

# MCG CAPITAL CORP

## FORM 10-Q (Quarterly Report)

Filed 11/03/11 for the Period Ending 09/30/11

Address	1100 WILSON BLVD SUITE 3000 ARLINGTON, VA 22209
Telephone	7032477500
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Symbol	MCGC
Industry	Investment Services
Sector	Financial
Fiscal Year	12/31

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

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**FORM 10-Q**

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(Mark One)

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

For the quarterly period ended September 30, 2011

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 0-33377

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**MCG CAPITAL CORPORATION**

(Exact name of registrant as specified in its charter)

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**Delaware**  
(State or other jurisdiction  
of incorporation or organization)

**54-1889518**  
(I.R.S. Employer  
Identification No.)

**1100 Wilson Boulevard, Suite 3000**  
**Arlington, VA**  
(Address of principal executive offices)

**22209**  
(Zip Code)

**(703) 247-7500**  
(Registrant's telephone number, including area code)

**None**  
(Former name, former address and former fiscal year, if changed since last report)

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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 whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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

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

As of October 28, 2011, there were 77,043,042 shares of the registrant's \$0.01 par value Common Stock outstanding.

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### PART I. FINANCIAL INFORMATION

#### Item 1. Financial Statements

#### MCG Capital Corporation Consolidated Balance Sheets

	<b>September 30,</b>	<b>December 31,</b>
<i>(in thousands, except per share amounts)</i>	<u><b>2011</b></u>	<u><b>2010</b></u>
	<i>(unaudited)</i>	
<b>Assets</b>		
Cash and cash equivalents	\$ 53,956	\$ 44,970
Cash, securitization accounts	99,416	42,245
Cash, restricted	16,982	29,383
Investments at fair value		
Non-affiliate investments (cost of \$593,285 and \$684,785, respectively)	606,710	646,116
Affiliate investments (cost of \$42,497 and \$43,721, respectively)	55,107	53,300
Control investments (cost of \$424,461 and \$517,167, respectively)	<u>162,356</u>	<u>310,289</u>
Total investments (cost of \$1,060,243 and \$1,245,673, respectively)	824,173	1,009,705
Interest receivable	3,182	5,453
Other assets	<u>11,381</u>	<u>13,521</u>
<b>Total assets</b>	<b><u>\$1,009,090</u></b>	<b><u>\$1,145,277</u></b>
<b>Liabilities</b>		
Borrowings (maturing within one year of \$80,173 and \$18,858, respectively)	\$ 490,019	\$ 546,882
Interest payable	1,578	2,291
Dividends payable	13,101	10,735
Other liabilities	<u>7,911</u>	<u>7,353</u>
<b>Total liabilities</b>	<b><u>512,609</u></b>	<b><u>567,261</u></b>
<b>Stockholders' equity</b>		
Preferred stock, par value \$0.01, authorized 1 share, none issued and outstanding	—	—
Common stock, par value \$0.01, authorized 200,000 shares on September 30, 2011 and December 31, 2010, 77,035 issued and outstanding on September 30, 2011 and 76,662 issued and outstanding on December 31, 2010	770	767
Paid-in capital	1,009,211	1,008,823
Distributions in excess of earnings		
Paid-in capital	(166,029)	(166,029)
Other	(110,997)	(28,555)
Net unrealized depreciation on investments	<u>(236,474)</u>	<u>(236,990)</u>
<b>Total stockholders' equity</b>	<b><u>496,481</u></b>	<b><u>578,016</u></b>
<b>Total liabilities and stockholders' equity</b>	<b><u>\$1,009,090</u></b>	<b><u>\$1,145,277</u></b>
<b>Net asset value per common share at end of period</b>	<b>\$ 6.44</b>	<b>\$ 7.54</b>

*The accompanying notes are an integral part of these Condensed Consolidated Financial Statements*

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**MCG Capital Corporation**  
**Consolidated Statements of Operations**  
**(unaudited)**

<i>(in thousands, except per share amounts)</i>	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
<b>Revenue</b>				
Interest and dividend income				
Non-affiliate investments (less than 5% owned)	\$ 16,540	\$ 16,198	\$ 50,319	\$ 46,123
Affiliate investments (5% to 25% owned)	1,215	792	4,133	2,557
Control investments (more than 25% owned)	2,025	4,900	8,952	15,974
Total interest and dividend income	19,780	21,890	63,404	64,654
Advisory fees and other income				
Non-affiliate investments (less than 5% owned)	885	260	1,812	725
Control investments (more than 25% owned)	45	421	1,005	706
Total advisory fees and other income	930	681	2,817	1,431
Total revenue	20,710	22,571	66,221	66,085
<b>Operating expense</b>				
Interest expense	3,960	4,326	11,778	13,182
Employee compensation				
Salaries and benefits	2,683	3,527	9,567	12,065
Amortization of employee restricted stock awards	348	1,013	1,378	3,363
Total employee compensation	3,031	4,540	10,945	15,428
General and administrative expense	3,657	2,305	9,130	8,785
Restructuring expense	4,109	—	4,174	1
Total operating expense	14,757	11,171	36,027	37,396
<b>Net operating income before net investment loss, (loss) gain on extinguishment of debt and income tax provision</b>	5,953	11,400	30,194	28,689
<b>Net realized (loss) gain on investments</b>				
Non-affiliate investments (less than 5% owned)	281	7,383	(47,288)	7,837
Affiliate investments (5% to 25% owned)	(1)	—	(917)	—
Control investments (more than 25% owned)	(38,107)	(3,911)	(25,755)	(5,889)
Total net realized (loss) gain on investments	(37,827)	3,472	(73,960)	1,948
<b>Net unrealized appreciation (depreciation) on investments</b>				
Non-affiliate investments (less than 5% owned)	(2,634)	(6,854)	52,094	445
Affiliate investments (5% to 25% owned)	1,942	573	3,031	2,051
Control investments (more than 25% owned)	7,613	(6,890)	(55,227)	(29,836)
Derivative and other fair value adjustments	(146)	(101)	618	262
Total net unrealized appreciation (depreciation) on investments	6,775	(13,272)	516	(27,078)
<b>Net investment loss before income tax provision</b>	(31,052)	(9,800)	(73,444)	(25,130)
<b>(Loss) gain on extinguishment of debt before income tax provision</b>	—	(449)	(863)	2,983
<b>Income tax provision</b>	10	1,680	29	1,866
<b>Net (loss) earnings</b>	\$(25,109)	\$ (529)	\$(44,142)	\$ 4,676
(Loss) earnings per basic and diluted common share	\$ (0.33)	\$ (0.01)	\$ (0.58)	\$ 0.06
Cash distributions declared per common share	\$ 0.17	\$ 0.12	\$ 0.49	\$ 0.23
Weighted-average common shares outstanding—basic and diluted	76,404	75,486	76,173	76,469

*The accompanying notes are an integral part of these Condensed Consolidated Financial Statements*

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**MCG Capital Corporation**  
**Consolidated Statements of Changes in Net Assets**  
**(unaudited)**

<i>(in thousands, except per share amounts)</i>	Nine months ended September 30,	
	2011	2010
<b>Increase (decrease) in net assets from operations</b>		
Net operating income before net investment loss, (loss) gain on extinguishment of debt and income tax provision	\$ 30,194	\$ 28,689
Net realized (loss) gain on investments	(73,960)	1,948
Net unrealized appreciation (depreciation) on investments	516	(27,078)
(Loss) gain on extinguishment of debt	(863)	2,983
Income tax provision	(29)	(1,866)
Net (loss) income	(44,142)	4,676
<b>Distributions to stockholders</b>		
Distributions declared	(37,784)	(17,608)
Dividends forfeited	—	7
Net decrease in net assets resulting from stockholder distributions	(37,784)	(17,601)
<b>Capital share transactions</b>		
Amortization of restricted stock awards		
Employee awards accounted for as employee compensation	1,378	3,363
Employee awards accounted for as restructuring expense	431	—
Non-employee director awards accounted for as general and administrative expense	46	58
Common stock withheld to pay taxes applicable to the vesting of restricted stock	(1,453)	(86)
Net forfeitures of restricted common stock	(11)	(15)
Net increase in net assets resulting from capital share transactions	391	3,320
<b>Total decrease in net assets</b>	<b>(81,535)</b>	<b>(9,605)</b>
<b>Net assets</b>		
<b>Beginning of period</b>	<b>578,016</b>	<b>615,683</b>
<b>End of period</b>	<b>\$496,481</b>	<b>\$606,078</b>
<b>Net asset value per common share at end of period</b>	<b>\$ 6.44</b>	<b>\$ 7.92</b>
<b>Common shares outstanding at end of period</b>	<b>77,035</b>	<b>76,542</b>

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**MCG Capital Corporation**  
**Consolidated Statements of Cash Flows**  
**(unaudited)**

<i>(in thousands)</i>	<b>Nine months ended September 30,</b>	
	<b>2011</b>	<b>2010</b>
<b>Cash flows from operating activities</b>		
Net (loss) income	\$ (44,142)	\$ 4,676
Adjustments to reconcile net (loss) income to net cash provided by operating activities		
Investments in portfolio companies	(243,966)	(142,491)
Principal collections related to investment repayments or sales	336,172	177,340
Decrease in interest receivable, accrued payment-in-kind interest and dividends	21,453	3,166
Amortization of restricted stock awards		
Employee	1,809	3,363
Non-employee director	46	58
Decrease in cash—securitization accounts from interest collections	1,515	3,191
Increase in restricted cash—escrow accounts	(3,648)	—
Depreciation and amortization	2,936	3,073
Decrease in other assets	1,021	446
Increase (decrease) in other liabilities	428	(4,564)
Realized loss (gain) on investments	73,960	(1,948)
Net change in unrealized (appreciation) depreciation on investments	(516)	27,078
Loss (gain) on extinguishment of debt	863	(2,983)
Net cash provided by operating activities	<b>147,931</b>	<b>70,405</b>
<b>Cash flows from financing activities</b>		
Payments on borrowings	(62,726)	(73,466)
Proceeds from borrowings	5,000	27,500
Decrease (increase) in cash in restricted and securitization accounts		
Securitization accounts for repayment of principal on debt	(58,686)	(9,553)
Restricted cash	16,049	12,190
Payment of financing costs	(1,700)	(2,056)
Distributions paid	(35,418)	(8,421)
Common stock withheld to pay taxes applicable to the vesting of restricted stock	(1,453)	(86)
Net forfeitures of restricted common stock	(11)	(15)
Net cash used in financing activities	<b>(138,945)</b>	<b>(53,907)</b>
Net increase in cash and cash equivalents	<b>8,986</b>	<b>16,498</b>
<b>Cash and cash equivalents</b>		
Beginning balance	<b>44,970</b>	54,187
Ending balance	<b>\$ 53,956</b>	<b>\$ 70,685</b>
<b>Supplemental disclosure of cash flow information</b>		
Interest paid	<b>\$ 10,397</b>	\$ 11,341
Income taxes paid	<b>297</b>	1,469
Paid-in-kind interest collected	<b>20,410</b>	17,522
Dividend income collected	<b>12,355</b>	2,103

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### MCG Capital Corporation Consolidated Schedule of Investments September 30, 2011 (unaudited) (dollars in thousands)

Portfolio Company	Industry	Investment	Interest Rate <sup>(9)</sup>			Principal	Cost	Fair Value
			Current	PIK	Total			
<b>Control Investments <sup>(4)</sup> :</b>								
Broadview Networks Holdings, Inc. <sup>(6)</sup>	Communications	Series A Preferred Stock (12.0%, 87,254 shares)					\$ 81,984	\$ 13,443
		Series A-1 Preferred Stock (12.0%, 100,702 shares)					77,496	15,514
		Series B Preferred Stock (12.0%, 1,282 shares)					100	198
		Class A Common Stock (4,731,031 shares)					—	—
GMC Television Broadcasting, LLC <sup>(2)</sup>	Broadcasting	Senior Debt (Due 12/16) <sup>(1)</sup>	4.4%	—	4.4%	\$ 19,103	16,644	17,791
		Subordinated Debt (Due 12/16) <sup>(1)(7)</sup>	2.5%	—	2.5%	10,950	6,976	—
		Class B Voting Units (8.0%, 86,700 units)					9,071	—
Intran Media, LLC <sup>(6)</sup>	Other Media	Senior Debt (Due 12/15) <sup>(1)(7)</sup>	9.5%	—	9.5%	9,935	9,445	2,474
		Series A Preferred Units (10.0%, 36,300 units)					9,095	—
		Series B Preferred Units (10.0%, 12,700 units)					3,000	—
		Series C Preferred Units (10.0%, 15,000 units)					1,250	—
Jet Plastica Investors, LLC <sup>(2)</sup>	Plastic Products	Senior Debt A (Due 3/15) <sup>(1)</sup>	2.4%	7.0%	9.4%	15,046	15,007	15,007
		Senior Debt B (Due 6/15) <sup>(1)(7)</sup>	2.4%	5.0%	7.4%	23,459	19,110	16,227
		Senior Debt C (Due 6/16) <sup>(7)</sup>	—	2.5%	2.5%	6,265	6,250	—
		Senior Debt D (Due 3/13-9/16) <sup>(7)</sup>	—	2.5%	2.5%	28,834	21,560	—
		Series B Preferred Stock (8.0%, 10,000 shares)					10,000	—
		Preferred LLC Interest (8.0%, 301,595 units)					34,014	—
NPS Holding Group, LLC <sup>(2)(5)(6)</sup>	Business Services	Senior Debt Revolver (Due 6/13) <sup>(1)(7)</sup>	6.3%	3.3%	9.6%	3,859	2,360	3,621
		Senior Debt A1 (Due 6/13) <sup>(1)(7)</sup>	6.3%	—	6.3%	9,157	3,470	6,058
		Senior Debt A2 (Due 6/13) <sup>(1)(7)</sup>	6.3%	—	6.3%	2,069	1,905	—
		Senior Debt A3 (Due 6/13) <sup>(1)(7)</sup>	6.3%	—	6.3%	15,324	6,228	—
		Series A Preferred Units (504 units)					50	—
		Series B Preferred Units (5.0%, 10,731 units)					10,731	—
		Common Units (36,500 units)					—	—
Orbitel Holdings, LLC <sup>(2)</sup>	Cable	Senior Debt (Due 2/13) <sup>(1)</sup>	10.0%	—	10.0%	18,580	18,497	18,497
		Preferred LLC Interest (10.0%, 150,000 units) <sup>(1)</sup>					17,486	17,503
PremierGarage Holdings, LLC <sup>(2)(6)</sup>	Home Furnishings	Senior Debt (Due 12/10-9/11) <sup>(1)(7)</sup>	3.4%	4.7%	8.1%	11,198	9,498	1,035
		Preferred LLC Units (400 units)					400	—
		Common LLC Units (79,935 units)					4,971	—
RadioPharmacy Investors, LLC <sup>(2)</sup>	Healthcare	Senior Debt (Due 12/12) <sup>(1)</sup>	7.5%	—	7.5%	8,176	8,176	8,176
		Subordinated Debt (Due 12/12) <sup>(1)</sup>	12.0%	3.0%	15.0%	10,373	10,365	10,365
		Preferred LLC Interest (19.7%, 70,000 units)					9,322	16,447
<b>Total Control Investments (represents 19.7% of total investments at fair value)</b>							<b>424,461</b>	<b>162,356</b>

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**MCG Capital Corporation**  
**Consolidated Schedule of Investments**  
**September 30, 2011 (unaudited)**  
**(dollars in thousands)**

Portfolio Company	Industry	Investment	Interest Rate <sup>(9)</sup>			Principal	Cost	Fair Value	
			Current	PIK	Total				
<b>Affiliate Investments <sup>(3)</sup> :</b>									
Advanced Sleep Concepts, Inc. <sup>(2)</sup>	Home Furnishings	Senior Debt (Due 1/14) <sup>(1)</sup>	13.4%	—	13.4%	\$ 5,859	\$ 5,850	\$ 5,850	
		Subordinated Debt (Due 1/14) <sup>(1)</sup>	12.0%	4.0%	16.0%	5,583	5,554	5,554	
		Series A Preferred Stock (20.0%, 49 shares)					344	71	
		Series B Preferred Stock (1,000 shares)					—	310	
		Common Stock (423 shares)					524	—	
		Warrants to purchase Common Stock (expire 10/16)				348	—		
Cherry Hill Holdings, Inc.	Entertainment	Series A Preferred Stock (9.8%, 750 shares)				769	769	769	
Contract Datascan Holdings, Inc.	Business Services	Subordinated Debt (Due 3/16) <sup>(1)</sup>	12.0%	2.0%	14.0%	7,875	7,270	7,351	
		Series A Preferred Stock (10.0%, 2,292 shares) <sup>(1)</sup>					2,367	2,367	
		Common Stock (4,751 shares) <sup>(1)</sup>					472	145	
Stratford School Holdings, Inc. <sup>(2)</sup>	Education	Senior Debt (Due 12/15) <sup>(1)</sup>	7.5%	—	7.5%	17,500	17,406	17,406	
		Series A Convertible Preferred Stock (12.0%, 10,000 shares)					93	10,214	
		Warrants to purchase Common Stock (expire 5/15) <sup>(1)</sup>					—	3,187	
Velocity Technology Enterprises, Inc. <sup>(2)(6)(13)</sup>	Business Services	Series A Preferred Stock (1,506,602 shares)				1,500	1,883		
<b>Total Affiliate Investments (represents 6.7% of total investments at fair value)</b>							<b>42,497</b>	<b>55,107</b>	

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**MCG Capital Corporation**  
**Consolidated Schedule of Investments**  
**September 30, 2011 (unaudited)**  
**(dollars in thousands)**

