	December 14, 2007	December 31, 2007
\$ 0.43	March 17, 2008	March 31, 2008
\$ 0.43	June 16, 2008	June 30, 2008
\$ 0.43	September 15, 2008	September 30, 2008
\$ 0.43	December 15, 2008	December 31, 2008
\$ 0.16	March 20, 2009	April 3, 2009

[Table of Contents](#)

Dividend Amount Per Share Outstanding	Record Date	Payment Date
\$ 0.16	June 19, 2009	July 2, 2009
\$ 0.16	September 18, 2009	October 2, 2009
\$ 0.32	December 21, 2009	January 4, 2010
\$ 0.32	March 22, 2010	April 5, 2010
\$ 0.32	May 17, 2010	July 2, 2010
\$ 0.32	September 17, 2010	October 1, 2010
\$ 0.32	December 20, 2010	January 3, 2011
\$ 0.32	March 18, 2011	April 1, 2011

Tax characteristics of all dividends are reported to stockholders on Form 1099 after the end of the calendar year.

We have elected to be taxed as a RIC under Subchapter M of the Code. In order to maintain favorable RIC tax treatment, we must distribute annually to our stockholders 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 must distribute during each calendar year an amount at least equal to the sum of:

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

We may, at our discretion, carry forward taxable income in excess of calendar year distributions and pay a 4% excise tax on this income. If we choose to do so, all other things being equal, this would increase expenses and reduce the amounts available to be distributed to our stockholders. We will accrue excise tax on estimated taxable income as required. In addition, although we currently intend to distribute realized net capital gains (i.e., 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 in the future decide to retain such capital gains for investment. For the years ended December 31, 2010, 2009 and 2008, we recorded a provision for federal excise taxes of \$298,322, \$1,012,791 and \$436,733, respectively. Undistributed taxable income carried forward from 2010, currently estimated to be approximately \$8,900,000 or \$0.12 per share, will be paid out as dividends to stockholders in 2011.

We maintain an “opt out” dividend reinvestment plan for our common stockholders. As a result, if we declare a dividend, stockholders’ cash dividends will be automatically reinvested in additional shares of our common stock, unless they specifically “opt out” of the dividend reinvestment plan so as to receive cash dividends. With respect to our dividends and distributions paid to stockholders during the years ended December 31, 2010, 2009 and 2008, dividends reinvested pursuant to our dividend reinvestment plan totaled \$5,468,133, \$9,083,849 and \$28,689,391, respectively.

Under the terms of an amendment to our dividend reinvestment plan adopted on March 4, 2009, dividends may be paid in newly issued or treasury shares of our common stock at a price equal to 95% of the market price on the dividend payment date. This feature of the plan means that, under certain circumstances, we may issue shares of our common stock at a price below net asset value per share, which could cause our stockholders to experience dilution.

We may not be able to achieve operating results that will allow us to make dividends and distributions at a specific level or to increase the amount of these dividends and distributions from time to time. Also, we may be limited in our ability to make dividends and distributions due to the asset coverage test applicable to us as a BDC under the 1940 Act and due to provisions in our existing and future debt arrangements. If we do not distribute a certain percentage of our income annually, we will suffer adverse tax consequences, including possible loss of favorable RIC tax treatment. In addition, in accordance with U.S. generally accepted accounting principles and tax regulations, we include in income certain amounts that we have not yet received in cash, such as payment-in-kind interest, which represents contractual interest added to the loan balance that becomes due at the end of the loan term, or the accrual of original issue or market discount. Since we may recognize income before or without receiving cash representing such income, we may have difficulty meeting the requirement to distribute at least 90% of our investment company taxable income to obtain tax benefits as a RIC and may be subject to an excise tax.

With respect to dividends paid to stockholders, income we receive from origination, structuring, closing, commitment and other upfront fees associated with investments in portfolio companies is treated as taxable income when received and accordingly, distributed to stockholders. For the years ended December 31, 2010, 2009 and 2008, these fees totaled \$9,917,939, zero and \$2,571,938, respectively. For financial reporting purposes, such fees are recorded as

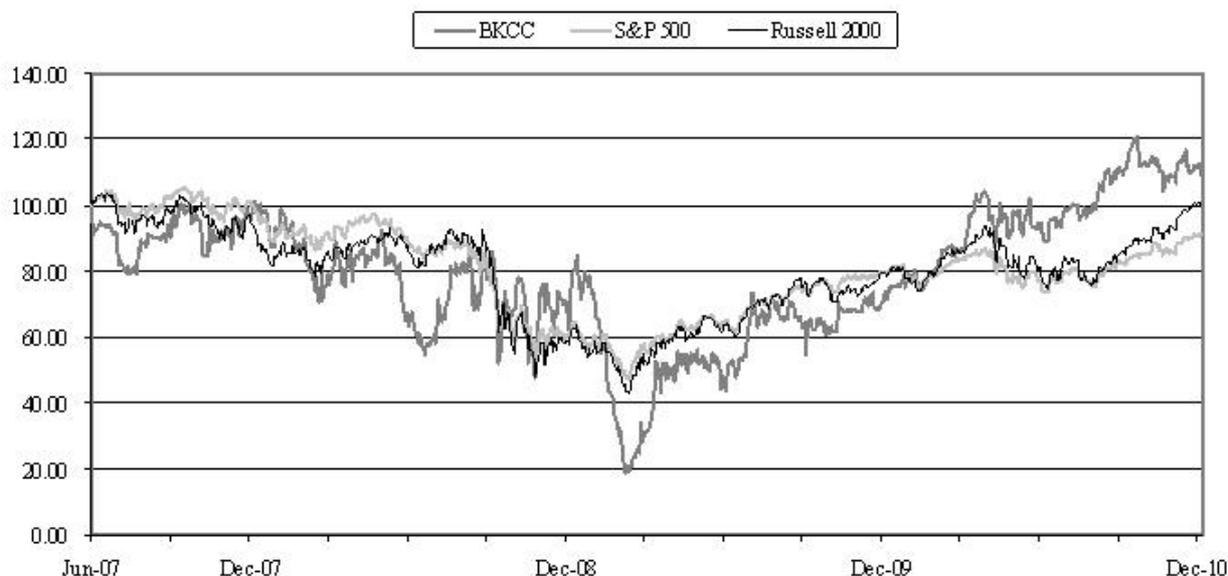
[Table of Contents](#)

unearned income and accreted/amortized over the life of the respective investment. We anticipate earning additional upfront fees in the future and such fees may cause our taxable income to exceed our GAAP income, although the differences are expected to be temporary in nature.

In order to satisfy the annual distribution requirement applicable to RICs, we have the ability to declare a large portion of a dividend in shares of our common stock instead of in cash. As long as a portion of such dividend is paid in cash (which portion can be as low as 10% for our taxable years ending prior to 2012) and certain requirements are met, the entire distribution would be treated as a dividend for U.S. federal income tax purposes.

Stock performance graph

The following graph compares the return on our common stock with that of the Standard & Poor’s 500 Stock Index and the Russell 2000 Financial Services Index for the period June 27, 2007 (the date our common stock began to trade on The NASDAQ Global Select Market in connection with our initial public offering) through December 31, 2010. The graph assumes that, on June 27, 2007, a person invested \$100 in each of our common stock (“BKCC” in the graph), the S&P 500 Index (“S&P 500”), and the Russell 2000 Financial Services Index (“Russell 2000”). The graph measures total shareholder return, which takes into account both changes in stock price and dividends. It assumes that dividends paid are invested in like securities.



The graph and other information furnished under this part II Item 5 of this Form 10-K shall not be deemed to be “soliciting material” or to be “filed” with the SEC or subject to Regulation 14A or 14C, or to the liabilities of Section 18 of the Securities Exchange Act of 1934, or the Exchange Act. The stock price performance included in the above graph is not necessarily indicative of future stock performance.

[Table of Contents](#)

ITEM 6. SELECTED FINANCIAL DATA

The unaudited Statement of Operations Data, Per Share Data and Balance Sheet Data for each of the five years in the period ended December 31, 2010 are derived from our financial statements which have been audited by Deloitte & Touche LLP, our independent registered public accounting firm. This selected financial data should be read in conjunction with our financial statements and related notes thereto and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” included elsewhere in this Annual Report.

	Year ended December 31, 2010	Year ended December 31, 2009	Year ended December 31, 2008	Year ended December 31, 2007	Year ended December 31, 2006
(Dollars in thousands, except per share data)					
Statement of Operations Data:					
Total Investment Income	\$ 105,871	\$ 124,884	\$ 143,196	\$ 127,776	\$ 53,892
Net Expenses (including excise taxes):					
Before Base Management Fee Waiver	46,020	48,831	48,093	53,987	18,314
After Base Management Fee Waiver(1)	46,020	48,831	48,093	51,930	14,000
Net Investment Income	59,851	76,053	95,103	75,846	39,892
Net Realized and Unrealized Gain (Loss)	11,699	(8,813)	(245,610)	(59,626)	1,662
Net Increase (Decrease) in Net Assets Resulting from Operations	71,550	67,240	(150,507)	16,219	41,555
Per Share Data:					
Net Asset Value Per Common Share at Year End	\$ 9.62	\$ 9.55	\$ 9.23	\$ 13.78	\$ 14.93
Market Price at Year End(2)	11.06	8.52	9.86	15.28	—
Net Investment Income	0.96	1.36	1.76	1.66	1.09
Net Realized and Unrealized Gain (Loss)	0.18	(0.16)	(4.54)	(1.31)	0.04
Net Increase (Decrease) in Net Assets Resulting from Operations	1.14	1.20	(2.78)	0.35	1.13
Dividends Declared	1.28	0.80	1.72	1.69	1.15
Balance Sheet Data at Year End:					
Total Assets	\$ 915,608	\$ 879,526	\$ 966,192	\$1,121,942	\$ 766,259
Borrowings Outstanding	170,000	296,000	426,000	381,300	164,000
Total Net Assets	698,480	539,563	510,296	728,192	561,800
Other Data:					
Total Return(3)	48.4%	(5.9)%	(23.9)%	3.4%	7.8%
Number of Portfolio Companies at Year End	50	57	63	60	49
Value of Investments at Year End	\$ 880,086	\$ 846,742	\$ 926,845	\$1,098,261	\$ 754,168
Yield on Investments at Year End(4)	10.9%	11.2%	11.0%	12.4%	12.5%

(1) The base management fee waiver terminated on June 30, 2007.

(2) Our common stock commenced trading on The NASDAQ Global Select Market on June 27, 2007. There was no established public trading market for the stock prior to that date.

(3) For the years ended December 31, 2010, 2009 and 2008, total return is based on the change in market price during the respective years. For the years ended December 31, 2007 and 2006, total return is based on the change in net asset value per common share during the respective years. The total return for the period June 26, 2007 through December 31, 2007 based on the change in market price per common share during such period was 1.2%. Total return calculations take into account dividends and distributions, if any, reinvested in accordance with our dividend reinvestment plan and do not reflect brokerage commissions. Total return is not annualized.

(4) Yield on investments at year end represents the weighted average yield on the debt and income producing equity securities in our portfolio at their current cost basis. Yields are computed using interest rates and dividend yields at year end and include amortization of loan origination and commitment fees, original issue discount and market premium or discount. Yields exclude common equity investments, preferred equity investments with no stated dividend rate, short-term investments, cash and cash equivalents.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The information contained in this section should be read in conjunction with the Selected Financial Data and our financial statements and notes thereto appearing elsewhere in this Annual Report.

Forward-looking statements

This report, and other statements that we may make, may contain forward-looking statements with respect to future financial or business performance, strategies or expectations. Forward-looking statements are typically identified by words or phrases such as “trend,” “opportunity,” “pipeline,” “believe,” “comfortable,” “expect,” “anticipate,” “current,” “intention,” “estimate,” “position,” “assume,” “potential,” “outlook,” “continue,” “remain,” “maintain,” “sustain,” “seek,” “achieve” and similar expressions, or future or conditional verbs such as “will,” “would,” “should,” “could,” “may” or similar expressions.

Forward-looking statements are subject to numerous assumptions, risks and uncertainties, which change over time. Forward-looking statements speak only as of the date they are made, and we assume no duty to and do not undertake to update forward-looking statements. Actual results could differ materially from those anticipated in forward-looking statements and future results could differ materially from historical performance.

In addition to factors previously disclosed in our SEC reports and those identified elsewhere in this report, including the “Risk Factors” section, the following factors, among others, could cause actual results to differ materially from forward-looking statements or historical performance:

- 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, including our ability to obtain continued financing on favorable terms;
- the timing of cash flows, if any, from the operations of our portfolio companies;
- the impact of increased competition;
- the ability of the Advisor to locate suitable investments for us and to monitor and administer our investments;
- potential conflicts of interest in the allocation of opportunities between us and other investment funds managed by the Advisor or its affiliates;
- the ability of the Advisor to attract and retain highly talented professionals;
- fluctuations in foreign currency exchange rates; and
- the impact of changes to tax legislation and, generally, our tax position.

Overview

We were incorporated in Delaware on April 13, 2005 and were initially funded on July 25, 2005. Our investment objective is to provide a combination of current income and capital appreciation. We intend to invest primarily in debt and equity securities of private and certain public U.S. middle-market companies.

We are externally managed and have elected to be regulated as a BDC under the 1940 Act. As a BDC, we are required to comply with certain regulatory requirements. For instance, we generally have to invest at least 70% of our total assets in “qualifying assets,” including securities of private or thinly traded public U.S. companies, cash, cash equivalents, U.S. Government securities and high-quality debt investments that mature in one year or less.

Investments

Our level of investment activity can and does vary substantially from period to period depending on many factors, including the amount of debt and equity capital available to middle-market companies, the level of merger and acquisition activity, the general economic environment and the competitive environment for the types of investments we make.

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). Qualifying assets include investments in “eligible portfolio companies.” Under the relevant SEC rules, the term “eligible portfolio company” includes all private companies and companies whose securities are not listed on a national securities exchange, as well as certain public companies that have listed their securities on a national securities exchange and have a market capitalization of less than \$250 million. These rules also permit us to include as qualifying assets certain follow-on investments in companies that were eligible portfolio companies at the time of initial investment but that no longer meet the definition.

Revenues

We generate revenues primarily in the form of interest on the debt we hold, dividends on our equity interests and capital gains on the sale of warrants and other debt or equity interests that we acquire in portfolio companies. Our investments in fixed income instruments generally have an expected maturity of three to ten years, although we have no lower or upper constraint on maturity, and typically bear interest at a fixed or floating rate. Interest on our debt securities is generally payable quarterly or semi-annually. Payments of principal of our debt investments may be amortized over the stated term of the investment, deferred for several years or due entirely at maturity. In some cases, our debt instruments and preferred stock investments may defer payments of cash interest or dividends or pay interest or dividends in-kind. Any outstanding principal amount of our debt securities and any accrued but unpaid interest will generally become due at the maturity date. In addition, we may generate revenue in the form of prepayment fees, commitment, origination, structuring or due diligence fees, fees for providing significant managerial assistance and consulting fees.

Expenses

Our primary operating expenses include the payment of a base management fee and, depending on our operating results, an incentive management fee, expenses reimbursable under the management agreement, administration fees and the allocable portion of overhead under the administration agreement. The base management fee and incentive management fee compensate the Advisor for work in identifying, evaluating, negotiating, closing and monitoring our investments. Our management agreement with the Advisor provides that we will reimburse the Advisor for costs and expenses incurred by the Advisor for office space rental, office equipment and utilities allocable to the Advisor under the management agreement, as well as any costs and expenses incurred by the Advisor relating to any non-investment advisory, administrative or operating services provided by the Advisor to us. We bear all other costs and expenses of our operations and transactions, including those relating to:

- our organization;
- calculating our net asset value (including the cost and expenses of any independent valuation firms);
- expenses incurred by the Advisor payable to third parties in monitoring our investments and performing due diligence on prospective portfolio companies;
- interest payable on debt, if any, incurred to finance our investments;
- the costs of future offerings of common shares and other securities, if any;
- the base management fee and any incentive management fee;
- dividends and distributions on our preferred shares, if any, and common shares;
- administration fees payable under the administration agreement;
- fees payable to third parties relating to, or associated with, making investments;
- transfer agent and custodial fees;
- registration fees;
- listing fees;
- taxes;
- independent director fees and expenses;

Table of Contents

- costs of preparing and filing reports or other documents with the SEC;
- the costs of any reports, proxy statements or other notices to our stockholders, including printing costs;
- our fidelity bond;
- directors and officers/errors and omissions liability insurance, and any other insurance premiums;
- indemnification payments;
- direct costs and expenses of administration, including audit and legal costs; and
- all other expenses reasonably incurred by us or the Administrator in connection with administering our business, such as the allocable portion of overhead under the administration agreement, including rent and other allocable portions of the cost of certain of our officers and their respective staffs.

Additionally, the management agreement provides that the Advisor or its affiliates may be entitled to the Incentive Fee under certain circumstances. The determination of the Incentive Fee will result in the Advisor or its affiliates receiving no Incentive Fee payments if returns to our stockholders do not meet an 8.0% annualized rate of return and will result in the Advisor or its affiliates receiving less than the full amount of the Incentive Fee percentage until returns to stockholders exceed an approximate 13.3% annualized rate of return. Annualized rate of return in this context is computed by reference to our net asset value and does not take into account changes in the market price of our common stock. The determination of the Incentive Fee is subject to any applicable limitations under the 1940 Act and the Advisers Act.

Critical accounting policies

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. Management considers the following critical accounting policies important to understanding the financial statements. In addition to the discussion below, our critical accounting policies are further described in the notes to the financial statements. See Note 2 to the financial statements for a description of recently issued accounting pronouncements.

Valuation of portfolio investments

Investments for which market quotations are readily available are valued at such market quotations unless they are deemed not to represent fair value. We obtain market quotations, when available, from an independent pricing service or one or more broker-dealers or market makers and utilize the average of the range of bid and ask quotations as a practical expedient for fair value. However, debt investments with remaining maturities within 60 days are valued at amortized cost, which approximates fair value. Debt and equity securities for which market quotations are not readily available or for which market quotations are deemed not to represent fair value are valued at fair value as determined in good faith by or under the direction of our Board of Directors. Because we expect that there will not be a readily available market value for substantially all of the investments in our portfolio, we expect to value substantially all of our portfolio investments at fair value as determined in good faith under the direction of our Board of Directors using a consistently applied valuation process in accordance with a documented valuation policy that has been reviewed and approved by our Board of Directors. Due to the inherent uncertainty and subjectivity of determining the fair value of investments that do not have a readily available market value, the fair value of our investments may differ significantly from the values that would have been used had a readily available market value existed for such investments and may differ materially from the values that we may ultimately realize. In addition, changes in the market environment and other events may have differing impacts on the market quotations used to value some of our investments than on the fair values of our investments for which market quotations are not readily available. Market quotations may be deemed not to represent fair value in certain circumstances where the Advisor believes that facts and circumstances applicable to an issuer, a seller or purchaser or the market for a particular security cause current market quotations to not reflect the fair value of the security. Examples of these events could include cases where a security trades infrequently causing a quoted purchase or sale price to become stale, where there is a “forced” sale by a distressed seller, where markets quotations vary substantially among market makers, or where there is a wide bid-ask spread or significant increase in the bid-ask spread.

With respect to investments for which market quotations are not readily available or for which 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:

[Table of Contents](#)

- our quarterly valuation process begins with each portfolio company or investment being initially evaluated and rated by the investment professionals of the Advisor responsible for the portfolio investment;
- the investment professionals provide recent portfolio company financial statements and other reporting materials to independent valuation firms engaged by our Board of Directors, such firms conduct independent appraisals each quarter and their preliminary valuation conclusions are documented and discussed with senior management of the Advisor;
- the audit committee of our Board of Directors reviews the preliminary valuations prepared by the independent valuation firms; and
- the Board of Directors discusses valuations and determines the fair value of each investment in our portfolio in good faith based on the input of the Advisor, the respective independent valuation firms and the audit committee.

Those investments for which market quotations are not readily available or for which market quotations are deemed not to represent fair value are valued utilizing a market approach, an income approach, or both approaches, as appropriate. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities (including a business). The income approach uses valuation techniques to convert future amounts (for example, cash flows or earnings) to a single present amount (discounted). The measurement is based on the value indicated by current market expectations about those future amounts. In following these approaches, 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, M&A comparables, our principal market (as the reporting entity) and enterprise values.

Until the end of the second calendar quarter following its acquisition, each unquoted investment in a new portfolio company generally is valued at cost, which the Advisor believes approximates fair value under the circumstances. As of that date, an independent valuation firm conducts an initial independent appraisal of the investment.

Accounting Standards Codification ("ASC") 820-10, *Fair Value Measurements and Disclosures* ("ASC 820-10"), defines fair value, establishes a framework for measuring fair value and requires enhanced disclosures about fair value measurements. ASC 820-10 defines fair value as the price that a company would receive upon selling an investment or pay to transfer a liability in an orderly transaction to a market participant in the principal or most advantageous market for the investment. ASC 820-10 emphasizes that valuation techniques maximize the use of observable market inputs and minimize the use of unobservable inputs. Inputs refer broadly to the assumptions that market participants would use in pricing an asset or liability, including assumptions about risk. Inputs may be observable or unobservable. Observable inputs are inputs that reflect the assumptions market participants would use in pricing an asset or liability developed based on market data obtained from sources independent of us. Unobservable inputs are inputs that reflect our assumptions about the assumptions market participants would use in pricing an asset or liability developed based on the best information available in the circumstances.

ASC 820-10 establishes a hierarchy that classifies these inputs into the three broad levels listed below:

Level 1 – Valuations based on unadjusted quoted prices in active markets for identical assets or liabilities that a company has the ability to access.

Level 2 – Valuations based on unadjusted quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly.

Level 3 – Valuations based on inputs that are unobservable and significant to the overall fair value measurement. The inputs into the determination of fair value may require significant management judgment or estimation. Even if observable market data is available, such information may be the result of consensus pricing information or broker quotes which include a disclaimer that the broker would not be held to such a price in an actual transaction. The non-binding nature of consensus pricing and/or quotes accompanied by disclaimer would result in classification as Level 3 information, assuming no additional corroborating evidence.

Transfers between levels, if any, represent the value as of the beginning of the period of any investment where a change in the pricing level occurred from the beginning to the end of the period.

