

THE BDC ALTERNATIVE: Is It Right for You?

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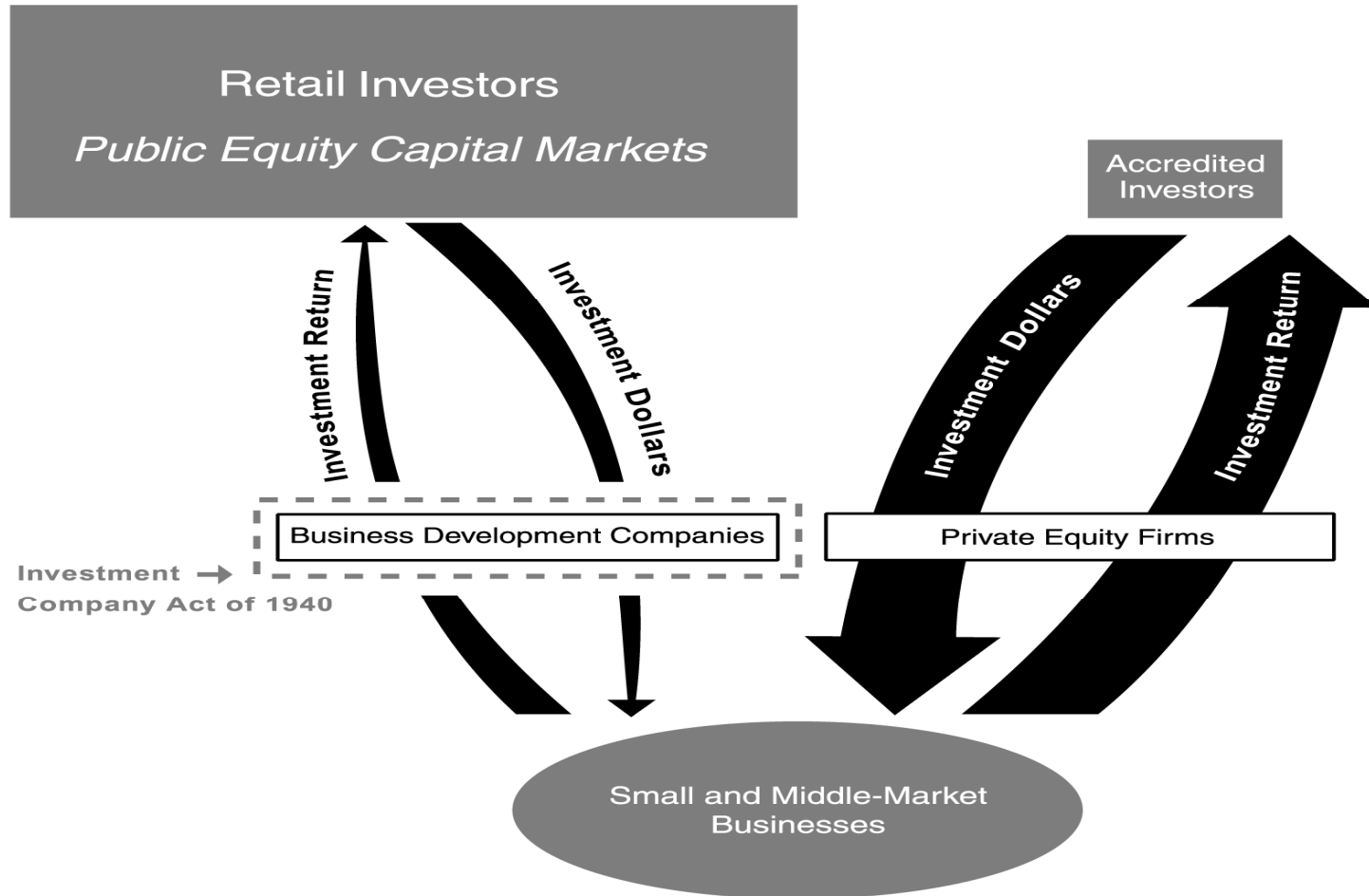
What is a Business Development Company?

- Created by the Small Business Investment Incentive Act of 1980 (the “1980 Amendments”) as a result of a perceived crisis in the capital markets in the 1970s.
- Private equity and venture capital firms believed the “small private investment company” exemption (Section 3(c)(1) of 1940 Act) limited their capacity to provide financing to small, growing businesses.
- Regulated Investment Company (RIC) Status in 1990.