Portfolio Company	Industry	Investment	Interest Rate <sup>(9)</sup>			Principal	Cost	Fair Value
			Current	PIK	Total			
<b>Non-Affiliate Investments (less than 5% owned):</b>								
BarBri, Inc.	Publishing	Senior Debt (Due 6/17) <sup>(1)</sup>	6.0%	—	6.0%	\$ 7,000	\$ 6,933	\$ 6,873
Bentley Systems, Incorporated	Information Services	Senior Debt (Due 12/16) <sup>(1)</sup>	5.8%	—	5.8%	9,925	9,831	9,627
Capstone Logistics, LLC <sup>(12)</sup>	Logistics	Senior Debt (Due 9/16) <sup>(1)</sup>	10.5%	—	10.5%	30,000	29,853	29,853
Chase Doors Holdings, Inc.	Manufacturing	Senior Debt (Due 12/15) <sup>(1)</sup>	9.5%	—	9.5%	24,425	24,191	24,191
Coastal Sunbelt Holding, Inc. <sup>(2)</sup>	Food Services	Senior Debt (Due 8/14-12/15) <sup>(1)</sup>	9.1%	—	9.1%	20,261	20,105	20,105
		Subordinated Debt (Due 8/15) <sup>(1)</sup>	16.0%	—	16.0%	9,038	8,964	9,042
Coastal Sunbelt Real Estate, Inc. <sup>(14)</sup>	Real Estate Investments	Subordinated Unsecured Debt (Due 7/12)	15.0%	—	15.0%	2,257	2,254	2,254
		Series A-2 Preferred Stock (12.0%, 20,000 shares)					2,816	4,730
		Warrants to purchase Class B Common Stock					—	—
Construction Trailer Specialists, Inc. <sup>(2)</sup>	Auto Parts	Senior Debt (Due 6/13) <sup>(1)</sup>	8.6%	6.3%	14.9%	8,060	7,914	7,484
Cruz Bay Publishing, Inc.	Publishing	Subordinated Debt (Due 12/13) <sup>(1)(8)</sup>	5.1%	8.0%	13.1%	26,154	22,890	18,983
CWP/RMK Acquisition Corp. <sup>(2)(6)</sup>	Home Furnishings	Senior Debt (Due 12/16) <sup>(7)</sup>	3.0%	—	3.0%	600	569	529
Data Based Systems International, Inc.	Business Services	Subordinated Debt (Due 8/16) <sup>(1)</sup>	10.0%	4.0%	14.0%	9,220	9,042	9,235
Education Management, Inc.	Education	Senior Debt (Due 6/15) <sup>(1)</sup>	9.3%	—	9.3%	25,000	24,759	24,759
Focus Brands Inc.	Restaurants	Senior Debt (Due 11/16) <sup>(1)</sup>	5.3%	—	5.3%	9,993	9,993	9,893
Gans Communications, L.P. <sup>(2)</sup>	Cable	Senior Debt (Due 10/17) <sup>(1)</sup>	5.3%	—	5.3%	5,785	5,768	5,630
G&L Investment Holdings, LLC <sup>(2)</sup>	Insurance	Subordinated Debt (Due 5/14) <sup>(1)</sup>	9.8%	—	9.8%	17,690	17,349	17,349
		Series A Preferred Shares (14.0%, 5,000,000 shares)					8,191	7,288
		Class C Shares (621,907 shares)					529	—
Golden Knight II CLO, Ltd.	Diversified Financial Services	Income Notes (Due 4/19)	8.0%	—	8.0%		3,065	2,154
Goodman Global, Inc.	Manufacturing	Senior Debt (Due 10/16) <sup>(1)</sup>	5.8%	—	5.8%	5,599	5,631	5,556
GSDM Holdings Corp. <sup>(2)</sup>	Healthcare	Senior Debt (Due 1/16) <sup>(1)</sup>	11.5%	6.0%	17.5%	26,373	26,124	26,124
		Series B Preferred Stock (12.5%, 852,950 shares)					5,130	9,914
		Senior Debt (Due 12/15) <sup>(1)</sup>	10.5%	—	10.5%	17,000	16,809	17,022
Haws Corporation	Manufacturing	Senior Debt (Due 9/16) <sup>(1)</sup>	10.0%	—	10.0%	22,747	22,508	22,508
Industrial Safety Technologies, LLC	Manufacturing	Senior Debt (Due 9/16) <sup>(1)</sup>	10.0%	—	10.0%	22,747	22,508	22,508
Jenzabar, Inc.	Technology	Senior Preferred Stock (11.0%, 3,750 shares)					6,741	6,741
		Subordinated Preferred Stock (109,800 shares)					1,098	1,098
		Warrants to purchase Common Stock (expire 4/16) <sup>(10)</sup>					423	28,435
Legacy Cabinets Holdings II, Inc. <sup>(6)</sup>	Home Furnishings	Class B-1 Common Stock (2,000 shares)					2,185	51
Mailsouth, Inc.	Publishing	Senior Debt (Due 12/16) <sup>(1)</sup>	6.8%	—	6.8%	4,975	4,910	4,826
Maverick Healthcare Equity, LLC	Healthcare	Preferred Units (10.0%, 1,250,000 units)					1,701	1,836
		Class A Common Units (1,250,000 units)					—	543
Metropolitan Telecommunications Holding Company <sup>(2)</sup>	Communications	Senior Debt (Due 3/14-12/16) <sup>(1)</sup>	8.0%	—	8.0%	24,770	24,612	24,612
Miles Media Group, LLC <sup>(2)</sup>	Business Services	Senior Debt (Due 6/16) <sup>(1)</sup>	12.5%	—	12.5%	17,738	17,429	17,285
		Warrants to purchase Class A Units (expire 3/21) <sup>(1)</sup>					123	386
MLM Holdings, Inc.	Information Services	Senior Debt (Due 12/16) <sup>(1)</sup>	7.0%	—	7.0%	14,355	14,167	14,104
NDSSI Holdings, LLC <sup>(2)</sup>	Electronics	Senior Debt (Due 12/12) <sup>(1)</sup>	12.8%	1.0%	13.8%	29,789	29,633	28,617
		Series D Preferred Units (30.0%, 2,000,000 units)					2,000	3,774
		Series A Preferred Units (516,691 units)					718	—
		Series B Convertible Preferred Units (165,003 units)					142	—
		Class A Common Units (1,000,000 units)					333	—

*The accompanying notes are an integral part of these Condensed Consolidated Financial Statements*

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### MCG Capital Corporation Consolidated Schedule of Investments September 30, 2011 (unaudited) (dollars in thousands)

Portfolio Company	Industry	Investment	Interest Rate <sup>(9)</sup>			Principal	Cost	Fair Value
			Current	PIK	Total			
Orbitz Worldwide, Inc.	Personal Transportation	Senior Debt (Due 7/14) <sup>(1)</sup>	3.3%	—	3.3%	\$ 3,014	\$ 2,871	\$ 2,592
Ozburn-Hessey Holding Company LLC	Logistics	Senior Debt (Due 4/16) <sup>(1)</sup>	7.5%	—	7.5%	4,937	4,988	4,407
Philadelphia Media Network, Inc. <sup>(6)</sup>	Newspaper	Class A Common Stock (1,000 shares)					5,070	49
Qualawash Holdings, LLC	Repair Services	Subordinated Debt (Due 1/16) <sup>(1)</sup>	12.0%	—	12.0%	20,000	19,829	20,175
Sagamore Hill Broadcasting, LLC <sup>(2)</sup>	Broadcasting	Senior Debt (Due 8/14) <sup>(1)</sup>	12.0%	1.0%	13.0%	13,833	13,730	13,730
Sally Holdings LLC	Cosmetics	Senior Debt (Due 11/13) <sup>(1)</sup>	2.5%	—	2.5%	8,531	8,542	8,408
SC Academy Holdings, Inc.	Education	Subordinated Debt (Due 7/16) <sup>(1)</sup>	12.0%	—	12.0%	13,500	13,392	13,499
Scotsman Industries, Inc.	Manufacturing	Senior Debt (Due 4/16) <sup>(1)</sup>	5.8%	—	5.8%	5,337	5,338	5,231
Service Champ, Inc.	Auto Parts	Subordinated Unsecured Debt ( Due 2/17) <sup>(1)</sup>	12.0%	2.3%	14.3%	12,042	11,934	12,157
ShowPlex Cinemas, Inc.	Entertainment	Senior Debt (Due 5/15) <sup>(1)</sup>	11.0%	—	11.0%	13,624	13,486	13,024
Softlayer Technologies, Inc.	Business Services	Senior Debt (Due 11/16) <sup>(1)</sup>	7.3%	—	7.3%	13,895	13,747	13,704
Summit Business Media Parent Holding Company LLC <sup>(6)(11)</sup>	Information Services	Class E Series I Units (636 units) <sup>(1)</sup>					4,120	205
		Class E Series II Units (276 units) <sup>(1)</sup>					1,788	—
Sunshine Media Group, Inc. <sup>(2)(6)</sup>	Publishing	Warrants to purchase Common Stock (expire 1/21)					—	—
Tank Intermediate Holding Corp.	Manufacturing	Senior Debt (Due 4/16) <sup>(1)</sup>	5.0%	—	5.0%	5,506	5,493	5,451
The e-Media Club I, LLC <sup>(6)</sup>	Investment Fund	LLC Interest (74 units)					88	11
The Gavilon Group, LLC	Agriculture	Senior Debt (Due 12/16) <sup>(1)</sup>	6.0%	—	6.0%	9,625	9,513	9,539
The Matrixx Group, Incorporated	Plastic Products	Subordinated Debt (Due 6/14) <sup>(1)</sup>	10.8%	—	10.8%	12,500	12,500	12,650
Virtual Radiologic Corporation	Healthcare	Senior Debt (Due 12/16) <sup>(1)</sup>	7.8%	—	7.8%	13,925	13,732	13,298
Visant Corporation	Consumer Products	Senior Debt (Due 12/16) <sup>(1)</sup>	5.3%	—	5.3%	5,112	5,128	4,692
VS&A-PBI Holding LLC <sup>(6)</sup>	Publishing	LLC Interest					500	—
West World Media, LLC	Information Services	Senior Debt (Due 9/15) <sup>(1)</sup>	11.0%	3.0%	14.0%	11,259	10,501	10,501
		Class A Membership Units (25,000 units)					1	271
		Warrant to purchase Class A Membership Units (expire 9/15)					324	719
Xpressdocs Holdings, Inc. <sup>(2)</sup>	Business Services	Senior Debt (Due 4/12-4/13) <sup>(1)</sup>	10.9%	0.9%	11.8%	18,934	18,737	18,930
		Series A Preferred Stock (161,870 shares)					500	56
<b>Total Non-Affiliate Investments (represents 73.6% of total investments at fair value)</b>							<b>593,285</b>	<b>606,710</b>
<b>Total Investments</b>							<b>\$1,060,243</b>	<b>\$824,173</b>

*The accompanying notes are an integral part of these Condensed Consolidated Financial Statements*

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### MCG Capital Corporation Consolidated Schedule of Investments December 31, 2010 (dollars in thousands)

Portfolio Company	Industry	Investment	Interest Rate <sup>(9)</sup>			Principal	Cost	Fair Value
			Current	PIK	Total			
<b>Control Investments <sup>(4)</sup>:</b>								
Avenue Broadband LLC <sup>(2)</sup>	Cable	Subordinated Debt (Due 3/14) <sup>(1)</sup>	9.0%	5.0%	14.0%	\$ 15,182	\$ 15,115	\$ 15,115
		Preferred Units (10.8%, 17,100 units) <sup>(1)</sup>					23,151	35,371
		Warrants to purchase Class B Common Stock					—	—
Broadview Networks Holdings, Inc. <sup>(6)</sup>	Communications	Series A Preferred Stock (12.0%, 87,254 shares)					81,984	47,477
		Series A-1 Preferred Stock (12.0%, 100,702 shares)					77,495	54,794
		Series B Preferred Stock (12.0%, 1,282 shares)					100	698
		Class A Common Stock (4,731,031 shares)					—	—
GMC Television Broadcasting, LLC <sup>(2)</sup>	Broadcasting	Senior Debt (Due 12/16) <sup>(1)</sup>	4.3%	—	4.3%	23,720	21,240	21,656
		Subordinated Debt (Due 12/16) <sup>(1)(7)</sup>	14.0%	—	14.0%	10,446	6,975	—
		Subordinated Unsecured Debt (Due 12/16) <sup>(7)</sup>	16.0%	—	16.0%	1,248	1,000	—
		Class B Voting Units (8.0%, 86,700 units)					9,071	—
Intran Media, LLC	Other Media	Senior Debt (Due 12/11) <sup>(1)</sup>	9.5%	—	9.5%	9,200	9,164	7,430
		Series A Preferred Units (10.0%, 86,000 units)					9,095	—
		Series B Preferred Units (10.0%, 30,000 units)					3,000	—
Jet Plastica Investors, LLC <sup>(2)</sup>	Plastic Products	Senior Debt (Due 12/12) <sup>(1)</sup>	13.3%	—	13.3%	14,052	13,990	13,990
		Subordinated Debt A (Due 3/13) <sup>(1)(7)</sup>	3.7%	11.5%	15.2%	22,038	19,365	7,143
		Subordinated Debt B (Due 3/13) <sup>(1)(7)</sup>	17.0%	—	17.0%	27,485	21,560	—
		Preferred LLC Interest (8.0%, 301,595 units)					34,014	—
MTP Holding, LLC <sup>(6)</sup>	Communications	Common LLC Interest (79,171 units)					1	—
NPS Holding Group, LLC <sup>(2)(5)(6)</sup>	Business Services	Senior Debt A1 (Due 6/13) <sup>(1)(7)</sup>	6.0%	—	6.0%	4,702	3,470	3,348
		Senior Debt A2 (Due 6/13) <sup>(1)(7)</sup>	6.0%	—	6.0%	2,070	1,905	—
		Senior Debt A3 (Due 6/13) <sup>(1)(7)</sup>	6.0%	—	6.0%	7,872	6,228	—
		Series A Preferred Units (347 units)					—	—
		Series B Preferred Units (5.0%, 10,731 units)					10,731	—
		Common Units (36,500 units)					—	—
Orbitel Holdings, LLC <sup>(2)</sup>	Cable	Senior Debt (Due 3/12) <sup>(1)</sup>	9.0%	—	9.0%	14,915	14,874	14,874
		Preferred LLC Interest (10.0%, 120,000 units)					14,138	13,515
PremierGarage Holdings, LLC <sup>(2)(6)</sup>	Home Furnishings	Senior Debt (Due 12/10-9/11) <sup>(1)(7)</sup>	8.0%	—	8.0%	10,441	8,998	5,916
		Preferred LLC Units (400 units)					400	—
		Common LLC Units (79,935 units)					4,971	—
RadioPharmacy Investors, LLC <sup>(2)</sup>	Healthcare	Senior Debt (Due 10/11) <sup>(1)</sup>	7.0%	—	7.0%	8,500	8,500	8,500
		Subordinated Debt (Due 12/12) <sup>(1)</sup>	12.0%	3.0%	15.0%	10,372	10,357	10,357
		Preferred LLC Interest (8.0%, 70,000 units)					8,123	7,219
Superior Industries Investors, LLC <sup>(2)</sup>	Sporting Goods	Subordinated Debt (Due 3/13) <sup>(1)</sup>	7.0%	9.0%	16.0%	23,662	23,603	23,603
		Preferred Units (8.0%, 125,400 units)					16,495	19,283
Total Sleep Holdings, Inc. <sup>(2)(6)</sup>	Healthcare	Subordinated Debt (Due 9/11) <sup>(7)</sup>	8.0%	—	8.0%	13,044	11,780	—
		Unsecured Note (Due 6/11) <sup>(7)</sup>	0.0%	—	0.0%		375	—
		Series A Preferred Stock (10.0%, 3,700 shares)					3,793	—
		Series B Preferred Stock (10.0%, 2,752 shares)					21,149	—
		Common Stock (40,469 shares)					1,000	—
<b>Total Control Investments (represents 30.7% of total investments at fair value)</b>							<b>517,167</b>	<b>310,289</b>

*The accompanying notes are an integral part of these Condensed Consolidated Financial Statements*

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**MCG Capital Corporation  
Consolidated Schedule of Investments  
December 31, 2010  
(dollars in thousands)**

Portfolio Company	Industry	Investment	Interest Rate <sup>(9)</sup>			Principal	Cost	Fair Value
			Current	PIK	Total			
<b>Affiliate Investments <sup>(3)</sup> :</b>								
Advanced Sleep Concepts, Inc. <sup>(2)</sup>	Home Furnishings	Senior Debt (Due 10/11) <sup>(1)</sup>	13.6%	—	13.6%	\$ 5,355	\$ 5,322	\$ 5,322
		Subordinated Debt (Due 4/12) <sup>(1)</sup>	12.0%	4.0%	16.0%	5,336	5,285	5,274
		Series A Preferred Stock (20.0%, 49 shares)					297	104
		Common Stock (423 shares)					524	—
		Warrants to purchase Common Stock (expire 10/16)					348	—
Cherry Hill Holdings, Inc.	Entertainment	Series A Preferred Stock (10.0%, 750 shares)					945	1,076
Contract Datascan Holdings, Inc.	Business Services	Subordinated Debt (Due 3/16) <sup>(1)</sup>	12.0%	2.0%	14.0%	7,756	7,074	7,074
		Series A Preferred Stock (1,987 shares) <sup>(1)</sup>					1,983	1,983
		Common Stock (4,135 shares) <sup>(1)</sup>					410	410
Stratford School Holdings, Inc. <sup>(2)</sup>	Education	Senior Debt (Due 12/15) <sup>(1)</sup>	7.5%	—	7.5%	19,000	18,885	18,885
		Series A Convertible Preferred Stock (12.0%, 10,000 shares)					3	8,534
		Warrants to purchase Common Stock (expire 5/15) <sup>(1)</sup>					—	2,910
Sunshine Media Delaware, LLC <sup>(2)(6)</sup>	Publishing	Common Stock (145 shares)					581	116
		Class A LLC Interest (8.0%, 563,808 units)					564	112
		Options to acquire Warrants to purchase Class B LLC Interest (expire 5/14)					—	—
Velocity Technology Enterprises, Inc. <sup>(2)(6)</sup>	Business Services	Series A Preferred Stock (1,506,602 shares)					1,500	1,500
<b>Total Affiliate Investments (represents 5.3% of total investments at fair value)</b>							<u>43,721</u>	<u>53,300</u>

*The accompanying notes are an integral part of these Condensed Consolidated Financial Statements*

**MCG Capital Corporation**  
**Consolidated Schedule of Investments**  
**December 31, 2010**  
**(dollars in thousands)**

Portfolio Company	Industry	Investment	Interest Rate <sup>(9)</sup>			Principal	Cost	Fair Value
			Current	PIK	Total			
<b>Non-Affiliate Investments (less than 5% owned):</b>								
Active Brands International, Inc. <sup>(2)(6)</sup>	Consumer Products	Senior Debt (Due 6/12) <sup>(1)(7)</sup>	10.4%	—	10.4%	\$ 29,263	\$26,328	\$ 1,939
		Subordinated Debt (Due 9/12) <sup>(1)(7)</sup>	—	17.0%	17.0%	18,066	12,053	—
		Class A-1 Common Stock (3,056 shares)					3,056	—
		Warrants to purchase Class A-1 Common Stock (expire 6/17)					331	—
Allen's T.V. Cable Service, Inc.	Cable	Senior Debt (Due 12/12) <sup>(1)</sup>	7.3%	—	7.3%	5,080	5,069	5,069
		Subordinated Debt (Due 12/12) <sup>(1)</sup>	10.0%	—	10.0%	2,415	2,384	2,343
		Warrants to purchase Common Stock (expire 11/15)					—	47
Chase Doors Holdings, Inc.	Manufacturing	Senior Debt (Due 12/15) <sup>(1)</sup>	9.5%	—	9.5%	29,250	28,935	28,935
Coastal Sunbelt Holding, Inc. <sup>(2)</sup>	Food Services	Senior Debt (Due 8/14-2/15) <sup>(1)</sup>	9.1%	—	9.1%	21,411	21,239	21,239
		Subordinated Debt (Due 8/15) <sup>(1)</sup>	12.0%	4.0%	16.0%	8,859	8,795	8,795
Coastal Sunbelt Real Estate, Inc.	Real Estate Investments	Subordinated Unsecured Debt (Due 7/12)	15.0%	—	15.0%	2,257	2,251	2,251
		Series A-2 Preferred Stock (12.0%, 20,000 shares)					2,656	2,318
		Warrants to purchase Class B Common Stock					—	—
Construction Trailer Specialists, Inc. <sup>(2)</sup>	Auto Parts	Senior Debt (Due 06/13) <sup>(1)</sup>	14.9%	—	14.9%	7,690	7,531	6,889
Crux Bay Publishing, Inc.	Publishing	Subordinated Debt (Due 12/13) <sup>(1)(8)</sup>	5.0%	8.0%	13.0%	24,630	22,855	17,365
CWP/RMK Acquisition Corp. <sup>(2)(6)</sup>	Home Furnishings	Senior Debt (Due 12/16) <sup>(7)</sup>	3.0%	—	3.0%	600	583	518
Empower IT Holdings, Inc. <sup>(2)</sup>	Information Services	Senior Debt (Due 5/12) <sup>(1)</sup>	11.0%	—	11.0%	3,387	3,343	3,343
Equibrand Holding Corporation <sup>(16)</sup>	Leisure Activities	Senior Debt (Due 6/11) <sup>(1)</sup>	9.5%	—	9.5%	4,244	4,234	4,234
		Subordinated Debt (Due 12/11) <sup>(1)</sup>	12.0%	5.0%	17.0%	10,142	10,109	10,109
Focus Brands Inc.	Restaurants	Senior Debt (Due 11/16) <sup>(1)</sup>	7.3%	—	7.3%	11,018	11,047	11,150
G&L Investment Holdings, LLC <sup>(2)</sup>	Insurance	Subordinated Debt (Due 5/14) <sup>(1)</sup>	9.8%	—	9.8%	17,500	17,129	17,129
		Series A Preferred Shares (14.0%, 5,000,000 shares)					7,651	7,651
		Class C Shares (621,907 shares)					529	213
Golden Knight II CLO, Ltd. <sup>(6)</sup>	Diversified Financial Services	Income Notes (Due 4/19)	8.0%	—	8.0%		3,038	2,395
Goodman Global, Inc.	Business Services	Senior Debt (Due 10/16) <sup>(1)</sup>	5.8%	—	5.8%	2,993	2,993	3,013
GSDM Holdings, LLC <sup>(2)</sup>	Healthcare	Senior Debt (Due 12/13) <sup>(1)</sup>	12.9%	—	12.9%	26,130	25,980	25,980
		Series B Preferred Units (12.5%, 4,213,333 units)					4,679	5,052
Haws Corporation	Manufacturing	Senior Debt (Due 12/15) <sup>(1)</sup>	10.5%	—	10.5%	22,500	22,230	22,230
Interactive Data Corporation	Diversified Financial Services	Senior Debt (Due 01/17) <sup>(1)</sup>	6.8%	—	6.8%	9,950	10,040	10,094
Jenzabar, Inc.	Technology	Senior Preferred Stock (11.0%, 3,750 shares)					6,431	6,431
		Subordinated Preferred Stock (109,800 shares)					1,098	1,098
		Warrants to purchase Common Stock (expire 4/16) <sup>(10)</sup>					423	27,798
Knology Inc.	Cable	Senior Debt (Due 10/16) <sup>(1)</sup>	5.5%	—	5.5%	6,090	6,098	6,133
Lambeau Telecom Company, LLC <sup>(6)</sup>	Communications	Senior Debt (Due 2/13) <sup>(7)</sup>	12.0%	—	12.0%	1,067	1,002	675
Legacy Cabinets Holdings II, Inc. <sup>(6)</sup>	Home Furnishings	Class B-1 Common Stock (2,000 shares)					2,185	17
LMS INTELLIBOUND, INC. <sup>(2)(12)</sup>	Logistics	Senior Debt (Due 3/14-6/14) <sup>(1)</sup>	8.7%	—	8.7%	16,320	16,114	16,114
		Subordinated Debt (Due 9/14) <sup>(1)</sup>	12.0%	4.0%	16.0%	7,000	6,879	6,879
Mailsouth, Inc.	Publishing	Senior Debt (Due 12/16)	7.0%	—	7.0%	5,000	4,925	4,950
Massage Envy, LLC	Leisure Activities	Senior Debt (Due 12/14) <sup>(1)</sup>	11.0%	—	11.0%	10,222	10,023	10,023
Maverick Healthcare Equity, LLC	Healthcare	Subordinated Debt (Due 4/14) <sup>(1)</sup>	12.5%	3.5%	16.0%	13,357	13,223	13,223
		Preferred Units (10.0%, 1,250,000 units)					1,580	1,710
		Class A Common Units (1,250,000 units)					—	271