[Table of Contents](#)

Our valuation policy and fair value disclosures are consistent with ASC 820-10. We evaluate the source of inputs, including any markets in which our investments are trading, in determining fair value and categorize each investment within the fair value hierarchy pursuant to ASC 820-10.

Determination of fair value involves subjective judgments and estimates. Accordingly, the notes to our financial statements express the uncertainty with respect to the possible effect of such valuations, and any change in such valuations, on the financial statements.

Revenue recognition

We record interest income, adjusted for amortization of premium and accretion of discount, and dividend income on an accrual basis to the extent that we expect to collect such amounts. For loans and securities with payment-in-kind (“PIK”) income, which represents contractual interest or dividends accrued and added to the principal balance and generally due at maturity, PIK income is accrued only to the extent that the portfolio company valuation indicates that the PIK income is likely to be collected. We may not accrue PIK income if the portfolio company valuation indicates that the PIK income is not collectible. Origination, structuring, closing, commitment and other upfront fees and discounts and premiums on investments purchased are accreted/amortized over the life of the respective investment. Unamortized origination, structuring, closing, commitment and other upfront fees are recorded as unearned income. Upon the prepayment of a loan or debt security, we record any prepayment penalties and unamortized loan origination, structuring, closing, commitment and other upfront fees as interest income. Expenses are recorded on an accrual basis.

With respect to the dividends paid to stockholders, income we receive from origination, structuring, closing, commitment and other upfront fees associated with investments in portfolio companies is treated as taxable income when received and, accordingly, distributed to stockholders. For the years ended December 31, 2010, 2009 and 2008, these fees totaled \$9,917,939, zero and \$2,571,938, respectively. For financial reporting purposes, such fees are recorded as unearned income and accreted/amortized over the life of the respective investment. We anticipate earning additional upfront fees in the future and such fees may cause our taxable income to exceed our GAAP income, although the differences are expected to be temporary in nature.

Net realized gains or losses and net change in unrealized appreciation or depreciation

We measure realized gains or losses by the difference between the net proceeds from the repayment or sale and the amortized cost basis of the investment, without regard to unrealized appreciation or depreciation previously recognized, but considering unamortized upfront fees and prepayment fees. Realized gains and losses are computed using the specific identification method. Net change in unrealized appreciation or depreciation reflects the change in portfolio investment values during the reporting period, including the reversal of previously recorded unrealized appreciation or depreciation, when gains or losses are realized.

Federal income taxes

We have elected to be taxed as a RIC under Subchapter M of the Code and currently qualify, and intend to continue to qualify each year, as a RIC under the Code. In order to qualify as a RIC, we are required to distribute annually at least 90% of investment company taxable income, as defined by the Code, to our stockholders. To avoid federal excise taxes, we must distribute annually at least 98% of our income from the current year (both ordinary income and net capital gains) and any undistributed ordinary income and net capital gains from the preceding years. We may, at our discretion, carry forward taxable income in excess of calendar year distributions and pay a 4% excise tax on this income. If we choose to do so, all other things being equal, this would increase expenses and reduce the amount available to be distributed to our stockholders. We will accrue excise tax on estimated excess taxable income as required. For the years ended December 31, 2010, 2009 and 2008, we recorded a provision for federal excise taxes of \$298,322, \$1,012,791 and \$436,733, respectively. Undistributed taxable income carried forward from 2010, currently estimated to be approximately \$8,900,000 or \$0.12 per share, will be paid out as dividends to stockholders in 2011.

Financial and operating highlights

At December 31, 2010:

Investment Portfolio: \$882.2 million
Net Assets: \$698.5 million
Indebtedness (borrowings under Credit Facility): \$170.0 million
Net Asset Value per share: \$9.62

[Table of Contents](#)

Portfolio Activity for the Year Ended December 31, 2010:

Cost of investments during period: \$406.0 million
Sales, repayments and other exits during period: \$395.3 million
Number of portfolio companies at end of period: 50

Operating Results for the Year Ended December 31, 2010:

Net investment income per share: \$0.96
Dividends declared per share: \$1.28
Earnings per share: \$1.14
Net investment income: \$59.9 million
Net realized and unrealized losses: \$11.7 million
Net increase in net assets from operations: \$71.5 million

Portfolio and investment activity

During the year ended December 31, 2010, we invested approximately \$406.0 million across eight new and several existing portfolio companies. The new investments consisted primarily of senior loans secured by first liens (\$105.6 million, or 26% of the total) or second liens (\$108.9 million, or 27%), unsecured or subordinated debt securities (\$118.3 million, or 29%), senior secured notes (\$45.4 million, or 11%) and equity securities (\$27.8 million, or 7%). Additionally, we received proceeds from sales, repayments and other exits of investment principal of approximately \$395.3 million during the year ended December 31, 2010.

At December 31, 2010, our net portfolio of \$882 million (at fair value) consisted of 50 portfolio companies and was invested 50% in senior secured loans, 26% in unsecured or subordinated debt securities, 14% in equity investments, 10% in senior secured notes and less than 1% in cash and cash equivalents. Our average portfolio company investment at amortized cost was approximately \$19.7 million. Our largest portfolio company investment by value was approximately \$53.1 million and our five largest portfolio company investments by value comprised approximately 26% of our portfolio at December 31, 2010. At December 31, 2009, our net portfolio of \$853 million (at fair value) consisted of 57 portfolio companies and was invested 59% in senior secured loans, 30% in unsecured or subordinated debt securities, 6% in senior secured notes, 5% in equity investments and less than 1% in cash and cash equivalents. Our average portfolio company investment at amortized cost was approximately \$18.5 million at December 31, 2009. Our largest portfolio company investment by value was approximately \$56.1 million and our five largest portfolio company investments by value comprised approximately 26% of our portfolio at December 31, 2009.

The weighted average yield of the debt and income producing equity securities in our portfolio at fair value was 12.4% at December 31, 2010 and 13.7% at December 31, 2009. The weighted average yields on our senior secured loans and other debt securities at fair value were 11.3% and 14.3%, respectively, at December 31, 2010, versus 11.6% and 17.2% at December 31, 2009. The weighted average yield of the debt and income producing equity securities in our portfolio at their current cost basis was 10.9% at December 31, 2010 and 11.2% at December 31, 2009. The weighted average yields on our senior secured loans and other debt securities at their current cost basis were 10.1% and 12.1%, respectively, at December 31, 2010, versus 9.4% and 14.2% at December 31, 2009. Yields are computed using interest rates and dividend yields as of the balance sheet date and include amortization of loan origination and commitment fees, original issue discount and market premium or discount. Yields exclude common equity investments, preferred equity investments with no stated dividend rate, short-term investments, cash and cash equivalents.

At December 31, 2010, 45% of our debt investments bore interest based on floating rates, such as LIBOR, EURIBOR, the Federal Funds Rate or the Prime Rate, and 55% bore interest at fixed rates. The percentage of our total debt investments that bore floating rate interest subject to an interest rate floor was 25% at December 31, 2010. At December 31, 2009, 41% of our debt investments bore interest based on floating rates and 59% bore interest at fixed rates. The percentage of our total debt investments that bore floating rate interest subject to an interest rate floor was 5% at December 31, 2009.

Results of operations

Results comparisons are for the years ended December 31, 2010, 2009 and 2008.

Investment income

Investment income totaled \$105,870,837, \$124,884,057 and \$143,195,713, respectively, for the years ended December 31, 2010, 2009 and 2008, of which \$57,321,456, \$68,096,154 and \$86,676,943 were attributable to interest and fees on senior secured loans, \$44,042,992, \$54,112,822 and \$52,957,970 to interest earned on other debt securities,

[Table of Contents](#)

\$4,385,525, \$2,590,001, and \$3,022,861 to dividends from equity securities, \$8,610, \$11,509 and \$321,162 to interest earned on short-term investments and cash equivalents, and \$112,254, \$73,571 and \$216,777 to other income, respectively. The decrease in investment income compared to the prior year primarily reflects a reduction in the size of our portfolio due to sales, repayments and other exits. Total investments at their current cost basis were \$985,677,505 at December 31, 2010, compared to \$1,054,820,003 at December 31, 2009. In addition, since net new investment activity was strongest in the latter half of 2010, its impact on investment income for the year was somewhat diminished.

Expenses

Total expenses for the years ended December 31, 2010, 2009 and 2008 were \$45,721,726, \$47,818,496 and \$47,655,991, respectively, which consisted of \$16,877,854, \$18,498,189 and \$22,716,602 in base management fees, \$15,108,049, \$16,818,602 and zero in incentive management fees owed to the Advisor, \$6,233,689, \$6,416,888 and \$18,667,097 in interest expense and fees related to the Credit Facility, \$2,136,038, \$683,552 and \$654,460 in amortization of debt issuance costs, \$1,622,957, \$1,466,563, and \$1,027,135 in Advisor expenses, \$877,930, \$1,126,665 and \$1,775,146 in professional fees, \$763,876, \$807,837 and \$1,037,712 in administrative services, \$581,428, \$569,201 and \$535,420 in insurance expenses, \$385,750, \$360,095 and \$286,834 in director fees and \$1,134,155, \$1,070,904 and \$955,585 in other expenses, respectively. In addition, we recorded a provision for federal excise taxes of \$298,322, \$1,012,791 and \$436,733 for the years ended December 31, 2010, 2009 and 2008, respectively. The decreases in base management and incentive management fees primarily reflect a reduction in the size of our portfolio due to sales, repayment and other exits. The increase in amortization of debt issuance costs reflects the incurrence of structuring and arrangement fees as a result of our Credit Facility amendment in April 2010.

Net investment income

Net investment income was \$59,850,789, \$76,052,770 and \$95,102,989 respectively, for the years ended December 31, 2010, 2009 and 2008. The decrease is primarily a result of a decline in interest income partially offset by a reduction in expenses.

Net realized gain or loss

Net realized loss of \$(90,236,723) for the year ended December 31, 2010 was the result of \$(89,301,764) in net losses realized from the disposition or restructuring of our investments and \$(934,959) in net loss realized on foreign currency transactions. Net realized loss on investments for the year ended December 31, 2010 resulted primarily from the restructuring of our investments in Electrical Components International, Inc., Marsico Capital entities and Penton Media, Inc. Nearly the entire net realized loss on investments represents amounts that had been reflected in unrealized depreciation on investments in prior periods. Foreign currency losses mainly represent losses on forward currency contracts used to mitigate the impact that changes in foreign exchange rates would have on our investments denominated in foreign currencies. For the year ended December 31, 2009, net realized loss was \$(110,238,068) as a result of \$(106,531,541) in net losses realized from the disposition of investments and \$(3,706,527) in net loss realized on foreign currency transactions. For the year ended December 31, 2008 net realized gain was \$6,127,856 as a result of \$258,257 in net gains realized from the disposition of investments and \$5,869,599 in net gain realized on foreign currency transactions.

Net unrealized appreciation or depreciation

For the years ended December 31, 2010, 2009 and 2008, the change in net unrealized appreciation or depreciation was a decrease (increase) in net unrealized depreciation of \$101,935,495, \$101,425,021 and \$(251,738,227), respectively. The decrease in net unrealized depreciation for the year ended December 31, 2010 was comprised of a decrease in net unrealized depreciation on investments of \$102,486,118 and a net unrealized foreign currency translation loss of \$(550,623). The decrease in net unrealized depreciation on investments for the year ended December 31, 2010 was primarily represents reversals of prior years' net unrealized depreciation as a result of the investment restructurings and dispositions described above and improved capital market conditions. The valuations of our investments were favorably impacted by market-wide decreases in interest yields, as well as increases in multiples used to estimate the fair value of some of our investments. Market-wide movements and trading multiples are not necessarily indicative of any fundamental change in the condition or prospects of our portfolio companies. The decrease in net unrealized depreciation for the year ended December 31, 2009 was comprised of a decrease in net unrealized depreciation on investments of \$100,908,828 and a net foreign currency gain of \$516,193. The increase in net unrealized depreciation for the year ended December 31, 2008 was comprised of an increase in net unrealized depreciation on investments of \$(251,872,831) and a net unrealized foreign currency gain of \$134,604.

Net increase or decrease in net assets resulting from operations

The net increase or decrease in net assets resulting from operations was an increase of \$71,549,561 for the year ended December 31, 2010 and an increase (decrease) of \$67,239,732 and \$(150,507,382) for the years ended December 31, 2009 and 2008, respectively. As compared to the prior periods, the increase primarily reflects the decrease in net unrealized depreciation on investments, net of realized gains and losses, for the year ended December 31, 2010.

Financial condition, liquidity and capital resources

During the year ended December 31, 2010, we generated operating cash flows primarily from interest earned and fees received on senior secured loans and other debt securities, as well as from sales of selected portfolio company investments and repayments of principal.

Net cash provided by operating activities during the year ended December 31, 2010 was \$37,837,994. Our primary source of cash from operating activities during 2010 was a net increase in net assets from operations of \$71,549,561.

We used \$41,503,171 for financing activities during the year ended December 31, 2010. Our primary uses of cash for financing activities were \$69,837,299 of dividend distributions, \$126,000,000 of net repayments under our Credit Facility and \$8,020,996 of debt issuance costs incurred in connection with our Credit Facility amendment and January 2011 private placement of Senior Secured Notes. During the year ended December 31, 2010, we raised \$162,355,124 in net proceeds from two add-on public offerings of our common stock.

Our senior secured, multi-currency Credit Facility provides us with \$375,000,000 in total availability, consisting of \$275,000,000 of revolving loan commitments and \$100,000,000 of term loan commitments. Non-extending lender commitments of \$245,000,000 matured on December 6, 2010. The Credit Facility is secured by substantially all of the assets in the Company's portfolio, including cash and cash equivalents. The Credit Facility has a stated maturity date of December 6, 2013 and the interest rate applicable to borrowings thereunder is generally LIBOR plus an applicable spread of either 3.00% or 3.25% for revolving loans, based on a pricing grid depending on the Company's credit rating, and LIBOR plus 3.00% for term loans. The Credit Facility does not contain a LIBOR floor requirement. At December 31, 2010, the effective LIBOR spread under the Credit Facility was 3.17%. Term loan commitments under the Credit Facility have been fully drawn and, once repaid, may not be reborrowed. The Credit Facility also includes an "accordion" feature that allows the Company, under certain circumstances, to increase the size of the Credit Facility by up to an additional \$275,000,000 of revolving loan commitments and \$250,000,000 of term loan commitments. The Credit Facility is used to supplement the Company's equity capital to make additional portfolio investments and for other general corporate purposes. At December 31, 2010, we had \$170,000,000 drawn and outstanding under the Credit Facility, with \$205,000,000 available to us, subject to compliance with customary affirmative and negative covenants, including the maintenance of a minimum stockholders' equity, the maintenance of a ratio of not less than 200% of total assets (less total liabilities other than indebtedness) to total indebtedness, and restrictions on certain payments and issuance of debt. In addition, borrowings under the Credit Facility (and the incurrence of certain other permitted debt) are subject to compliance with a borrowing base that applies different advance rates to different types of assets in the Company's portfolio. At December 31, 2010, we were in compliance with all financial and operational covenants required by the Credit Facility.

At December 31, 2010, we had \$2,160,871 in cash and cash equivalents.

The primary use of existing funds is expected to be purchases of investments in portfolio companies, cash distributions to our stockholders, repayment of indebtedness and other general corporate purposes.

On June 7, 2010, our stockholders approved an amendment to our Certificate of Incorporation to increase the number of authorized shares of our common stock from 100,000,000 to 200,000,000. The amendment became effective on that date.

Our shelf registration permits us to offer, from time to time, up to approximately \$830 million of our common stock, preferred stock, debt securities, warrants representing rights to purchase shares of our common stock, preferred stock or debt securities and subscription rights. As a closed-end investment company regulated as a BDC under the 1940 Act, we are prohibited from selling shares of our common stock at a price below the current net asset value of the stock, or NAV, unless our stockholders approve such a sale and our Board of Directors makes certain determinations.

Contractual obligations

A summary of our significant contractual payment obligations for the repayment of outstanding borrowings under our Credit Facility at December 31, 2010 is as follows:

Table of Contents

	Payments Due By Period (dollars in millions)				
	Total	Less than 1 year	1-3 years	3-5 years	After 5 years
Credit Facility Payable(1)	\$170.0	\$ —	\$ 170.0	\$ —	\$ —
Interest and Commitment Fees Payable on Credit Facility	\$ 0.3	\$ —	\$ 0.3	\$ —	\$ —

(1) At December 31, 2010, \$205 million remained unused under our Credit Facility.

We have entered into several contracts under which we have future commitments. Pursuant to an investment management agreement, the Advisor manages our day-to-day operations and provides investment advisory services to us. Payments under the investment management agreement are equal to a percentage of the value of our gross assets and an incentive management fee, plus reimbursement of certain expenses incurred by the Advisor. Under our administration agreement, the Administrator provides us with administrative services, facilities and personnel. Payments under the administration agreement are equal to an allocable portion of overhead and other expenses incurred by the Administrator in performing its obligations to us, including rent and our allocable portion of the cost of certain of our officers and their respective staffs. Pursuant to various other agreements, subsidiaries of The Bank of New York Mellon Corporation provide custodian services, administrative and accounting services, transfer agency and compliance support services to us. Payments under such agreements are generally equal to a percentage of our average net assets plus reimbursement of reasonable expenses, and a base fee. Either party may terminate each of the investment management agreement, administration agreement and such other agreements without penalty upon not less than 60 days' written notice to the other. See Note 3 to our financial statements for more information regarding these agreements.

Off-balance sheet financing

In the normal course of business, the Company may enter into guarantees on behalf of portfolio companies. Under these arrangements, the Company would be required to make payments to third parties if the portfolio companies were to default on their related payment obligations. The Company's only such guarantee outstanding at December 31, 2010 and 2009 was terminated on January 17, 2011 with no payments having been made thereunder.

Dividends

Our quarterly dividends, if any, are determined by our Board of Directors. Dividends are declared considering our estimate of annual taxable income available for distribution to stockholders and the amount of taxable income carried over from the prior year for distribution in the current year. We cannot assure stockholders that they will receive any dividends and distributions or dividends and distributions at a particular level. Dividends declared by the Company since July 25, 2005 (inception of operations) have been as follows:

Dividend Amount Per Share Outstanding	Record Date	Payment Date
\$ 0.20	December 31, 2005	January 31, 2006
\$ 0.20	March 15, 2006	March 31, 2006
\$ 0.23	June 15, 2006	June 30, 2006
\$ 0.30	September 15, 2006	September 29, 2006
\$ 0.42	December 31, 2006	January 31, 2007
\$ 0.42	March 15, 2007	March 30, 2007
\$ 0.42	May 15, 2007	May 31, 2007
\$ 0.42	September 14, 2007	September 28, 2007
\$ 0.43	December 14, 2007	December 31, 2007
\$ 0.43	March 17, 2008	March 31, 2008
\$ 0.43	June 16, 2008	June 30, 2008
\$ 0.43	September 15, 2008	September 30, 2008
\$ 0.43	December 15, 2008	December 31, 2008
\$ 0.16	March 20, 2009	April 3, 2009
\$ 0.16	June 19, 2009	July 2, 2009
\$ 0.16	September 18, 2009	October 2, 2009
\$ 0.32	December 21, 2009	January 4, 2010
\$ 0.32	March 22, 2010	April 5, 2010
\$ 0.32	May 17, 2010	July 2, 2010

[Table of Contents](#)

Dividend Amount Per Share Outstanding	Record Date	Payment Date
\$ 0.32	September 17, 2010	October 1, 2010
\$ 0.32	December 20, 2010	January 3, 2011
\$ 0.32	March 18, 2011	April 1, 2011

Tax characteristics of all dividends are reported to stockholders on Form 1099 after the end of the calendar year.

We have elected to be taxed as a RIC under Subchapter M of the Code. In order to maintain favorable RIC tax treatment, we must distribute annually to our stockholders 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 must distribute during each calendar year an amount at least equal to the sum of:

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

We may, at our discretion, carry forward taxable income in excess of calendar year distributions and pay a 4% excise tax on this income. If we choose to do so, all other things being equal, this would increase expenses and reduce the amounts available to be distributed to our stockholders. We will accrue excise tax on estimated taxable income as required. In addition, although we currently intend to distribute realized net capital gains (i.e., 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 in the future decide to retain such capital gains for investment. For the years ended December 31, 2010, 2009 and 2008, we recorded a provision for federal excise taxes of \$298,322, \$1,012,791 and \$436,733, respectively. Undistributed taxable income carried forward from 2010, currently estimated to be approximately \$8,900,000 or \$0.12 per share, will be paid out as dividends to stockholders in 2011.

We maintain an “opt out” dividend reinvestment plan for our common stockholders. As a result, if we declare a dividend, stockholders’ cash dividends will be automatically reinvested in additional shares of our common stock, unless they specifically “opt out” of the dividend reinvestment plan so as to receive cash dividends. With respect to our dividends and distributions paid to stockholders during the years ended December 31, 2010, 2009 and 2008, dividends reinvested pursuant to our dividend reinvestment plan totaled \$5,468,133, \$9,083,849 and \$28,689,391, respectively.

Under the terms of an amendment to our dividend reinvestment plan adopted on March 4, 2009, dividends may be paid in newly issued or treasury shares of our common stock at a price equal to 95% of the market price on the dividend payment date. This feature of the plan means that, under certain circumstances, we may issue shares of our common stock at a price below net asset value per share, which could cause our stockholders to experience dilution.

We may not be able to achieve operating results that will allow us to make dividends and distributions at a specific level or to increase the amount of these dividends and distributions from time to time. Also, we may be limited in our ability to make dividends and distributions due to the asset coverage test applicable to us as a BDC under the 1940 Act and due to provisions in our existing and future debt arrangements. If we do not distribute a certain percentage of our income annually, we will suffer adverse tax consequences, including possible loss of favorable RIC tax treatment. In addition, in accordance with U.S. generally accepted accounting principles and tax regulations, we include in income certain amounts that we have not yet received in cash, such as payment-in-kind interest, which represents contractual interest added to the loan balance that becomes due at the end of the loan term, or the accrual of original issue or market discount. Since we may recognize income before or without receiving cash representing such income, we may have difficulty meeting the requirement to distribute at least 90% of our investment company taxable income to obtain tax benefits as a RIC and may be subject to an excise tax.