What is a Business Development Company? (con't)

- Several of the entities that elected to be BDCs were Small Business Investment Companies, or SBICs.
- Publicly traded closed-end funds that:
 - Provide small, growing companies access to capital
 - Enable private equity funds to access the public capital markets
 - Enable retail investors to participate in the upside of pre-IPO investing with complete liquidity
- Hybrid between an operating company and an investment company.

What is a Business Development Company? (con't)



What are the Benefits of the BDC as an Investment Vehicle?

- Access to public capital markets
- Shares are traded on exchanges or Nasdaq
- Flow-through tax treatment
- Reduced burden under 1940 Act
- External model permits management fee and “carried interest” incentive fee structure
- Publicly available financial information through quarterly reporting
- Portfolio is typically diversified which reduces risk to investors associated with private equity investments
- Restrictions on leverage/affiliated transactions

How Did the BDC Industry Develop?

- Prior to 2003, the largest BDCs were primarily internally-managed. This choice was a reflection of the success of the internally managed, income producing BDC model.
- In 2004 Apollo Investment Corporation raised \$930 million in less than three months which ignited the BDC industry.
- There has been a steady stream of BDC IPOs since that period, raising approximately \$2.4 billion.
- Financial crisis has affected the BDC market requiring companies to deleverage and reduce or eliminate dividends.
- In the past four months, BDCs have raised over \$538.6 million in follow on transactions.

What are Some Recent Trends and Developments for BDCs?

- Over 25 BDCs currently on NYSE, Nasdaq, NYSE AMEX, or OTCBB
- Nine IPOs from 2007 through August of 2009, including:
 - Keating Capital, Inc. (06-11-09)
 - Fifth Street Finance Corp. (06-17-08)
 - Main Street Capital Corporation (10-4-07)
 - Blackrock Kelso Capital Corp. (6-27-07)
 - PennantPark Investment Corporation (4-19-07)
 - Triangle Capital Corporation (2-14-07)
- Over 7 follow on equity offerings since March 2009 raising over \$602 million, including Main Street Capital Corporation (\$16.3 million) and Triangle Capital Corporation (\$14.6 million)
- Pending IPOs
 - Solar Capital Ltd.
 - THL Credit, Inc.

What is the BDC Industry's Role in the Current Economy?