*The accompanying notes are an integral part of these Condensed Consolidated Financial Statements*

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### MCG Capital Corporation Consolidated Schedule of Investments December 31, 2010 (dollars in thousands)

Portfolio Company	Industry	Investment	Interest Rate <sup>(9)</sup>			Principal	Cost	Fair Value
			Current	PIK	Total			
Metropolitan Telecommunications Holding Company <sup>(2)</sup>	Communications	Senior Debt (Due 3/14-12/16) <sup>(1)</sup>	8.0%	—	8.0%	\$ 27,770	\$ 27,534	\$ 27,534
Miles Media Group, LLC <sup>(2)</sup>	Business Services	Senior Debt (Due 6/13) <sup>(1)</sup>	12.5%	—	12.5%	16,238	16,049	16,049
MLM Holdings, Inc.	Information Services	Senior Debt (Due 12/16) <sup>(1)</sup>	7.0%	—	7.0%	14,464	14,248	14,301
NDSSI Holdings, LLC <sup>(2)</sup>	Electronics	Senior Debt (Due 9/14) <sup>(1)</sup>	14.8%	—	14.8%	30,132	29,928	29,928
		Series A Preferred Units (516,691 units)					718	125
		Series B Convertible Preferred Units (165,003 units)					142	356
		Class A Common Units (1,000,000 units)					333	—
Orbitz Worldwide, Inc.	Personal Transportation	Senior Debt (Due 07/14) <sup>(1)</sup>	3.3%	—	3.3%	3,140	2,960	2,949
Ozburn-Hessey Holding Company LLC	Logistics	Senior Debt (Due 04/16) <sup>(1)</sup>	7.5%	—	7.5%	4,975	5,034	5,043
Philadelphia Media Network, Inc. <sup>(6)</sup>	Newspaper	Class A Common Stock (1,000 shares)					5,070	48
Provo Craft & Novelty Inc.	Leisure Activities	Senior Debt (Due 3/16) <sup>(1)</sup>	8.0%	—	8.0%	8,077	7,841	7,850
Restaurant Technologies, Inc.	Food Services	Senior Debt (Due 2/12) <sup>(1)</sup>	17.6%	—	17.6%	42,742	42,607	42,607
		Common Stock (47,512 shares)					353	81
		Warrants to purchase Common Stock (expire 6/14)					—	685
Rural/Metro Operating Company, LLC	Healthcare	Senior Debt (Due 11/16) <sup>(1)</sup>	6.0%	—	6.0%	4,000	3,980	4,046
Sagamore Hill Broadcasting, LLC <sup>(2)</sup>	Broadcasting	Senior Debt (Due 8/11) <sup>(1)</sup>	14.0%	—	14.0%	27,169	26,360	26,183
Savvis Communications Corporation	Business Services	Senior Debt (Due 08/16) <sup>(1)</sup>	6.8%	—	6.8%	9,975	10,029	10,148
SC Academy Holdings, Inc.	Education	Subordinated Debt (Due 7/16) <sup>(1)</sup>	12.0%	—	12.0%	13,500	13,375	13,375
Service Champ, Inc.	Auto Parts	Subordinated Unsecured Debt (Due 1/16) <sup>(1)</sup>	14.3%	—	14.3%	10,158	10,070	10,070
ShowPlex Cinemas, Inc.	Entertainment	Senior Debt (Due 5/15) <sup>(1)</sup>	9.0%	—	9.0%	11,025	10,882	10,706
Softlayer Technologies, Inc.	Business Services	Senior Debt (Due 11/16) <sup>(1)</sup>	7.8%	—	7.8%	14,000	13,830	14,003
Summit Business Media Intermediate Holding Company, LLC <sup>(6)(11)</sup>	Information Services	Subordinated Debt (Due 7/14) <sup>(1)(7)</sup>	11.0%	—	11.0%	7,158	5,996	296
Teleguam Holdings, LLC <sup>(2)</sup>	Communications	Subordinated Debt (Due 10/12) <sup>(1)</sup>	7.3%	—	7.3%	20,000	19,921	19,729
The e-Media Club I, LLC <sup>(6)</sup>	Investment Fund	LLC Interest (74 units)					88	10
The Gavilon Group, LLC	Agriculture	Senior Debt (Due 12/16) <sup>(1)</sup>	6.0%	—	6.0%	8,500	8,373	8,418
The Matrixx Group, Incorporated	Plastic Products	Subordinated Debt (Due 6/14) <sup>(1)</sup>	10.8%	—	10.8%	12,500	12,500	12,500
The SI Organization, Inc.	Defense	Senior Debt (Due 11/16) <sup>(1)</sup>	5.8%	—	5.8%	3,000	3,000	3,030
The Telx Group, Inc.	Business Services	Senior Debt (Due 6/15) <sup>(1)</sup>	8.0%	—	8.0%	13,930	13,680	13,860
Visant Corporation	Consumer Products	Senior Debt (Due 12/16) <sup>(1)</sup>	7.0%	—	7.0%	6,983	6,849	7,077
VOX Communications Group Holdings, LLC <sup>(2)(6)</sup>	Broadcasting	Senior Debt (Due 3/09) <sup>(1)(7)</sup>	13.5%	—	13.5%	11,717	10,388	6,157
		Convertible Preferred Subordinated Notes (12.5%, Due 6/15-6/17) <sup>(7)</sup>					2,459	1,414
VS&A-PBI Holding LLC <sup>(6)</sup>	Publishing	LLC Interest					500	—
Wireco Worldgroup Inc.	Industrial Equipment	Senior Debt (Due 2/14) <sup>(1)</sup>	5.3%	—	5.3%	3,850	3,856	3,807
Xpressdocs Holdings, Inc. <sup>(2)</sup>	Business Services	Senior Debt (Due 4/12-4/13) <sup>(1)</sup>	11.6%	—	11.6%	19,533	19,328	19,522
		Series A Preferred Stock (161,870 shares)					500	—
<b>Total Non-Affiliate Investments (represents 64.0% of total investments at fair value)</b>							<b>684,785</b>	<b>646,116</b>
<b>Total Investments</b>							<b>\$1,245,673</b>	<b>\$1,009,705</b>

*The accompanying notes are an integral part of these Condensed Consolidated Financial Statements*

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**MCG Capital Corporation**  
**Consolidated Schedule of Investments**  
**December 31, 2010**  
**(dollars in thousands)**

<u>Counterparty</u>	<u>Instrument</u>	<u>Pay Fixed</u>	<u>Receive Floating</u>	<u>Expiring</u>	<u>Notional</u>	<u>Cost</u>	<u>Fair Value <sup>(a)</sup></u>
	<u>Rate of</u>	<u>Rate of</u>					
<b>Interest Rate Swaps</b>							
SunTrust Bank		13.0%	11.0%	08/11	\$12,500	\$—	\$ (183)
	Interest Rate Swap—Pay Fixed/Receive Floating						
	Interest Rate Swap—Pay Fixed/Receive Floating	9.0%	7.0%	08/11	8,681	—	(127)
<b>Total Interest Rate Swaps</b>					<b>\$21,181</b>	<b>\$—</b>	<b>\$ (310)</b>

(a) We include the fair value of these interest rate swaps in other liabilities on our *Consolidated Balance Sheets* .

- (1) Some or all of this security is held by our SBIC subsidiary or one of our other financing subsidiaries and may have been pledged as collateral in connection therewith. See *Note 5—Borrowings* to the Condensed Consolidated Financial Statements.
- (2) Includes securities issued by one or more of the portfolio company’s affiliates.
- (3) Affiliate investments represent companies in which we own at least 5%, but not more than 25% of the portfolio company’s voting securities.
- (4) Control investments represent companies in which we own more than 25% of the portfolio company’s voting securities.
- (5) Represents a non-majority-owned control portfolio company of which we own at least 25%, but not more than 50% of the portfolio company’s voting securities.
- (6) Portfolio company is non-income producing at period-end.
- (7) Loan or debt security is on non-accrual status.
- (8) We did not recognize paid-in-kind, or PIK, interest or accretion income because the fair value of our investment was below its cost basis. However, we continue to accrue interest that is receivable in cash from the portfolio company.
- (9) Interest rates represent the weighted-average annual stated interest rate on debt securities, presented by nature of indebtedness for a single issuer. PIK interest represents contractually deferred interest that is added to the principal balance of the debt security and compounded if not paid on a current basis. PIK may be prepaid by either contract or the portfolio company’s choice, but generally is paid at the end of the loan term. The maturity dates represent the earliest and the latest maturity dates. Rates on preferred stock and preferred LLC interests, where applicable, represent the contractual rate.
- (10) On February 24, 2010, we exercised warrants to purchase 100,000 shares of common stock of Jenzabar, Inc. and we submitted the requisite payments for this stock. Our receipt of the common stock certificates from Jenzabar is pending.
- (11) On January 25, 2011, Summit Business Media Intermediate Holding Company, LLC filed for Chapter 11 bankruptcy protection.
- (12) In September 2011, LMS Intellibound, Inc. (a non-affiliate portfolio Company) and Progressive Logistics Systems (an unaffiliated company) entered into a combination where they are now subsidiaries of Capstone Logistics, LLC.
- (13) In October 2011, we sold our Series A Preferred Stock investment in Velocity Technology Enterprises, Inc. for \$1.9 million.
- (14) In October 2011, Costal Sunbelt Real Estate, Inc. re-paid our subordinated unsecured debt investment in full and made a distribution in the amount of \$2.6 million in respect of our series A-2 preferred stock investment in connection with the sale of the real estate previously owned by its subsidiary, Coastal Sunbelt Real Estate, L.L.C.

*The accompanying notes are an integral part of these Condensed Consolidated Financial Statements*

MCG Capital Corporation

Notes to the Condensed Consolidated Financial Statements (Unaudited)

NOTE 1—DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

These *Condensed Consolidated Financial Statements* present the results of operations, financial position and cash flows of MCG Capital Corporation and its consolidated subsidiaries. The terms “we,” “our,” “us” and “MCG” refer to MCG Capital Corporation and its consolidated subsidiaries.

We are a solutions-focused commercial finance company that provides capital and advisory services to middle-market companies throughout the United States. We are an internally managed, non-diversified, closed-end investment company that elected to be regulated as a business development company, or BDC, under the *Investment Company Act of 1940*, as amended, or the 1940 Act. Our organization includes the following categories of subsidiaries:

*Wholly Owned Special-Purpose Financing Subsidiaries*—These subsidiaries are bankruptcy remote, special-purpose entities to which we transfer certain loans. Each financing subsidiary, in turn, transfers the loans to a Delaware statutory trust. For accounting purposes, the transfers of the loans to the Delaware statutory trusts are structured as on-balance sheet securitizations.

*Small Business Investment Subsidiaries*—We own Solutions Capital I, L.P., a wholly owned subsidiary licensed by the United States Small Business Administration, or SBA, which operates as a small business investment company, or SBIC, under the *Small Business Investment Act of 1958*, as amended, or SBIC Act. In March 2011, we formed another wholly owned subsidiary, Solutions Capital II, L.P., and in May 2011, we submitted a license to the SBA to obtain an SBIC license for Solutions Capital II, L.P. On September 30, 2011, after discussions with the SBA, we elected to withdraw our application for a second license. MCG is also the sole member of Solutions Capital G.P., LLC, which acts as the general partner of Solutions Capital I, L.P.

*Taxable Subsidiaries*—We currently qualify as a regulated investment company, or RIC, for federal income tax purposes and, therefore, are not required to pay corporate income taxes on any income or gains that we distribute to our stockholders. We have certain wholly owned taxable subsidiaries, or Taxable Subsidiaries, each of which holds one or more portfolio investments listed on our *Consolidated Schedules of Investments*. The purpose of these Taxable Subsidiaries is to permit us to hold portfolio companies organized as limited liability companies, or LLCs, (or other forms of pass-through entities) and still satisfy the RIC tax requirement that at least 90% of our gross revenue for income tax purposes must consist of investment income. Absent the Taxable Subsidiaries, a portion of the gross income of any LLC (or other pass-through entity) portfolio investment would flow through directly to us, and be included in the calculation of the 90% test. To the extent that such income did not consist of investment income, it could jeopardize our ability to qualify as a RIC and, therefore, cause us to incur significant federal income taxes. The income of the LLCs (or other pass-through entities) owned by Taxable Subsidiaries is taxed to the Taxable Subsidiaries and does not flow through to us, thereby helping us preserve our RIC status and resultant tax advantages. We do not consolidate the Taxable Subsidiaries for income tax purposes and they may generate income tax expense because of the Taxable Subsidiaries’ ownership of the portfolio companies. We reflect any such income tax expense on our *Consolidated Statements of Operations*.

The accompanying financial statements reflect the consolidated accounts of MCG and the following subsidiaries: Solutions Capital I, L.P.; Solutions Capital II, L.P.; Solutions Capital G.P., LLC; and MCG’s special-purpose financing subsidiaries: MCG Finance V, LLC and MCG Finance VII, LLC.

BASIS OF PRESENTATION AND USE OF ESTIMATES

These unaudited financial statements and the accompanying notes are prepared in accordance with accounting principles generally accepted in the United States of America and conform to Regulation S-X under the *Securities Exchange Act of 1934*, as amended. We believe we have made all necessary adjustments so that the financial statements are presented fairly and that all such adjustments are of a normal recurring nature. We eliminated all significant intercompany balances. In accordance with Article 6 of Regulation S-X of the *Securities Act of 1933*, as amended, and the *Securities Exchange Act of 1934*, as amended, we do not consolidate portfolio company investments, including those in which we have a controlling interest. Further, in connection with the preparation of these *Condensed Consolidated Financial Statements*, we have evaluated subsequent events that occurred after the balance sheet date as of September 30, 2011 through the date these financial statements were issued.

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Preparing financial statements requires us to make estimates and assumptions that affect the amounts reported on our *Condensed Consolidated Financial Statements* and accompanying notes. Although we believe the estimates and assumptions used in preparing these *Condensed Consolidated Financial Statements* and related notes are reasonable, actual results could differ materially.

Interim results are not necessarily indicative of results for a full year. You should read these *Condensed Consolidated Financial Statements* in conjunction with the *Consolidated Financial Statements* included in our *Annual Report on Form 10-K* for the year ended December 31, 2010.

### RECENT ACCOUNTING PRONOUNCEMENTS

In April 2011, Financial Accounting Standards Board, or FASB, issued *Accounting Standards Update 2011-02—A Creditor’s Determination of Whether a Restructuring is a Troubled Debt Restructuring*, or ASU 2011-02. This standard amends previous guidance provided in *Accounting Standards Codification 310-40—Receivables—Troubled Debt Restructurings by Creditors*. ASU 2011-02 provides additional guidance and criteria on how companies should determine whether a restructuring or refinancing of an existing financial receivable represents a troubled debt restructuring. Companies must assess whether the restructuring or refinancing of an existing financial receivable is a troubled debt restructuring in order to determine how to account for the remaining unamortized portion of certain fees, such as origination fees, associated with the original debt investment. ASU 2011-02 is effective for the first interim period beginning on or after June 15, 2011. We adopted this standard beginning with the quarter ended September 30, 2011. Our adoption of this update did not have a material impact on our financial position or results of operations.

In May 2011, the FASB issued *Accounting Standards Update No. 2011-04—Fair Value Measurement: Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*, or ASU 2011-04. ASU 2011-04 clarifies the application of existing fair value measurement and disclosure requirements, changes the application of some requirements for measuring fair value and requires additional disclosure for fair value measurements. The disclosure requirements are expanded to include for fair value measurements categorized in Level 3 of the fair value hierarchy: 1) a quantitative disclosure of the unobservable inputs and assumptions used in the measurement; 2) a description of the valuation processes in place; and 3) a narrative description of the sensitivity of the fair value to changes in unobservable inputs and interrelationships between those inputs. ASU 2011-04 is effective for interim and annual periods beginning after December 15, 2011, for public entities. We will adopt this standard beginning on January 1, 2012. We are evaluating the impact, if any, that our adoption of this update may have on our financial position or results of operations. However, since this accounting standards update primarily requires expanded disclosure related to Category 3 financial assets and liabilities, we do not anticipate that the implementation of this standard will have a significant impact on our process for measuring fair values, our financial position or results of operations.

### NOTE 2—INVESTMENT PORTFOLIO

The following table summarizes the composition of our investment portfolio *at cost* :

<i>(dollars in thousands)</i>	September 30, 2011		December 31, 2010	
	Investments at Cost	Percent of Total Portfolio	Investments at Cost	Percent of Total Portfolio
<b>Debt investments</b>				
Senior secured debt	\$ 588,951	55.5%	\$ 597,046	47.9%
Subordinated debt				
Secured	134,131	12.7	266,333	21.4
Unsecured	14,188	1.3	15,067	1.2
<b>Total debt investments</b>	<b>737,270</b>	<b>69.5</b>	<b>878,446</b>	<b>70.5</b>
<b>Equity investments</b>				
Preferred equity	301,174	28.4	345,960	27.8
Common/common equivalents equity	21,799	2.1	21,267	1.7
<b>Total equity investments</b>	<b>322,973</b>	<b>30.5</b>	<b>367,227</b>	<b>29.5</b>
<b>Total investments</b>	<b>\$1,060,243</b>	<b>100.0%</b>	<b>\$1,245,673</b>	<b>100.0%</b>

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The following table summarizes the composition of our investment portfolio *at fair value* :

<i>(dollars in thousands)</i>	September 30, 2011		December 31, 2010	
	Investments at Fair Value	Percent of Total Portfolio	Investments at Fair Value	Percent of Total Portfolio
<b>Debt investments</b>				
Senior secured debt	\$ 535,247	64.9%	\$ 555,667	55.0%
Subordinated debt				
Secured	124,203	15.1	190,309	18.9
Unsecured	14,411	1.8	12,321	1.2
<b>Total debt investments</b>	<b>673,861</b>	<b>81.8</b>	<b>758,297</b>	<b>75.1</b>
<b>Equity investments</b>				
Preferred equity	116,310	14.1	218,690	21.7
Common/common equivalents equity	34,002	4.1	32,718	3.2
<b>Total equity investments</b>	<b>150,312</b>	<b>18.2</b>	<b>251,408</b>	<b>24.9</b>
<b>Total investments</b>	<b>\$ 824,173</b>	<b>100.0%</b>	<b>\$ 1,009,705</b>	<b>100.0%</b>

Our debt instruments bear contractual interest rates ranging from 2.5% to 17.5%, a portion of which may be in the form of paid in kind interest. As of September 30, 2011, approximately 88.6% of the fair value of our loan portfolio had variable interest rates, based on a LIBOR benchmark or prime rate, and 11.4% of the fair value of our loan portfolio had fixed interest rates. As of September 30, 2011, approximately 76.8% of our loan portfolio, at fair value, had LIBOR floors between 1.0% and 3.0% on the LIBOR base index and prime floors between 1.75% and 6.0%. At origination, our loans generally have four- to eight-year stated maturities. Borrowers typically pay an origination fee based on a percent of the total commitment and a fee on undrawn commitments.