With respect to dividends paid to stockholders, income we receive from origination, structuring, closing, commitment and other upfront fees associated with investments in portfolio companies is treated as taxable income when received and accordingly, distributed to stockholders. For the years ended December 31, 2010, 2009 and 2008, these fees totaled \$9,917,939, zero and \$2,571,938, respectively. For financial reporting purposes, such fees are recorded as unearned income and accreted/amortized over the life of the respective investment. We anticipate earning additional upfront fees in the future and such fees may cause our taxable income to exceed our GAAP income, although the differences are expected to be temporary in nature.

[Table of Contents](#)

In order to satisfy the annual distribution requirement applicable to RICs, we have the ability to declare a large portion of a dividend in shares of our common stock instead of in cash. As long as a portion of such dividend is paid in cash (which portion can be as low as 10% for our taxable years ending prior to 2012) and certain requirements are met, the entire distribution would be treated as a dividend for U.S. federal income tax purposes.

Recent developments

On January 18, 2011, we closed a private placement issuance of \$158 million in aggregate principal amount of five-year, senior secured notes with a fixed interest rate of 6.50% and a maturity date of January 18, 2016 and \$17 million in aggregate principal amount of seven-year, senior secured notes with a fixed interest rate of 6.60% and a maturity date of January 18, 2018 (collectively, the "Senior Secured Notes"). The Senior Secured Notes were sold to certain institutional accredited investors pursuant to an exemption from registration under the Securities Act of 1933, as amended. Interest on the Senior Secured Notes is due semi-annually on January 18 and July 18, commencing on July 18, 2011. The proceeds from the issuance of the Senior Secured Notes were used to fund new portfolio investments, reduce outstanding borrowings under the Credit Facility and for general corporate purposes.

On March 1, 2011, our Board of Directors declared a dividend of \$0.32 per share, payable on April 1, 2011 to stockholders of record at the close of business on March 18, 2010.

Notice is hereby given in accordance with Section 23(c) of the 1940 Act that from time to time the Company may purchase shares of its common stock in the open market at prevailing market prices.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

We are subject to financial market risks, including changes in interest rates. At December 31, 2010, 45% of our debt investments bore interest based on floating rates, such as LIBOR, EURIBOR, the Federal Funds Rate or the Prime Rate. The interest rates on such investments generally reset by reference to the current market index after one to six months. At December 31, 2010, the percentage of our total debt investments that bore floating rate interest subject to an interest rate floor was 25%. Floating rate investments subject to a floor generally reset by reference to the current market index after one to six months only if the index exceeds the floor.

To illustrate the potential impact of changes in interest rates, we have performed the following analysis based on our December 31, 2010 balance sheet and assuming no changes in our investment structure. Net asset value is analyzed using the assumptions that interest rates, as defined by the LIBOR and U.S. Treasury yield curves, increase or decrease and that the yield curves of the rate shocks will be parallel to each other. Under this analysis, an instantaneous 100 basis point increase in LIBOR and U.S. Treasury yields would cause a decline of approximately \$13,000,000, or \$0.18 per share, in the value of our net assets at December 31, 2010 and a corresponding 100 basis point decrease in LIBOR and U.S. Treasury yields would cause an increase of approximately \$11,500,000, or \$0.16 per share, in the value of our net assets on that date.

While hedging activities may help to insulate us against adverse changes in interest rates, they also may limit our ability to participate in the benefits of lower interest rates with respect to our portfolio of investments. During the years ended December 31, 2010, 2009 and 2008, we did not engage in any interest rate hedging activity.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

See the Index to Financial Statements on page F-1.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

(a) **Evaluation of Disclosure Controls and Procedures.** The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act) as of the end of the period covered by this report. Based upon such evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective, as of December 31, 2010, to provide assurance that information that is required to be disclosed by the Company in the reports that it files or

[Table of Contents](#)

submits under the Exchange Act is recorded, processed, summarized, and reported, within the time periods specified by the SEC's rules and forms. Disclosure controls and procedures, include without limitation, controls and procedures designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

(b) **Management's Report on Internal Control Over Financial Reporting.** The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act). Under the supervision and with the participation of management, including the Chief Executive Officer and Chief Financial Officer, the Company conducted an evaluation of the effectiveness of the Company's internal control over financial reporting based on the criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on the Company's evaluation under the framework in *Internal Control—Integrated Framework*, management concluded that the Company's internal control over financial reporting was effective as of December 31, 2010. The Company's internal control over financial reporting as of December 31, 2010 has been audited by our independent registered public accounting firm, Deloitte & Touche LLP, as stated in its report titled "Report of Independent Registered Public Accounting Firm" on the following page.

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

(c) **Attestation Report of the Registered Public Accounting Firm.** Our independent registered public accounting firm, Deloitte & Touche LLP, has issued an attestation report on the Company's internal control over financial reporting, which is set forth on the following page.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of
BlackRock Kelso Capital Corporation:

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

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

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

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2010, based on the criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the statement of assets and liabilities, including the schedule of investments, as of December 31, 2010, and the related statements of operations, changes in net assets, cash flows and financial highlights for the year then ended of the Company and our report dated March 8, 2011 expressed an unqualified opinion on those financial statements.

/s/ Deloitte & Touche LLP

New York, New York
March 8, 2011

[Table of Contents](#)

(d) **Changes in Internal Control Over Financial Reporting.** There have been no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act) during our most recently completed fiscal quarter, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

None

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information required by this item is contained in the Registrant's definitive Proxy Statement for its 2011 Annual Stockholders Meeting to be filed with the Securities and Exchange Commission within 120 days after December 31, 2010 and is incorporated herein by reference.

ITEM 11. EXECUTIVE COMPENSATION

The information required by this item is contained in the Registrant's definitive Proxy Statement for its 2011 Annual Stockholders Meeting to be filed with the Securities and Exchange Commission within 120 days after December 31, 2010 and is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDERS MATTERS

The information required by this item is contained in the Registrant's definitive Proxy Statement for its 2011 Annual Stockholders Meeting to be filed with the Securities and Exchange Commission within 120 days after December 31, 2010 and is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information required by this item is contained in the Registrant's definitive Proxy Statement for its 2011 Annual Stockholders Meeting to be filed with the Securities and Exchange Commission within 120 days after December 31, 2010 and is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information required by this item is contained in the Registrant's definitive Proxy Statement for its 2011 Annual Stockholders Meeting to be filed with the Securities and Exchange Commission within 120 days after December 31, 2010 and is incorporated herein by reference.

PART IV**ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

The following documents are filed as part of this Annual Report:

- (1) Financial Statements – See the Index to Financial Statements on page F-1.
- (2) Financial Statement Schedules – None. We have omitted financial statements schedules because they are not required or are not applicable, or the required information is shown in the financial statements or notes to the financial statements.
- (3) Exhibits – Please note that the agreements included as exhibits to this Form 10-K are included to provide information regarding their terms and are not intended to provide any other factual or disclosure information about BlackRock Kelso Capital Corporation or the other parties to the agreements. The agreements contain representations and warranties by each of the parties to the applicable agreement that have been made solely for the benefit of the other parties to the applicable agreement and may not describe the actual state of affairs as of the date they were made or at any other time.

<u>Number</u>	<u>Description</u>
3.1	Certificate of Incorporation of the Registrant (1)
3.2	Certificate of Amendment to the Certificate of Incorporation of the Registrant (2)
3.3	Amended and Restated By-laws of the Registrant (3)
4.1	Form of Stock Certificate of the Registrant (4)
10.1	Investment Management Agreement between the Registrant and BlackRock Kelso Capital Advisors LLC (4)
10.2	Administration Agreement between the Registrant and BlackRock Financial Management, Inc. (5)
10.3	Amended and Restated Dividend Reinvestment Plan (6)
10.4	Custodian Services Agreement between PFPC Trust Company and the Registrant (5)
10.5	Foreign Custody Manager Agreement among Citibank, N.A., PFPC Trust Company and the Registrant (4)
10.6	Transfer Agency Services Agreement between PNC Global Investment Servicing Inc. and the Registrant (5)
10.7	Sub-Administration and Accounting Services Agreement by and among the Registrant, PNC Global Investment Servicing Inc. and BlackRock Financial Management, Inc. (5)
10.8	Waiver Reliance Letter between the Registrant and BlackRock Kelso Capital Advisors LLC (5)
10.9	Amended and Restated Senior Secured Credit Agreement, dated as of December 28, 2007, among the Registrant, the lenders party thereto and Citibank, N.A., as Administrative Agent (7)
10.10	Amendment No. 1 to Amended and Restated Senior Secured Credit Agreement, dated as of April 20, 2010, among the Registrant, the lenders and assuming lenders party thereto and Citibank, N.A., as Administrative Agent (8)
10.11	Note Purchase Agreement, dated as of January 18, 2011, among the Registrant and the purchasers party thereto (9)
14.1	Code of Ethics of the Registrant (10)
14.2	Code of Ethics and Business Conduct of the Registrant (11)
14.3	Code of Ethics of the Advisor (5)

Table of Contents

21.1*	Subsidiaries of the Registrant
31.1*	Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934
31.2*	Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934
32.1*	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U. S. C. 1350)

* Filed herewith.

- (1) Previously filed with the Registrant's Registration Statement on Form 10 (Commission File No. 000-51327), as amended, originally filed on May 24, 2005.
- (2) Filed with the Registrant's Form 8-K dated as of June 7, 2010.
- (3) Filed with the Registrant's Form 8-K dated as of November 9, 2009.
- (4) Previously filed with the Registrant's Registration Statement on Form N-2 (Commission File No. 333-141090), as amended, originally filed on March 6, 2007.
- (5) Previously filed with the Registrant's Form 10-K for the year ended December 31, 2005.
- (6) Previously filed with the Registrant's Form 8-K dated as of March 4, 2009.
- (7) Previously filed with the Registrant's Form 8-K dated as of January 2, 2008.
- (8) Previously filed with the Registrant's Form 8-K dated as of April 20, 2010.
- (9) Previously filed with the Registrant's Form 8-K dated as of January 18, 2011.
- (10) Previously filed with the Registrant's Form 10-K for the year ended December 31, 2009.
- (11) Previously filed with the Registrant's Form 10-K for the year ended December 31, 2008.

[Table of Contents](#)

INDEX TO FINANCIAL STATEMENTS

Report of Independent Registered Public Accounting Firm	F-2
Statements of Assets and Liabilities	F-3
Statements of Operations	F-4
Statements of Changes in Net Assets	F-5
Statements of Cash Flows	F-6
Schedules of Investments	F-7
Notes to Financial Statements	F-22

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of
BlackRock Kelso Capital Corporation:

We have audited the accompanying statements of assets and liabilities of BlackRock Kelso Capital Corporation (the “Company”), including the schedules of investments, as of December 31, 2010 and 2009, and the related statements of operations, changes in net assets, and cash flows for each of the three years ended December 31, 2010 and the financial highlights for each of the five years ended December 31, 2010. These financial statements and financial highlights are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. Our procedures included confirmation of investments as of December 31, 2010 and 2009, by correspondence with the custodian, loan agent or borrower; where replies were not received, we performed other auditing procedures. We believe that our audits provide a reasonable basis for our opinion.

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

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company’s internal control over financial reporting as of December 31, 2010, based on the criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 8, 2011 expressed an unqualified opinion on the Company’s internal control over financial reporting.

/s/ Deloitte & Touche LLP

New York, New York
March 8, 2011

BlackRock Kelso Capital Corporation
Statements of Assets and Liabilities

	December 31, 2010	December 31, 2009
Assets:		
Investments at fair value:		
Non-controlled, non-affiliated investments (amortized cost of \$822,763,237 and \$963,463,604)	\$ 707,262,774	\$ 810,035,780
Non-controlled, affiliated investments (amortized cost of \$80,424,668 and \$63,942,195)	77,376,201	26,793,989
Controlled investments (amortized cost of \$82,489,600 and \$27,414,204)	95,446,691	9,912,276
Total investments at fair value (amortized cost of \$985,677,505 and \$1,054,820,003)	880,085,666	846,742,045
Cash and cash equivalents	1,344,159	5,048,136
Cash denominated in foreign currencies (cost of \$798,560 and \$759,760)	816,712	759,765
Unrealized appreciation on forward foreign currency contracts	—	203,998
Receivable for investments sold	5,316,189	—
Interest receivable	10,763,333	18,441,527
Dividends receivable	9,849,927	6,620,903
Prepaid expenses and other assets	7,431,688	1,710,105
Total Assets	<u>\$ 915,607,674</u>	<u>\$ 879,526,479</u>
Liabilities:		
Payable for investments purchased	\$ 2,726,437	\$ 557,483
Unrealized depreciation on forward foreign currency contracts	368,445	—
Credit facility payable	170,000,000	296,000,000
Interest payable on credit facility	256,084	959,458
Dividend distributions payable	23,222,287	18,072,063
Base management fees payable	4,355,021	4,547,129
Incentive management fees payable	14,614,098	16,818,602
Accrued administrative services	80,164	201,728
Other accrued expenses and payables	1,505,214	2,807,254
Total Liabilities	<u>217,127,750</u>	<u>339,963,717</u>
Net Assets:		
Common stock, par value \$.001 per share, 200,000,000 and 100,000,000 common shares authorized, 73,531,317 and 57,436,875 issued and 72,569,638 and 56,475,196 outstanding	73,531	57,437
Paid-in capital in excess of par	994,200,522	826,617,395
Undistributed (distributions in excess of) net investment income	(4,029,341)	19,463,949
Accumulated net realized loss	(180,403,836)	(93,279,572)
Net unrealized depreciation	(105,935,052)	(207,870,547)
Treasury stock at cost, 961,679 and 961,679 shares held	(5,425,900)	(5,425,900)
Total Net Assets	<u>698,479,924</u>	<u>539,562,762</u>
Total Liabilities and Net Assets	<u>\$ 915,607,674</u>	<u>\$ 879,526,479</u>
Net Asset Value Per Share	\$ 9.62	\$ 9.55

The accompanying notes are an integral part of these financial statements.

BlackRock Kelso Capital Corporation
Statements of Operations

	Year ended December 31, 2010	Year ended December 31, 2009	Year ended December 31, 2008
Investment Income:			
From non-controlled, non-affiliated investments:			
Interest	\$ 92,169,396	\$ 119,051,462	\$ 134,491,870
Dividends	3,101,377	1,479,116	1,760,131
Other income	62,254	23,571	166,777
From non-controlled, affiliated investments:			
Interest	6,403,192	2,255,171	4,246,547
Dividends	1,284,148	1,110,885	1,262,730
Other income	—	—	50,000
From controlled investments:			
Interest	2,800,470	913,852	1,217,658
Other income	50,000	50,000	—
Total investment income	105,870,837	124,884,057	143,195,713
Expenses:			
Base management fees	16,877,854	18,498,189	22,716,602
Incentive management fees	15,108,049	16,818,602	—
Interest and credit facility fees	6,233,689	6,416,888	18,667,097
Amortization of debt issuance costs	2,136,038	683,552	654,460
Investment advisor expenses	1,622,957	1,466,563	1,027,135
Professional fees	877,930	1,126,665	1,775,146
Administrative services	763,876	807,837	1,037,712
Insurance	581,428	569,201	535,420
Director fees	385,750	360,095	286,834
Other	1,134,155	1,070,904	955,585
Total expenses	45,721,726	47,818,496	47,655,991
Net investment income before excise taxes	60,149,111	77,065,561	95,539,722
Excise tax expense	(298,322)	(1,012,791)	(436,733)
Net Investment Income	59,850,789	76,052,770	95,102,989
Realized and Unrealized Gain (Loss):			
Net realized gain (loss):			
Non-controlled, non-affiliated investments	(53,083,081)	(63,987,289)	145,474
Non-controlled, affiliated investments	(36,221,198)	12,240	112,783
Controlled investments	2,515	(42,556,492)	—
Foreign currency	(934,959)	(3,706,527)	5,869,599
Net realized gain (loss)	(90,236,723)	(110,238,068)	6,127,856
Net change in unrealized appreciation or depreciation on:			
Non-controlled, non-affiliated investments	32,535,681	86,293,709	(208,150,014)
Non-controlled, affiliated investments	39,491,418	(22,969,287)	(22,758,886)
Controlled investments	30,459,019	37,584,406	(20,963,931)
Foreign currency translation	(550,623)	516,193	134,604
Net change in unrealized appreciation or depreciation	101,935,495	101,425,021	(251,738,227)
Net realized and unrealized gain (loss)	11,698,772	(8,813,047)	(245,610,371)
Net Increase (Decrease) in Net Assets Resulting from Operations	\$ 71,549,561	\$ 67,239,723	\$ (150,507,382)
Net Investment Income Per Share	\$ 0.96	\$ 1.36	\$ 1.76
Earnings (Loss) Per Share	\$ 1.14	\$ 1.20	\$ (2.78)
Basic and Diluted Weighted-Average Shares Outstanding	62,663,002	55,923,757	54,043,069
Dividends Declared Per Share	\$ 1.28	\$ 0.80	\$ 1.72

The accompanying notes are an integral part of these financial statements.

BlackRock Kelso Capital Corporation
Statements of Changes in Net Assets

	Year ended December 31, 2010	Year ended December 31, 2009	Year ended December 31, 2008
Net Increase (Decrease) in Net Assets Resulting from Operations:			
Net investment income	\$ 59,850,789	\$ 76,052,770	\$ 95,102,989
Net realized gain (loss)	(90,236,723)	(110,238,068)	6,127,856
Net change in unrealized appreciation or depreciation	101,935,495	101,425,021	(251,738,227)
Net increase (decrease) in net assets resulting from operations	<u>71,549,561</u>	<u>67,239,723</u>	<u>(150,507,382)</u>
Dividend Distributions to Stockholders from:			
Net investment income	(80,455,656)	(44,582,894)	(92,157,734)
Net realized gains	—	(238,525)	(729,635)
Total dividend distributions	<u>(80,455,656)</u>	<u>(44,821,419)</u>	<u>(92,887,369)</u>
Capital Share Transactions:			
Proceeds from shares sold	170,861,250	—	—
Less offering costs	(8,506,126)	—	—
Reinvestment of dividends	5,468,133	9,083,849	28,689,391
Purchases of treasury stock	—	(2,234,892)	(3,191,008)
Net increase in net assets resulting from capital share transactions	<u>167,823,257</u>	<u>6,848,957</u>	<u>25,498,383</u>
Total Increase (Decrease) in Net Assets	<u>158,917,162</u>	<u>29,267,261</u>	<u>(217,896,368)</u>
Net assets at beginning of year	539,562,762	510,295,501	728,191,869
Net assets at end of year	<u>\$698,479,924</u>	<u>\$ 539,562,762</u>	<u>\$ 510,295,501</u>
Capital Share Activity:			
Shares issued from subscriptions	15,525,000	—	—
Shares issued from reinvestment of dividends	569,442	1,766,281	2,845,485
Purchases of treasury stock	—	(583,572)	(378,107)
Total increase in shares	<u>16,094,442</u>	<u>1,182,709</u>	<u>2,467,378</u>
Undistributed (distributions in excess of) net investment income at end of year	<u>\$ (4,029,341)</u>	<u>\$ 19,463,949</u>	<u>\$ 3,855,016</u>

The accompanying notes are an integral part of these financial statements.

BlackRock Kelso Capital Corporation
Statements of Cash Flows

	Year ended December 31, 2010	Year ended December 31, 2009	Year ended December 31, 2008
Operating Activities:			
Net increase (decrease) in net assets resulting from operations	\$ 71,549,561	\$ 67,239,723	\$(150,507,382)
Adjustments to reconcile net increase (decrease) in net assets resulting from operations to net cash provided by operating activities:			
Proceeds from dispositions of short-term investments—net	358,276	—	—
Purchases of investments	(405,956,515)	(46,757,709)	(197,266,147)
Sales (purchases) of foreign currency—net	(931,542)	(5,182,402)	5,942,467
Proceeds from sales/repayments of investments	395,269,097	128,224,448	120,312,897
Net change in unrealized appreciation or depreciation on investments	(102,486,118)	(100,908,828)	251,872,831
Net change in unrealized appreciation or depreciation on foreign currency translations	550,623	(516,193)	(134,604)
Net realized loss (gain) on investments	89,301,764	106,531,541	(258,257)
Net realized loss (gain) on foreign currency	934,959	3,706,527	(5,869,599)
Amortization of premium/discount—net	(9,829,869)	(5,537,815)	(3,275,791)
Amortization of debt issuance costs	2,136,038	683,552	654,460
Increase in receivable for investments sold	(5,316,189)	—	—
Decrease (increase) in interest receivable	7,678,194	(2,140,990)	(2,040,271)
Increase in dividends receivable	(3,229,024)	(2,459,657)	(2,364,631)
Decrease (increase) in prepaid expenses and other assets	163,375	(12,669)	(614,883)
Increase (decrease) in payable for investments purchased	2,168,954	(447,618)	1,005,101
Increase (decrease) in interest payable on credit facility	(703,374)	123,967	(672,786)
Increase (decrease) in base management fees payable	(192,108)	(1,177,900)	118,816
Increase (decrease) in incentive management fees payable	(2,204,504)	16,818,602	—
Increase (decrease) in accrued administrative services payable	(121,564)	31,283	(190,673)
Increase (decrease) in other accrued expenses and payables	(1,302,040)	1,164,212	551,889
Net cash provided by operating activities	<u>37,837,994</u>	<u>159,382,074</u>	<u>17,263,437</u>
Financing Activities:			
Proceeds from issuance of common stock—net of offering costs	162,355,124	—	—
Dividend distributions paid	(69,837,299)	(37,128,672)	(48,045,418)
Borrowings under credit facility	314,700,000	72,400,000	202,700,000
Repayments under credit facility	(440,700,000)	(202,400,000)	(158,000,000)
Increase in deferred debt issuance costs	(8,020,996)	—	(25,612)
Purchases of treasury stock	—	(2,234,891)	(3,191,008)
Net cash used in financing activities	<u>(41,503,171)</u>	<u>(169,363,563)</u>	<u>(6,562,038)</u>
Effect of exchange rate changes on cash and cash equivalents	18,147	3,119	(3,687)
Net increase (decrease) in cash	(3,647,030)	(9,978,370)	10,697,712
Cash and cash equivalents, beginning of year	5,807,901	15,786,271	5,088,559
Cash and cash equivalents, end of year	<u>\$ 2,160,871</u>	<u>\$ 5,807,901</u>	<u>\$ 15,786,271</u>
Supplemental disclosure of cash flow information and non-cash financing activities:			
Cash paid during year for:			
Interest	\$ 5,653,301	\$ 5,967,197	\$ 19,093,363
Taxes	\$ 1,111,018	\$ 515,351	\$ 132,484
Dividend distributions reinvested	\$ 5,468,133	\$ 9,083,849	\$ 28,689,391

The accompanying notes are an integral part of these financial statements.