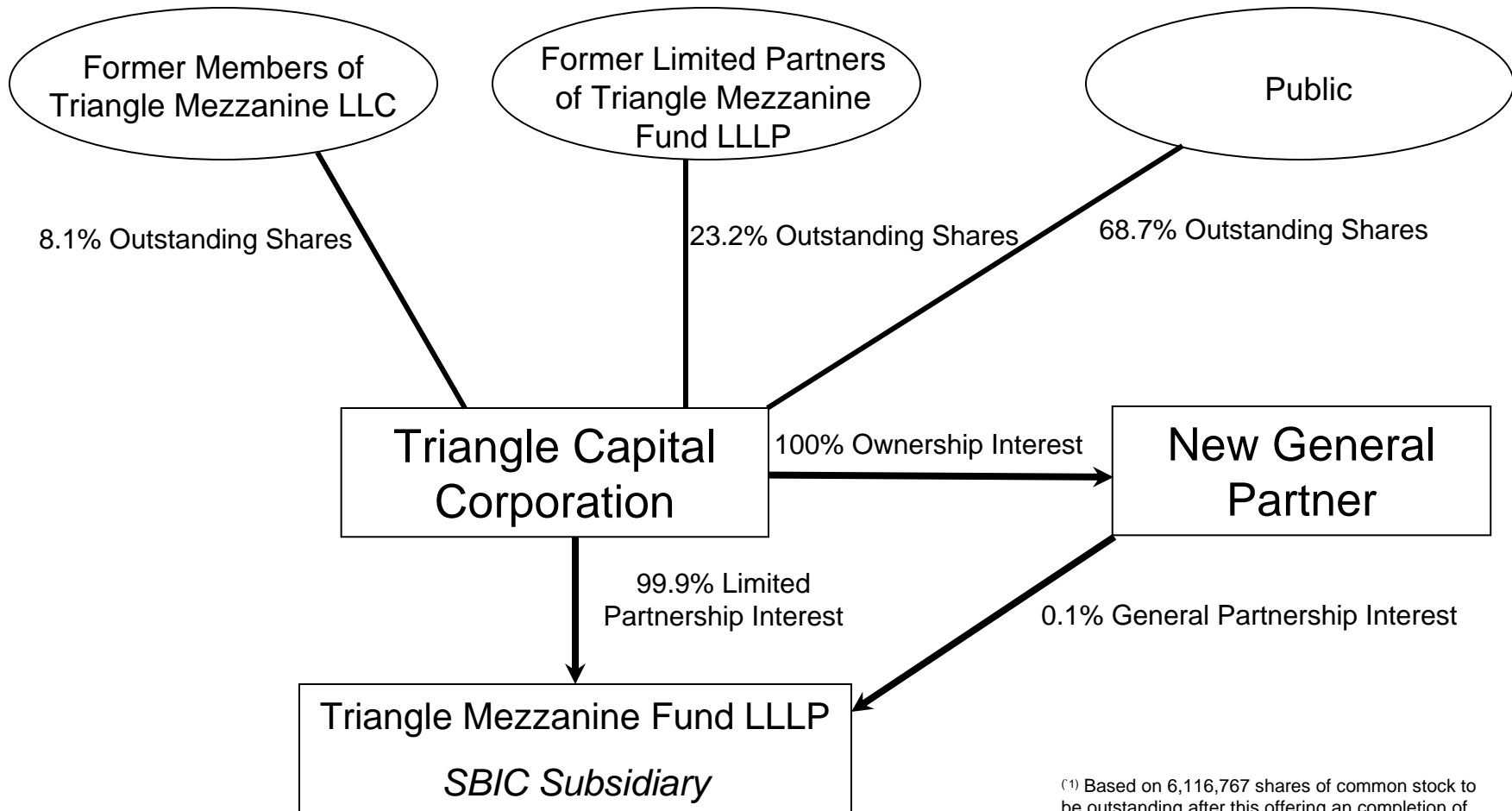
- **Market Position:**
 - At the height of the market, BDCs had aggregate portfolio assets of approximately \$27.5 billion invested in approximately 1,500 small and middle market companies across the United States.
 - Actively traded BDCs had approximately \$21 billion in assets as of June 2009.
- **Contribution to Economy:**
 - It is estimated that the BDC industry in the aggregate currently sustains companies that provide approximately 1.5 million U.S. jobs.
 - BDCs can continue to play a significant role in the future success of middle market companies by providing a much needed source of financing.

Are There BDCs That Have SBIC Subsidiaries?

- Two (2) SBICs elected to become BDCs and conducted successful IPOs
 - Main Street Capital Corporation/\$64,500,000
 - Triangle Capital Corporation/\$71,550,000
- BDCs that have received an SBIC license for a wholly-owned subsidiary
 - Hercules Technology Growth Capital, Inc.
 - Medallion Financial Corp.
 - MCG Capital Corporation
 - Rand Capital Corporation