When one of our loans becomes more than 90 days past due, or if we otherwise do not expect the customer to be able to service its debt and other obligations, we will, as a general matter, place the loan on non-accrual status and generally will cease recognizing interest income on that loan until all principal and interest has been brought current through payment or due to a restructuring such that the interest income is deemed to be collectible. However, we may make exceptions to this policy if the loan has sufficient collateral value and is in the process of collection. If the fair value of a loan is below cost, we may cease recognizing paid-in-kind, or PIK, interest and/or the accretion of a discount on the debt investment until such time that the fair value equals or exceeds cost.

The following table summarizes the *cost* of loans more than 90 days past due and loans on non-accrual status:

<i>(dollars in thousands)</i>	September 30, 2011		December 31, 2010	
	Investments at Cost	% of Loan Portfolio	Investments at Cost	% of Loan Portfolio
<b>Loans greater than 90 days past due</b>				
On non-accrual status	\$ 23,461	3.18%	\$ 10,388	1.18%
Not on non-accrual status	—	—	—	—
<b>Total loans greater than 90 days past due</b>	<b>\$ 23,461</b>	<b>3.18%</b>	<b>\$ 10,388</b>	<b>1.18%</b>
<b>Loans on non-accrual status</b>				
0 to 90 days past due	\$ 63,910	8.67%	\$ 128,989	14.69%
Greater than 90 days past due	23,461	3.18	10,388	1.18
<b>Total loans on non-accrual status</b>	<b>\$ 87,371</b>	<b>11.85%</b>	<b>\$ 139,377</b>	<b>15.87%</b>

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The following table summarizes the *fair value* of loans more than 90 days past due and loans on non-accrual status:

<i>(dollars in thousands)</i>	September 30, 2011		December 31, 2010	
	Investments at Fair Value	% of Loan Portfolio	Investments at Fair Value	% of Loan Portfolio
<b>Loans greater than 90 days past due</b>				
On non-accrual status	\$ 10,714	1.59%	\$ 6,157	0.81%
Not on non-accrual status	—	—	—	—
<b>Total loans greater than 90 days past due</b>	<b>\$ 10,714</b>	<b>1.59%</b>	<b>\$ 6,157</b>	<b>0.81%</b>
<b>Loans on non-accrual status</b>				
0 to 90 days past due	\$ 19,230	2.85%	\$ 19,835	2.62%
Greater than 90 days past due	10,714	1.59	6,157	0.81
<b>Total loans on non-accrual status</b>	<b>\$ 29,944</b>	<b>4.44%</b>	<b>\$ 25,992</b>	<b>3.43%</b>

The following table summarizes the changes in the cost and fair value of the loans on non-accrual status from December 31, 2010 through September 30, 2011:

<i>(In thousands)</i>	Nine months ended September 30, 2011	
	Cost	Fair Value
<b>Non-accrual loan balance as of December 31, 2010</b>	<b>\$ 139,377</b>	<b>\$ 25,992</b>
Additional loans on non-accrual status—other media	9,247	4,235
Advances to companies on non-accrual status	9,543	9,543
Loans converted to equity	(5,904)	(5,904)
Payments received on loans on non-accrual status	(7,458)	(7,458)
Change in valuation of loans on non-accrual status	—	(256)
Reversal of previously recognized unrealized loss on non-accrual loans	—	61,226
Realized loss on non-accrual loans	(57,434) <sup>(a)</sup>	(57,434) <sup>(a)</sup>
<b>Total change in non-accrual loans</b>	<b>(52,006)</b>	<b>3,952</b>
<b>Non-accrual loan balance as of September 30, 2011</b>	<b>\$ 87,371</b>	<b>\$ 29,944</b>

<sup>(a)</sup> Primarily reflects our sales of Active Brands International, Inc. and Vox Communications Group Holdings, LLC, as well as the write-off of our investment in Total Sleep Holdings, Inc. during the nine months ended September 30, 2011. Our investments in the debt issued by these portfolio companies were on non-accrual status as of December 31, 2010. Upon the sales and write-off of these investments, we reversed the previously unrealized depreciation and recorded realized losses.

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The following table summarizes our investment portfolio by industry at cost:

<i>(dollars in thousands)</i>	September 30, 2011		December 31, 2010	
	Investments at Cost	Percent of Total Portfolio	Investments at Cost	Percent of Total Portfolio
Healthcare	\$ 74,550	7.0%	\$ 114,476	9.2%
Business services	95,931	9.0	106,717	8.6
Manufacturing	79,970	7.5	54,158	4.3
Education	55,650	5.2	32,263	2.6
Communications	184,192	17.4	208,037	16.7
Plastic products	118,441	11.2	101,429	8.1
Cable	41,751	3.9	80,829	6.5
Technology	8,262	0.8	7,952	0.6
Information services	40,732	3.8	23,587	1.9
Logistics	34,841	3.3	28,027	2.3
Electronics	32,826	3.1	31,121	2.5
Broadcasting	46,421	4.4	76,448	6.1
Publishing	35,233	3.3	29,425	2.4
Food services	29,069	2.7	72,994	5.9
Insurance	26,069	2.5	25,309	2.0
Repair services	19,829	1.9	—	—
Auto parts	19,848	1.9	17,601	1.4
Entertainment	14,255	1.4	11,827	0.9
Home furnishings	30,243	2.9	28,913	2.3
Restaurants	9,993	0.9	11,047	0.9
Agriculture	9,513	0.9	8,373	0.7
Cosmetics	8,542	0.8	—	—
Consumer products	5,128	0.5	48,617	3.9
Other media	22,790	2.2	21,259	1.7
Diversified financial services	3,065	0.3	13,078	1.1
Leisure activities	—	—	32,207	2.6
Sporting goods	—	—	40,098	3.2
Other <sup>(a)</sup>	13,099	1.2	19,881	1.6
<b>Total</b>	<b>\$1,060,243</b>	<b>100.0%</b>	<b>\$1,245,673</b>	<b>100.0%</b>

<sup>(a)</sup> No individual industry within this category exceeds 1%.

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The following table summarizes our investment portfolio by industry at *fair value* :

<i>(dollars in thousands)</i>	September 30, 2011		December 31, 2010	
	Investments at Fair Value	Percent of Total Portfolio	Investments at Fair Value	Percent of Total Portfolio
Healthcare	\$ 86,703	10.5%	\$ 76,358	7.6%
Business services	81,021	9.8	87,897	8.7
Manufacturing	79,959	9.7	54,178	5.4
Education	69,065	8.4	43,704	4.3
Communications	53,767	6.5	150,907	14.9
Plastic products	43,884	5.3	33,633	3.3
Cable	41,630	5.1	92,467	9.2
Technology	36,274	4.4	35,327	3.5
Information services	35,427	4.3	17,940	1.8
Logistics	34,260	4.2	28,036	2.8
Electronics	32,391	3.9	30,409	3.0
Broadcasting	31,521	3.8	53,996	5.3
Publishing	30,682	3.7	22,543	2.2
Food services	29,147	3.5	73,407	7.3
Insurance	24,637	3.0	24,993	2.5
Repair services	20,175	2.4	—	—
Auto parts	19,641	2.4	16,959	1.7
Entertainment	13,793	1.7	11,782	1.2
Home furnishings	13,400	1.6	17,151	1.7
Restaurants	9,893	1.2	11,150	1.1
Agriculture	9,539	1.2	8,418	0.8
Cosmetics	8,408	1.0	—	—
Consumer products	4,692	0.6	9,016	0.9
Other media	2,474	0.3	7,430	0.7
Diversified financial services	2,154	0.3	12,489	1.2
Leisure activities	—	—	32,216	3.2
Sporting goods	—	—	42,886	4.2
Other <sup>(a)</sup>	9,636	1.2	14,413	1.5
<b>Total</b>	<b>\$ 824,173</b>	<b>100.0%</b>	<b>\$ 1,009,705</b>	<b>100.0%</b>

<sup>(a)</sup> No individual industry within this category exceeds 1%.

We manage our interest rate exposure and financing facility requirements on an ongoing basis by comparing our interest rate sensitive assets to our interest rate sensitive liabilities, and from time to time, may enter into interest rate swaps. We include the fair value of these interest rate swaps in other liabilities on our Consolidated Balance Sheets. We do not designate any of our interest rate swaps as hedges for accounting purposes. Each quarter, we settle these interest rate swaps for cash. During each of the nine months ended September 30, 2011 and 2010, we reported changes in the fair value of these interest rate swaps in net unrealized appreciation (depreciation) on investments on our *Consolidated Statements of Operations*.

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Our remaining interest rate swaps expired in August 2011; therefore, as of September 30, 2011, we had no unexpired interest rate swaps. As of December 31, 2010, the notional amount of our interest rate swaps was \$21.2 million, and the fair value of these interest rate swaps included in our liabilities was \$0.3 million. The following table summarizes our interest rate swaps with SunTrust Bank, as the counterparty for which we paid fixed interest rates and received floating interest rates as of December 31, 2010:

<i>(dollars in thousands)</i>				As of December 31, 2010		
Date		Pay Fixed Interest Rate	Receive Floating	Notional	Cost	Fair Value
Entered	Expired		Interest Rate			
03/09	08/11	13.0%	11.0%	\$12,500	\$—	\$(183)
03/09	08/11	9.0%	7.0%	8,681	—	(127)
<b>Total</b>				<b><u>\$21,181</u></b>	<b><u>\$—</u></b>	<b><u>\$(310)</u></b>

The following table summarizes the realized and unrealized gains and losses that we recorded on our interest rate swaps for the nine months ended September 30, 2011 and 2010:

<i>(in thousands)</i>	Realized Loss	Unrealized Appreciation (Depreciation)	Reversal of Unrealized Depreciation	Net Gain (Loss)
<b>Nine months ended September 30:</b>				
2011	\$ (229)	\$ 81	\$ 229	\$ 81
2010	(906)	(359)	906	(359)

### NOTE 3—FAIR VALUE MEASUREMENT

We account for our investments in portfolio companies under Accounting Standard Codification Topic 820—*Fair Value Measurements and Disclosures*, or ASC 820. ASC 820 defines fair value, establishes a framework for measuring fair value and expands disclosures about assets and liabilities measured at fair value. ASC 820 defines “fair value” as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This fair value definition focuses on exit price in the principal, or most advantageous, market and prioritizes, within a measurement of fair value, the use of market-based inputs over entity-specific inputs.

#### Fair Value Hierarchy

ASC 820 establishes the following three-level hierarchy, based upon the transparency of inputs to the fair value measurement of an asset or liability as of the measurement date:

ASC 820 Fair Value Hierarchy	<i>Inputs to Fair Value Methodology</i>
<b>Level 1</b>	Quoted prices in active markets for identical assets or liabilities
<b>Level 2</b>	Quoted prices for similar assets or liabilities; quoted markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the financial instrument; inputs other than quoted prices that are observable for the asset or liability; or inputs that are derived principally from, or corroborated by, observable market information
<b>Level 3</b>	Pricing models, discounted cash flow methodologies or similar techniques and at least one significant model assumption is unobservable or when the estimation of fair value requires significant management judgment

We categorize a financial instrument in the fair value hierarchy based on the lowest level of input that is significant to its fair value measurement. In the event that transfers between these levels were to occur in the future, we would recognize those transfers as of the ending balance sheet date, based on changes in the use of observable and unobservable inputs utilized to perform the valuation for the period.

Our investment portfolio is not composed of homogeneous debt and equity securities that can be valued with a small number of inputs. Instead, the majority of our investment portfolio is composed of complex debt and equity securities with unique contract terms and conditions. As such, our valuation of each investment in our portfolio is unique and complex, often factoring in numerous unique inputs, including the historical and forecasted financial and operational performance of the portfolio company, projected cash flows, market multiples, comparable market transactions, the priority of our securities compared with those of other investors, credit risk, interest rates, independent valuations and reviews and other inputs too numerous to list quantitatively herein.

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### Assets and Liabilities Measured at Fair Value on a Recurring Basis

The following table presents the assets and liabilities that we report at fair value on our *Consolidated Balance Sheets* by ASC 820 hierarchy:

	As of September 30, 2011		
	Internal Models with Significant		Total Fair Value
	Observable Market Parameters	Unobservable Market Parameters	
(in thousands)	(Level 2)	(Level 3)	Reported in Consolidated Balance Sheet
<b>A SSETS</b>			
<b>Non-affiliate investments</b>			
Senior secured debt	\$ 123,831	\$ 299,274	\$ 423,105
Subordinated secured debt	—	100,933	100,933
Unsecured subordinated debt	—	14,411	14,411
Preferred equity	2,154	35,437	37,591
Common/common equivalents	—	30,670	30,670
<b>Total non-affiliate investments</b>	<b>125,985</b>	<b>480,725</b>	<b>606,710</b>
<b>Affiliate investments</b>			
Senior secured debt	—	23,256	23,256
Subordinated secured debt	—	12,905	12,905
Preferred equity	—	15,614	15,614
Common/common equivalents	—	3,332	3,332
<b>Total affiliate investments</b>	<b>—</b>	<b>55,107</b>	<b>55,107</b>
<b>Control investments</b>			
Senior secured debt	—	88,886	88,886
Subordinated secured debt	—	10,365	10,365
Preferred equity	—	63,105	63,105
<b>Total control investments</b>	<b>—</b>	<b>162,356</b>	<b>162,356</b>
<b>Total assets at fair value</b>	<b>\$ 125,985</b>	<b>\$ 698,188</b>	<b>\$ 824,173</b>

As of September 30, 2011, we had no investments that had quoted market prices in active markets, which we would categorize as Level 1 investments under ASC 820.

### Valuation Methodologies

As required by the 1940 Act, we classify our investments by level of control. Control investments include both majority-owned control investments and non-majority owned control investments. A majority-owned control investment represents a security in which we own more than 50% of the voting interest of the portfolio company and generally control its board of directors. A non-majority owned control investment represents a security in which we own 25% to 50% of the portfolio company's equity. Non-control investments represent both affiliate and non-affiliate securities for which we do not have a controlling interest. Affiliate investments represent securities in which we own 5% to 25% of the portfolio company's equity. Non-affiliate investments represent securities in which we own less than 5% of the portfolio company's equity.

- **Majority-Owned Control Investments**—Majority-owned control investments comprise 18.5% of our investment portfolio as of September 30, 2011. Market quotations are not readily available for these investments; therefore, we use a combination of market and income approaches to determine their fair value. Typically, private companies are bought and sold based on multiples of EBITDA, cash flows, net income, revenues or, in limited cases, book value. Generally, we apply multiples that we observe for other comparable companies to relevant financial data for the portfolio company. Also, in a limited number of cases, we use income approaches to determine the fair value of these securities, based on our projections of the discounted future free cash flows that the portfolio company will likely generate, as well as industry derived capital costs. Our valuation approaches for majority-owned investments estimate the value were we to sell or exit the investment. These valuation approaches assume the highest and best use of the investment by market participants and consider the value of our ability to control the portfolio company's capital structure and the timing of a potential exit.
- **Non-Majority-Owned Control Investments**— Non-majority-owned control investments comprise 1.2% of our investment portfolio as of September 30, 2011. For our non-majority-owned control equity investments, we use the same market and income valuation approaches used to value our majority-owned control investments. For non-majority owned control debt investments, we estimate fair value using the market-yield approach based on the expected future cash flows discounted at the loans' effective interest rates, based on our estimate of current market rates. We may adjust discounted cash flow calculations to reflect other market conditions or the perceived credit risk of the borrower.

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- *Non-Control Investments*—Non-control investments comprise 80.3% of our investment portfolio as of September 30, 2011. Quoted prices are not available for 81.0% of our non-control investments as of September 30, 2011. For our non-control equity investments, we use the same market and income approaches used to value our control investments. For non-control debt investments, we estimate fair value using a market-yield approach based on the expected future cash flows discounted at the loans' effective interest rates, based on our estimate of current market rates. We may adjust discounted cash flow calculations to reflect other market conditions or the perceived credit risk of the borrower.
- *Thinly Traded and Over-the-Counter Securities*—Generally, we value securities that are traded in the over-the-counter market or on a stock exchange at the average of the prevailing bid and ask prices on the date of the relevant period end. However, we may apply a discount to the market value of restricted or thinly traded public securities to reflect the impact that these restrictions have on the value of these securities. We review factors including the trading volume, total securities outstanding and our percentage ownership of securities to determine whether the trading levels are active (Level 1) or inactive (Level 2). As of September 30, 2011, these securities represented 15.3% of our investment portfolio.

Our valuation analyses incorporate the impact that key events could have on the securities' values, including public and private mergers and acquisitions, purchase transactions, public offerings, letters of intent and subsequent debt or equity sales. Our valuation analyses also include key external data, such as market changes and industry valuation benchmarks. We also use independent valuation firms to provide additional data points for our quarterly valuation analyses. Our general practice is to obtain an independent valuation or review of valuation at least once per year for each portfolio investment that had a fair value in excess of \$5.0 million, unless the fair value has otherwise been derived through a sale of some or all of our investment in the portfolio company or is a new investment made within the last twelve months. As set forth in more detail in the following table, in total, either we obtained a valuation or review from an independent firm, considered new investments made or used market quotes in the preceding twelve month period for 99.2% of the fair value of our investment portfolio as of September 30, 2011.

	September 30, 2011					
	Investments at Fair Value			Percent of		
	Debt	Equity	Total	Debt Portfolio	Equity Portfolio	Total Portfolio
<i>(dollars in thousands)</i>						
<b>Independent valuations/reviews, recent transactions or market quotes</b>						
<b>Independent valuation/review prepared</b>						
Third quarter 2011	\$152,917	\$ 39,336	\$192,253	22.7%	26.2%	23.3%
Second quarter 2011	56,809	16,833	73,642	8.4	11.2	8.9
First quarter 2011	104,997	3,830	108,827	15.6	2.5	13.2
Fourth quarter 2010	116,748	69,061	185,809	17.3	45.9	22.5
<b>Total independent valuations/reviews</b>	<b>431,471</b>	<b>129,060</b>	<b>560,531</b>	<b>64.0</b>	<b>85.8</b>	<b>67.9</b>
<b>Fair value from</b>						
Market quotes (Level 2)	116,958	2,154	119,112	17.4	1.4	14.5
Pending sales of investments or letters of intent	28,378	14,644	43,022	4.2	9.8	5.2
<b>Fair value from market quotes and pending sales</b>	<b>145,336</b>	<b>16,798</b>	<b>162,134</b>	<b>21.6</b>	<b>11.2</b>	<b>19.7</b>
<b>New investments made during the 12 months ended September 30, 2011</b>						
	<b>94,051</b>	<b>1,195</b>	<b>95,246</b>	<b>14.0</b>	<b>0.8</b>	<b>11.6</b>
<b>Total portfolio evaluated</b>	<b>670,858</b>	<b>147,053</b>	<b>817,911</b>	<b>99.6</b>	<b>97.8</b>	<b>99.2</b>
<b>Not evaluated during the 12 months ended September 30, 2011</b>	<b>3,003</b>	<b>3,259</b>	<b>6,262</b>	<b>0.4</b>	<b>2.2</b>	<b>0.8</b>
<b>Total investment portfolio</b>	<b>\$673,861</b>	<b>\$150,312</b>	<b>\$824,173</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

The majority of the valuations performed by the independent valuation firms utilize proprietary models and inputs. We have used, and intend to continue to use, independent valuation firms to provide additional support for our internal analyses. Our board of directors considers our valuations, as well as the independent valuations and reviews, in its determination of the fair value of our investments. The fair value of our interest rate swaps was based on a binding broker quote, which was based on the estimated net present value of the future cash flows using a forward interest rate yield-curve in effect as of the measurement period.