BlackRock Kelso Capital Corporation
**Schedules of Investments
December 31, 2010**

<u>Portfolio Company</u>	<u>Industry(a)</u>	<u>Principal Amount or Number of Shares/Units</u>	<u>Cost(b)</u>	<u>Fair Value(c)</u>
Senior Secured Notes—12.6%				
AGY Holding Corp., Second Lien, 11.00%, 11/15/14	Glass Yarns/ Fibers	\$23,500,000	\$ 23,191,282	\$ 21,385,000
American Residential Services L.L.C. et al., Second Lien, 12.00%, 4/15/15, acquired 4/9/10(d)	HVAC/ Plumbing Services	40,000,000	39,836,651	40,400,000
TriMark USA, Inc., Second Lien, 11.50% (LIBOR + 1.75% cash, 2.00% PIK), 11/30/13	Food Service Equipment	32,136,228	32,136,228	26,480,252
Total Senior Secured Notes			<u>95,164,161</u>	<u>88,265,252</u>
Unsecured Debt—1.0%				
Big Dumpster Acquisition, Inc., 13.50% PIK, 7/5/15	Waste Management Equipment	49,067,970	45,096,414	2,208,059
Maple Hill Acquisition LLC, 13.50%, 10/1/15	Rigid Packaging	5,000,000	5,000,000	5,000,000
Total Unsecured Debt			<u>50,096,414</u>	<u>7,208,059</u>
Subordinated Debt—32.2%				
A & A Manufacturing Co., Inc., 14.00%, 5/16/16	Protective Enclosures	27,403,430	27,403,430	27,403,430
Aspen Marketing Holdings, Inc., 13.00%, 8/12/16	Marketing Services	50,000,000	50,000,000	50,000,000
Conney Safety Products, LLC, 16.00%, 10/1/14(e)	Safety Products	30,582,734	29,383,496	29,665,252
Mattress Giant Corporation, 11.00% PIK, 12/31/12(e)	Bedding —Retail	6,404,461	3,911,894	1,229,657
MediMedia USA, Inc., 11.38%, 11/15/14, acquired multiple dates(d)	Information Services	8,000,000	8,048,532	7,528,000
MedQuist Inc. et al., 13.00%, 10/15/16	Medical Transcription	43,000,000	43,000,000	43,000,000
The Pay-O-Matic Corp., 14.00% (12.00% cash, 2.00% PIK), 1/15/15	Financial Services	15,366,867	15,366,867	15,520,536
PGA Holdings, Inc., 12.50%, 3/12/16	Healthcare Services	5,000,000	4,935,425	5,000,000
Samova HC, LLC et al., 14.00% (12.00% cash, 2.00% PIK), 4/6/16	Healthcare Products	25,375,474	25,375,474	25,375,474
Sentry Security Systems, LLC, 16.00% (14.00% cash, 2.00% PIK), 8/7/12	Security Services	11,056,053	11,056,053	11,056,053
U.S. Security Holdings, Inc., 13.00% (11.00% cash, 2.00% PIK), 5/8/14, acquired 5/10/06(d)	Security Services	7,000,000	7,000,000	7,000,000
Wastequip, Inc., 13.00% (10.00% cash, 3.00% PIK), 2/5/15	Waste Management Equipment	8,510,274	8,163,533	2,153,099
Total Subordinated Debt			<u>233,644,704</u>	<u>224,931,501</u>

The accompanying notes are an integral part of these financial statements.

BlackRock Kelso Capital Corporation

Schedules of Investments—(Continued)

December 31, 2010

<u>Portfolio Company</u>	<u>Industry(a)</u>	<u>Principal Amount or Number of Shares/Units</u>	<u>Cost(b)</u>	<u>Fair Value(c)</u>
Senior Secured Loans—64.5%(f)				
Advantage Sales & Marketing Inc., Second Lien, 9.25% (LIBOR + 7.75%), 6/17/18	Marketing Services	\$10,000,000	\$ 9,850,494	\$10,000,000
Alpha Media Group Inc., First Lien, 12.00% PIK, 7/15/13	Publishing	4,468,967	3,325,429	1,625,395
Al Solutions, Inc., First Lien, 10.00%, 6/28/13(g)	Metals	115,000	115,000	115,000
American SportWorks LLC, Second Lien, 13.00%, 6/16/15(g)	Utility Vehicles	8,000,000	8,000,000	7,200,000
AmQuip Crane Rental LLC, Second Lien, 6.04% (LIBOR + 5.75%), 6/29/14	Construction Equipment	24,017,329	22,622,302	20,871,059
Arclin US Holdings Inc., Second Lien, 7.75% (LIBOR + 6.00%), 1/15/15(e)(h)	Chemicals	3,559,198	2,831,246	3,459,541
Ascend Learning, LLC, Second Lien, 12.25% (Base Rate + 9.00%), 12/6/17	Education	20,000,000	20,000,000	20,000,000
Ashton Woods USA L.L.C., Second Lien, 11.75%, 7/6/15	Homebuilding	37,500,000	37,500,000	37,500,000
Bankruptcy Management Solutions, Inc., Term Loan A, First Lien, 7.50% (LIBOR + 6.00%), 8/20/14(g)	Financial Services	2,000,000	2,000,000	2,000,000
Bankruptcy Management Solutions, Inc., Second Lien, 8.26% (LIBOR + 1.00% cash, 7.00% PIK), 8/20/15(g)	Financial Services	27,221,976	18,515,769	21,342,029
The Bargain! Shop Holdings Inc., Term Loan A, First Lien, 16.00%, 6/29/12(h)	Discount Stores	12,381,187(i)	12,084,951	12,460,310
The Bargain! Shop Holdings Inc., Term Loan B, First Lien, 16.00%, 7/1/12(h)	Discount Stores	17,018,813(i)	15,971,842	17,127,573
Berlin Packaging L.L.C., Second Lien, 6.78% (LIBOR + 6.50%), 8/17/15	Rigid Packaging	24,000,000	23,582,963	23,400,000
Electrical Components International, Inc., Tranche B, First Lien, 9.50% (LIBOR + 6.50%), 5/14/15(g)	Electronics	1,641,718	1,641,718	1,641,718
Event Rentals, Inc., Acquisition Loan, First Lien, 7.75% (LIBOR + 4.25% cash, 2.00% PIK), 12/19/13	Party Rentals	3,123,427	3,123,427	2,529,976
Facet Technologies, LLC, Second Lien, 17.50% PIK, 7/26/12	Medical Devices	40,828,460	36,865,344	—
Facet Technologies, LLC, Guaranty(j)	Medical Devices	—	—	—
Fitness Together Franchise Corporation, First Lien, 11.50% (9.50% cash, 2.00% PIK), 11/10/13(g)(k)	Personal Fitness	7,166,047	7,166,047	6,119,804
Heartland Automotive Services II, Inc. et al., Term Loan A, First Lien, 7.25% (Base Rate + 4.00%), 1/30/14	Automobile Repair	3,263,070	3,262,020	3,073,812
Heartland Automotive Services II, Inc. et al., Term Loan B, First Lien, 9.25% (Base Rate + 4.00% cash, 2.00% PIK), 1/30/14	Automobile Repair	2,305,090	2,304,957	2,076,887

The accompanying notes are an integral part of these financial statements.

BlackRock Kelso Capital Corporation

Schedules of Investments—(Continued)

December 31, 2010

<u>Portfolio Company</u>	<u>Industry(a)</u>	<u>Principal Amount or Number of Shares/Units</u>	<u>Cost(b)</u>	<u>Fair Value(c)</u>
Henniges Automotive Holdings, Inc., First Lien, 12.00% (LIBOR + 10.00%), 11/30/16	Automotive	\$40,000,000	\$ 40,000,000	\$ 40,000,000
Hoffmaster Group, Inc., First Lien, 7.00% (LIBOR + 5.00%), 6/2/16	Consumer Products	4,791,367	4,791,367	4,791,367
Hoffmaster Group, Inc., Second Lien, 13.50%, 6/2/17	Consumer Products	33,000,000	33,000,000	33,000,000
InterMedia Outdoors, Inc., Second Lien, 7.05% (LIBOR + 6.75%), 1/31/14	Printing/Publishing	10,000,000	10,000,000	8,630,000
MCCI Group Holdings, LLC, Second Lien, 7.51% (LIBOR + 7.25%), 6/21/13	Healthcare Services	29,000,000	28,972,454	29,000,000
Navilyst Medical, Inc., Second Lien, 13.00%, 8/14/15	Healthcare Services	15,000,000	14,838,003	14,865,000
Physiotherapy Associates, Inc. et al., Second Lien, 12.00% (Base Rate + 8.75%), 12/31/13	Rehabilitation Centers	17,000,000	17,000,000	17,000,000
Total Safety U.S., Inc., Second Lien, 6.79% (LIBOR + 6.50%), 12/8/13	Industrial Safety Equipment	9,000,000	9,000,000	8,829,000
United Subcontractors, Inc., First Lien, 1.80% (LIBOR + 1.50%), 6/30/15(e)	Building and Construction	1,842,354	1,780,989	1,589,952
Volume Services America, Inc. et al., Term Loan B, First Lien, 10.50% (LIBOR + 8.50%), 9/16/16	Concession Services	44,887,500	44,887,500	44,887,500
Water Pik, Inc., Second Lien, 5.76% (LIBOR + 5.50%), 6/15/14	Consumer Products	30,000,000	30,000,000	30,000,000
WBS Group LLC et al., Second Lien, 10.50% (LIBOR + 9.00%), 6/7/13	Software	20,000,000	20,000,000	18,000,000
Westward Dough Operating Company, LLC, Term Loan A, First Lien, 4.31% (LIBOR + 4.00%), 3/30/11	Restaurants	6,850,000	6,850,000	2,829,050
Westward Dough Operating Company, LLC, Term Loan B, First Lien, 7.31% (LIBOR + 7.00%), 3/30/11(k)	Restaurants	8,334,656	8,334,656	4,379,893
Total Senior Secured Loans			<u>500,218,478</u>	<u>450,344,866</u>
Preferred Stock—0.9%				
Alpha Media Group Holdings Inc., Series A-2(l)	Publishing	5,000	—	—
Facet Holdings Corp., Class A, 12.00% PIK(k)	Medical Devices	900	900,000	—
Fitness Together Holdings, Inc., Series A(g)(l)	Personal Fitness	187,500	173,326	—
Fitness Together Holdings, Inc., Series A-1(g)(l)	Personal Fitness	49,056	49,056	—
Fitness Together Holdings, Inc., Series B Convertible(g)(l)	Personal Fitness	15,881,325	9,100,000	1,478,000
M & M Tradition Holdings Corp., Series A Convertible, 16.00% PIK(e)	Sheet Metal Fabrication	4,968	4,968,000	5,117,040
Total Preferred Stock			<u>15,190,382</u>	<u>6,595,040</u>

The accompanying notes are an integral part of these financial statements.

BlackRock Kelso Capital Corporation

Schedules of Investments—(Continued)

December 31, 2010

<u>Portfolio Company</u>	<u>Industry(a)</u>	<u>Principal Amount or Number of Shares/Units</u>	<u>Cost(b)</u>	<u>Fair Value(c)</u>
Common Stock—11.9%(l)				
Alpha Media Group Holdings Inc., Class B	Publishing	12,500	\$ —	\$ —
Arclin Cayman Holdings Ltd.(e)(h)	Chemicals	572,553	11,399,992	8,370,000
Bankruptcy Management Solutions, Inc.(g)	Financial Services	259,229	9,539,238	4,516,560
BKC ARS Blocker, Inc. (American Residential)(m)	HVAC/Plumbing Services	1,000	20,798	1,118,000
BKC ASW Blocker, Inc. (American SportWorks)(g)(n)	Utility Vehicles	1,000	7,428,827	—
BKC CSP Blocker, Inc. (Conney Safety)(e)(o)	Safety Products	100	888,910	1,062,247
BKC DVSH Blocker, Inc. (DynaVox Systems)(p)	Augmentative Communication Products	100	758,068	723,813
BKC MTCH Blocker, Inc. (Marquette Transportation)(q)	Transportation	1,000	5,000,000	3,511,963
ECI Holdco, Inc., Class A-1 (Electrical Components)(g)	Electronics	18,848,836	18,848,836	51,480,000
Facet Holdings Corp.	Medical Devices	10,000	100,000	—
Fitness Together Holdings, Inc.(g)	Personal Fitness	173,547	118,500	—
M & M Tradition Holdings Corp.(e)	Sheet Metal Fabrication	500,000	5,000,000	5,000,000
MGHC Holding Corporation (Mattress Giant)(e)	Bedding—Retail	2,285,815	2,285,815	—
USI Senior Holdings, Inc. (United Subcontractors)(e)	Building and Construction	97,519	7,309,066	7,379,489
Total Common Stock			<u>68,698,050</u>	<u>83,162,072</u>
Limited Partnership/Limited Liability Company Interests—3.3%				
Big Dumpster Coinvestment, LLC(l)	Waste Management Equipment	—	5,333,333	—
Marsico Holdings, LLC, acquired 11/12/10(d)(l)	Financial Services	91,445	1,848,077	424,305
Penton Business Media Holdings LLC(e)(l)	Information Services	—	9,050,000	9,050,000
PG Holdco, LLC (Press Ganey), 15.00% PIK	Healthcare Services	333	280,739	280,739
PG Holdco, LLC (Press Ganey), Class A(l)	Healthcare Services	16,667	166,667	300,000
Sentry Security Systems Holdings, LLC(l)	Security Services	147,271	147,271	3,830
Sentry Security Systems Holdings, LLC, 8.00% PIK	Security Services	602,729	602,729	602,729
VSS-AHC Holdings LLC (Advanstar)(l)	Printing/Publishing	352,941	4,199,161	6,390,228
WBS Group Holdings, LLC, Class B-1, 16.00% PIK	Software	8,000	8,000,000	6,336,096
Total Limited Partnership/Limited Liability Company Interests			<u>29,627,977</u>	<u>23,387,927</u>

The accompanying notes are an integral part of these financial statements.

BlackRock Kelso Capital Corporation

Schedules of Investments—(Continued)

December 31, 2010

<u>Portfolio Company</u>	<u>Industry(a)</u>	<u>Principal Amount or Number of Shares/Units</u>	<u>Cost(b)</u>	<u>Fair Value(c)</u>
Equity Warrants/Options—0.8%(l)				
Arclin Cayman Holdings Ltd., Tranche 1, expire 1/15/14(e)(h)	Chemicals	230,159	\$ 403,815	\$ 1,378,850
Arclin Cayman Holdings Ltd., Tranche 2, expire 1/15/15(e)(h)	Chemicals	230,159	323,052	1,553,288
Arclin Cayman Holdings Ltd., Tranche 3, expire 1/15/14(e)(h)	Chemicals	230,159	484,578	1,164,424
Arclin Cayman Holdings Ltd., Tranche 4, expire 1/15/15(e)(h)	Chemicals	230,159	403,815	1,356,461
Bankruptcy Management Solutions, Inc., expire 10/1/17(g)	Financial Services	22,544	365,583	125,880
BLB Worldwide Holdings, Inc., Contingent Value Rights, expire 11/5/17	Gaming	1,000	5,000	5,000
Marsico Superholdco SPV, LLC, expire 12/14/19, acquired 11/28/07(d)	Financial Services	455	444,450	—
Total Equity Warrants/Options			<u>2,430,293</u>	<u>5,583,903</u>
TOTAL INVESTMENTS INCLUDING UNEARNED INCOME			995,070,459	889,478,620
UNEARNED INCOME—(1.3)%			<u>(9,392,954)</u>	<u>(9,392,954)</u>
TOTAL INVESTMENTS—126.0%			<u>\$985,677,505</u>	<u>880,085,666</u>
OTHER ASSETS & LIABILITIES (NET)—(26.0)%				<u>(181,605,742)</u>
NET ASSETS—100.0%				<u>\$ 698,479,924</u>

(a) Unaudited

(b) Represents amortized cost for fixed income securities and cost for preferred and common stock, limited partnership/limited liability company interests and equity warrants/options.

(c) Fair value is determined by or under the direction of the Company's Board of Directors (see Note 2).

(d) Security is exempt from registration under Rule 144A of the Securities Act of 1933. Such securities may be resold in transactions that are exempt from registration, normally to qualified institutional buyers. In the aggregate, these securities represent 7.9% of the Company's net assets at December 31, 2010.

(e) Transaction and other information for "non-controlled, affiliated" investments under the Investment Company Act of 1940, whereby the Company owns 5% or more (but not more than 25%) of the portfolio company's outstanding voting securities, is as follows:

The accompanying notes are an integral part of these financial statements.

Table of Contents

Non-controlled, Affiliated Investments	Fair Value at December 31, 2009	Gross Additions (Cost)*	Gross Reductions (Cost)**	Net Unrealized Gain (Loss)	Fair Value at December 31, 2010	Net Realized Gain (Loss)***	Interest Income***	Dividend Income***
Arclin Cayman Holdings Ltd.:								
Common Stock	\$ —	\$ 7,087,791	\$ —	\$ 1,282,209	\$ 8,370,000	\$ —	\$ —	\$ —
Warrants	—	3,955,050	—	1,497,973	5,453,023	—	—	—
Arclin US Holdings Inc.								
Senior Secured Loan	—	3,437,181	(8,298)	30,658	3,459,541	667	39,137	—
BKC CSP Blocker, Inc.								
Common Stock	—	888,910	—	173,337	1,062,247	—	—	—
Conney Safety Products, LLC								
Subordinated Debt	—	25,366,592	—	4,298,660	29,665,252	—	4,966,138	—
M&M Tradition Holdings Corp.:								
Preferred Stock	5,117,040	—	—	—	5,117,040	—	—	1,284,148
Common Stock	5,000,000	—	—	—	5,000,000	—	—	—
Mattress Giant Corporation								
Subordinated Debt	3,521,162	1,390,692	—	(3,682,197)	1,229,657	—	1,390,894	—
MGHC Holding Corporation								
Common Stock	—	—	—	—	—	—	—	—
Penton Business Media Holdings LLC								
Limited Liability Co. Interest	515,870	9,050,000	(14,943,201)	14,427,331	9,050,000	(14,426,995)	—	—
Penton Media, Inc.								
Senior Secured Loan	4,290,000	14,571	(25,694,870)	21,390,299	— †	(21,794,870)	(25,073)	—
United Subcontractors, Inc.								
Senior Secured Loan	1,447,864	163,319	—	(21,231)	1,589,952	—	32,096	—
USI Senior Holdings, Inc.								
Common Stock	6,902,053	383,057	—	94,379	7,379,489	—	—	—
Totals	\$ 26,793,989	\$51,737,163	\$ (40,646,369)	\$39,491,418	\$ 77,376,201	\$ (36,221,198)	\$ 6,403,192	\$ 1,284,148

* Gross additions include increases in the cost basis of investments resulting from new portfolio investments, payment-in-kind interest or dividends, the amortization of unearned income, the exchange of one or more existing securities for one or more new securities and the movement of an existing portfolio company into this category from a different category.

** Gross reductions include decreases in the cost basis of investments resulting from principal collections related to investment repayments or sales, the exchange of one or more existing securities for one or more new securities and the movement of an existing portfolio company out of this category into a different category.

*** For the year ended December 31, 2010.

† Investment no longer held at December 31, 2010.

The aggregate fair value of non-controlled, affiliated investments at December 31, 2010 represents 11.1% of the Company's net assets.

- (f) Approximately 71% of the senior secured loans to the Company's portfolio companies bear interest at a floating rate that may be determined by reference to the London Interbank Offered Rate (LIBOR) or other base rate (commonly the Federal Funds Rate or the Prime Rate), at the borrower's option. In addition, approximately 35% of such senior secured loans have floors of 1.50% to 3.25% on the LIBOR base rate. The borrower under a senior secured loan generally has the option to select from interest reset periods of one, two, three or six months and may alter that selection at the end of any reset period. The stated interest rate represents the weighted average interest rate at December 31, 2010 of all contracts within the specified loan facility.
- (g) Transaction and other information for "controlled" investments under the Investment Company Act of 1940, whereby the Company owns more than 25% of the portfolio company's outstanding voting securities, is as follows:

The accompanying notes are an integral part of these financial statements.

Table of Contents

Controlled Investments	Fair Value at December 31, 2009	Gross Additions (Cost)*	Gross Reductions (Cost)**	Net Unrealized Gain (Loss)	Fair Value at December 31, 2010	Net Realized Gain***	Interest/ Other Income***
AI Solutions, Inc.							
Senior Secured Loan	\$ 150,000	\$ 221	\$ (32,638)	\$ (2,583)	\$ 115,000	\$ 2,362	\$ 14,207
American SportWorks LLC							
Senior Secured Loan	3,262,261	2,000,000	(7,178,673)	9,116,412	7,200,000	153	650,218
Bankruptcy Management Solutions, Inc.:							
Senior Secured Loan	—	4,000,000	(2,000,000)	—	2,000,000	—	148,011
Senior Secured Loan	—	18,515,769	—	2,826,260	21,342,029	—	675,666
Common Stock	—	9,539,238	—	(5,022,678)	4,516,560	—	—
Warrants	—	365,583	—	(239,703)	125,880	—	—
BKC ASW Blocker, Inc.							
Common Stock	163,289	7,353,826	(175,000)	(7,342,115)	—	—	—
Electrical Components International, Inc.:							
Senior Secured Loan	—	1,649,968	(8,250)	—	1,641,718	—	100,913
Senior Secured Loan	—	12,000,000	(12,000,000)	—	— †	—	218,183
Senior Secured Loan	—	12,000,000	(12,000,000)	—	— †	—	218,168
ECI Holdco, Inc.							
Common Stock	—	18,848,836	—	32,631,164	51,480,000	—	—
Fitness Together Franchise Corporation							
Senior Secured Loan	5,807,656	143,488	—	168,660	6,119,804	—	825,104
Fitness Together Holdings, Inc.:							
Preferred Stock Series A	—	—	—	—	—	—	—
Preferred Stock Series A-1	—	—	—	—	—	—	—
Preferred Stock Series B Convertible	779,000	2,600,000	—	(1,901,000)	1,478,000	—	—
Common Stock	—	—	—	—	—	—	—
Less: Unearned Income	(249,930)	(905,248)	358,276	224,602	(572,300)	—	—
Totals	<u>\$9,912,276</u>	<u>\$ 88,111,681</u>	<u>\$(33,036,285)</u>	<u>\$30,459,019</u>	<u>\$95,446,691</u>	<u>\$2,515</u>	<u>\$2,850,470</u>

* Gross additions include increases in the cost basis of investments resulting from new portfolio investments, payment-in-kind interest or dividends, the amortization of unearned income, the exchange of one or more existing securities for one or more new securities and the movement of an existing portfolio company into this category from a different category.