TRIANGLE CAPITAL CORPORATION

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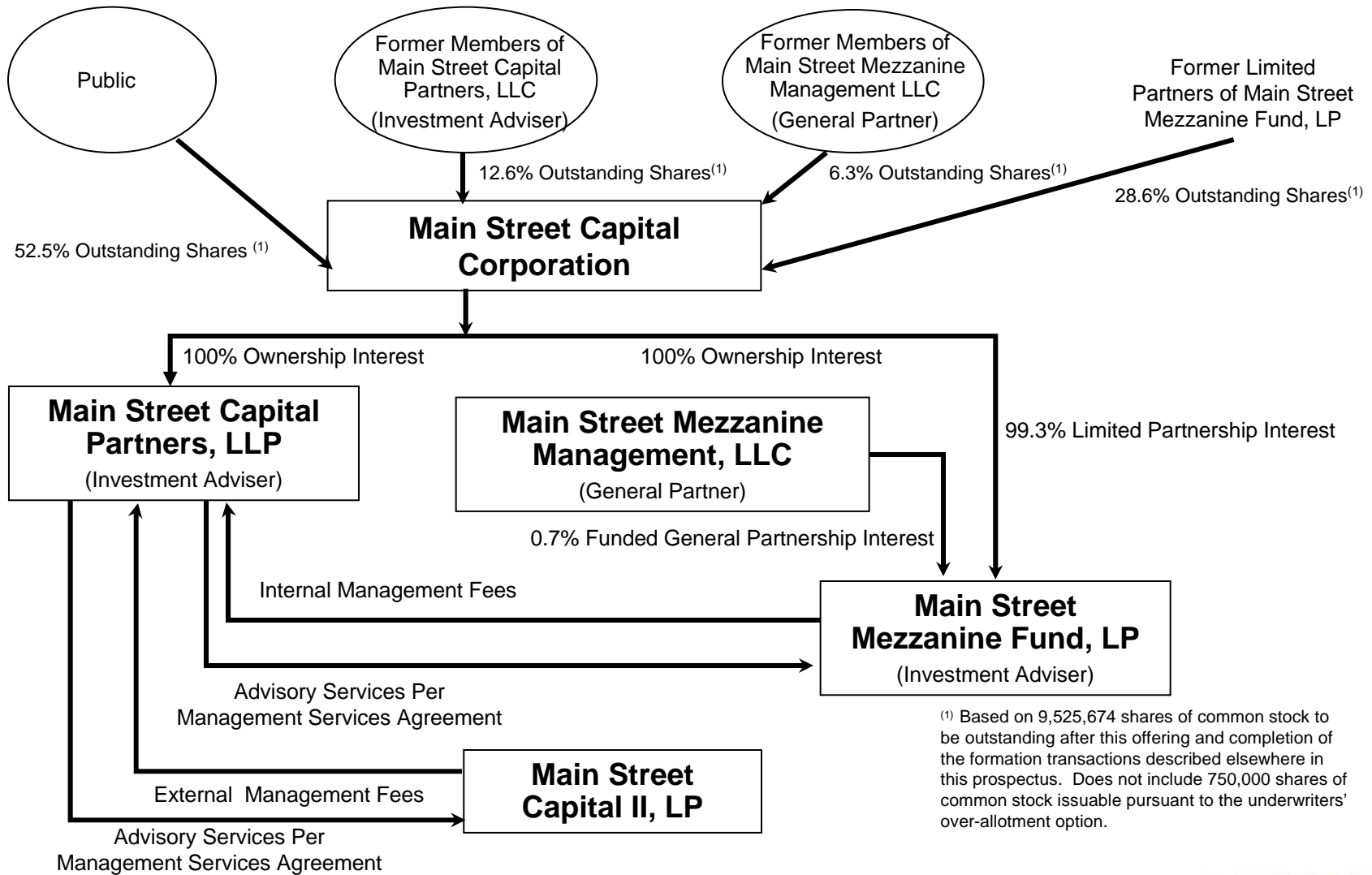


⁽¹⁾ Based on 6,116,767 shares of common stock to be outstanding after this offering an completion of the formation transactions. Does not include 630,000 shares of common stock pursuant to the underwriters' over-allotment option.

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MAIN STREET CAPITAL CORPORATION



⁽¹⁾ Based on 9,525,674 shares of common stock to be outstanding after this offering and completion of the formation transactions described elsewhere in this prospectus. Does not include 750,000 shares of common stock issuable pursuant to the underwriters' over-allotment option.

How Does an SBIC Convert to a BDC?

- Conversion Transaction
 - Approval of LPs in advance of valuation and merger
 - Merger of SBIC into subsidiary of BDC
 - Amend Limited Partnership Agreement
 - SBA Approval

- SEC Review
 - Affiliate Transaction Issues
 - Compensation Issues
 - Disclosure Issues

Exemptive Relief

- Relief to get SBIC leverage treatment at BDC level
- Section 18(a):
 - Question of whether BDC with an SBIC subsidiary must comply with the asset coverage requirements of Section 18(a) (as modified by Section 61(a) for BDCs) on a consolidated basis.
 - The senior securities issued by the SBIC Subsidiary would be excluded from the SBIC Subsidiary's individual asset coverage ratio by Section 18(k) if the SBIC Subsidiary were a BDC.
 - Exemption requested- senior securities representing indebtedness issued by the SBIC Subsidiary may be excluded from the BDC's consolidated asset coverage ratio.

What are the Incentives for an SBIC to Convert to a BDC?

Why Are BDCs Attractive to SBICs?

- Ability to Access Public Market
- Flexibility in Funding Portfolio Investments
- Permanent Capital Base
- Additional Compensation Incentives

Why Are SBICs Attractive to the BDC Market?