Due to the uncertainty inherent in the valuation process, such estimates of fair value may differ significantly from the values that would have been used had a ready market for the securities existed, and such differences could be material. In addition, changes in the market environment and other events that may occur over the life of the investments may cause the gains or losses ultimately realized on these investments to differ from the valuations currently assigned.

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### Changes in Level 3 Fair Value Measurements

We classify securities in the Level 3 valuation hierarchy based on the significance of the unobservable factors to the overall fair value measurement. Our fair value approach for Level 3 securities primarily uses unobservable inputs, but may also include observable, actively quoted components derived from external sources. Accordingly, the gains and losses in the table below include fair value changes due, in part, to observable factors. Additionally, we transfer investments in and out of Level 1, 2 and 3 securities as of the ending balance sheet date, based on changes in the use of observable and unobservable inputs utilized to perform the valuation for the period. During each of the three months ended September 30, 2011 and 2010, there were no transfers in or out of Level 1, 2 or 3.

The following table provides a reconciliation of fair value changes during the three-month period ended September 30, 2011 for all investments for which we determine fair value using unobservable (Level 3) factors.

<i>(in thousands)</i>	Fair value measurements using unobservable inputs (Level 3)			
	Non-affiliate Investments	Affiliate Investments	Control Investments	Total
<b>Fair value June 30, 2011</b>				
Senior secured debt	\$ 270,181	\$ 24,483	\$ 93,702	\$ 388,366
Subordinated secured debt	109,638	12,829	10,363	132,830
Unsecured subordinated debt	14,353	—	—	14,353
Preferred equity	30,610	13,466	86,724	130,800
Common/common equivalents equity	29,916	3,332	—	33,248
<b>Total fair value June 30, 2011</b>	<b>454,698</b>	<b>54,110</b>	<b>190,789</b>	<b>699,597</b>
<b>Realized/unrealized gain (loss)</b>				
Senior secured debt	(1,072)	—	(6,417)	(7,489)
Subordinated secured debt	189	(85)	59	163
Unsecured subordinated debt	(17)	—	(87)	(104)
Preferred equity	2,659	2,028	(24,024)	(19,337)
Common/common equivalents equity	494	—	—	494
<b>Total realized/unrealized gain (loss)</b>	<b>2,253</b>	<b>1,943</b>	<b>(30,469)</b>	<b>(26,273)</b>
<b>Purchases</b>				
Preferred equity	2,000	—	—	2,000
<b>Total purchases</b>	<b>2,000</b>	<b>—</b>	<b>—</b>	<b>2,000</b>
<b>Issuances</b>				
Senior secured debt	53,768	510	1,971	56,249
Subordinated secured debt	659	161	82	902
Unsecured subordinated debt	75	—	—	75
Preferred equity	380	120	408	908
Common/common equivalents equity	325	—	—	325
<b>Total issuances</b>	<b>55,207</b>	<b>791</b>	<b>2,461</b>	<b>58,459</b>
<b>Settlements</b>				
Senior secured debt	(23,603)	(1,737)	(370)	(25,710)
Subordinated secured debt	(9,553)	—	(139)	(9,692)
Unsecured subordinated debt	—	—	87	87
Preferred equity	(212)	—	(3)	(215)
<b>Total settlements</b>	<b>(33,368)</b>	<b>(1,737)</b>	<b>(425)</b>	<b>(35,530)</b>
<b>Sales</b>				
Common/common equivalents equity	(65)	—	—	(65)
<b>Total sales</b>	<b>(65)</b>	<b>—</b>	<b>—</b>	<b>(65)</b>
<b>Fair value as of September 30, 2011</b>				
Senior secured debt	299,274	23,256	88,886	411,416
Subordinated secured debt	100,933	12,905	10,365	124,203
Unsecured subordinated debt	14,411	—	—	14,411
Preferred equity	35,437	15,614	63,105	114,156
Common/common equivalents equity	30,670	3,332	—	34,002
<b>Total fair value as of September 30, 2011</b>	<b>\$ 480,725</b>	<b>\$ 55,107</b>	<b>\$ 162,356</b>	<b>\$ 698,188</b>

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The following table provides a reconciliation of fair value changes during the three-month period ended September 30, 2010 for all investments for which we determine fair value using unobservable (Level 3) factors.

<i>(in thousands)</i>	Fair value measurements using unobservable inputs (Level 3)			
	Non-affiliate Investments	Affiliate Investments	Control Investments	Total
<b>Fair value June 30, 2010</b>				
Senior secured debt	\$ 295,129	\$ 8,920	\$ 80,810	\$ 384,859
Subordinated secured debt	158,615	11,857	66,754	237,226
Unsecured subordinated debt	12,161	—	28,687	40,848
Preferred equity	24,646	10,106	212,243	246,995
Common/common equivalents equity	49,131	2,004	—	51,135
<b>Total fair value June 30, 2010</b>	<b>539,682</b>	<b>32,887</b>	<b>388,494</b>	<b>961,063</b>
<b>Realized/unrealized gain (loss)</b>				
Senior secured debt	(9,783)	—	(4,615)	(14,398)
Subordinated secured debt	831	—	(10,424)	(9,593)
Preferred equity	5,742	573	4,237	10,552
Common/common equivalents equity	2,916	1	—	2,917
<b>Total realized/unrealized gain (loss)</b>	<b>(294)</b>	<b>574</b>	<b>(10,802)</b>	<b>(10,522)</b>
<b>Issuances</b>				
Senior secured debt	5,460	11,779	546	17,785
Subordinated secured debt	14,429	106	3,645	18,180
Unsecured subordinated debt	80	—	2,931	3,011
Preferred equity	600	47	915	1,562
<b>Total issuances</b>	<b>20,569</b>	<b>11,932</b>	<b>8,037</b>	<b>40,538</b>
<b>Settlements</b>				
Senior secured debt	(20,710)	(470)	—	(21,180)
Subordinated secured debt	(51,153)	(6,742)	—	(57,895)
Preferred equity	(362)	—	(785)	(1,147)
<b>Total settlements</b>	<b>(72,225)</b>	<b>(7,212)</b>	<b>(785)</b>	<b>(80,222)</b>
<b>Sales</b>				
Unsecured subordinated debt	—	—	(31,618)	(31,618)
Preferred equity	(1,754)	—	(13,494)	(15,248)
Common/common equivalents equity	(12,531)	—	—	(12,531)
<b>Total sales</b>	<b>(14,285)</b>	<b>—</b>	<b>(45,112)</b>	<b>(59,397)</b>
<b>Fair value as of September 30, 2010</b>				
Senior secured debt	270,096	20,229	76,741	367,066
Subordinated secured debt	122,722	5,221	59,975	187,918
Unsecured subordinated debt	12,241	—	—	12,241
Preferred equity	28,872	10,726	203,116	242,714
Common/common equivalents equity	39,516	2,005	—	41,521
<b>Total fair value as of September 30, 2010</b>	<b>\$ 473,447</b>	<b>\$ 38,181</b>	<b>\$ 339,832</b>	<b>\$ 851,460</b>

There were no purchases of Level 3 investments during the three months ended September 30, 2010.

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### Unrealized (Depreciation) Appreciation of Level 3 Investments

The following table summarizes the unrealized (depreciation) appreciation that we recognized on those investments for which we determined fair value using unobservable inputs (Level 3) for the three months ended September 30, 2011 and 2010.

(in thousands)	Three months ended September 30, 2011				Three months ended September 30, 2010			
	Non-affiliate Investments	Affiliate Investments	Control Investments	Total	Non-affiliate Investments	Affiliate Investments	Control Investments	Total
<b>Change in unrealized appreciation (depreciation)</b>								
Senior secured debt	\$ (1,072)	\$ —	\$ (6,417)	\$ (7,489)	\$ (6,316)	\$ —	\$ (4,615)	\$ (10,931)
Subordinated secured debt	189	(85)	11,780	11,884	831	—	(10,424)	(9,593)
Unsecured subordinated debt	(17)	—	332 <sup>(a)</sup>	315	—	—	—	—
Preferred equity	2,447	2,028	916	5,391	4,383	573	8,148	13,104
Common/common equivalents equity	429	—	1,000	1,429	(6,615)	1	—	(6,614)
<b>Total change in unrealized appreciation (depreciation) on Level 3 investments</b>	<b>\$ 1,976</b>	<b>\$ 1,943</b>	<b>\$ 7,611</b>	<b>\$ 11,530</b>	<b>\$ (7,717)</b>	<b>\$ 574</b>	<b>\$ (6,891)</b>	<b>\$ (14,034)</b>

<sup>(a)</sup> Reflects a \$24.9 million reversal of accrued unrealized depreciation that we previously recognized on our investment in Total Sleep Holdings, Inc., or Total Sleep, which we wrote-off on September 30, 2011. The impact of this reversal was offset primarily by the recognition of \$24.7 million of additional unrealized depreciation on our investment in Broadview Networks Holdings, Inc., or Broadview.

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The following table provides a reconciliation of fair value changes during the nine-month period ended September 30, 2011 for all investments for which we determine fair value using unobservable (Level 3) factors.

(in thousands)	Fair value measurements using unobservable inputs (Level 3)			
	Non-affiliate Investments	Affiliate Investments	Control Investments	Total
<b>Fair value December 31, 2010</b>				
Senior secured debt	\$ 325,874	\$ 24,207	\$ 75,714	\$ 425,795
Subordinated secured debt	121,743	12,348	56,218	190,309
Unsecured subordinated debt	12,321	—	—	12,321
Preferred equity	24,741	13,197	178,357	216,295
Common/common equivalents equity	29,170	3,548	—	32,718
<b>Total fair value December 31, 2010</b>	<b>513,849</b>	<b>53,300</b>	<b>310,289</b>	<b>877,438</b>
<b>Realized/unrealized gain (loss)</b>				
Senior secured debt	(2,746)	—	(36,608)	(39,354)
Subordinated secured debt	2,714	93	33,706	36,513
Unsecured subordinated debt	223	—	(87)	136
Preferred equity	7,611	2,073	(78,194)	(68,510)
Common/common equivalents equity	2,805	(50)	—	2,755
<b>Total realized/unrealized gain (loss)</b>	<b>10,607</b>	<b>2,116</b>	<b>(81,183)</b>	<b>(68,460)</b>
<b>Purchases</b>				
Senior secured debt	—	—	11,863	11,863
Preferred equity	2,000	—	4,300	6,300
Common/common equivalents equity	123	—	—	123
<b>Total purchases</b>	<b>2,123</b>	<b>—</b>	<b>16,163</b>	<b>18,286</b>
<b>Issuances</b>				
Senior secured debt	90,790	3,995	44,185	138,970
Subordinated secured debt	30,253	464	1,143	31,860
Unsecured subordinated debt	1,867	—	—	1,867
Preferred equity	1,580	1,136	12,507	15,223
Common/common equivalents equity	533	62	—	595
<b>Total issuances</b>	<b>125,023</b>	<b>5,657</b>	<b>57,835</b>	<b>188,515</b>
<b>Settlements</b>				
Senior secured debt	(104,438)	(4,946)	(6,268)	(115,652)
Subordinated secured debt	(53,777)	—	(80,702)	(134,479)
Unsecured subordinated debt	—	—	87	87
Preferred equity	(212)	(792)	(12,171)	(13,175)
Common/common equivalents equity	(17)	(228)	—	(245)
<b>Total settlements</b>	<b>(158,444)</b>	<b>(5,966)</b>	<b>(99,054)</b>	<b>(263,464)</b>
<b>Sales</b>				
Senior secured debt	(10,206)	—	—	(10,206)
Preferred equity	(283)	—	(41,694)	(41,977)
Common/common equivalents equity	(1,944)	—	—	(1,944)
<b>Total sales</b>	<b>(12,433)</b>	<b>—</b>	<b>(41,694)</b>	<b>(54,127)</b>
<b>Fair value as of September 30, 2011</b>				
Senior secured debt	299,274	23,256	88,886	411,416
Subordinated secured debt	100,933	12,905	10,365	124,203
Unsecured subordinated debt	14,411	—	—	14,411
Preferred equity	35,437	15,614	63,105	114,156
Common/common equivalents equity	30,670	3,332	—	34,002
<b>Total fair value as of September 30, 2011</b>	<b>\$ 480,725</b>	<b>\$ 55,107</b>	<b>\$ 162,356</b>	<b>\$ 698,188</b>

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The following table provides a reconciliation of fair value changes during the nine-month period ended September 30, 2010 for all investments for which we determine fair value using unobservable (Level 3) factors.

(in thousands)	Fair value measurements using unobservable inputs (Level 3)			
	Non-affiliate	Affiliate	Control	Total
	Investments	Investments	Investments	
<b>Fair value December 31, 2009</b>				
Senior secured debt	\$ 273,319	\$ 21,789	\$ 80,995	\$ 376,103
Subordinated secured debt	183,684	11,511	80,202	275,397
Unsecured subordinated debt	2,179	—	28,439	30,618
Preferred equity	26,587	9,242	220,320	256,149
Common/common equivalents equity	40,885	1,846	28	42,759
<b>Total fair value December 31, 2009</b>	<b>526,654</b>	<b>44,388</b>	<b>409,984</b>	<b>981,026</b>
<b>Realized/unrealized (loss)</b>				
Senior secured debt	(13,674)	297	(4,527)	(17,904)
Subordinated secured debt	1,986	218	(28,821)	(26,617)
Unsecured subordinated debt	2	—	—	2
Preferred equity	8,215	1,377	(2,408)	7,184
Common/common equivalents equity	11,161	159	27	11,347
<b>Total realized/unrealized loss</b>	<b>7,690</b>	<b>2,051</b>	<b>(35,729)</b>	<b>(25,988)</b>
<b>Issuances</b>				
Senior secured debt	58,795	11,892	1,455	72,142
Subordinated secured debt	19,863	369	8,626	28,858
Unsecured subordinated debt	10,060	—	3,179	13,239
Preferred equity	1,687	107	2,733	4,527
Common/common equivalents equity	1	—	—	1
<b>Total issuances</b>	<b>90,406</b>	<b>12,368</b>	<b>15,993</b>	<b>118,767</b>
<b>Settlements</b>				
Senior secured debt	(48,294)	(13,749)	(1,182)	(63,225)
Subordinated secured debt	(82,811)	(6,877)	(32)	(89,720)
Preferred equity	(465)	—	(905)	(1,370)
<b>Total settlements</b>	<b>(131,570)</b>	<b>(20,626)</b>	<b>(2,119)</b>	<b>(154,315)</b>
<b>Sales</b>				
Senior secured debt	(50)	—	—	(50)
Unsecured subordinated debt	—	—	(31,618)	(31,618)
Preferred equity	(7,152)	—	(16,624)	(23,776)
Common/common equivalents equity	(12,531)	—	(55)	(12,586)
<b>Total sales</b>	<b>(19,733)</b>	<b>—</b>	<b>(48,297)</b>	<b>(68,030)</b>
<b>Fair value as of September 30, 2010</b>				
Senior secured debt	270,096	20,229	76,741	367,066
Subordinated secured debt	122,722	5,221	59,975	187,918
Unsecured subordinated debt	12,241	—	—	12,241
Preferred equity	28,872	10,726	203,116	242,714
Common/common equivalents equity	39,516	2,005	—	41,521
<b>Total fair value as of September 30, 2010</b>	<b>\$ 473,447</b>	<b>\$ 38,181</b>	<b>\$ 339,832</b>	<b>\$ 851,460</b>

There were no purchases of Level 3 investments during the nine months ended September 30, 2010.

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### Unrealized (Depreciation) Appreciation of Level 3 Investments

The following table summarizes the unrealized appreciation (depreciation) that we recognized on those investments for which we determined fair value using unobservable inputs (Level 3) for the nine months ended September 30, 2011 and 2010.

<i>(in thousands)</i>	Nine months ended September 30, 2011				Nine months ended September 30, 2010			
	Non-affiliate Investments	Affiliate Investments	Control Investments	Total	Non-affiliate Investments	Affiliate Investments	Control Investments	Total
<b>Change in unrealized appreciation (depreciation)</b>								
Senior secured debt	\$ 28,109	\$ —	\$ (36,608)	\$ (8,499)	\$ (9,264)	\$ 297	\$ (4,527)	\$ (13,494)
Subordinated secured debt	14,742	93	45,563	60,398	1,986	218	(28,821)	(26,617)
Unsecured subordinated debt	1,662	—	1,332	2,994	2	—	—	2
Preferred equity	7,116	2,990	(66,514) <sup>(a)</sup>	(56,408)	3,191	1,377	3,534	8,102
Common/common equivalents equity	4,583	(50)	1,000	5,533	1,916	159	(26)	2,049
<b>Total change in unrealized appreciation (depreciation) on Level 3 investments</b>	<b>\$ 56,212</b>	<b>\$ 3,033</b>	<b>\$ (55,227)</b>	<b>\$ 4,018</b>	<b>\$ (2,169)</b>	<b>\$ 2,051</b>	<b>\$ (29,840)</b>	<b>\$ (29,958)</b>

<sup>(a)</sup> Primarily reflects the recognition of \$73.8 million of additional unrealized depreciation on our investment in Broadview, partially offset by a \$24.9 million reversal of previously accrued unrealized depreciation on our investment in Total Sleep, which we wrote-off on September 30, 2011.

#### NOTE 4—CONCENTRATIONS OF INVESTMENT RISK

During the nine months ended September 30, 2011, we had concentrations in certain industries, including the healthcare, business services and communications industries. The following table summarizes, our fair value and revenue concentrations in each of those industries:

<i>(dollars in thousands)</i>	Investments at Fair Value				Revenue for the nine months ended			
	As of September 30, 2011		As of December 31, 2010		September 30, 2011		September 30, 2010	
	Amount	% of Total	Amount	% of Total	Amount	Revenue	Amount	Revenue
<b>Industry</b>								
Healthcare	\$ 86,703	10.5%	\$ 76,358	7.6%	\$8,287	12.5%	\$8,586	13.0%
Business services	81,021	9.8	87,897	8.7	7,295	11.0	3,150	4.8
Communications <sup>(a)</sup>	53,767	6.5	150,907	14.9	2,379	3.6	2,781	4.2

<sup>(a)</sup> Includes Broadview, which represented \$29.2 million, or 3.5%, and \$103.0 million, or 10.2%, of the fair value of our investment portfolio as of September 30, 2011 and December 31, 2010, respectively.

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### Note 5—BORROWINGS

As of September 30, 2011, we reported \$490.0 million of borrowings on our Consolidated Balance Sheets at cost. We estimate that the fair value of these borrowings as of September 30, 2011 was approximately \$472.7 million, based on market data and current interest rates. The following table summarizes our borrowing facilities and the facility amounts and amounts outstanding and contingent borrowing eligibility of Solutions Capital I, L.P., a wholly owned subsidiary, as an SBIC, under the SBIC Act.