** Gross reductions include decreases in the cost basis of investments resulting from principal collections related to investment repayments or sales, the exchange of one or more existing securities for one or more new securities and the movement of an existing portfolio company out of this category into a different category.

*** For the year ended December 31, 2010. There was no dividend income from these securities during the year.

† Investment no longer held at December 31, 2010.

The aggregate fair value of controlled investments at December 31, 2010 represents 13.7% of the Company's net assets.

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

(i) Principal amount is denominated in Canadian dollars.

(j) Guaranty by the Company on behalf of portfolio company Facet Technologies, LLC. This guaranty was terminated on January 17, 2011 with no payments having been made thereunder.

(k) Non-accrual status (in default) at December 31, 2010 and therefore non-income producing. At December 31, 2010, the aggregate fair value and amortized cost of the Company's debt investments on non-accrual status represents 1.4% and 1.8% of total debt investments at fair value and amortized cost, respectively.

(l) Non-income producing equity securities at December 31, 2010.

(m) The Company is the sole stockholder of BKC ARS Blocker, Inc., which is the beneficiary of less than 5% of the voting securities of American Residential Services L.L.C. and thus a non-controlled, non-affiliated investment.

(n) The Company is the sole stockholder of BKC ASW Blocker, Inc., which is the beneficiary of more than 25% of the voting securities of American SportWorks LLC. and thus a controlled investment.

The accompanying notes are an integral part of these financial statements.

Table of Contents

- (o) The Company is the sole stockholder of BKC CSP Blocker, Inc., which is the beneficiary of more than 5% (but less than 25%) of the voting securities of Conney Prime Holdings, LLC and thus a non-controlled, affiliated investment.
 - (p) The Company is the sole stockholder of BKC DVSH Blocker, Inc., which is the beneficiary of less than 5% of the voting securities of DynaVox Systems LLC and thus a non-controlled, non-affiliated investment.
 - (q) The Company is the sole stockholder of BKC MTCH Blocker, Inc., which is the beneficiary of less than 5% of the voting securities of Marquette Transportation Company Holdings, LLC and thus a non-controlled, non-affiliated investment.
- PIK Payment-in-kind.

The accompanying notes are an integral part of these financial statements.

BlackRock Kelso Capital Corporation
**Schedules of Investments
December 31, 2009**

<u>Portfolio Company</u>	<u>Industry(a)</u>	<u>Principal Amount or Number of Shares/Units</u>	<u>Cost(b)</u>	<u>Fair Value(c)</u>
Senior Secured Notes—9.0%				
AGY Holding Corp., Second Lien, 11.00%, 11/15/14	Glass Yarns/ Fibers	\$23,500,000	\$ 23,131,937	\$ 19,740,000
TriMark Acquisition Corp., Second Lien, 11.50% (9.50% cash, 2.00% PIK), 11/30/13	Food Service Equipment	31,503,017	31,503,017	28,667,746
Total Senior Secured Notes			<u>54,634,954</u>	<u>48,407,746</u>
Unsecured Debt—23.5%				
ASM Intermediate Holdings Corp. II, 12.00% PIK, 12/27/13	Marketing Services	57,401,749	57,401,749	56,138,911
Big Dumpster Acquisition, Inc., 13.50% PIK, 7/5/15	Waste Management Equipment	42,889,344	42,889,344	14,024,815
Marquette Transportation Company Holdings, LLC, 14.75% PIK, 3/21/14	Transportation	52,253,576	52,253,576	51,365,265
Marsico Parent Holdco, LLC et al., 12.50% PIK, 7/15/16, acquired 11/28/07(d)	Financial Services	11,279,758	11,279,758	3,508,005
Marsico Parent Superholdco, LLC et al., 14.50% PIK, 1/15/18, acquired 11/28/07(d)	Financial Services	7,791,207	7,483,674	1,947,802
Total Unsecured Debt			<u>171,308,101</u>	<u>126,984,798</u>
Subordinated Debt—24.7%				
A & A Manufacturing Co., Inc., 16.00% (14.00% cash, 2.00% PIK), 4/2/14	Protective Enclosures	19,542,243	19,542,243	14,871,647
Conney Safety Products, LLC, 18.00% (16.00% cash, 2.00% PIK), 10/1/14	Safety Products	30,300,750	30,300,750	25,452,630
DynaVox Systems LLC, 15.00%, 6/23/15	Augmentative Communication Products	25,000,000	25,000,000	25,950,000
Mattress Giant Corporation, 11.00% PIK, 12/31/12(e)	Bedding —Retail	5,744,147	2,521,202	3,521,162
MediMedia USA, Inc., 11.38%, 11/15/14, acquired multiple dates(d)	Information Services	8,000,000	8,058,173	6,728,000
The Pay-O-Matic Corp., 14.00% (12.00% cash, 2.00% PIK), 1/15/15	Financial Services	15,366,867	15,366,867	15,643,470
PGA Holdings, Inc., 12.50%, 3/12/16	Healthcare Services	5,000,000	4,923,000	5,100,000
Sentry Security Systems, LLC, 16.00% (14.00% cash, 2.00% PIK), 8/7/12	Security Services	10,834,674	10,834,674	10,607,146
Tri-anim Health Services, Inc. et al., 14.00% (12.00% cash, 2.00% PIK), 6/4/15	Healthcare Products	15,021,667	15,021,667	15,322,100
U.S. Security Holdings, Inc., 13.00% (11.00% cash, 2.00% PIK), 5/8/14, acquired 5/10/06(d)	Security Services	7,000,000	7,000,000	7,000,000
Wastequip, Inc., 12.50% (10.00% cash, 2.50% PIK), 2/5/15	Waste Management Equipment	7,947,596	7,947,596	3,035,981
Total Subordinated Debt			<u>146,516,172</u>	<u>133,232,136</u>

The accompanying notes are an integral part of these financial statements.

BlackRock Kelso Capital Corporation
Schedules of Investments—(Continued)
December 31, 2009

<u>Portfolio Company</u>	<u>Industry(a)</u>	<u>Principal Amount or Number of Shares/Units</u>	<u>Cost(b)</u>	<u>Fair Value(c)</u>
Senior Secured Loans—93.3%(f)				
Alpha Media Group Inc., First Lien, 12.00% PIK, 7/15/13	Publishing	\$ 3,964,202	\$ 2,669,800	\$ 2,055,532
Al Solutions, Inc., First Lien, 10.00%, 6/28/13(g)	Metals	150,000	147,418	150,000
American Residential Services L.L.C., Second Lien, 12.00% (10.00% cash, 2.00% PIK), 4/17/15	HVAC/ Plumbing	41,215,100	41,215,100	40,102,293
American Safety Razor Company, LLC, Second Lien, 6.51% (LIBOR + 6.25%), 1/30/14	Consumer Products	10,000,000	10,000,000	9,090,000
American SportWorks LLC, Second Lien, 20.00%, 6/27/14(g)(h)	Utility Vehicles	13,403,274	13,403,274	3,262,261
AmQuip Crane Rental LLC, Second Lien, 6.01% (LIBOR + 5.75%), 6/29/14	Construction Equipment	24,089,541	22,267,464	22,403,273
Applied Tech Products Corp. et al., Tranche A, First Lien, 7.75% (Base Rate + 4.50%), 10/24/10(h)	Plastic Packaging	731,669	730,747	275,359
Arclin US Holdings Inc., First Lien, 7.00% (Base Rate + 3.75%), 7/10/14(h)	Chemicals	6,423,655	3,357,410	5,607,851
Arclin US Holdings Inc., Second Lien, 10.75% (Base Rate + 7.50%), 7/10/15(h)	Chemicals	14,500,000	14,500,000	3,335,290
Bankruptcy Management Solutions, Inc., Second Lien, 6.48% (LIBOR + 6.25%), 7/31/13	Financial Services	24,187,500	24,187,500	17,802,000
The Bargain! Shop Holdings Inc., Term Loan A, First Lien, 14.50% (13.50% cash, 1.00% PIK), 6/29/12(i)	Discount Stores	13,602,460(j)	13,211,257	12,975,113
The Bargain! Shop Holdings Inc., Term Loan B, First Lien, 14.50% (13.50% cash, 1.00% PIK), 7/1/12(i)	Discount Stores	18,697,540(j)	17,511,078	17,835,208
Berlin Packaging L.L.C., Second Lien, 6.76% (LIBOR + 6.50%), 8/17/15	Rigid Packaging	24,000,000	23,492,840	22,680,000
Champion Energy Corporation et al., First Lien, 14.50%, 5/22/11	Heating and Oil Services	30,000,000	30,000,000	30,210,000
Custom Direct, Inc. et al., Second Lien, 6.31% (LIBOR + 6.00%), 12/31/14	Printing	10,000,000	10,000,000	7,990,000
Deluxe Entertainment Services Group Inc., Second Lien, 11.00% (LIBOR + 9.00%), 11/11/13	Entertainment	12,000,000	12,000,000	11,148,000
Electrical Components International, Inc., First Lien, 9.25% (Base Rate + 6.00%), 5/1/14	Electronics	2,974,210	2,052,126	2,562,460
Electrical Components International, Inc., Second Lien, 11.50% (Base Rate + 8.25%), 5/1/14(h)	Electronics	26,000,000	22,891,103	8,874,840
Event Rentals, Inc., Acquisition Loan, First Lien, 7.75% (LIBOR + 4.25% cash, 2.00% PIK), 12/19/13	Party Rentals	3,217,840	3,217,840	2,622,540
Facet Technologies, LLC, Second Lien, 17.50% PIK, 7/26/12	Medical Devices	34,321,490	34,321,490	10,000,012
Facet Technologies, LLC, Guaranty(k)	Medical Devices	—	—	(225,000)

The accompanying notes are an integral part of these financial statements.

BlackRock Kelso Capital Corporation

Schedules of Investments—(Continued)

December 31, 2009

<u>Portfolio Company</u>	<u>Industry(a)</u>	<u>Principal Amount or Number of Shares/Units</u>	<u>Cost(b)</u>	<u>Fair Value(c)</u>
Fitness Together Franchise Corporation, First Lien, 11.50% (9.50% cash, 2.00% PIK), 11/10/13(g)	Personal Fitness	\$ 7,022,559	\$ 7,022,559	\$ 5,807,656
Heartland Automotive Services II, Inc. et al., Term Loan A, First Lien, 7.25% (Base Rate + 4.00%), 1/30/14	Automobile Repair	3,325,862	3,324,445	3,026,535
Heartland Automotive Services II, Inc. et al., Term Loan B, First Lien, 9.25% (Base Rate + 4.00% cash, 2.00% PIK), 1/30/14	Automobile Repair	2,258,858	2,258,680	1,951,653
HIT Entertainment, Inc., Second Lien, 5.78% (LIBOR + 5.50%), 2/26/13	Entertainment	1,000,000	1,000,000	550,000
InterMedia Outdoors, Inc., Second Lien, 7.00% (LIBOR + 6.75%), 1/31/14	Printing/ Publishing	10,000,000	10,000,000	8,520,000
Isola USA Corp., First Lien, 13.00% (Base Rate + 9.75%), 12/18/12	Electronics	10,901,316	10,002,294	10,138,224
Isola USA Corp., Second Lien, 17.75% (Base Rate + 14.50%), 12/18/13	Electronics	25,000,000	25,000,000	22,050,000
LJVH Holdings Inc., Second Lien, 5.75% (LIBOR + 5.50%), 1/19/15(i)	Specialty Coffee	25,000,000	25,000,000	22,700,000
MCCI Group Holdings, LLC, Second Lien, 7.51% (LIBOR + 7.25%), 6/21/13	Healthcare Services	29,000,000	28,961,307	28,710,000
Navilyst Medical, Inc., Second Lien, 12.25%, 8/14/15	Healthcare Services	15,000,000	14,802,935	14,700,000
New Enterprise Stone & Lime Co., Inc., Second Lien, 12.50%, 7/11/14	Mining/ Construction	35,000,000	34,752,695	35,000,000
Oriental Trading Company, Inc., Second Lien, 6.24% (LIBOR + 6.00%), 1/31/14	Party Supplies and Novelties	3,000,000	3,000,000	802,500
Penton Media, Inc. et al., Second Lien, 5.28% (LIBOR + 5.00%), 2/1/14(e)	Information Services	26,000,000	25,680,299	4,290,000
Physiotherapy Associates, Inc. et al., Second Lien, 12.00% (Base Rate + 8.75%), 12/31/13	Rehabilitation Centers	17,000,000	17,000,000	15,759,000
PQ Corporation, Second Lien, 6.74% (LIBOR + 6.50%), 7/30/15	Specialty Chemicals	10,000,000	8,970,517	8,520,000
Premier Yachts, Inc. et al., Term A, First Lien, 3.98% (LIBOR + 3.75%), 8/22/12	Entertainment Cruises	5,973,418	5,960,283	5,973,418
Premier Yachts, Inc. et al., Term B, First Lien, 7.23% (LIBOR + 7.00%), 8/22/13	Entertainment Cruises	1,265,983	1,263,002	1,265,983
Sunrise Medical LTC LLC et al., Second Lien, 6.74% (LIBOR + 6.50%), 12/28/13	Healthcare Equipment	14,400,000	14,400,000	14,097,600
Total Safety U.S., Inc., Second Lien, 6.74% (LIBOR + 6.50%), 12/8/13	Industrial Safety Equipment	9,000,000	9,000,000	8,514,000
United Subcontractors, Inc., First Lien, 1.76% (LIBOR + 1.50%), 6/30/15(e)	Building and Construction	1,626,814	1,617,669	1,447,864
Water Pik, Inc., Second Lien, 5.73% (LIBOR + 5.50%), 6/15/14	Consumer Products	30,000,000	30,000,000	30,000,000
WBS Group LLC et al., Second Lien, 6.54% (LIBOR + 6.25%), 6/7/13	Software	20,000,000	20,000,000	17,000,000

The accompanying notes are an integral part of these financial statements.

BlackRock Kelso Capital Corporation
Schedules of Investments—(Continued)
December 31, 2009

<u>Portfolio Company</u>	<u>Industry(a)</u>	<u>Principal Amount or Number of Shares/Units</u>	<u>Cost(b)</u>	<u>Fair Value(c)</u>
Wembley, Inc., Second Lien, 8.50% (Base Rate + 5.25%), 8/22/12(h)	Gaming	\$ 1,000,000	\$ 1,000,000	\$ 67,500
Westward Dough Operating Company, LLC, Term Loan A, First Lien, 4.25% (LIBOR + 4.00%), 3/30/11	Restaurants	6,850,000	6,850,000	4,719,650
Westward Dough Operating Company, LLC, Term Loan B, First Lien, 7.25% (LIBOR + 7.00%), 3/30/11(h)	Restaurants	8,334,656	8,334,656	6,784,379
Total Senior Secured Loans			<u>616,377,788</u>	<u>503,152,994</u>
Preferred Stock—1.1%				
Alpha Media Group Holdings Inc., Series A-2(l)	Publishing	5,000	—	—
Facet Holdings Corp., Class A, 12.00% PIK(h)	Medical Devices	900	900,000	—
Fitness Together Holdings, Inc., Series A(g)(l)	Personal Fitness	187,500	173,326	—
Fitness Together Holdings, Inc., Series A-1(g)(l)	Personal Fitness	49,056	49,056	—
Fitness Together Holdings, Inc., Series B Convertible(g)(l)	Personal Fitness	11,343,804	6,500,000	779,000
M & M Tradition Holdings Corp., Series A Convertible, 16.00% PIK(e)	Sheet Metal Fabrication	4,968	4,968,000	5,117,040
Total Preferred Stock			<u>12,590,382</u>	<u>5,896,040</u>
Common Stock—3.5%(l)				
Alpha Media Group Holdings Inc., Class B	Publishing	12,500	—	—
BKC ARS Blocker, Inc. (American Residential)(m)	HVAC/Plumbing Services	1,000	192,418	1,610,000
BKC ASW Blocker, Inc. (American SportWorks)(g)(n)	Utility Vehicles	1,000	250,001	163,289
BKC DVSH Blocker, Inc. (DynaVox Systems)(o)	Augmentative Communication Products	100	1,000,000	2,560,000
BKC MTCH Blocker, Inc. (Marquette Transportation)(p)	Transportation	1,000	5,000,000	2,635,000
Facet Holdings Corp.	Medical Devices	10,000	100,000	—
Fitness Together Holdings, Inc.(g)	Personal Fitness	173,547	118,500	—
M & M Tradition Holdings Corp.(e)	Sheet Metal Fabrication	500,000	5,000,000	5,000,000
MGHC Holding Corporation (Mattress Giant)(e)	Bedding—Retail	2,285,815	2,285,815	—
USI Senior Holdings, Inc. (United Subcontractors)(e)	Building and Construction	79,237	6,926,008	6,902,053
Total Common Stock			<u>20,872,742</u>	<u>18,870,342</u>

The accompanying notes are an integral part of these financial statements.

BlackRock Kelso Capital Corporation

Schedules of Investments—(Continued)

December 31, 2009

<u>Portfolio Company</u>	<u>Industry(a)</u>	<u>Principal Amount or Number of Shares/Units</u>	<u>Cost(b)</u>	<u>Fair Value(c)</u>
Limited Partnership/Limited Liability Company Interests—2.4%				
Big Dumpster Coinvestment, LLC(l)	Waste Management Equipment	—	\$ 5,333,333	\$ —
Marsico Parent Superholdco, LLC, 16.75% PIK, acquired 11/28/07(d)(h)	Financial Services	1,750	1,650,005	—
PG Holdco, LLC (Press Ganey), 15.00% PIK	Healthcare Services	333	333,333	346,654
PG Holdco, LLC (Press Ganey), Class A(l)	Healthcare Services	16,667	166,667	250,000
Prism Business Media Holdings LLC (Penton Media)(e)(l)	Information Services	68	14,943,201	515,870
Sentry Security Systems Holdings, LLC(l)	Security Services	147,271	147,271	479
Sentry Security Systems Holdings, LLC, 8.00% PIK	Security Services	602,729	602,729	602,729
VSS-AHC Holdings LLC (Advanstar)(l)	Printing/Publishing	352,941	4,199,161	4,198,939
WBS Group Holdings, LLC, Class B, 16.00% PIK	Software	8,000	8,000,000	7,167,857
Total Limited Partnership/Limited Liability Company Interests			35,375,700	13,082,528
Equity Warrants/Options—0.2%(l)				
Kaz, Inc., expire 12/8/16	Consumer Products	49	512,000	770,160
Kaz, Inc., expire 12/8/16	Consumer Products	16	64,000	136,373
Kaz, Inc., expire 12/8/16	Consumer Products	16	24,000	75,141
Kaz, Inc., expire 12/8/16	Consumer Products	16	9,000	43,073
Marsico Superholdco SPV, LLC, expire 12/14/19, acquired 11/28/07(d)	Financial Services	455	444,450	—
Total Equity Warrants/Options			1,053,450	1,024,747
TOTAL INVESTMENTS INCLUDING UNEARNED INCOME			1,058,729,289	850,651,331
UNEARNED INCOME—(0.7)%			(3,909,286)	(3,909,286)
TOTAL INVESTMENTS—156.9%			\$1,054,820,003	846,742,045
OTHER ASSETS & LIABILITIES (NET)—(56.9)%				(307,179,283)
NET ASSETS—100.0%				\$ 539,562,762

(a) Unaudited.

(b) Represents amortized cost for fixed income securities and cost for preferred and common stock, limited partnership/limited liability company interests and equity warrants/options.

(c) Fair value is determined by or under the direction of the Company's Board of Directors (see Note 2).

(d) Security is exempt from registration under Rule 144A of the Securities Act of 1933. Such securities may be resold in transactions that are exempt from registration, normally to qualified institutional buyers. In the aggregate, these securities represent 3.6% of the Company's net assets at December 31, 2009.

(e) Transaction and other information for "non-controlled, affiliated" investments under the Investment Company Act of 1940, whereby the Company owns 5% or more (but not more than 25%) of the portfolio company's outstanding voting securities, is as follows:

The accompanying notes are an integral part of these financial statements.

Table of Contents

Non-controlled, Affiliated Investments	Fair Value at December 31, 2008	Gross Additions (Cost)*	Gross Reductions (Cost)**	Net Unrealized Gain (Loss)	Fair Value at December 31, 2009	Net Realized Gain***	Interest Income***	Dividend Income***
American SportWorks LLC								
Senior Secured Loan	\$ 5,716,023	\$ —	\$(3,572,448)	\$ (2,143,575)	\$ — †	\$ —	\$ 27,617	\$ —
BKC ASW Blocker, Inc.								
Common Stock	16,399	—	(5,883)	(10,516)	— †	—	—	—
M&M Tradition Holdings Corp.:								
Preferred Stock	5,537,280	—	(408,000)	(12,240)	5,117,040	12,240	—	1,110,885
Common Stock	6,095,000	—	—	(1,095,000)	5,000,000	—	—	—
Mattress Giant Corporation								
Subordinated Debt	—	2,521,202	—	999,960	3,521,162	—	773,581	—
MGHC Holding Corporation								
Common Stock	—	2,285,815	—	(2,285,815)	—	—	—	—
Penton Media, Inc.								
Senior Secured Loan	18,226,000	78,211	—	(14,014,211)	4,290,000	—	1,437,763	—
Prism Business Media Holdings LLC								
Limited Liability Co. Interest	4,730,000	—	—	(4,214,130)	515,870	—	—	—
United Subcontractors, Inc.								
Senior Secured Loan	—	1,617,669	—	(169,805)	1,447,864	—	16,210	—
USI Senior Holdings, Inc.								
Common Stock	—	6,926,008	—	(23,955)	6,902,053	—	—	—
Less: Unearned Income	(305,622)	305,622	—	—	—	—	—	—
Totals	\$ 40,015,080	\$13,734,527	\$(3,986,331)	\$(22,969,287)	\$ 26,793,989	\$ 12,240	\$ 2,255,171	\$ 1,110,885

* Gross additions include increases in the cost basis of investments resulting from new portfolio investments, payment-in-kind interest or dividends, the amortization of unearned income, the exchange of one or more existing securities for one or more new securities and the movement of an existing portfolio company into this category from a different category.