- Existing Portfolio – not blind pool
- Existing management team with track record
- Market niche – lower middle market
- Additional leverage capacity

How Does a Company Become a BDC?

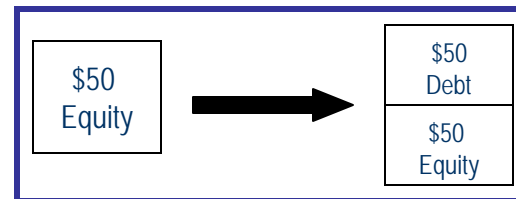
- Organize the BDC as a Delaware or a Maryland corporation
- Register a class of securities under the 1934 Act
- Make an election to be a BDC- file a Form N-54A (Notification of election to be subject to sections 55 through 65 of the 1940 Act)
- Register a class of securities on Form N-2 under the 1940 Act
- List securities on the New York Stock Exchange (NYSE), the Nasdaq Stock Market, Inc. (Nasdaq), or the NYSE AMEX, or the BDC can be a non-traded BDC
- Comply with the Sarbanes-Oxley Act of 2002
- Comply with regulatory requirements of the 1940 Act

What Must a BDC Invest In?

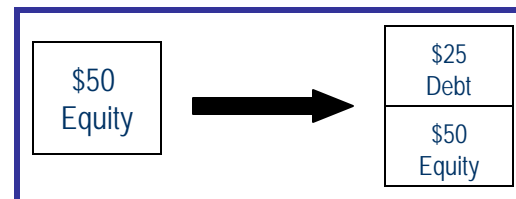
- A BDC can invest in assets (“bad assets”) that do not fall within the “70% basket” if the investment:
 - Is in a publicly traded company whose success may be revived by new capital or managerial assistance;
 - Provides a source of cash flow to the BDC, which otherwise invests in securities generating little income; or
 - Diversifies the portfolio, which may contribute to attracting capital from investors.
- SBIC investments generally meet the eligible portfolio company definition.

What are the Borrowing Limitations?

- BDCs Must have 200% asset coverage (Total Assets/Total Debt)
 - For example, a BDC with \$50 in equity can borrow up to \$50
 - A BDC would be able to invest \$100 in growing businesses



- Other investment companies are restricted to a 300% asset coverage requirement with respect to issuing debt



- BDCs may exclude leverage at the SBIC level if the Securities and Exchange Commission grants exemptive relief (for example, Allied Capital Corporation and Hercules Technology Capital Growth, Inc.)

Can a BDC Engage in Transactions with Affiliates?

- Section 57 addresses the ability of BDCs to engage in certain types of transactions with affiliates:
 - Section 57 is less onerous than its counterpart for registered investment companies, Section 17
- Depending on the nature of the affiliation with the BDC, transactions involving a BDC and one or more of its affiliates require either:
 - Authorization by the required majority of the board of directors, which consists of a majority of the board, including a majority of disinterested board members; or
 - An order of the Commission.
- An order from the Commission will also provide an exemption from SBA regulations.

What are the 1940 Act Operational Requirements?

- BDC must have a majority of independent directors - persons who are not “interested persons” as defined in Section 2(a)(19) of the 1940 Act.
- BDCs must make available significant managerial assistance to these companies
 - SBICs generally already provide managerial assistance to the portfolio company
- **Custodian Agreement**
 - A BDC generally must place and maintain its securities and similar investments in the custody of a bank qualified under Section 26(a)(1) of the 1940 Act or a broker dealer.
- **Fidelity Bond**
 - A BDC must provide and maintain a bond issued by a reputable fidelity insurance company to protect the company against larceny and embezzlement. The bond must cover each officer and employee with access to securities and funds of the company.

What are the 1940 Act Operational Requirements? (con't)

- **Restrictions on Investing in Other Investment Companies**
 - A BDC may not invest:
 - in more than 3% of the outstanding voting stock of an investment company;
 - more than 5% of the value of its total assets in an investment company; or
 - more than an aggregate of 10% of its total assets in investment companies.
- **Restrictions on investment funds investing in a BDC**
 - Neither a public (i.e. registered) or private investment fund may own more than 3% of the outstanding voting stock of a BDC
- **Code of Ethics**
- **Limitations on Indemnification**
 - A BDC is prohibited from protecting any director or officer against any liability to the company, or its security holders, arising from willful misfeasance, bad faith, gross negligence or reckless disregard of the duties involved in the conduct of such person's office.