<i>(dollars in thousands)</i>	Maturity Date	September 30, 2011		December 31, 2010	
		Total Facility/Program	Amount Outstanding	Total Facility/Program	Amount Outstanding
<i>Private Placement Notes</i>					
Series 2005-A	October 2011	\$ —	\$ —	\$ 17,434	\$ 17,434
Series 2007-A	October 2012	8,717	8,717	8,717	8,717
<i>Commercial Loan Funding Trust</i>					
Variable Funding Note	January 2014 <sup>(a)</sup>	150,000	55,822	150,000	100,251
<i>Commercial Loan Trust 2006-1</i>					
Series 2006-1 Class A-1 Notes	April 2018 <sup>(b)</sup>	106,250	106,250	106,250	106,250
Series 2006-1 Class A-2 Notes	April 2018 <sup>(b)</sup>	5,000	5,000	50,000	—
Series 2006-1 Class A-3 Notes	April 2018 <sup>(b)</sup>	85,000	85,000	85,000	85,000
Series 2006-1 Class B Notes	April 2018 <sup>(b)</sup>	58,750	58,750	58,750	58,750
Series 2006-1 Class C Notes <sup>(c)</sup>	April 2018 <sup>(b)</sup>	45,000	32,000	45,000	32,000
Series 2006-1 Class D Notes <sup>(d)</sup>	April 2018 <sup>(b)</sup>	47,500	29,880	47,500	29,880
<i>SBIC (Maximum borrowing potential) <sup>(e)</sup></i>	<sup>(f)</sup>	150,000	108,600	130,000	108,600
Total borrowings		<u>\$656,217</u>	<u>\$ 490,019</u>	<u>\$698,651</u>	<u>\$ 546,882</u>

<sup>(a)</sup> In January 2011, the lender renewed this facility through January 2013 and the legal final maturity date was extended to January 2014.

<sup>(b)</sup> Borrowings under the MCG Commercial Loan Trust 2006-1 facility are listed based on the contractual maturity date. The reinvestment period for this facility ended on July 20, 2011 and we will use all future principal collections from collateral in the facility to repay the securitized debt. On October 20, 2011, the next payment date for this facility, we used \$80.2 million of securitized cash in that facility (primarily representing previous principal collections of collateral in the facility) to repay a portion of the facility.

<sup>(c)</sup> Amount outstanding excludes \$5.0 million of notes that we repurchased in December 2008 for \$1.6 million and \$8.0 million of notes that we repurchased in April 2010 for \$4.4 million. As part of the consolidation process, we eliminated the notes that MCG, the parent company, purchased.

<sup>(d)</sup> Amount outstanding excludes \$10.1 million of notes that we repurchased in December 2008 for \$2.4 million and \$7.5 million of notes that we repurchased in January 2009 for \$2.1 million. As part of the consolidation process, we eliminated the notes that MCG, the parent company, purchased.

<sup>(e)</sup> As of September 30, 2011, we had the potential to borrow up to \$150.0 million of SBA-guaranteed debentures under the SBIC program. As of September 30, 2011, the SBA had approved and committed up to \$150.0 million in borrowings to the SBIC. As of September 30, 2011, we have funded \$75.0 million, which allows us to utilize the full \$150.0 million borrowing potential approved and committed by the SBA under this program. Based on our funded capital as of September 30, 2011, Solutions Capital I, L.P., subject to the SBA's approval, may borrow up to an additional \$41.4 million to originate investments.

<sup>(f)</sup> As of September 30, 2011, we could originate new borrowings under the \$150.0 million commitment made by the SBA through September 2015. We must repay borrowings under the SBIC program within ten years after the borrowing date, which will occur between September 2018 and September 2025.

Each of our credit facilities has certain collateral requirements and/or financial covenants. As of September 30, 2011, the net worth covenant of our Commercial Loan Funding Trust, or SunTrust Warehouse, requires that we maintain a consolidated tangible net worth of not less than \$450.0 million, plus 50% of any equity raised after February 26, 2009. Under these covenants, we must also maintain an asset coverage ratio of at least 180%.

As a BDC, we are not permitted to incur indebtedness or issue senior securities, including preferred stock, unless immediately after such borrowing we have an asset coverage for total borrowings (excluding borrowings by our SBIC facility) of at least 200%. In addition, we may not be permitted to declare any cash dividend or other distribution on our outstanding common shares, or purchase any such shares, unless, at the time of such declaration or purchase, we have an asset coverage ratio of at least 200% after deducting the amount of such dividend, distribution or purchase price. If we are unable to meet this asset coverage requirement, we may not be able to incur additional debt. As of September 30, 2011, our ratio of total assets to total borrowings and other senior securities was 230%.

We fund all of our current debt facilities, except our Series 2007-A unsecured notes, through our bankruptcy remote, special-purpose, wholly owned subsidiaries. Therefore, these subsidiaries' assets may not be available to our creditors. In some cases, advances under our debt facilities are subject to certain collateral levels, collateral quality, leverage and other restrictive covenants. We continue to service the portfolio investments that we use as collateral in our secured borrowing facilities.



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The following table summarizes repayments of our borrowings based on the final legal maturity or the contractual principal collections of the outstanding loans that comprise the collateral, where applicable. Certain of our borrowing facilities contain provisions that require that we apply a portion of the proceeds we receive from monetizations to pay down a portion of the outstanding balances. Actual repayments could differ significantly due to future prepayments by our borrowers, modifications of our borrowers' existing loan agreements, and monetizations.

<i>(in thousands)</i>	September 30, 2011		
	Debt with	Debt without	Total
	Recourse	Recourse	
2011 <sup>(a)</sup>	\$ —	\$ 80,173	\$ 80,173
2012	8,717	—	8,717
2013	—	—	—
2014	—	55,822	55,822
2015	—	—	—
Thereafter <sup>(b)</sup>	<u>75,000</u>	<u>270,307</u>	<u>345,307</u>
<b>Total</b>	<b><u>\$83,717</u></b>	<b><u>\$ 406,302</u></b>	<b><u>\$490,019</u></b>

<sup>(a)</sup> Borrowings under the MCG Commercial Loan Trust 2006-1 facility are listed based on the contractual maturity date. The reinvestment period for this facility ended on July 20, 2011 and we will use all future principal collections from collateral in the facility to repay the securitized debt. On October 20, 2011, the next payment date for this facility, we used \$80.2 million of securitized cash in that facility (primarily representing previous principal collections of collateral in the facility) to repay a portion of the facility.

<sup>(b)</sup> Our maximum exposure with respect to the indebtedness of Solutions Capital was \$75.0 million, which represents the \$75.0 million that MCG had funded in Solutions Capital as of September 30, 2011.

The following table summarizes our aggregate outstanding borrowings as of September 30, 2011 and December 31, 2010, by interest rate benchmark:

<i>(in thousands)</i>	September 30, 2011	December 31, 2010
<b>Interest rate benchmark</b>		
LIBOR	\$ 316,880	\$ 311,880
Commercial paper rate	55,822	100,251
Fixed rate	117,317	134,751
<b>Total borrowings</b>	<b><u>\$ 490,019</u></b>	<b><u>\$ 546,882</u></b>

As of September 30, 2011, we were in compliance with all key financial covenants under each of our borrowing facilities, although there can be no assurance regarding compliance in future periods. The following sections provide additional detail about each of our borrowing facilities.

### PRIVATE PLACEMENT NOTES

In October 2005, we issued \$50.0 million of Series 2005-A unsecured notes, at a fixed-interest rate of 6.73% per annum. In October 2007, we issued an additional \$25.0 million of Series 2007-A unsecured notes at a fixed-interest rate of 6.71% per annum. Both of these tranches, or the Private Placement Notes, were issued as five-year notes that require semi-annual interest payments. In 2009, the Private Placement Notes were amended. In connection with the amendments, the interest rate for the Series 2005-A unsecured notes was adjusted to 9.98% and the interest rate for the Series 2007-A unsecured notes was adjusted to 8.96%. The Series 2005-A unsecured notes were prepaid in March 2011 and the maturity date of the Series 2007-A unsecured notes is October 2012.

The amendments also require us to offer to repurchase the Private Placement Notes with a portion of certain monetization proceeds at a purchase price of 102% of the principal amount to be purchased. In addition, we agreed to limit the amount of debt from the 2006-1 Trust and our common stock that we may repurchase. For every \$5.0 million of Private Placement Notes we offer to purchase after February 26, 2009, we may repurchase \$2.5 million of debt from the 2006-1 Trust. We may also repurchase \$1.0 million of shares of our common stock for every \$5.0 million increment of Private Placement Notes offered to be repurchased after February 26, 2009, provided that the amount of permitted debt repurchases under the 2006-1 Trust shall be reduced by the amount of any of our common stock repurchases made.

Since the execution of these amendments in 2009, we have repurchased or prepaid a total of \$66.3 million of Private Placement Notes as of September 30, 2011, including the prepayment of the remaining balance of the Series 2005-A Notes on March 29, 2011. In connection with the March 2011 prepayment of the Series 2005-A unsecured notes and pursuant to the terms set forth in the Series 2005-A unsecured notes note purchase

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agreement, we paid to the noteholders \$17.4 million of principal, \$0.8 million in accrued interest and \$0.9 million in prepayment fees. We initially issued \$50.0 million of the Series 2005-A unsecured notes in October 2005 and, prior to the March 2011 repayment, had repurchased or prepaid in the aggregate \$32.6 million in principal. The outstanding principal balance under the Series 2007-A Private Placement Notes was \$8.7 million as of September 30, 2011.

Under the 2009 amendments, we must offer to repurchase the remaining Series 2007-A unsecured notes with 45% of the cash net proceeds of any sale of unencumbered assets to reduce amounts outstanding under these notes as, and when, such sales occur in the event of proceeds of \$5.0 million or more or otherwise on a semi-annual basis, unless an event of default under one of the financing subsidiary debt facilities has occurred and is continuing, in which case the percentage of net proceeds would increase to 60%.

The following table summarizes the reductions in the borrowing capacity from monetization proceeds:

<i>(in thousands)</i>	Series 2005-A		Series 2007-A		Total	
	Monetization	Outstanding	Monetization	Outstanding	Monetization	Outstanding
		Balances After		Balances After		Balances After
Quarter/Year Ended	Payment	Monetization Payment	Payment	Monetization Payment	Payment (a)(c)	Monetization Payment
Fiscal 2009 (b)	\$ 15,693	\$ 34,307	\$ 7,846	\$ 17,154	\$ 23,539	\$ 51,461
March 31, 2010	1,928	32,379	965	16,189	2,893	48,568
June 30, 2010	—	32,379	—	16,189	—	48,568
September 30, 2010	14,945	17,434	7,472	8,717	22,417	26,151
December 31, 2010	—	17,434	—	8,717	—	26,151
March 31, 2011 (c)	17,434	—	—	8,717	17,434	8,717
June 30, 2011	—	—	—	8,717	—	8,717
September 30, 2011	—	—	—	8,717	—	8,717
Total to date	<u>\$ 50,000</u>		<u>\$ 16,283</u>		<u>\$ 66,283</u>	

(a) Private Placement Notes were repurchased at a price of 102% of the principal amount repurchased. In 2010 and 2009, the premiums paid on repurchases of Private Placement Notes were \$0.5 million and \$0.4 million, respectively. These premiums reduce our gain on extinguishment of debt on the *Consolidated Statements of Operations*.

(b) In 2009, the Private Placement Notes were amended and we made a \$5.0 million prepayment at par.

(c) The Series 2005-A notes were prepaid in full and terminated on March 29, 2011. We paid \$0.9 million in prepayment fees in connection with the repayment.

### COMMERCIAL LOAN FUNDING TRUST

Through MCG Commercial Loan Funding Trust, we have a \$150.0 million warehouse financing facility funded through Three Pillars Funding LLC, an asset-backed commercial paper conduit administered by SunTrust Robinson Humphrey, Inc. The SunTrust Warehouse, which is structured to operate like a revolving credit facility, is secured primarily by MCG Commercial Loan Funding Trust's assets, including commercial loans that we sold to the trust. The pool of commercial loans in the trust must meet certain requirements, such as term, average life, investment rating, agency rating and industry diversity requirements. The pool of commercial loans must also meet certain requirements related to portfolio performance, including required minimum portfolio yield and limitations on delinquencies and charge-offs. The facility is funded by third parties through the commercial paper market with SunTrust Bank providing a liquidity backstop through January 2013.

In January 2011, SunTrust Bank renewed this liquidity facility. In connection with this renewal, the legal final maturity date of the SunTrust Warehouse was extended to January 2014 and the scheduled termination date was extended to January 2013. If a new agreement or extension is not executed by January 25, 2013, the SunTrust Warehouse enters a 12-month amortization period during which principal under the facility is paid down through orderly monetizations of portfolio company assets that are financed in the facility. Additionally, prior to the commencement of any amortization period, net proceeds from monetizations of collateral financed in the SunTrust Warehouse must be reinvested in additional collateral or used to repay outstanding borrowings. The interest rate on the SunTrust Warehouse is the commercial paper rate plus 3.25%, a 0.75% increase over the rate as of December 31, 2010. We paid a \$1.5 million, or 1.0%, facility fee for this renewal.

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Advances under this facility may be up to 64% of eligible collateral. The SunTrust Warehouse is non-recourse to us; therefore, in the event of a termination event or upon the legal final maturity date, the lenders under the SunTrust Warehouse may only look to the collateral to satisfy the outstanding obligations under this facility. The following table summarizes the fair value of the collateral under the Commercial Loan Funding Trust as of September 30, 2011 and December 31, 2010:

<i>(dollars in thousands)</i>	September 30, 2011		December 31, 2010	
	Amount	%	Amount	%
<b>Securitized assets</b>				
Senior secured debt	\$ 99,205	72.4%	\$128,330	69.0%
Subordinated secured debt	24,744	18.0	50,932	27.5
<b>Total securitized assets</b>	<b>123,949</b>	<b>90.4</b>	179,262	96.5
Cash, securitization accounts	13,099	9.6	6,539	3.5
<b>Total collateral</b>	<b>\$137,048</b>	<b>100.0%</b>	<b>\$185,801</b>	<b>100.0%</b>

### COMMERCIAL LOAN TRUST 2006-1

In April 2006, we completed a \$500.0 million debt securitization through Commercial Loan Trust 2006-1, a wholly owned subsidiary. The 2006-1 Trust issued \$106.25 million of Class A-1 Notes, \$50.0 million of Class A-2 Notes, \$85.0 million of Class A-3 Notes, \$58.75 million of Class B Notes, \$45.0 million of Class C Notes and \$47.5 million of Class D Notes. The respective classes of notes bear interest at LIBOR plus 0.33%, 0.35%, 0.33%, 0.58%, 1.05% and 2.25%.

All of the notes are secured by the assets of the 2006-1 Trust. The following table summarizes the fair value of the assets securitized under this facility as of September 30, 2011 and December 31, 2010:

<i>(dollars in thousands)</i>	September 30, 2011		December 31, 2010	
	Amount	%	Amount	%
<b>Securitized assets</b>				
Senior secured debt	\$291,444	69.2%	\$285,854	68.2%
Subordinated secured debt	43,403	10.3	97,881	23.3
Common Equity	205	0.1	—	—
<b>Total securitized assets</b>	<b>335,052</b>	<b>79.6</b>	383,735	91.5
Cash, securitization accounts	86,317 <sup>(a)</sup>	20.4	35,706	8.5
<b>Total collateral</b>	<b>\$421,369</b>	<b>100.0%</b>	<b>\$419,441</b>	<b>100.0%</b>

<sup>(a)</sup> On October 20, 2011, the next payment date for this facility, we used \$80.2 million of securitized cash in that facility (primarily representing previous principal collections of collateral in the facility) to repay a portion of the facility.

We retain all of the equity in the securitization. The securitization included a five-year reinvestment period, which ended in July 2011.

The Class A-1, Class B, Class C and Class D Notes are term notes. The Class A-2 Notes were, but are no longer, a revolving class of secured notes with a five-year revolving period. Therefore, we may not increase the principal amount of the A-2 notes beyond the \$5 million principal balance that was outstanding as of September 30, 2011. The Class A-3 Notes are a delayed draw class of secured notes, which were drawn in full between July 2006 and April 2007. The pool of commercial loans in the trust must meet certain requirements, such as asset mix and concentration, collateral coverage, term, agency rating, minimum coupon, minimum spread and sector diversity requirements.

### SBIC DEBENTURES

In December 2004, we formed a wholly owned subsidiary, Solutions Capital I, L.P. Solutions Capital I, L.P. has a license from the SBA to operate as an SBIC under the SBIC Act. As of September 30, 2011, the license gave Solutions Capital I, L.P. the potential to borrow up to \$150.0 million. The SBA approved and committed \$150.0 million in borrowings to Solutions Capital I, L.P., subject to certain capital requirements and customary procedures. These funds can be used to provide debt and equity capital to qualifying small businesses. We may use the borrowings from the SBA to fund new originations; however, we may not use these borrowings to originate debt to certain companies that are currently in our portfolio without SBA approval. In addition, we may not use these funds for MCG's, the parent company's, working capital.

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To utilize the full \$150.0 million potential borrowing for which we were approved under this program, we needed to fund a total of \$75.0 million to Solutions Capital I, L.P., which we had done as of September 30, 2011. Based on our funded capital as of September 30, 2011, Solutions Capital I, L.P. may borrow, subject to the SBA's approval, up to an additional \$41.4 million to originate new investments.

The maximum amount of outstanding leverage available to single-license SBIC companies is \$150.0 million. The maximum amount of outstanding leverage available to SBIC companies with multiple licenses is \$225.0 million on an aggregate basis. In March 2011, we formed Solutions Capital II, L.P., and in May 2011, we submitted to the SBA our application for a second SBIC license under Solutions Capital II, L.P. After discussions with the SBA, we elected to withdraw our application for a second license until such time as the SBA has an opportunity to evaluate, among other things, the organizational impact of our recent restructuring and changes in management. We may seek to re-file our application for a second license within six months. There is no assurance that, if filed, the SBA will grant the additional license.

As of September 30, 2011 and December 31, 2010, we had \$185.8 million and \$144.9 million, respectively, of investments in our SBIC and we had \$10.1 million and \$29.4 million, respectively, of restricted cash to be used for additional investments in our SBIC.

Once drawn, the SBIC debt bears an interim interest rate of LIBOR plus 30 basis points. The rate becomes fixed at the time of SBA pooling, which is within nine months of funding, and is set to the then-current 10-year treasury rate plus a spread and an annual SBA charge. As of September 30, 2011, the SBIC had \$108.6 million of borrowings outstanding summarized in the following table:

	Amount Outstanding		Rate	Treasury Rate at Pooling Date	Spread in basis points	
	September 30, 2011	December 31, 2010				
<i>(dollars in thousands)</i>						
<b>Tranche</b>						
2008-10B	\$ 2,600	\$ 2,600	6.44%	Fixed	3.80%	264
2009-10A	12,000	12,000	5.34%	Fixed	2.81%	253
2009-10B	13,000	13,000	4.95%	Fixed	3.44%	151
2010-10B	27,500	27,500	3.93%	Fixed	2.56%	137
2011-10A	8,500	8,500	4.80%	Fixed	3.50%	130
2011-10A	45,000	45,000	4.80%	Fixed	3.50%	130
<b>Total</b>	<b>\$ 108,600</b>	<b>\$ 108,600</b>	4.63%		3.14%	149

In October 2008, we received exemptive relief from the SEC, which effectively allows us to exclude debt issued by Solutions Capital I, L.P. from the calculation of our consolidated BDC asset coverage ratio.

### NOTE 6—CAPITAL STOCK

We have one class of common stock and one class of preferred stock authorized. Our board of directors is authorized to: provide for the issuance of shares of preferred stock in one or more series; establish the number of shares to be included in each such series; and establish the designations, voting powers, preferences and rights of the shares of each such series, and any qualifications, limitations or restrictions thereof, subject to the conditions set forth in the 1940 Act.

The following table summarizes our distributions per share declared since January 1, 2010.