** Gross reductions include decreases in the cost basis of investments resulting from principal collections related to investment repayments or sales, the exchange of one or more existing securities for one or more new securities and the movement of an existing portfolio company out of this category into a different category.

*** For the year ended December 31, 2009.

† Investment moved out of the non-controlled, affiliated category into the controlled category during the year.

The aggregate fair value of non-controlled, affiliated investments at December 31, 2009 represents 5.0% of the Company's net assets.

- (f) Approximately 66% of the senior secured loans to the Company's portfolio companies bear interest at a floating rate that may be determined by reference to the London Interbank Offered Rate (LIBOR) or other base rate (commonly the Federal Funds Rate or the Prime Rate), at the borrower's option. In addition, approximately 9% of such senior secured loans have floors of 1.50% to 3.25% on the LIBOR base rate. The borrower under a senior secured loan generally has the option to select from interest reset periods of one, two, three or six months and may alter that selection at the end of any reset period. The stated interest rate represents the weighted average interest rate at December 31, 2009 of all contracts within the specified loan facility.
- (g) Transaction and other information for "controlled" investments under the Investment Company Act of 1940, whereby the Company owns more than 25% of the portfolio company's outstanding voting securities, is as follows:

The accompanying notes are an integral part of these financial statements.

[Table of Contents](#)

<u>Controlled Investments</u>	<u>Fair Value at December 31, 2008</u>	<u>Gross Additions (Cost)*</u>	<u>Net Unrealized Gain (Loss)</u>	<u>Fair Value at December 31, 2009</u>	<u>Net Realized Loss**</u>	<u>Interest/Other Income**</u>
AI Solutions, Inc.:						
Senior Secured Loan	\$ —	\$ 147,418	\$ 2,582	\$ 150,000	\$ —	\$ 5,821
Subordinated Debt	—	71,373	(71,373)	—	(13,395,134)	71,373
American SportWorks LLC						
Senior Secured Loan	—	3,572,448	(310,187)	3,262,261	—	78,075
BKC ASW Blocker, Inc.						
Common Stock	—	5,883	157,406	163,289	—	—
Fitness Together Franchise Corporation						
Senior Secured Loan	6,496,555	140,615	(829,514)	5,807,656	—	808,583
Fitness Together Holdings, Inc.:						
Preferred Stock Series A	—	—	—	—	—	—
Preferred Stock Series A-1	—	—	—	—	—	—
Preferred Stock Series B Convertible	4,700,000	—	(3,921,000)	779,000	—	—
Common Stock	—	—	—	—	—	—
Tygem Holdings, Inc.:						
Preferred Stock	—	—	—	—	(10,826,867)	—
Preferred Stock Series B Convertible	—	—	—	—	(14,725,535)	—
Common Stock	—	—	—	—	(3,608,956)	—
Less: Unearned Income	—	(249,930)	—	(249,930)	—	—
Totals	<u>\$11,196,555</u>	<u>\$3,687,807</u>	<u>\$(4,972,086)</u>	<u>\$9,912,276</u>	<u>\$(42,556,492)</u>	<u>\$ 963,852</u>

* Gross additions include increases in the cost basis of investments resulting from new portfolio investments, payment-in-kind interest or dividends, the amortization of unearned income, the exchange of one or more existing securities for one or more new securities and the movement of an existing portfolio company into this category from a different category.

** For the year ended December 31, 2009. There was no dividend income from these securities during the year.

The aggregate fair value of controlled investments at December 31, 2009 represents 1.8% of the Company's net assets.

(h) Non-accrual status (in default) at December 31, 2009 and therefore non-income producing. At December 31, 2009, the aggregate fair value and amortized cost of the Company's debt investments on non-accrual status represents 3.5% and 6.5% of total debt investments at fair value and amortized cost, respectively.

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

(j) Principal amount is denominated in Canadian dollars.

(k) Guaranty by the Company on behalf of portfolio company Facet Technologies, LLC. Expires December 31, 2011. Maximum potential future payments under this guaranty are \$6,000,000 at December 31, 2009.

(l) Non-income producing equity securities at December 31, 2009.

(m) The Company is the sole stockholder of BKC ARS Blocker, Inc., which is the beneficiary of less than 5% of the voting securities of American Residential Services L.L.C. and thus a non-controlled, non-affiliated investment.

(n) The Company is the sole stockholder of BKC ASW Blocker, Inc., which is the beneficiary of more than 25% of the voting securities of American SportWorks LLC and thus a controlled investment.

(o) The Company is the sole stockholder of BKC DVSH Blocker, Inc., which is the beneficiary of less than 5% of the voting securities of DynaVox Systems LLC and thus a non-controlled, non-affiliated investment.

(p) The Company is the sole stockholder of BKC MTCH Blocker, Inc., which is the beneficiary of less than 5% of the voting securities of Marquette Transportation Company Holdings, LLC and thus a non-controlled, non-affiliated investment.

PIK Payment-in-kind.

The accompanying notes are an integral part of these financial statements.

BlackRock Kelso Capital Corporation

Notes to Financial Statements

1. Organization

BlackRock Kelso Capital Corporation (the “Company”) was organized as a Delaware corporation on April 13, 2005 and was initially funded on July 25, 2005. The Company has elected to be regulated as a business development company (“BDC”) under the Investment Company Act of 1940 (the “1940 Act”). In addition, for tax purposes the Company has qualified and has elected to be treated as a regulated investment company (“RIC”) under the Internal Revenue Code of 1986 (the “Code”). The Company’s investment objective is to generate both current income and capital appreciation through debt and equity investments. The Company invests primarily in middle-market companies in the form of senior and junior secured and unsecured debt securities and loans, each of which may include an equity component, and by making direct preferred, common and other equity investments in such companies.

On July 25, 2005, the Company completed a private placement of 35,366,589 shares of its common stock at a price of \$15.00 per share receiving net proceeds of approximately \$529 million. On July 2, 2007, the Company completed an initial public offering through which it sold an additional 10,000,000 shares of its common stock at a price of \$16.00 per share and listed its shares on The NASDAQ Global Select Market. The Company received net proceeds of approximately \$150 million from this offering. Offering costs were charged against paid-in capital.

The accompanying financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”). Certain prior year amounts have been reclassified to conform to the current year presentation.

2. Significant accounting policies

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

The significant accounting policies consistently followed by the Company are:

- (a) Investments for which market quotations are readily available are valued at such market quotations unless they are deemed not to represent fair value. The Company obtains market quotations, when available, from an independent pricing service or one or more broker-dealers or market makers and utilizes the average of the range of bid and ask quotations as a practical expedient for fair value. However, debt investments with remaining maturities within 60 days are valued at amortized cost, which approximates fair value. Debt and equity securities for which market quotations are not readily available or for which market quotations are deemed not to represent fair value are valued at fair value as determined in good faith by or under the direction of the Company’s Board of Directors. Because the Company expects that there will not be a readily available market value for substantially all of the investments in its portfolio, the Company expects to value substantially all of its portfolio investments at fair value as determined in good faith by or under the direction of the Board of Directors using a consistently applied valuation process in accordance with a documented valuation policy that has been reviewed and approved by the Board of Directors. Due to the inherent uncertainty and subjectivity of determining the fair value of investments that do not have a readily available market value, the fair value of the Company’s investments may differ significantly from the values that would have been used had a readily available market value existed for such investments and may differ materially from the values that the Company may ultimately realize. In addition, changes in the market environment and other events may have differing impacts on the market quotations used to value some of the Company’s investments than on the fair values of the Company’s investments for which market quotations are not readily available. Market quotations may be deemed not to represent fair value in certain circumstances where BlackRock Kelso Capital Advisors LLC, the Company’s investment advisor (the “Advisor”), believes that facts and circumstances applicable to an issuer, a seller or purchaser or the market for a particular security cause current market quotations to not reflect the fair value of the security. Examples of these events could include cases where a security trades infrequently causing a quoted purchase or sale price to become stale, where there is a “forced” sale by a distressed seller, where market quotations vary substantially among market makers, or where there is a wide bid-ask spread or significant increase in the bid-ask spread.

Table of Contents

With respect to the Company's investments for which market quotations are not readily available or for which market quotations are deemed not to represent fair value, the Board of Directors has approved a multi-step valuation process each quarter, as described below:

- (i) The quarterly valuation process begins with each portfolio company or investment being initially evaluated and rated by the investment professionals of the Advisor responsible for the portfolio investment;
- (ii) The investment professionals provide recent portfolio company financial statements and other reporting materials to independent valuation firms engaged by the Board of Directors, such firms conduct independent appraisals each quarter and their preliminary valuation conclusions are documented and discussed with senior management of the Advisor;
- (iii) The audit committee of the Board of Directors reviews the preliminary valuations prepared by the independent valuation firms; and
- (iv) The Board of Directors discusses valuations and determines the fair value of each investment in the portfolio in good faith based on the input of the Advisor, the respective independent valuation firms and the audit committee.

Those investments for which market quotations are not readily available or for which market quotations are deemed not to represent fair value are valued utilizing a market approach, an income approach, or both approaches, as appropriate. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities (including a business). The income approach uses valuation techniques to convert future amounts (for example, cash flows or earnings) to a single present amount (discounted). The measurement is based on the value indicated by current market expectations about those future amounts. In following these approaches, the types of factors that the Company may take into account in determining the fair value of its 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, M&A comparables, the Company's principal market (as the reporting entity) and enterprise values.

Until the end of the second calendar quarter following its acquisition, each unquoted investment in a new portfolio company generally is valued at cost, which the Advisor believes approximates fair value under the circumstances. As of that date, an independent valuation firm conducts an initial independent appraisal of the investment.

Accounting Standards Codification ("ASC") 820-10, *Fair Value Measurements and Disclosures* ("ASC 820-10"), issued by the Financial Accounting Standards Board ("FASB"), defines fair value, establishes a framework for measuring fair value and requires enhanced disclosures about fair value measurements. ASC 820-10 defines fair value as the price that the Company would receive upon selling an investment or pay to transfer a liability in an orderly transaction to a market participant in the principal or most advantageous market for the investment. ASC 820-10 emphasizes that valuation techniques maximize the use of observable market inputs and minimize the use of unobservable inputs. Inputs refer broadly to the assumptions that market participants would use in pricing an asset or liability, including assumptions about risk. Inputs may be observable or unobservable. Observable inputs are inputs that reflect the assumptions market participants would use in pricing an asset or liability developed based on market data obtained from sources independent of the Company. Unobservable inputs are inputs that reflect the Company's assumptions about the assumptions market participants would use in pricing an asset or liability developed based on the best information available in the circumstances.

Level 1 – Valuations based on unadjusted quoted prices in active markets for identical assets or liabilities that the Company has the ability to access.

Level 2 – Valuations based on unadjusted quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly.

Level 3 – Valuations based on inputs that are unobservable and significant to the overall fair value measurement. The inputs into the determination of fair value may require significant management judgment or estimation. Even if observable market data is available, such information may be the result of consensus pricing information or broker quotes which include a disclaimer that the broker would not be held to such a price in an

Table of Contents

actual transaction. The non-binding nature of consensus pricing and/or quotes accompanied by disclaimer would result in classification as Level 3 information, assuming no additional corroborating evidence.

Transfers between levels, if any, represent the value as of the beginning of the period of any investment where a change in the pricing level occurred from the beginning to the end of the period.

The Company's valuation policy and fair value disclosures are consistent with ASC 820-10. The Company evaluates the source of inputs, including any markets in which its investments are trading, in determining fair value and categorizes each investment within the fair value hierarchy pursuant to ASC 820-10.

- (b) Cash equivalents include short-term liquid investments in a money market fund.
- (c) Security transactions are accounted for on the trade date unless there are substantial conditions to the purchase.
- (d) Gains or losses on the disposition of investments are calculated using the specific identification method.
- (e) Interest income, adjusted for amortization of premium and accretion of discount, and dividend income is recorded on an accrual basis to the extent that the Company expects to collect such amounts. For loans and securities with payment-in-kind ("PIK") income, which represents contractual interest or dividends accrued and added to the principal balance and generally due at maturity, PIK income is accrued only to the extent that the portfolio company valuation indicates that the PIK income is likely to be collected. Origination, structuring, closing, commitment and other upfront fees and discounts and premiums on investments purchased are accreted/amortized over the life of the respective investment. Unamortized origination, structuring, closing, commitment and other upfront fees are recorded as unearned income. Upon the prepayment of a loan or debt security, any prepayment penalties and unamortized loan origination, structuring, closing, commitment and other upfront fees are recorded as interest income. Expenses are recorded on an accrual basis.
- (f) The Company has elected to be taxed as a RIC under Subchapter M of the Code and operates in a manner so as to qualify for the tax treatment applicable to RICs.

In order to qualify for favorable tax treatment as a RIC, the Company is required to distribute annually to its stockholders at least 90% of its investment company taxable income, as defined by the Code. To avoid federal excise taxes, the Company must distribute annually at least 98% of its income (both ordinary income and net capital gains). The Company, at its discretion, may carry forward taxable income in excess of calendar year distributions and pay a 4% excise tax on this income. If the Company chooses to do so, all other things being equal, this would increase expenses and reduce the amount available to be distributed to stockholders. The Company will accrue excise tax on estimated excess taxable income as required.

The Company holds 100% of the common stock of certain companies as indicated in the accompanying schedules of investments. The Company carries its investments in such wholly owned companies at fair value in the statements of assets and liabilities, net of any applicable income tax liabilities. An income tax provision has been provided at the wholly owned company level on all income of such companies, including realized and unrealized gains. Such wholly owned companies are held in connection with the Company's election to be taxed as a RIC. In general, these wholly owned companies earn income that, if earned directly by the Company, would not be qualifying income for purposes of the Company qualifying as a RIC. Dividends from these wholly owned companies and gains from the sale of their stock are qualifying income for this purpose. The Company makes investments in securities in accordance with its investment policies through these wholly owned companies.

In accordance with GAAP, book and tax basis differences relating to distributions to stockholders and other permanent book and tax differences are reclassified to capital in excess of par. In addition, the character of income and gains to be distributed is determined in accordance with income tax regulations that may differ from GAAP.

- (g) Dividends and distributions to common stockholders are recorded on the ex-dividend date. The amount to be paid out as a dividend is determined by the Board of Directors. Net realized capital gains, if any, generally are distributed at least annually, although the Company may decide to retain such capital gains for investment.

The Company has adopted a dividend reinvestment plan that provides for reinvestment of distributions on behalf of stockholders, unless a stockholder elects to receive cash. As a result, if the Board of Directors authorizes, and the Company declares, a cash dividend, then stockholders who have not "opted out" of the dividend reinvestment plan will have their cash dividends automatically reinvested in additional shares of Common Stock, rather than receiving the cash dividends.

- (h) Foreign currency amounts are translated into United States dollars on the following basis:

Table of Contents

- (i) market value of investment securities, other assets and liabilities—at the spot exchange rate on the last business day of the period; and
- (ii) purchases and sales of investment securities, income and expenses—at the rates of exchange prevailing on the respective dates of such transactions, income or expenses.

Although net assets and fair values are presented based on the applicable foreign exchange rates described above, the Company does not isolate that portion of the results of operations resulting from changes in foreign exchange rates on investments from the fluctuations arising from changes in fair values of investments held. Such fluctuations are included with the net realized and unrealized gain or loss from investments.

Investments denominated in foreign currencies and foreign currency transactions may involve certain considerations and risks not typically associated with those of domestic origin, including unanticipated movements in the value of the foreign currency relative to the U.S. dollar.

- (i) Debt issuance costs are being amortized over the term of the related debt using the straight line method.
- (j) The Company records registration expenses related to its shelf registration statement and related SEC filings as prepaid assets. These expenses are charged as a reduction of capital upon utilization, in accordance with ASC 946, *Financial Services—Investment Companies*.
- (k) Loans or debt securities are placed on non-accrual status, as a general matter, when principal or interest payments are past due 30 days or more or when there is reasonable doubt that principal or interest will be collected. Accrued interest generally is reversed when a loan or debt security is placed on non-accrual status. Interest payments received on non-accrual loans or debt securities may be recognized as income or applied to principal depending upon management's judgment. Non-accrual loans and debt securities are restored to accrual status when past due principal and interest is paid and, in management's judgment, are likely to remain current. The Company may make exceptions to this treatment if the loan has sufficient collateral value and is in the process of collection.
- (l) The Company discloses subsequent events in accordance with ASC 855-10, *Subsequent Events* ("ASC 855-10"), which provides guidance to establish general standards of accounting for and disclosures of events that occur after the balance sheet date but before financial statements are issued or are available to be issued and ASU 2010-09, *Amendments to Certain Recognition and Disclosure Requirements*, which amends ASC 855-10 to clarify that an SEC filer is not required to disclose the date through which subsequent events have been evaluated in the financial statements. See Note 14.
- (m) Recently Issued Accounting Pronouncements:

In January 2010, the FASB issued Accounting Standards Update 2010-06, *Fair Value Measurements and Disclosures* ("ASU 2010-06"). ASU 2010-06 amends ASC 820-10 to require new disclosures with regard to transfers into and out of Levels 1 and 2 and separate disclosures about purchases, sales, issuances, and settlements within the Level 3 fair value rollforward. ASU 2010-06 also clarifies existing fair value disclosures about the appropriate level of disaggregation and about inputs and valuation techniques for both recurring and nonrecurring fair value measurements that fall in either Level 2 or Level 3. The new disclosures and clarifications of existing disclosures are effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances and settlements in the rollforward of activity in Level 3 fair value measurements, which are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The adoption on January 1, 2010 of the applicable additional disclosure requirements of ASU 2010-06 did not materially impact the Company's financial statements. The adoption of the additional disclosure requirements, which will be effective in 2011, is not expected to materially impact the Company's financial statement disclosures.

3. Agreements and related party transactions

The Company has entered into an Investment Management Agreement (the "Management Agreement") with the Advisor, under which the Advisor, subject to the overall supervision of the Company's Board of Directors, manages the day-to-day operations of, and provides investment advisory services to, the Company. For providing these services, the Advisor receives a base management fee (the "Management Fee") from the Company quarterly in arrears at an annual rate of 2.0% of the Company's total assets, including any assets acquired with the proceeds of leverage.

For the years ended December 31, 2010, 2009 and 2008, the Advisor earned \$16,877,854, \$18,498,189 and \$22,716,602, respectively, in base management fees under the management agreement.

The Management Agreement provides that the Advisor or its affiliates may be entitled to an incentive management fee (the "Incentive Fee") under certain circumstances. The determination of the Incentive Fee, as

[Table of Contents](#)

described in more detail below, will result in the Advisor or its affiliates receiving no Incentive Fee payments if returns to Company stockholders do not meet an 8.0% annualized rate of return during the applicable fee measurement period and will result in the Advisor or its affiliates receiving less than the full amount of the Incentive Fee percentage until returns to stockholders exceed an approximate 13.3% annualized rate of return during such period. Annualized rate of return in this context is computed by reference to the Company's net asset value and does not take into account changes in the market price of the Company's common stock.

The Advisor will be entitled to receive the Incentive Fee if the Company's performance exceeds a "hurdle rate" during different measurement periods: the transition period; trailing four quarters' periods (which applies only to the portion of the Incentive Fee based on income); and annual periods (which applies only to the portion of the Incentive Fee based on capital gains). The "transition period" began on July 1, 2007 and ended on June 30, 2008. The initial "trailing four quarters' periods" ended on September 30, 2008. In other words, beginning for the quarterly period ended on September 30, 2008 and for each calendar quarter thereafter, the income portion of the Incentive Fee payable for the quarter was determined by reference to such calendar quarter and the three preceding calendar quarters. The term "annual period" means the period beginning on July 1 of each calendar year and ending on June 30 of the next calendar year.

The hurdle rate for each measurement period is 2.0% multiplied by the Company's net asset values at the beginning of each calendar quarter during the measurement period, calculated after giving effect to any distributions that occurred during the measurement period. A portion of the Incentive Fee is based on the Company's income and a portion is based on capital gains. Each portion of the Incentive Fee is described below.

Quarterly Incentive Fee Based on Income. For each of the first two measurement periods referred to above (the transition period and each rolling four quarters' period), the Company pays the Advisor an Incentive Fee based on the amount by which (A) aggregate distributions and amounts distributable out of taxable net income (excluding any capital gain and loss) during the period less the amount, if any, by which net unrealized capital depreciation exceeds net realized capital gains during the period exceeds (B) the hurdle rate for the period. The amount of the excess of (A) over (B) described in this paragraph for each period is referred to as the excess income amount.

The portion of the Incentive Fee based on income for each period will equal 50% of the period's excess income amount, until the cumulative Incentive Fee payments for the period equal 20% of the period's income amount distributed or distributable to stockholders as described in clause (A) of the preceding paragraph. Thereafter, the portion of the Incentive Fee based on income for the period will equal 20% of the period's remaining excess income amount.

Annual Incentive Fee Based on Capital Gains. The portion of the Incentive Fee based on capital gains is calculated on an annual basis. For each annual period, the Company pays the Advisor an Incentive Fee based on the amount by which (A) net realized capital gains, if any, to the extent they exceed gross unrealized capital depreciation, if any, occurring during the period exceeds (B) the amount, if any, by which the period's hurdle rate exceeds the amount of income used in the determination of the Incentive Fee based on income for the period. The amount of the excess of (A) over (B) described in this paragraph is referred to as the excess gain amount.