What are the 1940 Act Operational Requirements? (con't)

- Bookkeeping and Records Requirements - BDCs are required to maintain records as set forth in Rules 31a-1(b), 31a-2(a) and 31a-3 under the 1940 Act.
- Examinations by the SEC
- Compliance Policies and Procedures for the BDC – Rule 38a-1
 - Rule 38a-1 under the 1940 Act requires a BDC to:
 - adopt and implement policies and procedures designed to prevent violation of the federal securities laws;
 - review these policies and procedures annually for their adequacy and the effectiveness of their implementation; and
 - appoint a chief compliance officer to administer the compliance policies and procedures.
- Compliance Policies and Procedures for the investment adviser– Rule 206(4)-7 of the Investment Advisers Act of 1940
 - requires an investment adviser BDC to adopt and implement policies and procedures.

What are the Reporting Requirements?

- Form 10-K (Annual Report)
- Form 10-Q (Quarterly Report)
- Form 8-K (Current Report)
- Proxy Statements
- Sections 13 and 16 Filings
 - Forms 3, 4 or 5 for reporting beneficial ownership by insiders
 - Schedules 13D and 13G for reporting beneficial ownership by others
- Regulation G and Regulation FD
- Comply with the Sarbanes-Oxley Act of 2002

What are the NYSE/Nasdaq/NYSE AMEX Reporting Requirements?

- BDCs that have their securities listed or traded on the NYSE, Nasdaq or NYSE AMEX must comply with the corporate governance listing standards of the relevant association or exchange. For example:
 - A listed BDC must have an audit committee composed solely of “independent directors” (as defined by the applicable exchange or association);
 - For internally managed funds, the compensation of a BDC’s executive officers must be subject to the oversight of the BDC’s “independent directors”;
 - The non-management, or “independent,” directors of the BDC must hold regularly scheduled executive sessions; and
 - The BDC must adopt a code of business conduct and ethics, various committee charters and, in the case of NYSE listed BDCs, corporate governance guidelines.
 - All such documents must be posted on the company’s website.

How Are a BDC's Assets Valued?

- Assets must be valued on a quarterly basis
 - Market value is used for those assets for which market quotations are readily available
 - “Fair value,” as determined by the board of directors, is used for other securities and assets
 - Each debt and equity security is separately valued
- There is no single standard for determining fair value in good faith
- Determining fair value requires that judgment be applied to the specific facts and circumstances of each portfolio investment while employing a consistently applied valuation process
- FAS 157- requires that public companies' financial instruments generally be valued at their current market price (i.e., “mark to market”)
- SBIC valuation policy may be different from the SEC regulations

How Can an Internally Managed BDC Compensate Management?

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- Certain performance-based compensation permitted, including:
 - Issuance of at-the-market options, warrants, or rights pursuant to an executive compensation plan;
 - OR
 - Maintenance of a profit sharing plan.
- Otherwise, BDC must use cash assets as compensation
- Restricted stock – exemptive orders have been issued to Hercules Growth Technology, Inc., MCG Capital Corporation and Main Street Capital Corporation

How Can an Externally Managed BDC Compensate the Adviser?

- The investment adviser must be registered under the Investment Advisers Act of 1940
- Section 205(b)(3) of the Advisers Act permits external investment advisers to BDCs to receive incentive fees, provided that the BDCs do not have outstanding any equity-based compensation arrangement or profit-sharing plan.
 - Section 205(b)(3) provides an exception from the general prohibition on an investment adviser charging an incentive fee based on a share of capital gains.
 - May assess an incentive performance fee of up to 20% on a BDC's realized capital gains net of all realized capital losses and unrealized capital depreciation over a specified period.
- The Advisers Act contains no prohibition against an adviser taking an incentive fee against income, although the market has effectively capped these fees at 20%, usually subject to a hurdle.

How are BDCs Taxed?

- A BDC may elect to be taxed as a regulated investment company (“RIC”) under the Internal Revenue Code
 - Taxation as a RIC
 - Allows “pass through” tax treatment for income and capital gains that are distributed to shareholders
 - A BDC must distribute at least 90% of its investment income to shareholders annually
 - The BDC may retain, distribute or “deem distribute” capital gains
 - BDC must meet minimum source of income requirements annually and meet requirements on a quarterly basis with respect to the portfolio diversification
 - Conversion to RIC status

Questions

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Q & A