Date Declared	Record Date	Payment Date	Amount
October 31, 2011	December 15, 2011	January 13, 2012	\$ 0.17
August 1, 2011	September 14, 2011	October 14, 2011	\$ 0.17
May 5, 2011	June 15, 2011	July 15, 2011	\$ 0.17
March 1, 2011	March 15, 2011	April 15, 2011	\$ 0.15
November 2, 2010	December 9, 2010	January 6, 2011	\$ 0.14
August 3, 2010	September 7, 2010	October 4, 2010	\$ 0.12
April 29, 2010	June 2, 2010	July 2, 2010	\$ 0.11

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### NOTE 7—SHARE-BASED COMPENSATION

#### EMPLOYEE SHARE-BASED COMPENSATION

##### Third Amended and Restated 2006 Employee Restricted Stock Plan

From time to time, we award shares of restricted common stock to employees under our *Third Amended and Restated 2006 Employee Restricted Stock Plan*, or the 2006 Plan, which our stockholders initially approved in June 2006. In May 2010, our stockholders approved an amendment to the 2006 Plan increasing the number of shares we may award from 3,500,000 to 6,050,000 shares. Shares of restricted common stock awarded under the 2006 Plan may be subject to the employees' meeting service or performance conditions specified at the time of award. The award date is the date on which the shares are awarded by the Compensation Committee or our board of directors, while the fair value of the respective stock award is based on the closing price of our common stock on the NASDAQ Global Select Market on the award date. We amortize restricted stock awards on a straight-line basis over the requisite service period and report this expense as amortization of employee restricted stock awards on our *Consolidated Statements of Operations*.

During the nine months ended September 30, 2011, we issued 726,250 shares of restricted stock under the 2006 Plan with a weighted-average fair value per share of common stock at the award date of \$6.16. These awards included 114,750 of shares of restricted stock issued under the *MCG Capital Corporation 2011 Retention Program*, or the Retention Program. The forfeiture provisions for 50% of the shares of restricted stock issued under the Retention Program will lapse on each of March 31, 2012 and September 30, 2012. For additional information about the Retention Program, see *Note 11—Corporate Restructuring and 2011 Retention Program*. The awards made during the nine months ended September 30, 2011, under the 2006 Plan also included 86,500 shares of restricted stock awarded under the *Long-Term Incentive Plan* (discussed in more detail below). In addition to shares awarded under the Retention Program and the *Long-Term Incentive Plan*, during the nine months ended September 30, 2011, we also awarded 525,000 shares of restricted stock under the 2006 Plan to employees that will vest ratably over four years. During the nine months ended September 30, 2010, we issued 216,250 shares of restricted stock under the 2006 plan, at weighted-average fair value of \$2.12 per share. All shares that we awarded during the nine months ended September 30, 2010 were awarded under the *Long-Term Incentive Plan*, which is discussed in more detail below.

During the nine months ended September 30, 2011 and 2010, we recognized \$1.4 million and \$3.4 million, respectively, of compensation expense related to share-based compensation awards. In addition, during the nine months ended September 30, 2011, we recognized \$0.4 million of amortization of restricted stock awards as restructuring expense. As of September 30, 2011, all the restricted share awards for which forfeiture provisions had not lapsed carried non-forfeitable dividend rights to the holder of the restricted shares. We record dividends paid on shares of restricted common stock for which forfeiture provisions are expected to lapse to retained earnings, while we record dividends paid on shares of restricted common stock for which forfeiture provisions are not expected to lapse to compensation expense. No dividends paid during either the nine months ended September 30, 2011 or 2010 were recorded as compensation expense. As of September 30, 2011, we had \$3.0 million of unrecognized compensation cost related to restricted common stock awarded to employees. We will recognize these costs over the remaining weighted-average requisite service period of 2.6 years.

##### Long-Term Incentive Plan

On July 23, 2009, our board of directors approved the *Long-Term Incentive Plan*, or the LTIP, which is effective for the three-year period ending July 22, 2012. LTIP participants, including our executive officers and key, non-executive employees, were eligible, in the sole discretion of the Compensation Committee of our board of directors, to receive their respective portions of up to an aggregate of 865,000 shares of our restricted common stock to be issued under the 2006 Plan and up to \$5.2 million of cash bonuses if the closing price of our common stock achieves specific price thresholds for 20 consecutive trading days.

All of the 865,000 shares of restricted stock under the LTIP were issued during 2009 through 2011, following our achievement of share price thresholds set forth in the following table and authorization of the Compensation Committee of our board of directors. Forfeiture provisions for two-thirds of the respective stock awards lapsed immediately, with the forfeiture provisions for the remaining one-third of the respective stock awards lapsing twelve months later. Similarly, cash awards under the LTIP were subject to the achievement of the share price thresholds set forth in the following table. Upon satisfaction of a price threshold and the authorization of the Compensation Committee, the LTIP provides for the immediate payout of two-thirds of the associated cash with the remainder to be paid twelve months later.

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The following table summarizes the price thresholds, the cumulative percentage, number of shares and cash bonus associated with each stock price threshold set forth in the LTIP. In addition, the following table summarizes the market thresholds that were achieved and the associated stock and cash awards through September 30, 2011.

Share Price	Market Thresholds, Shares and Cash Bonus Eligible for Award under <i>Long-Term Incentive Plan</i>			Date Market Thresholds Achieved and Shares and Dollar Amounts Awarded		
	Potential Stock Awards		Aggregate Dollar Amount for Each Share Price threshold Achieved	Date Share Price Achieved	Number of Shares Awarded <sup>(a)</sup>	Dollar Amount Awarded <sup>(b)</sup>
	% of Award	Number of Shares				
\$3.00	25%	216,250	\$ —	October 2009	216,250	\$ —
\$4.00	25%	216,250	—	October 2009	216,250	—
\$5.00	25%	216,250	1,000,000	April 2010	216,250	1,000,000
\$6.00	15%	129,750	996,000	November 2010	129,750	996,000
\$7.00	10%	86,500	1,006,000	March 2011	86,500	1,006,000
\$8.00 <sup>(c)</sup>	— %	—	2,209,000			
	100%	865,000	\$ 5,211,000		865,000	\$3,002,000

<sup>(a)</sup> As of September 30, 2011, we awarded 865,000 shares under the LTIP program, for which the forfeiture provision have lapsed on 807,500 shares. Assuming that the associated LTIP participants meet the continuing service requirements, the forfeiture provisions for 33,250 shares and 22,170 shares will lapse in November 2011 and February 2012, respectively.

<sup>(b)</sup> As of September 30, 2011, we awarded \$3,002,000 of cash awards under the plan, of which \$2,001,000 was paid out upon achievement of the market threshold. Cash in the amount of \$468,000 was paid to LTIP participants in 2011 after satisfaction of the participants' service requirement. Assuming that the associated LTIP participants meet the continuing service requirements, \$256,000 will be paid in November 2011 and \$258,000 will be paid in February 2012.

<sup>(c)</sup> We are under no obligation to pay the cash award for the \$8.00 tranche. The Compensation Committee of our board of directors has the sole discretion for making such determination, regardless of whether the \$8.00 share price has been achieved. Cash awards in the amount of \$511,000 were forfeited by employees upon resignation/termination from the Company.

We account for the restricted stock awards as *equity awards*. As of the July 23, 2009 grant date for the LTIP, we estimated the fair value of these awards was \$1.9 million, and we are amortizing this amount on a straight-line basis over the derived service period. During the nine months ended September 30, 2011, we recognized less than \$0.1 million of compensation expense for these equity awards. During the nine months ended September 30, 2010, we recognized \$0.5 million of compensation expense for these equity awards.

We account for the cash portion of the LTIP as *liability awards*. As liability awards, we are required to account for the awards based on the fair value of the award at the end of each reporting period and to recognize the expense over the then-current estimated requisite service period. In total, during the nine months ended September 30, 2011, we reversed \$0.3 million of previously recognized compensation expense for the cash awards under the LTIP and during the nine months ended September 30, 2010, we recognized \$1.7 million of compensation expense for the cash awards under the LTIP. As of September 30, 2011, the fair value of the \$8.00 tranche was less than \$0.1 million. However the total fair value of this tranche could, vary from zero to \$1.7 million over the term of the LTIP because we adjust the fair value of the LTIP awards each quarter.

### Non-Employee Director Share-Based Compensation

During June 2006, our stockholders initially approved the *2006 Non-Employee Director Restricted Stock Plan*, which was subsequently amended and restated and which we refer to as the 2006 Non-Employee Plan. In May 2010, our stockholders approved an amendment to the 2006 Non-Employee Plan that increased the number of shares we may award from 100,000 to 150,000 shares. During the nine months ended September 30, 2011 and 2010, we awarded 15,000 shares and 7,500 shares, respectively, of restricted common stock to non-employee directors. During each of the nine months ended September 30, 2011 and 2010, we recognized less than \$0.1 million of compensation costs related to share-based awards to non-employee directors. We include this compensation cost in general and administrative expense on our *Consolidated Statements of Operations*. As of September 30, 2011, we had less than \$0.1 million of unrecognized compensation cost related to restricted common stock awarded to non-employee directors, which we expect to recognize over the remaining weighted-average requisite service period of 2.0 years.

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### SUMMARY OF EMPLOYEE AND NON-EMPLOYEE DIRECTOR SHARE-BASED COMPENSATION

The following table summarizes our restricted stock award activity during the nine months ended September 30, 2011:

	<u>Shares</u>	<u>Weighted-Average Grant Date Fair Value per Share</u>
Subject to forfeiture provisions as of December 31, 2010	932,200	\$ 3.92
Awarded	741,250	6.17
Forfeiture provision satisfied	(977,910)	3.98
Forfeited	(134,520)	6.88
<b>Subject to forfeiture provisions as of September 30, 2011</b>	<b><u>561,020</u></b>	<b>\$ 6.01</b>

### NOTE 8—INCOME TAXES

As a RIC, we are taxed under Subchapter M of the Internal Revenue Code. As such, our income generally is not taxable to the extent we distribute it to stockholders and we meet certain qualification tests as outlined in the Internal Revenue Code. However, income from certain investments owned by our wholly owned subsidiaries is subject to federal, state and local income taxes. During 2010, we declared and paid distributions from ordinary income that were sufficient to meet our distribution requirements as a RIC. On a continuing basis, we monitor distribution requirements in order to comply with Subchapter M of the Internal Revenue Code.

We use the asset and liability method to account for our Taxable Subsidiaries' income taxes. Using this method, we recognize deferred tax assets and liabilities for the estimated future tax effects attributable to temporary differences between financial reporting and the tax bases of assets and liabilities. In addition, we recognize deferred tax benefits associated with net operating carryforwards that we may use to offset future tax obligations. We measure deferred tax assets and liabilities using the enacted tax rates expected to apply to taxable income in the years in which we expect to recover or settle those temporary differences. During the nine months ended September 30, 2011, we accrued a \$29,000 income tax provision, which was primarily attributable to unrealized depreciation or appreciation and flow-through taxable income on certain investments held by our subsidiaries. During the nine months ended September 30, 2010, we accrued a \$1.9 million income tax provision of which \$1.6 million was attributable to the sale of JetBroadband Holdings, LLC in July 2010 and the remainder was attributable primarily to unrealized depreciation or appreciation and flow-through taxable income on certain investments held by our subsidiaries.

Historically, we have declared dividends that were paid the following quarter. From December 2001 through September 30, 2011, we declared distributions per share of \$12.64. Each year, we mail statements on Form 1099-DIV to our stockholders that identify whether we made distributions from ordinary income, net capital gains on the sale of securities, which are each taxable distributions, and/or a return of paid-in-capital surplus, which is a nontaxable distribution. A portion of our distributions may represent a return of capital to our stockholders, to the extent that the total distributions paid in a given year exceed current and accumulated taxable earnings and profits. A portion of the distributions that we paid to stockholders during fiscal years 2008, 2006, 2005, 2004 and 2003 represented a return of capital.

We determine the tax attributes of our distributions as of the end of our fiscal year based upon our taxable income for the full year and distributions paid during the full year. Therefore, a determination of tax attributes made on a quarterly basis may not be representative of the actual tax attributes of distributions for a full year.

The following table summarizes the distributions that we declared during 2011:

<u>Date Declared</u>	<u>Record Date</u>	<u>Payable Date</u>	<u>Dividends per Share</u>
October 31, 2011	December 15, 2011	January 13, 2012	\$ 0.17
August 1, 2011	September 14, 2011	October 14, 2011	\$ 0.17
May 5, 2011	June 15, 2011	July 15, 2011	\$ 0.17
March 1, 2011	March 15, 2011	April 15, 2011	\$ 0.15

If we determined the tax attributes of these distributions as of September 30, 2011, 26% would be from ordinary income and 74% would be a return of capital. However, actual determinations of the tax attributes of our distributions, including determinations of return of capital, are made annually as of the end of our fiscal year, based upon our taxable income and distributions paid for the full year and will be reported to each stockholder on a Form 1099. Future distributions will take into account the requirements for us to distribute the majority of our

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taxable income to fulfill our distribution requirements as a RIC, together with an assessment of our current and forecasted gains and losses recognized or to be recognized for tax purposes, portfolio transactional events, liquidity, cash earnings and our asset coverage ratio at the time of such decision.

Taxable income differs from net income recognized in accordance with accounting principles generally accepted in the United States, or GAAP, because of temporary and permanent differences in income and expense recognition.

Taxable income generally excludes unrealized gains and losses from appreciation or depreciation of our investments, which are included in GAAP net income. Further, amounts recognized for financial reporting purposes may differ from amounts included in taxable income due to the accrued dividends on preferred stock, which increase the book basis but not the tax basis of our investments, and non-accrual interest on loans, which increase the tax basis but not the book basis.

The following table summarizes the cost as well as the unrealized appreciation and depreciation for federal income tax purposes, as of September 30, 2011 and December 31, 2010:

<i>(in thousands)</i>	September 30, 2011	December 31, 2010
<b>Cost for federal income tax purposes</b>	<b>\$ 996,300</b>	<b>\$ 1,144,899</b>
<b>Gross unrealized appreciation</b>		
Unrealized appreciation of fair value of portfolio investments (GAAP)	60,491	56,950
Book to tax differences	84,373	90,981
Gross unrealized appreciation—tax basis	144,864	147,931
<b>Gross unrealized depreciation</b>		
Unrealized depreciation of fair value of portfolio investments (GAAP)	(296,965)	(293,940)
Book to tax differences	(31,162)	(37,981)
Gross unrealized depreciation—tax basis	(328,127)	(331,921)
<b>Net unrealized depreciation—tax basis</b>	<b>(183,263)</b>	<b>(183,990)</b>
Plus: Unrealized appreciation of fair value of other assets and liabilities (GAAP)	405	1,023
<b>Gross realized depreciation</b>		
Book to tax differences	10,731	47,773
<b>Net realized depreciation—tax basis</b>	<b>10,731</b>	<b>47,773</b>
<b>Total investments at fair value (GAAP)</b>	<b>\$ 824,173</b>	<b>\$ 1,009,705</b>

The following table reconciles GAAP net loss to taxable income before deductions for distributions for the nine months ended September 30, 2011 and the year ended December 31, 2010:

<i>(in thousands)</i>	Nine months ended September 30, 2011	Year ended December 31, 2010
Net loss	\$ (44,142)	\$ (13,072)
Difference between book and tax losses on investments	48,950	(52,865)
Net change in unrealized (appreciation) depreciation on investments not taxable until realized	(516)	66,674
Capital losses in excess of capital gains	12,638	4,861
Timing difference related to deductibility of long-term incentive compensation	(6,085)	1,594
Taxable interest income on non-accrual loans <sup>(a)</sup>	(838)	14,857
Dividend income accrued for GAAP purposes that is not yet taxable	(5,840)	(7,368)
Distributions from taxable subsidiaries	1,828	3,529
Federal tax provision	29	1,801
Other, net	1,975	24
<b>Taxable income before deductions for distributions</b>	<b>\$ 7,999</b>	<b>\$ 20,035</b>

<sup>(a)</sup> Results for the period ended September 30, 2011 reflect the reversal of interest we previously recognized on non-accrual loans of portfolio investments that we monetized. In accordance with the Internal Revenue Service's Code, we are required to recognize as taxable interest income all interest that is owed to us by portfolio companies, including interest on those debt investments that are on non-accrual status for GAAP reporting purposes.

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### NOTE 9—(LOSS) EARNINGS PER SHARE

The following table sets forth the computation of basic and diluted (loss) earnings per common share for the three and nine months ended September 30, 2011 and 2010:

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
<i>(dollars in thousands, except per share amounts)</i>				
<b>Numerator for basic and diluted (loss) earnings per share</b>				
Net (loss) earnings	\$ (25,109)	\$ (529)	\$ (44,142)	\$ 4,676
Less: Dividends declared—common and restricted shares	(13,101)	(9,187)	(37,784)	(17,608)
<b>Undistributed loss</b>	<b>(38,210)</b>	<b>(9,716)</b>	<b>(81,926)</b>	<b>(12,932)</b>
Percentage allocated to common shares <sup>(a)</sup>	<b>100.0%</b>	100.0%	<b>100.0%</b>	98.5%
<b>Undistributed earnings—common shares</b>	<b>(38,210)</b>	<b>(9,716)</b>	<b>(81,926)</b>	<b>(12,738)</b>
Add: Dividends declared—common shares	13,101	9,187	37,784	17,344
<b>Numerator for common shares outstanding excluding participating shares</b>	<b>(25,109)</b>	<b>(529)</b>	<b>(44,142)</b>	<b>4,606</b>
Numerator for participating unvested shares only	—	—	—	70
<b>Numerator for basic and diluted (loss) earnings per share—total</b>	<b>\$ (25,109)</b>	<b>\$ (529)</b>	<b>\$ (44,142)</b>	<b>\$ 4,676</b>
<b>Denominator for basic and diluted weighted-average shares outstanding</b>				
Common shares outstanding	76,404	75,486	76,173	75,347
Participating unvested shares <sup>(b)</sup>	—	—	—	1,122
<b>Basic and diluted weighted-average common shares outstanding—total <sup>(b)</sup></b>	<b>76,404</b>	<b>75,486</b>	<b>76,173</b>	<b>76,469</b>
<b>(Loss) earnings per share—basic and diluted</b>				
Excluding participating unvested shares	\$ (0.33)	\$ (0.01)	\$ (0.58)	\$ 0.06
Including participating unvested shares	\$ (0.33)	\$ (0.01)	\$ (0.58)	\$ 0.06
<b>(a) Basic and diluted weighted-average common shares:</b>				
Weighted-average common shares outstanding	76,404	75,486	76,173	75,347
Weighted-average restricted shares	—	—	—	1,122
<b>Total basic and diluted weighted-average common shares</b>	<b>76,404</b>	<b>75,486</b>	<b>76,173</b>	<b>76,469</b>
Percentage allocated to common shares	<b>100.0%</b>	100.0%	<b>100.0%</b>	98.5%

<sup>(b)</sup> For the three months ended September 30, 2011 and 2010 and for the nine months ended September 30, 2011, we excluded 654; 1,071 and 813, respectively, weighted-average shares of restricted common stock from the calculation of diluted loss per share because the inclusion of these shares would have had an anti-dilutive impact on the calculation of loss per share.

Holders of unvested shares of our issued and outstanding restricted common stock are eligible to receive non-forfeitable dividends. As such, these unvested shares are participating securities requiring the two-class method of computing earnings per share. Pursuant to the two-class method, we report basic and diluted (loss) earnings per share both inclusive and exclusive of the impact of the participating securities.

### NOTE 10—CONTINGENCIES AND COMMITMENTS

#### LEGAL PROCEEDINGS

We are 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 the outcome of these legal proceedings cannot at this time be predicted with certainty, we do not expect that these proceedings will have a material effect on our financial condition or results of operations.

#### FINANCIAL INSTRUMENTS

During the normal course of business, we are party to certain financial instruments, including loans, participations in loans, guarantees, letters of credit and other financial commitments. We conduct extensive due diligence and, when appropriate, obtain collateral to limit our credit risk. Generally, these commitments have fixed expiration dates or other termination clauses, which may require payment of a fee by the counterparty. We expect many of these commitments will not be fully used before they expire; therefore, the total commitment amounts do not necessarily represent future cash requirements.



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We do not report the unused portions of these commitments on our *Consolidated Balance Sheets*. As of September 30, 2011 and December 31, 2010, we had \$23.1 million and \$32.3 million, respectively, of outstanding unused loan commitments. We estimate that as of September 30, 2011 and December 31, 2010, the fair value of these commitments was \$0.1 million and \$0.2 million, respectively, based on the fees that we currently charge to enter into similar arrangements, taking into account the creditworthiness of the counterparties. As of September 30, 2011 and December 31, 2010, we had no outstanding guarantees or standby letters of credit.