The portion of the Incentive Fee based on capital gains for each period will equal 50% of the period's excess gain amount, until such payments equal 20% of the period's capital gain amount distributed or distributable to stockholders. Thereafter, the portion of the Incentive Fee based on capital gains for the period equals an amount such that the portion of the Incentive Fee payments to the Advisor based on capital gains for the period equals 20% of the period's remaining excess gain amount. The result of this formula is that, if the portion of the Incentive Fee based on income for the period exceeds the period's hurdle, then the portion of the Incentive Fee based on capital gains will be capped at 20% of the capital gain amount.

In calculating whether the portion of the Incentive Fee based on capital gains is payable with respect to any period, the Company accounts for its assets on a security-by-security basis. In addition, the Company uses the "period-to-period" method pursuant to which the portion of the Incentive Fee based on capital gains for any period is based on realized capital gains for the period reduced by realized capital losses and gross unrealized capital depreciation for the period. Based on current interpretations of Section 205(b)(3) of the Investment Advisers Act of 1940 by the SEC and its staff, the calculation of unrealized depreciation for each portfolio security over a period is based on the fair value of the security at the end of the period compared to the fair value at the beginning of the period. Incentive Fees earned in any of the periods described above are not subject to modification or repayment based upon performance in a subsequent period.

[Table of Contents](#)

For the years ended December 31, 2010, 2009 and 2008, the Advisor earned \$15,108,049, \$16,818,602 and zero, respectively, in Incentive Fees from the Company.

The Management Agreement provides that the Company will reimburse the Advisor for costs and expenses incurred by the Advisor for office space rental, office equipment and utilities allocable to the Advisor under the Management Agreement, as well as any costs and expenses incurred by the Advisor relating to any non-investment advisory, administrative or operating services provided by the Advisor to the Company. For the years ended December 31, 2010, 2009 and 2008, the Company incurred \$1,622,957, \$1,466,563 and \$1,027,135, respectively, for such investment advisor expenses under the Management Agreement.

From time to time, the Advisor may pay amounts owed by the Company to third party providers of goods or services. The Company will subsequently reimburse the Advisor for such amounts paid on its behalf. Reimbursements to the Advisor for the years ended December 31, 2010, 2009 and 2008 were \$3,240,732, \$1,978,629 and \$1,691,420, respectively.

No person who is an officer, director or employee of the Advisor and who serves as a director of the Company receives any compensation from the Company for such services. Directors who are not affiliated with the Advisor receive compensation for their services and reimbursement of expenses incurred to attend meetings.

The Company also has entered into an administration agreement with BlackRock Financial Management, Inc. (the "Administrator") under which the Administrator provides administrative services to the Company. For providing these services, facilities and personnel, the Company reimburses the Administrator for the Company's allocable portion of overhead and other expenses incurred by the Administrator in performing its obligations under the administration agreement, including rent and the Company's allocable portion of the cost of certain of the Company's officers and their respective staffs. For the years ended December 31, 2010, 2009 and 2008, the Company incurred \$587,469, \$642,993 and \$847,387, respectively, for administrative services expenses payable to the Administrator under the administration agreement.

The PNC Financial Services Group, Inc. ("PNC") is a significant stockholder of the ultimate parent of the Administrator. BNY Mellon Investment Servicing (U.S.) Inc. ("BMIS"), formerly PNC Global Investment Servicing (U.S.) Inc. and until recently a subsidiary of PNC, provides administrative and accounting services to the Company pursuant to a Sub-Administration and Accounting Services Agreement. PFPC Trust Company, until recently another subsidiary of PNC, provides custodian services to the Company pursuant to a Custodian Services Agreement. Also, BMIS provides transfer agency and compliance support services to the Company pursuant to a Transfer Agency Agreement and a Compliance Support Services Agreement, respectively. Effective July 1, 2010, BMIS and PFPC Trust Company were acquired by subsidiaries of The Bank of New York Mellon Corporation and are no longer considered related parties of the Company as of and after that date.

For the services provided to the Company by BMIS and its affiliates, BMIS is entitled to an annual fee of 0.02% of the Company's average net assets plus reimbursement of reasonable expenses, and a base fee, payable monthly. PFPC Trust Company may charge the Company additional fees for cash overdraft balances or for sweeping excess cash balances. For the years ended December 31, 2010, 2009 and 2008, the Company incurred \$215,801, \$195,123 and \$234,332, respectively, for administrative, accounting, custodian and transfer agency services fees payable to BMIS and its affiliates under the related agreements.

At December 31, 2010 and 2009, cash equivalents of \$1,344,159 and \$5,048,136 consisted of short-term liquid investments in a money market fund managed by an affiliate of the Administrator.

In 2007, the Company's Board of Directors authorized the purchase by the Advisor from time to time in the open market of an indeterminate number of shares of the Company's common stock, in the Advisor's discretion, subject to compliance with the Company's and the Advisor's applicable policies and requirements of law. Pursuant to this authorization, during the years ended December 31, 2009 and 2008, the Advisor purchased 80,867 and 225,185 shares of the Company's common stock in the open market for \$312,322 and \$2,267,330, respectively, including brokerage commissions. There were no such purchases during the year ended December 31, 2010.

At December 31, 2010 and 2009, the Advisor owned and had the right to vote approximately 47,000 and 353,000 shares, respectively, of the Company's common stock, representing less than 1.0% of the total shares outstanding. On such dates, under compensation arrangements for its officers and employees the Advisor owned of record but did not have the right to vote an additional 426,000 and 202,000 shares, respectively, of the Company's common stock. At December 31, 2010 and 2009, other entities affiliated with the Administrator beneficially owned approximately 4,181,000 and 2,611,000 shares, respectively, of the Company's common stock, representing approximately 5.8% and 4.6% of the total shares outstanding. An entity affiliated with the Administrator has ownership and financial interests in the Advisor.

[Table of Contents](#)

4. Earnings (loss) per share

The following information sets forth the computation of basic and diluted net increase (decrease) in net assets per share (earnings (loss) per share) resulting from operations for the years ended December 31, 2010, 2009 and 2008.

	Year ended December 31, 2010	Year ended December 31, 2009	Year ended December 31, 2008
Numerator for basic and diluted net increase (decrease) in net assets per share	\$71,549,561	\$67,239,723	\$(150,507,382)
Denominator for basic and diluted weighted average shares	62,663,002	55,923,757	54,043,069
Basic/diluted net increase (decrease) in net assets per share resulting from operations	\$ 1.14	\$ 1.20	\$ (2.78)

Diluted net increase (decrease) in net assets per share resulting from operations equals basic net increase (decrease) in net assets per share resulting from operations for each year because there were no common stock equivalents outstanding during the above years.

5. Investments

Purchases of investments for the years ended December 31, 2010, 2009 and 2008 totaled \$405,956,515, \$46,757,709 and \$197,266,147, respectively. Proceeds from sales, repayments and other exits of investments for the years ended December 31, 2010, 2009 and 2008 totaled \$395,269,097, \$128,224,448 and \$120,312,897, respectively.

Under the 1940 Act, the Company is required to separately identify non-controlled investments where it owns 5% or more of a portfolio company's outstanding voting securities as investments in "affiliated" companies. In addition, under the 1940 Act, the Company is required to separately identify investments where it owns more than 25% of a portfolio company's outstanding voting securities as investments in "controlled" companies. Detailed information with respect to the Company's non-controlled affiliated and controlled investments is contained in the accompanying schedules of investments and other financial statements. The information in the tables below is presented on an aggregated portfolio basis, without segregating the non-controlled non-affiliated, non-controlled affiliated and controlled investment categories.

At December 31, 2010, investments consisted of the following:

	Cost	Fair Value
Senior secured notes	\$ 95,164,161	\$ 88,265,252
Unsecured debt	50,096,414	7,208,059
Subordinated debt	233,644,704	224,931,501
Senior secured loans:		
First lien	157,639,903	147,248,237
Second/other priority lien	342,578,575	303,096,629
Total senior secured loans	500,218,478	450,344,866
Preferred stock	15,190,382	6,595,040
Common stock	68,698,050	83,162,072
Limited partnership/limited liability company interests	29,627,977	23,387,927
Equity warrants/options	2,430,293	5,583,903
Total investments including unearned income	995,070,459	889,478,620
Unearned income	(9,392,954)	(9,392,954)
Total investments	<u>\$985,677,505</u>	<u>\$880,085,666</u>

[Table of Contents](#)

At December 31, 2009, investments consisted of the following:

	<u>Cost</u>	<u>Fair Value</u>
Senior secured notes	\$ 54,634,954	\$ 48,407,746
Unsecured debt	171,308,101	126,984,798
Subordinated debt	146,516,172	133,232,136
Senior secured loans:		
First lien	119,531,264	115,409,425
Second/other priority lien	496,846,524	387,743,569
Total senior secured loans	<u>616,377,788</u>	<u>503,152,994</u>
Preferred stock	12,590,382	5,896,040
Common stock	20,872,742	18,870,342
Limited partnership/limited liability company interests	35,375,700	13,082,528
Equity warrants/options	1,053,450	1,024,747
Total investments including unearned income	1,058,729,289	850,651,331
Unearned income	(3,909,286)	(3,909,286)
Total investments	<u>\$1,054,820,003</u>	<u>\$846,742,045</u>

The industry composition of the portfolio at fair value at December 31, 2010 and 2009 was as follows:

<u>Industry</u>	<u>December 31,</u>	
	<u>2010</u>	<u>2009</u>
Personal and Other Services	13.8%	9.4%
Business Services	11.8	12.6
Healthcare	10.6	10.0
Printing, Publishing and Media	8.5	3.2
Consumer Products	7.6	6.0
Manufacturing	7.1	7.6
Distribution	6.3	4.8
Electronics	6.1	8.5
Building and Real Estate	5.2	1.0
Financial Services	4.9	4.6
Automotive	4.5	—
Chemicals	4.4	4.4
Retail	4.0	4.6
Containers and Packaging	3.2	2.7
Beverage, Food and Tobacco	0.8	4.0
Entertainment and Leisure	0.8	2.6
Transportation	0.4	6.3
Metals	—	4.1
Utilities	—	3.6
Total	<u>100.0%</u>	<u>100.0%</u>

The geographic composition of the portfolio at fair value at December 31, 2010 was United States 94.7% and Canada 5.3%, and at December 31, 2009 was United States 93.7%, Canada 6.3% and United Kingdom and other less than 0.1%. The geographic composition is determined by the location of the corporate headquarters of the portfolio company.

In the normal course of business, the Company invests in securities and enters into transactions where risks exist due to fluctuations in the market (market risk) or failure of the issuer of a security to meet all its obligations (issuer credit risk). The value of securities held by the Company may decline in response to certain events, including those directly involving the issuers whose securities are owned by the Company; conditions affecting the general economy; overall market changes; local, regional or global political, social or economic instability; and currency and interest rate and price fluctuations. Similar to issuer credit risk, the Company may be exposed to counterparty credit risk, or the risk that an entity with which the Company has unsettled or open transactions may fail to or be unable to perform on its commitments. The Company manages counterparty risk by entering into transactions only with counterparties

[Table of Contents](#)

that they believe have the financial resources to honor their obligations and by monitoring the financial stability of those counterparties. Financial assets, which potentially expose the Company to market, issuer and counterparty credit risks, consist principally of investments in portfolio companies. The extent of the Company's exposure to market, issuer and counterparty credit risks with respect to these financial assets is generally approximated by their value recorded in the statements of assets and liabilities. The Company is also exposed to credit risk related to maintaining all of its cash at a major financial institution.

The Company has investments in lower rated and comparable quality unrated senior and junior secured, unsecured and subordinated debt securities and loans, which are subject to a greater degree of credit risk than more highly rated investments. The risk of loss due to default by the issuer is significantly greater for holders of such securities and loans, particularly in cases where the investment is unsecured or subordinated to other creditors of the issuer.

6. Derivatives

The Company may enter into forward foreign currency contracts from time to time to facilitate settlement of purchases and sales of investments denominated in foreign currencies or to help mitigate the impact that an adverse change in foreign exchange rates would have on the value of the Company's investments denominated in foreign currencies. A forward foreign currency contract is a commitment to purchase or sell a foreign currency at a future date (usually the security transaction settlement date) at a negotiated forward rate. These contracts are marked-to-market by recognizing the difference between the contract exchange rate and the current market rate as unrealized appreciation or depreciation. Realized gains or losses are recognized when contracts are settled. The Company's forward foreign currency contracts generally have terms of approximately three months. The volume of open contracts at the end of each year is reflective of the typical volume of transactions during each calendar quarter. Risks may arise as a result of the potential inability of the counterparties to meet the terms of their contracts. The Company attempts to limit this risk by dealing with creditworthy counterparties.

At December 31, 2010, details of open forward foreign currency contracts were as follows:

<u>Foreign Currency</u>	<u>Settlement Date</u>	<u>Amount and Transaction</u>	<u>US\$ Value at Settlement Date</u>	<u>US\$ Value at December 31, 2010</u>	<u>Unrealized Depreciation</u>
Canadian dollar	January 19, 2011	29,400,000 Sold	\$ 29,166,667	\$ 29,535,112	\$ (368,445)

At December 31, 2009, details of open forward foreign currency contracts were as follows:

<u>Foreign Currency</u>	<u>Settlement Date</u>	<u>Amount and Transaction</u>	<u>US\$ Value at Settlement Date</u>	<u>US\$ Value at December 31, 2009</u>	<u>Unrealized Appreciation</u>
Canadian dollar	January 27, 2010	795,444 Purchased	\$ (759,501)	\$ (760,561)	\$ 1,060
Canadian dollar	January 27, 2010	31,500,000 Sold	30,316,883	30,118,610	198,273
Canadian dollar	January 27, 2010	800,000 Sold	769,582	764,917	4,665
Total			<u>\$ 30,326,964</u>	<u>\$ 30,122,966</u>	<u>\$ 203,998</u>

All realized and unrealized gains and losses on forward foreign currency contracts are included in earnings (changes in net assets) and are reported as separate line items within the Company's statements of operations. Unrealized gains and losses on forward foreign currency contracts are also reported as separate line items within the Company's statements of assets and liabilities.

The Company holds warrants and options in certain portfolio companies in an effort to achieve additional investment return. In purchasing warrants and options, the Company bears the risk of an unfavorable change in the value of the underlying equity interest. The aggregate fair value of warrants and options at December 31, 2010 and 2009 represents 0.8% and 0.2%, respectively, of the Company's net assets.

The Company may enter into other derivative instruments and incur other exposures with other counterparties in the future.

7. Credit facility and borrowings

Under the terms of the Company's amended and restated Senior Secured, Multi-Currency Credit Agreement (the "Credit Facility"), as amended on December 28, 2007, certain lenders agreed to extend credit to the Company in an aggregate principal amount not to exceed \$545,000,000 outstanding, at any one time, consisting of \$400,000,000 in revolving loan commitments and \$145,000,000 in term loan commitments. On April 20, 2010, the Company amended the Credit Facility to extend through December 6, 2013 certain existing lenders' commitments. These

[Table of Contents](#)

extended commitments, together with the addition of commitments from new lenders, total \$375,000,000, consisting of \$275,000,000 of revolving loan commitments and \$100,000,000 of term loan commitments. Non-extending lender commitments of \$245,000,000 matured on December 6, 2010. The Credit Facility is secured by substantially all of the assets in the Company's portfolio, including cash and cash equivalents. Subject to certain exceptions, pricing for outstanding borrowings is at LIBOR plus an applicable spread of either 3.00% or 3.25% for revolving loans, based on a pricing grid depending on the Company's credit rating, and LIBOR plus 3.00% for term loans. The Credit Facility does not contain a LIBOR floor requirement. At December 31, 2010, the effective LIBOR spread under the Credit Facility was 3.17%. Term loan commitments under the Credit Facility have been fully drawn and, once repaid, may not be reborrowed. The Company has made certain representations and warranties and is required to comply with various covenants, reporting requirements and other customary requirements for similar revolving credit facilities, including covenants related to: (a) limitations on the incurrence of additional indebtedness and liens, (b) limitations on certain investments, (c) limitations on certain restricted payments, (d) maintaining minimum stockholders' equity, (e) maintaining a ratio of total assets (less total liabilities) to total indebtedness, of the Company and its subsidiaries, of not less than 2.0:1.0, (f) maintaining minimum liquidity, and (g) limitations on the creation or existence of agreements that prohibit liens on certain properties of the Company and its subsidiaries. In addition to the asset coverage ratio described above, borrowings under the Credit Facility (and the incurrence of certain other permitted debt) are subject to compliance with a borrowing base that applies different advance rates to different types of assets in the Company's portfolio. The Credit Facility also includes an "accordion" feature that allows the Company, under certain circumstances, to increase the size of the Credit Facility by up to an additional \$275,000,000 of revolving loan commitments and \$250,000,000 of term loan commitments. The Credit Facility is used to supplement the Company's equity capital to make additional portfolio investments and for other general corporate purposes.

At December 31, 2010, the Company had \$170,000,000 drawn on the Credit Facility versus \$296,000,000 at December 31, 2009. The average debt outstanding on the Credit Facility during the years ended December 31, 2010, 2009 and 2008 was \$205,151,507, \$397,464,757 and \$453,241,284, respectively. The maximum amounts borrowed during the years ended December 31, 2010, 2009 and 2008 were \$314,000,000, \$434,000,000 and \$491,000,000, respectively. Subject to compliance with applicable covenants and borrowing base limitations, the remaining amount available under the Credit Facility was \$205,000,000 at December 31, 2010.

The weighted average annual interest cost for the years ended December 31, 2010, 2009 and 2008 was 2.41%, 1.53% and 4.06%, respectively, exclusive of commitment fees and of other prepaid expenses related to establishing the Credit Facility. With respect to any unused portion of the commitments under the Credit Facility, the Company incurs an annual commitment fee of 0.50%. Commitment fees incurred for the years ended December 31, 2010, 2009 and 2008 were \$1,223,193, \$265,385 and \$187,579, respectively.

The April 2010 amendment to the Credit Facility did not substantially change the financial and operational covenants required under the previous agreement. At December 31, 2010, the Company was in compliance with all such covenants.

8. Capital stock

The following table summarizes the total shares issued and proceeds the Company received net of underwriter and offering costs for offerings closed during year ended December 31, 2010. There were no share offerings during the years ended December 31, 2009 and 2008.

	<u>Shares issued</u>	<u>Offering price per share</u>	<u>Proceeds net of underwriting and offering costs</u>
June 2010 public offering	8,625,000	\$ 10.25	\$ 83,892,007
October 2010 public offering	6,900,000	11.95	78,463,117
Total for the year ended December 31, 2010	<u>15,525,000</u>		<u>\$ 162,355,124</u>

In 2008, the Company's Board of Directors approved a share repurchase plan under which the Company may repurchase up to 2.5 percent of its outstanding shares of common stock from time to time in open market or privately negotiated transactions. In 2009, the Board of Directors approved an extension and increase to the plan which authorized the Company to repurchase up to an additional 2.5 percent of its outstanding shares of common stock. In May 2010, the repurchase plan was further extended through the earlier of June 30, 2011 or until the approved number of shares has been repurchased. During the year ended December 31, 2009, the Company purchased a total of 583,572 shares of its common stock on the open market for \$2,234,892, including brokerage commissions. During the year ended December 31, 2008, the Company purchased a total of 378,107 shares of its common stock on the

[Table of Contents](#)

open market for \$3,191,008, including brokerage commissions. There were no such purchases during the year ended December 31, 2010. At December 31, 2010, the total number of remaining shares authorized for repurchase was 1,794,971. The Company currently holds the shares it repurchased in treasury.

For the years ended December 31, 2010, 2009 and 2008, dividends and distributions paid to common stockholders were \$80,455,656, \$44,821,419 and \$92,887,369, respectively. For the years ended December 31, 2010, 2009 and 2008, dividends and distributions reinvested pursuant to the Company's dividend reinvestment plan were \$5,468,133, \$9,083,849 and \$28,689,391, respectively.

On June 7, 2010, the Company's stockholders approved an amendment to the Company's Certificate of Incorporation to increase the number of authorized shares of the Company's common stock from 100,000,000 to 200,000,000. The amendment was effective on that date.

9. Guarantees and contingencies

In the normal course of business, the Company may enter into guarantees on behalf of portfolio companies. Under these arrangements, the Company would be required to make payments to third parties if the portfolio companies were to default on their related payment obligations. The Company's only such guarantee outstanding at December 31, 2010 and 2009 was terminated on January 17, 2011 with no payments having been made thereunder.

In the normal course of business, the Company enters into contractual agreements that provide general indemnifications against losses, costs, claims and liabilities arising from the performance of individual obligations under such agreements. The Company has had no prior claims or payments pursuant to such agreements. The Company's individual maximum exposure under these arrangements is unknown, as this would involve future claims that may be made against the Company that have not yet occurred. However, based on management's experience, the Company expects the risk of loss to be remote.

From time to time, the Company may be a party to certain legal proceedings incidental to the normal course of its business, including the enforcement of the Company's rights under contracts with its portfolio companies. While the Company cannot predict the outcome of these legal proceedings with certainty, it does not expect that these proceedings will have a material effect on its financial statements.

10. Fair value of financial instruments

The carrying values of the Company's financial instruments approximate fair value. The carrying values of receivables, other assets, accounts payable and accrued expenses approximate fair value due to their short maturities. The carrying and fair values of the Company's Credit Facility payable were \$170,000,000 and \$169,150,000 at December 31, 2010 and \$296,000,000 and \$287,120,000 at December 31, 2009, respectively.

The following tables summarize the fair values of the Company's investments, forward foreign currency contracts and cash and cash equivalents based on the inputs used at December 31, 2010 and 2009 in determining such fair values:

	Fair Value at December 31, 2010	Fair Value Inputs at December 31, 2010		
		Price Quotations (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Senior secured notes	\$ 88,265,252	\$ —	\$ —	\$ 88,265,252
Unsecured debt	6,898,385	—	—	6,898,385
Subordinated debt	221,369,811	—	—	221,369,811
Senior secured loans	444,823,276	—	—	444,823,276
Preferred stock	6,595,040	—	—	6,595,040
Common stock	83,162,072	—	—	83,162,072
Limited partnership/limited liability company interests	23,387,927	—	—	23,387,927
Equity warrants/options	5,583,903	—	—	5,583,903
Total investments	880,085,666	—	—	880,085,666
Forward foreign currency contracts	(368,445)	—	(368,445)	—
Cash and cash equivalents	2,160,871	2,160,871	—	—
Total	<u>\$881,878,092</u>	<u>\$2,160,871</u>	<u>\$ (368,445)</u>	<u>\$880,085,666</u>

[Table of Contents](#)

	Fair Value Inputs at December 31, 2009			
	Fair Value at December 31, 2009	Price Quotations (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Senior secured notes	\$ 48,407,746	\$ —	\$ —	\$ 48,407,746
Unsecured debt	126,312,042	—	—	126,312,042
Subordinated debt	131,337,094	—	—	131,337,094
Senior secured loans	501,811,506	—	—	501,811,506
Preferred stock	5,896,040	—	—	5,896,040
Common stock	18,870,342	—	—	18,870,342
Limited partnership/limited liability company interests	13,082,528	—	—	13,082,528
Equity warrants/options	1,024,747	—	—	1,024,747
Total investments	846,742,045	—	—	846,742,045
Forward foreign currency contracts	203,998	—	203,998	—
Cash and cash equivalents	5,807,901	5,807,901	—	—
Total	\$852,753,944	\$5,807,901	\$ 203,998	\$846,742,045

In determining the fair values of the Company's forward foreign currency contracts at December 31, 2010 and 2009, the Company used unadjusted indicative price quotations for similar assets (Level 2). The following tables summarize the valuation techniques used at December 31, 2010 and 2009 in determining the fair values of the Company's investments for which significant unobservable inputs (Level 3) were used:

	Valuation Techniques at December 31, 2010		
	Fair Value at December 31, 2010	Broker Quote(s) for Identical or Similar Assets	Market Approach, Income Approach or Both, Utilizing Third-Party Valuation Firms
Senior secured notes	\$ 88,265,252	\$ —	\$ 88,265,252
Unsecured debt	6,898,385	—	6,898,385
Subordinated debt	221,369,811	—	221,369,811
Senior secured loans	444,823,276	2,529,976	442,293,300
Preferred stock	6,595,040	—	6,595,040
Common stock	83,162,072	—	83,162,072
Limited partnership/limited liability company interests	23,387,927	—	23,387,927
Equity warrants/options	5,583,903	5,000	5,578,903
Total investments	\$880,085,666	\$ 2,534,976	\$ 877,550,690

	Valuation Techniques at December 31, 2009		
	Fair Value at December 31, 2009	Broker Quote(s) for Identical or Similar Assets	Market Approach, Income Approach or Both, Utilizing Third-Party Valuation Firms
Senior secured notes	\$ 48,407,746	\$ —	\$ 48,407,746
Unsecured debt	126,312,042	—	126,312,042
Subordinated debt	131,337,094	—	131,337,094
Senior secured loans	501,811,506	4,042,540	497,768,966
Preferred stock	5,896,040	—	5,896,040
Common stock	18,870,342	—	18,870,342
Limited partnership/limited liability company interests	13,082,528	—	13,082,528
Equity warrants/options	1,024,747	—	1,024,747
Total investments	\$846,742,045	\$ 4,042,540	\$ 842,699,505

Table of Contents

The following is a reconciliation for the year ended December 31, 2010 of investments for which Level 3 inputs were used in determining fair value:

	Fair Value at December 31, 2009	Amortization of Premium/ Discount - Net	Net Realized Gain (Loss)	Net Change in Unrealized Appreciation or Depreciation	Net Purchases, Sales or Redemptions	Net Transfers in and/or out of Level 3	Fair Value at December 31, 2010
Senior secured notes	\$ 48,407,746	\$ 79,596	\$ 111,657	\$ (671,701)	\$ 40,337,954	\$ —	\$ 88,265,252
Unsecured debt	126,312,042	1,065,681	(17,892,200)	1,434,948	(104,022,086)	—	6,898,385
Subordinated debt	131,337,094	2,626,870	358	4,570,831	82,834,658	—	221,369,811
Senior secured loans	501,811,506	5,697,722	(61,219,811)	63,351,182	(64,817,323)	—	444,823,276
Preferred stock	5,896,040	—	—	(1,901,000)	2,600,000	—	6,595,040
Common stock	18,870,342	—	1,061,929	16,466,423	46,763,378	—	83,162,072
Limited partnership/limited liability company interests	13,082,528	—	(16,077,000)	16,053,122	10,329,277	—	23,387,927
Equity warrants/options	1,024,747	—	4,707,189	3,182,313	(3,330,346)	—	5,583,903
Total investments*	\$ 846,742,045	\$ 9,469,869	\$ (89,307,878)	\$ 102,486,118	\$ 10,695,512	\$ —	\$ 880,085,666

* Pursuant to fair value measurement and disclosure guidance, the Company currently categorizes investments by class as shown above.

The following is a reconciliation for the year ended December 31, 2009 of investments for which Level 3 inputs were used in determining fair value:

	Fair Value at December 31, 2008	Amortization of Premium/ Discount - Net	Net Realized Gain (Loss)	Net Change in Unrealized Appreciation or Depreciation	Net Purchases, Sales or Redemptions	Net Transfers in and/or out of Level 3	Fair Value at December 31, 2009
Debt investments	\$ 894,752,768	\$ 5,537,815	\$ (75,246,929)	\$ 76,021,263	\$ (93,196,529)	\$ —	\$ 807,868,388
Equity investments	32,092,158	—	(31,284,612)	24,887,565	13,178,546	—	38,873,657
Total investments*	\$ 926,844,926	\$ 5,537,815	\$ (106,531,541)	\$ 100,908,828	\$ (80,017,983)	\$ —	\$ 846,742,045

* Pursuant to fair value measurement and disclosure guidance, the Company formerly categorized investments by class as shown above.

There were no transfers between Levels for the year ended December 31, 2010 and 2009. All realized and unrealized gains and losses are included in earnings (changes in net assets) and are reported as separate line items within the Company's statements of operations.

The following table contains information with respect to net unrealized appreciation or depreciation on investments for which Level 3 inputs were used in determining fair value that are still held by the Company at December 31, 2010.

	Net Change in Unrealized Appreciation or Depreciation for the Year Ended December 31, 2010 on Investments Held at December 31, 2010	Net Unrealized Appreciation or Depreciation on Investments Held at December 31, 2010
Senior secured notes	\$ (671,701)	\$ (6,898,909)
Unsecured debt	(14,023,826)	(42,888,355)
Subordinated debt	672,711	(8,713,203)
Senior secured loans	(11,282,854)	(49,873,612)
Preferred stock	(1,900,999)	(8,595,342)
Common stock	16,466,422	14,464,022
Limited partnership/limited liability company interests	(24,214)	(6,240,050)
Equity warrants/options	3,598,061	3,153,610
Total investments*	\$ (7,166,400)	\$ (105,591,839)

* Pursuant to fair value measurement and disclosure guidance, the Company currently categorizes investments by class as shown above.

Table of Contents

The following table contains information with respect to net unrealized appreciation or depreciation on investments for which Level 3 inputs were used in determining fair value that were still held by the Company at December 31, 2009.

	Net Change in Unrealized Appreciation or Depreciation for the Year Ended December 31, 2009 on Investments Held at December 31, 2009	Net Unrealized Depreciation on Investments Held at December 31, 2009
Debt investments	\$ 1,367,682	\$ (177,059,341)
Equity investments	(6,401,663)	(31,018,617)
Total investments*	<u>\$ (5,033,981)</u>	<u>\$ (208,077,958)</u>

* Pursuant to fair value measurement and disclosure guidance, the Company formerly categorized investments by class as shown above.

11. Financial highlights

The following per share data and ratios have been derived from information provided in the financial statements. The following is a schedule of financial highlights for a common share outstanding for each of the five years in the period ended December 31, 2010.

	Year ended December 31, 2010	Year ended December 31, 2009	Year ended December 31, 2008	Year ended December 31, 2007	Year ended December 31, 2006
Per Share Data:					
Net asset value, beginning of year	\$ 9.55	\$ 9.23	\$ 13.78	\$ 14.93	\$ 14.95
Net investment income	0.96	1.36	1.76	1.66	1.09
Net realized and unrealized gain (loss)	0.18	(0.16)	(4.54)	(1.31)	0.04
Total from investment operations	1.14	1.20	(2.78)	0.35	1.13
Dividend distributions to stockholders from:					
Net investment income	(1.28)	(0.80)	(1.71)	(1.68)	(1.14)
Net realized gains	—	(0.00)	(0.01)	(0.01)	(0.01)
Total dividend distributions	(1.28)	(0.80)	(1.72)	(1.69)	(1.15)
Issuance of stock at prices above (below) net asset value	0.35	(0.13)	(0.11)	0.38	—
Offering costs	(0.14)	—	—	(0.19)	—
Purchases of treasury stock at prices below net asset value	—	0.05	0.06	—	—
Net increase in net assets	0.07	0.32	(4.55)	(1.15)	(0.02)
Net asset value, end of year	\$ 9.62	\$ 9.55	\$ 9.23	\$ 13.78	\$ 14.93
Market price, end of year(1)	\$ 11.06	\$ 8.52	\$ 9.86	\$ 15.28	\$ —
Total return(2)	48.40%	(5.86)%	(23.88)%	3.41%	7.76%
Ratios / Supplemental Data:					
Ratio of operating expenses to average net assets(3)	6.05%	7.94%	4.41%	4.60%	2.48%
Ratio of credit facility related expenses to average net assets	1.35%	1.35%	2.96%	3.04%	0.05%
Ratio of total expenses to average net assets(3)	7.40%	9.29%	7.37%	7.64%	2.53%
Ratio of net investment income to average net assets	9.68%	14.47%	14.56%	11.16%	7.21%
Net assets, end of year	\$698,479,924	\$539,562,762	\$510,295,501	\$728,191,869	\$561,799,922
Average debt outstanding	\$205,151,507	\$397,464,757	\$453,241,284	\$313,057,645	\$ 81,157,895
Weighted average shares outstanding	62,663,002	55,923,757	54,043,069	45,714,141	36,632,218
Average debt per share(4)	\$ 3.27	\$ 7.11	\$ 8.39	\$ 6.85	\$ 2.22
Portfolio turnover	49%	14%	11%	31%	36%

- (1) The Company's common stock commenced trading on The NASDAQ Global Select Market on June 27, 2007. There was no established public trading market for the stock prior to that date.
- (2) For the years ended December 31, 2010, 2009 and 2008, total return is based on the change in market price during the respective years. For the years ended December 31, 2007 and 2006, total return is based on the change in net asset value per common share during the respective years. The total return for the period June 26,

[Table of Contents](#)

2007 through December 31, 2007 based on the change in market price per common share during such period was 1.18%. Total return calculations take into account dividends and distributions, if any, reinvested in accordance with the Company's dividend reinvestment plan and do not reflect brokerage commissions. Total return is not annualized.

- (3) Through June 30, 2007, certain base management fee waivers were in effect. For the years ended December 31, 2007 and 2006, the ratio of operating expenses before management fee waiver to average net assets was 4.90% and 3.26%, respectively, and the ratio of total expenses before management fee waiver to average net assets was 7.94% and 3.31%, respectively.
- (4) Average debt per share is calculated as average debt outstanding divided by the weighted average shares outstanding during the applicable period.

12. Federal tax information

Dividends from net investment income and distributions from net realized capital gains are determined in accordance with U.S. federal income tax regulations, which may differ from those amounts determined in accordance with GAAP. These book/tax differences are either temporary or permanent in nature. To the extent these differences are permanent, they are charged or credited to paid-in-capital or accumulated net realized gain, as appropriate, in the period that the differences arise. The following temporary and permanent differences at December 31, 2010 and 2009 primarily attributable to differences in the tax treatment of certain loans, the tax characterization of income from partnership investments, foreign currency transactions, non-deductible expenses and differences in accounting for upfront fees (which are treated as taxable income when received and accreted/amortized over the life of the respective investment for financial reporting purposes), were reclassified for tax purposes as follows:

	December 31, 2010	December 31, 2009
Decrease in paid-in capital in excess of par	\$ (224,036)	\$ (1,092,603)
Decrease in undistributed (distributions in excess of) net investment income	\$(2,888,423)	\$(15,860,943)
Decrease in accumulated net realized loss	\$ 3,112,459	\$ 16,953,546

The following reconciles net increase in net assets resulting from operations to taxable income for the years ended December 31, 2010 and 2009:

	Year ended December 31, 2010	Year ended December 31, 2009
Net increase in net assets resulting from operations	\$ 71,549,561	\$ 67,239,723
Net unrealized appreciation not taxable	(101,935,495)	(101,425,021)
Deferral of post-October capital loss	23,613,827	28,594,710
Reversal of post-October capital loss	(28,594,710)	—
Deferral of post-October currency loss	733,702	1,008,793
Reversal of prior year post-October currency loss	(1,008,793)	(793,563)
Section 1256 currency contracts mark-to-market	(368,445)	203,998
Reversal of prior year Section 1256 currency contracts mark-to-market	(203,998)	336,193
Current year net capital losses	95,856,015	9,065,897
Taxable interest income on non-accrual loans	(1,046,547)	1,046,547
Upfront fees received, net of book amortization	5,985,578	(1,884,376)
Losses not currently taxable	(78,363)	55,483,408
Other taxable loss	(1,062,826)	(2,246,428)
Non-deductible excise and other taxes	298,322	1,014,240
Amortization of organizational costs	(3,804)	(3,804)
Taxable income before deductions for distributions	<u>\$ 63,734,024</u>	<u>\$ 57,640,317</u>

Taxable income generally differs from the change in net assets resulting from operations for financial reporting purposes due to temporary and permanent differences in the recognition of income and expenses, and generally excludes net unrealized appreciation or depreciation, as gains or losses are not included in taxable income until they are realized.

Table of Contents

At December 31, 2010, the cost of investments for tax purposes was \$1,050,058,918, resulting in net unrealized depreciation of \$(169,973,252), which was comprised of gross unrealized appreciation and depreciation of \$48,185,710 and \$(218,158,962), respectively. At December 31, 2009, the cost of investments for tax purposes was \$1,114,390,618, resulting in net unrealized depreciation of \$(267,648,573), which was comprised of gross unrealized appreciation and depreciation of \$12,086,887 and \$(279,735,460), respectively.

At December 31, 2010 and 2009, the components of accumulated net losses on a tax basis and reconciliation to accumulated net losses on a book basis were as follows:

	Year ended December 31, 2010	Year ended December 31, 2009
Undistributed ordinary income—net	\$ 8,885,367	\$ 25,714,876
Unrealized loss—net	(105,935,052)	(207,870,547)
Post-October capital loss	(23,613,827)	(28,594,710)
Section 1256 currency contracts mark-to-market	368,445	(203,998)
Post-October currency loss	(733,702)	(1,008,793)
Differences between book and tax loss on investments	(53,518,710)	(55,623,914)
Taxable interest income on non-accrual loans	—	(1,046,547)
Capital loss carryforward	(104,921,912)	(9,065,897)
Upfront fees adjustments	(12,513,816)	(5,862,812)
Non-deductible taxes	—	(36,978)
Expenses not currently deductible	(36,135)	(39,939)
Net income from limited liability companies	1,650,613	1,953,089
Total accumulated losses—net, book basis	<u>\$(290,368,229)</u>	<u>\$(281,686,170)</u>

For the tax year ended December 31, 2010, the Company had a net capital loss of \$104,921,912, of which \$9,065,897 expires in 2017 and \$95,856,015 expires in 2018. This amount will be available to offset future net capital gains to the extent provided by federal tax law. Under the recently enacted Regulated Investment Company Modernization Act of 2010, capital losses incurred by the Company after December 31, 2010 will not be subject to expiration. In addition, such losses must be utilized prior to the losses incurred in the years preceding enactment.

As a RIC, the Company is subject to a non-deductible federal excise tax of 4% if it does not distribute at least 98% of its ordinary income, excluding net short-term capital gains, in any calendar year; 98% of its capital gains in excess of capital losses for each one-year period ended October 31; and any ordinary income and net capital gains for preceding years that were not distributed during such years. For the calendar years ended December 31, 2010 and 2009 and the one-year periods ended October 31, 2010 and 2009, the Company did not distribute at least 98% of its ordinary income and capital gains and paid the 4% excise tax. Accordingly, for the years ended December 31, 2010 and 2009, a provision was recorded for federal excise taxes of \$298,322 and \$1,012,791, respectively.

For income tax purposes, distributions paid to stockholders are reported as ordinary income, non-taxable, capital gains, or a combination thereof. The tax character of distributions paid or declared during the years ended December 31, 2010, 2009 and 2008, respectively, was as follows:

Year ended	Ordinary income	Amount per share*	Long-term capital gain	Amount per share*	Total distributions	Total amount per share*
December 31, 2010	\$80,455,656	\$ 1.28	\$ —	\$ —	\$80,455,656	\$ 1.28
December 31, 2009	\$44,714,904	\$ 0.80	\$106,515	\$ 0.00	\$44,821,419	\$ 0.80
December 31, 2008	\$92,556,785	\$ 1.71	\$330,584	\$ 0.01	\$92,887,369	\$ 1.72

* Rounded to the nearest \$0.01.

ASC 740-10, *Income Taxes* (“ASC 740-10”) clarifies the accounting for income taxes by prescribing the minimum recognition threshold an uncertain tax position is required to meet before tax benefits associated with such uncertain tax position are recognized in the financial statements. Based on its analysis of its tax position, the Company has concluded that it does not have any uncertain tax positions that met the recognition or measurement criteria of ASC 740-10.

[Table of Contents](#)

The Company files U.S. federal and various state and local tax returns. No income tax returns are currently under examination. The statute of limitations on the Company's U.S. federal income tax returns remains open for each of the four years ended December 31, 2010. The statute of limitations on the Company's state and local tax returns may remain open for an additional year depending upon the jurisdiction.

13. Selected quarterly financial data (unaudited)

<u>Quarter Ended</u>	<u>Total Investment Income</u>	<u>Net Investment Income</u>	<u>Net Realized and Unrealized Gain (Loss)</u> (Dollars in thousands, except per share data)	<u>Net Increase (Decrease) in Net Assets Resulting from Operations</u>	<u>Basic and Diluted Earnings (Loss) per Common Share</u>	<u>Net Asset Value per Common Share at End of Quarter</u>
December 31, 2010	\$ 25,043	\$ 2,354	\$ 63	\$ 2,416	\$ 0.03	\$ 9.62
September 30, 2010	24,818	16,811	(496)	16,316	0.25	9.76
June 30, 2010	28,211	20,421	1,914	22,335	0.39	9.83
March 31, 2010	27,799	20,265	10,218	30,483	0.54	9.77
December 31, 2009	\$ 30,274	\$ 4,985	\$ 11,355	\$ 16,339	\$ 0.29	\$ 9.55
September 30, 2009	29,359	21,782	9,364	31,146	0.55	9.59
June 30, 2009	33,440	25,535	(1,714)	23,822	0.43	9.24
March 31, 2009	31,811	23,751	(27,818)	(4,067)	(0.07)	9.04
December 31, 2008	\$ 35,181	\$ 23,043	\$ (127,143)	\$ (104,099)	\$ (1.88)	\$ 9.23
September 30, 2008	37,446	25,582	(44,375)	(18,793)	(0.34)	11.52
June 30, 2008	34,874	23,264	(11,404)	11,859	0.22	12.31
March 31, 2008	35,695	23,214	(62,688)	(39,474)	(0.75)	12.60

14. Subsequent events

The Company has reviewed subsequent events occurring through the date that these financial statements were issued, and determined that no subsequent events occurred requiring accrual or disclosure, except as disclosed below and elsewhere in these Notes to Financial Statements.

On January 18, 2011, the Company closed a private placement issuance of \$158,000,000 in aggregate principal amount of five-year, senior secured notes with a fixed interest rate of 6.50% and a maturity date of January 18, 2016 and \$17,000,000 million in aggregate principal amount of seven-year, senior secured notes with a fixed interest rate of 6.60% and a maturity date of January 18, 2018 (collectively, the "Senior Secured Notes"). The Senior Secured Notes were sold to certain institutional accredited investors pursuant to an exemption from registration under the Securities Act of 1933, as amended. Interest on the Senior Secured Notes is due semi-annually on January 18 and July 18, commencing on July 18, 2011. The proceeds from the issuance of the Senior Secured Notes were used to fund new portfolio investments, reduce outstanding borrowings under the Credit Facility and for general corporate purposes.

On March 1, 2011, the Company's Board of Directors declared a dividend of \$0.32 per share, payable on April 1, 2011 to stockholders of record at the close of business on March 18, 2011.

SUBSIDIARIES OF BLACKROCK KELSO CAPITAL CORPORATION

<u>Name</u>	<u>Jurisdiction</u>
BKC ARS Blocker, Inc.	Delaware
BKC ASW Blocker, Inc.	Delaware
BKC CSP Blocker, Inc.	Delaware
BKC DVSH Blocker, Inc.	Delaware
BKC MTCH Blocker, Inc.	Delaware

In addition, we may be deemed to control certain portfolio companies identified as “Controlled Investments” in footnote (g) to the Schedule of Investments at December 31, 2010 included in the Financial Statements portion of BlackRock Kelso Capital Corporation’s Form 10-K for the year ended December 31, 2010.

CEO CERTIFICATION

I, James R. Maher, certify that:

1. I have reviewed this Annual Report on Form 10-K, for the fiscal year ended December 31, 2010 of BlackRock Kelso Capital Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)), for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 8, 2011

By: /s/ James R. Maher

James R. Maher
Chairman of the Board and
Chief Executive Officer

CFO CERTIFICATION

I, Frank D. Gordon, certify that:

1. I have reviewed this Annual Report on Form 10-K, for the fiscal year ended December 31, 2010 of BlackRock Kelso Capital Corporation;

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

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)), for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 8, 2011

By: /s/ Frank D. Gordon

Frank D. Gordon

Chief Financial Officer and Treasurer

**Certification of CEO and CFO Pursuant to
18 U.S.C. Section 1350,
as Adopted Pursuant to
Section 906 of the Sarbanes-Oxley Act of 2002**

In connection with the Annual Report on Form 10-K of BlackRock Kelso Capital Corporation (the "Company") for the annual period ended December 31, 2010 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), James R. Maher, as Chief Executive Officer of the Company, and Frank D. Gordon, as Chief Financial Officer of the Company, each hereby certifies, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ James R. Maher

Name: James R. Maher

Title: Chief Executive Officer

Date: March 8, 2011

/s/ Frank D. Gordon

Name: Frank D. Gordon

Title: Chief Financial Officer and Treasurer

Date: March 8, 2011