### LEASE OBLIGATIONS

We lease our headquarters and certain other offices and equipment under non-cancelable operating and capital leases which expire through 2013. We have sublet certain of our offices to third parties. Certain facility leases contain provisions for rental options and rent escalations based on scheduled increases, as well as increases resulting from a rise in certain costs incurred by the lessor. As of September 30, 2011, our obligation for the remaining terms of these leases was \$3.1 million, of which \$2.2 million will be payable during the twelve months ending September 30, 2012. These lease obligations are partially offset by \$0.1 million of sublease income due over the remaining term of the subleases, nearly all of which is due during the twelve months ending September 30, 2012.

### NOTE 11—CORPORATE RESTRUCTURING AND 2011 RETENTION PROGRAM

#### CORPORATE RESTRUCTURING

On August 1, 2011, our board of directors approved a plan, to reduce our workforce by 42%, including 22 current employees and 5 recent resignations. As of September 30, 2011, our headcount was 39 employees. Affected employees received severance pay, continuation of benefits and, for employees who had been awarded restricted stock, additional lapsing of restrictions associated with restricted stock awards. We have accounted for these costs in accordance with *ASC 420-10—Exit or Disposal Cost Obligations*.

During the nine-months ended September 30, 2011, we incurred \$4.2 million of restructuring expenses, which we reported as a separate line item on our *Consolidated Statements of Operations*. The following table summarizes the restructuring charges recognized during the quarter ended September 30, 2011 related to our 2011 corporate restructuring:

<i>(In thousands)</i>	Three months ended	Nine months ended
	September 30, 2011	September 30, 2011
<b>Severance benefits</b>		
Amortization of restricted stock <sup>(a)</sup>	\$ 431	\$ 431
Cash severance obligations	3,632	3,696
<b>Other restructuring costs <sup>(b)</sup></b>	<b>46</b>	<b>47</b>
<b>Total restructuring charge</b>	<b>\$ 4,109</b>	<b>\$ 4,174</b>

<sup>(a)</sup> Represents share-based compensation expenses associated with the lapsing of forfeiture restrictions applicable to restricted stock awards for affected employees over their respective severance periods. In total, the forfeiture provisions with respect to 67,742 shares of restricted stock will lapse during the former employees' respective severance periods.

<sup>(b)</sup> Includes \$11 for retirement of fixed assets associated with restructuring.

We include liabilities associated with our restructuring in Other Liabilities on our *Consolidated Balance Sheet*. The following table summarizes changes in the balance of our restructuring liabilities during the three and nine months ended September 2011:

<i>(in thousands)</i>	Three months ended September 30, 2011			Nine months ended September 30, 2011		
	Severance Benefits <sup>(a)</sup>	Other	Total	Severance Benefits <sup>(a)</sup>	Other	Total
<b>Beginning balance <sup>(b)</sup></b>	<b>\$ 242</b>	<b>\$ 71</b>	<b>\$ 313</b>	<b>\$ 178</b>	<b>\$ 85</b>	<b>\$ 263</b>
Additions	3,611	35	3,646	3,675	35	3,710
Accretion	21	—	21	21	1	22
Cash payments	(449)	(42)	(491)	(449)	(57)	(506)
<b>Ending balance</b>	<b>\$ 3,425</b>	<b>\$ 64</b>	<b>\$ 3,489</b>	<b>\$ 3,425</b>	<b>\$ 64</b>	<b>\$ 3,489</b>

<sup>(a)</sup> Includes the cost of severance and continuation of benefits.

<sup>(b)</sup> The December 31, 2010 balance relates to liabilities carried forward from our August 2008 corporate restructuring.

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### *2011 RETENTION PROGRAM*

On August 1, 2011, our board of directors approved the *MCG Capital Corporation 2011 Retention Program*, or the Retention Program, for the benefit of our employees, including one of our named executive officers, but excluding our: i) President and Chief Executive Officer; ii) Executive Vice President and Chief Financial Officer; iii) Executive Vice President of Business Development; and iv) Senior Vice President, General Counsel and Chief Compliance Officer. We designed the Retention Program to provide eligible employees with certain incentives related to their past service and continuing employment with MCG. The Retention Program consists of an aggregate of \$1.3 million in cash and up to 114,750 shares of restricted common stock.

Under the Retention Program, we awarded a cash bonus to eligible employees, representing a specified percentage of each eligible employee's respective annual cash bonus target for the fiscal year ending December 31, 2011. We will pay the incentive bonus to eligible employees in two equal installments on each of March 31, 2012 and September 30, 2012, subject to continued employment with MCG. Certain employees also received shares of restricted common stock under the *MCG Capital Corporation 2006 Employee Restricted Stock Plan*, as amended, or the 2006 Plan. The forfeiture provisions with respect to 50% of the shares of restricted common stock subject to each retention stock award will lapse on each of March 31, 2012 and September 30, 2012.

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### NOTE 12—FINANCIAL HIGHLIGHTS

The following schedule summarizes our financial highlights for the nine months ended September 30, 2011 and 2010:

<i>(in thousands, except per share amounts)</i>	Nine months ended September 30,	
	2011	2010
<b>P ER SHARE DATA</b>		
<b>Net asset value at beginning of period <sup>(a)</sup></b>	<b>\$ 7.54</b>	<b>\$ 8.06</b>
<b>Net (loss) income <sup>(b)</sup></b>		
Net operating income before investment loss, (loss) gain on extinguishment of debt and income tax provision	0.40	0.38
Net change in unrealized appreciation (depreciation) on investments	—	(0.35)
Net realized (loss) gain on investments	(0.97)	0.02
(Loss) gain on extinguishment of debt	(0.01)	0.04
Income tax provision	—	(0.03)
Net (loss) income	<u>(0.58)</u>	<u>0.06</u>
<b>Net decrease in net assets resulting from distributions</b>	<b>(0.49)</b>	<b>(0.23)</b>
<b>Net (decrease) increase in net assets relating to stock-based transactions</b>		
Issuance of shares of restricted common stock <sup>(c)</sup>	(0.05)	(0.02)
Net increase in stockholders' equity from restricted stock amortization	0.02	0.05
Net (decrease) increase in net assets relating to share issuances	<u>(0.03)</u>	<u>0.03</u>
Net asset value at end of period <sup>(a)</sup>	<b>\$ 6.44</b>	<b>\$ 7.92</b>
<b>M ARKET PRICE PER SHARE</b>		
Beginning of period	\$ 6.97	\$ 4.32
End of period	\$ 3.96	\$ 5.84
<b>T OTAL RETURN <sup>(d)</sup></b>	<b>(36.59)%</b>	<b>37.73%</b>
<b>S HARES OF COMMON STOCK OUTSTANDING <sup>(d)</sup></b>		
Weighted-average—basic and diluted	76,173	76,469
End of period	77,035	76,542
<b>N ET ASSETS</b>		
Average (annualized)	\$549,377	\$614,544
End of period	\$496,481	\$606,078
<b>R ATIOS ( ANNUALIZED )</b>		
Operating expenses to average net assets	8.77%	8.14%
Net operating income to average net assets	7.35%	6.24%
General and administrative expense to average net assets	2.22%	1.91%
Return on average equity	(10.74)%	1.02%

<sup>(a)</sup> Based on total number of shares outstanding.

<sup>(b)</sup> Based on weighted-average number of shares outstanding.

<sup>(c)</sup> Represents the effects of shares issued during the period and the lapsing of forfeiture provisions on restricted stock on earnings per share.

<sup>(d)</sup> Total return = [(ending market price per share – beginning market price per share + dividends paid per share) / beginning market price per share].

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### NOTE 13—SUBSEQUENT EVENTS

Effective October 31, 2011, or the Effective Date, Mr. Steven F. Tunney, Sr. resigned in order to pursue other interests and will no longer serve as Chief Executive Officer or President of the Company or as a member of our board of directors. In connection with Mr. Tunney's departure, on the Effective Date, we entered in to a letter agreement, or Letter Agreement, with Mr. Tunney, which sets forth the terms of his separation from the Company in accordance with his pre-existing employment agreement. Under the terms of the Letter Agreement, Mr. Tunney's resignation will be treated as a "termination without cause" for purposes of his employment agreement. Mr. Tunney will receive: (i) his accrued and unpaid base salary and paid time off and unreimbursed business expenses, in each case accrued through the Effective Date; (ii) full and immediate vesting and/or lapsing of forfeiture conditions of 67,135 shares of time-vesting restricted stock; (iii) his accrued balance under the Company's tax-qualified savings plan and Supplemental Non-Qualified Retirement Plan; and (iv) immediate payout of \$154,333.33 of long-term incentive cash awards. Mr. Tunney will also receive a severance amount of \$2,244,600, representing an amount equal to two times the sum of his current base salary and his target annual bonus, payable in installments over the 24-month period following the Effective Date. We will also pay the employer's portion of the insurance benefits for continuation of Mr. Tunney's participation in our group medical, dental and hospitalization plans for a period following the Effective Date. In addition, we will reimburse Mr. Tunney's attorney's fees in connection with the negotiation of the Letter Agreement. Receipt of certain separation benefits is subject to Mr. Tunney's execution and non-revocation of a release of claims against the Company and his continued compliance with certain non-competition and other obligations. During the quarter ending December 31, 2011, we will record a liability and recognize as a general and administrative expense of approximately \$2.5 million for severance and other obligations payable under the terms of the Letter Agreement.

Also on October 31, 2011, our board of directors appointed Mr. Richard W. Neu, 55, the chairman of our board of directors, as the Chief Executive Officer of the Company, and B. Hagen Saville, 50, our Executive Vice President of Business Development and a member of our board of directors, as our President and Chief Operating Officer. Concurrently, Mr. Neu stepped down from each of the audit committee and nominating and corporate governance committee of our board of directors, but will continue to serve on the investment and valuation committee. As of the date of this report, new compensation and benefit arrangements with Mr. Neu and Mr. Saville have not been determined.

Our SunTrust Warehouse contains a provision that if either Steven F. Tunney or B. Hagen Saville ceases to be involved actively in the management of MCG and is not replaced by a person reasonably acceptable to SunTrust within 90 consecutive calendar days of such occurrence, we would be in default under such facility. Mr. Tunney resigned from MCG effective October 31, 2011 and Richard W. Neu was appointed as the Chief Executive Officer. If SunTrust does not accept Mr. Neu as a reasonably acceptable replacement or if we lose the services of Mr. Saville and are unable to identify and hire a suitably qualified replacement, it could provide SunTrust with the right to accelerate the termination date of that facility and entitle the administrative agent thereunder to exercise available remedies, including selling the collateral securing this facility and applying the proceeds to reduce outstanding borrowings thereunder.

**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders  
MCG Capital Corporation

We have reviewed the accompanying consolidated balance sheet of MCG Capital Corporation, including the consolidated schedule of investments, as of September 30, 2011, and the related consolidated statements of operations, for the three- and nine- month periods ended September 30, 2011 and 2010, and the consolidated statements of changes in net assets, cash flows and financial highlights for the nine-month periods ended September 30, 2011 and 2010. These financial statements are the responsibility of MCG Capital Corporation's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the consolidated financial statements referred to above for them to be in conformity with U.S. generally accepted accounting principles.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of MCG Capital Corporation as of December 31, 2010, including the consolidated schedule of investments, and the related consolidated statements of operations, changes in net assets, cash flows, and financial highlights for the year then ended (not presented herein), and in our report dated March 4, 2011 we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying consolidated balance sheet as of December 31, 2010, including the consolidated schedule of investments, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ ERNST & YOUNG LLP

McLean, Virginia  
November 3, 2011

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### Selected Financial Data

The following table summarizes key financial data for MCG Capital Corporation for the three and nine months ended September 30, 2011 and 2010. You should refer to this data when reading our *Management's Discussion and Analysis of Financial Condition and Results of Operations* and our unaudited *Condensed Consolidated Financial Statements* and notes thereto.

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
<i>(in thousands, except per share amounts)</i>				
<b>I NCOME STATEMENT DATA</b>				
Revenue	\$ 20,710	\$ 22,571	\$ 66,221	\$ 66,085
Net operating income before net investment loss, loss on extinguishment of debt and income tax provision	5,953	11,400	30,194	28,689
Net investment loss before income tax provision	(31,052)	(9,800)	(73,444)	(25,130)
Distributable net operating income ("DNOI") <sup>(a)</sup>	6,732	12,413	32,003	32,052
Net (loss) income	(25,109)	(529)	(44,142)	4,676
<b>P ER COMMON SHARE DATA</b>				
Net operating income before net investment loss, (loss) gain on extinguishment of debt and income tax provision per common share—basic and diluted	\$ 0.08	\$ 0.15	\$ 0.40	\$ 0.38
DNOI per weighted-average common share—basic and diluted <sup>(a)</sup>	\$ 0.09	\$ 0.16	\$ 0.42	\$ 0.42
(Loss) earnings per weighted-average common share—basic and diluted	\$ (0.33)	\$ (0.01)	\$ (0.58)	\$ 0.06
Cash dividends declared per common share	\$ 0.17	\$ 0.12	\$ 0.49	\$ 0.23
<b>S ELECTED PERIOD - END BALANCES</b>				
Investment portfolio balances				
Fair value	\$ 824,173	\$ 924,253		
Cost	1,060,243	1,120,171		
Total assets	1,009,009	1,136,665		
Borrowings	490,019	508,899		
Total stockholders' equity	496,481	606,078		
Net asset value per common share outstanding <sup>(c)</sup>	\$ 6.44	\$ 7.92		
<b>O THER PERIOD - END DATA</b>				
Average size of investment				
Fair value	\$ 13,293	\$ 14,907		
Cost	17,101	18,067		
Number of portfolio companies	62	62		
Number of employees	39	66		
<b>R ECONCILIATION OF DNOI TO NET OPERATING INCOME BEFORE INVESTMENT LOSS , ( LOSS ) GAIN ON EXTINGUISHMENT OF DEBT AND INCOME TAX PROVISION</b>				
Net operating income before investment loss, (loss) gain on extinguishment of debt and income tax provision	\$ 5,953	\$ 11,400	\$ 30,194	\$ 28,689
Amortization of employee restricted stock awards <sup>(b)</sup>	779	1,013	1,809	3,363
DNOI <sup>(a)</sup>	\$ 6,732	\$ 12,413	\$ 32,003	\$ 32,052
<b>W EIGHTED - AVERAGE COMMON SHARES OUTSTANDING — BASIC AND DILUTED</b>	<b>76,404</b>	<b>75,486</b>	<b>76,173</b>	<b>76,469</b>
<b>N UMBER OF COMMON SHARES OUTSTANDING AT PERIOD - END</b>	<b>77,035</b>	<b>76,542</b>	<b>77,035</b>	<b>76,542</b>

<sup>(a)</sup> DNOI is net operating income before net investment loss, gain (loss) on extinguishment of debt and income tax provision, as determined in accordance with accounting principles generally accepted in the United States, or GAAP, adjusted for amortization of employee restricted stock awards. We view DNOI and the related per share measures as useful and appropriate supplements to net operating income, net (loss) income, earnings per share and cash flows from operating activities. These measures serve as an additional measure of MCG's operating performance exclusive of employee restricted stock amortization, which represents an expense of the company, but does not require settlement in cash. DNOI does include paid-in-kind, or PIK, interest and dividend income, which generally are not payable in cash on a regular basis, but rather at investment maturity or when declared. DNOI should not be considered as an alternative to net operating income, net (loss) income, earnings per share and cash flows from operating activities (each computed in accordance with GAAP). Instead, DNOI should be reviewed in connection with net operating income, net (loss) income, earnings per share and cash flows from operating activities in MCG's consolidated financial statements, to help analyze how MCG's business is performing.

<sup>(b)</sup> Results for the three and nine months ended September 30, 2011, include \$431 of amortization of employee restricted stock awards associated with our corporate restructuring. These amortization expenses are included in restructuring expense on our *Consolidated Statements of Operations*. See *Note 11—Corporate Restructuring and 2011 Retention Program* to our *Condensed Consolidated Financial Statements*.

Based on common shares outstanding at period-end.

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The following table summarizes key financial data for MCG Capital Corporation for the three months ended September 30, 2011 and 2010. You should refer to this data when reading our *Management's Discussion and Analysis of Financial Condition and Results of Operations* and our unaudited *Condensed Consolidated Financial Statements* and notes thereto.

<i>(in thousands, except per share amounts)</i>	September 30,	
	2011	2010
<b>P ORTFOLIO COMPANY DATA (F AIR V ALUE )</b>		
<b>Portfolio by type</b>		
<b>Debt investments</b>		
Senior secured debt	\$535,247	\$437,709
Subordinated debt		
Secured	124,203	187,918
Unsecured	14,411	12,241
Total debt investments	<u>673,861</u>	<u>637,868</u>
<b>Equity investments</b>		
Preferred equity	116,310	244,864
Common equity/equivalents	34,002	41,521
Total equity investments	<u>150,312</u>	<u>286,385</u>
<b>Total portfolio</b>	<u>\$824,173</u>	<u>\$924,253</u>
<b>Percentage of total portfolio</b>		
<b>Debt investments</b>		
Senior secured debt	64.9%	47.4%
Subordinated debt		
Secured	15.1	20.3
Unsecured	1.8	1.3
Total debt investments	<u>81.8</u>	<u>69.0</u>
<b>Equity investments</b>		
Preferred equity	14.1	26.5
Common equity/equivalents	4.1	4.5
Total equity investments	<u>18.2</u>	<u>31.0</u>
<b>Total portfolio</b>	<u>100.0%</u>	<u>100.0%</u>
<b>Y IELD ON AVERAGE LOAN PORTFOLIO AT FAIR VALUE</b>		
Average 90-Day LIBOR	0.3%	0.4%
Spread to average LIBOR on average loan portfolio	10.8	12.4
Impact of fee accelerations of unearned fees on paid/restructured loans	0.6	0.2
Impact of non-accrual loans	(0.8)	(1.0)
<b>Total yield on average loan portfolio</b>	<u>10.9%</u>	<u>12.0%</u>
<b>C OMPPOSITION OF LOAN PORTFOLIO BY INTEREST TYPE (F AIR V ALUE )</b>		
Percentage of loans with fixed interest rates	11.4%	30.7%
Percentage of loans with floating interest rates	88.6%	69.3%
<b>P ERCENTAGE OF TOTAL DEBT INVESTMENTS (F AIR V ALUE )</b>		
Loans on non-accrual status	4.4%	4.3%
Loans greater than 90 days past due	1.6%	1.0%
<b>P ERCENTAGE OF TOTAL DEBT INVESTMENTS (C OST )</b>		
Loans on non-accrual status	11.9%	18.3%
Loans greater than 90 days past due	3.2%	2.0%
<b>W EIGHTED - AVERAGE PORTFOLIO COMPANY OPERATING METRICS <sup>(a)</sup></b>		
Annual revenue <sup>(b)(c)</sup>	\$324,924	\$160,605
Annual EBITDA <sup>(b)(c)</sup>	33,423	29,873
Loan to value of non-broadly syndicated portfolio companies	59.8%	60.3%
Trailing twelve-month equity EBITDA multiple <sup>(b)(c)(d)</sup>	8.0x	7.6x
Forward twelve-month equity EBITDA multiple <sup>(b)(c)(d)</sup>	7.1x	7.4x
EBITDA to interest ratio <sup>(b)</sup>	3.8x	2.8x
Debt to EBITDA ratio on the debt portfolio <sup>(e)</sup>	4.8x	4.8x

<sup>(a)</sup> Weighted based on the portfolio company's fair value as of the respective period end.

<sup>(b)</sup> Excludes portfolio companies with limited or no operations.

<sup>(c)</sup> Excludes public equity portfolio companies.

<sup>(d)</sup> Excludes portfolio companies valued on a liquidation basis.

<sup>(e)</sup> The maximum debt to EBITDA ratio is limited to 15x.



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### ITEM 2. 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 Condensed Consolidated Financial Statements and notes thereto appearing elsewhere in this Quarterly Report on Form 10-Q.*

*This Quarterly Report on Form 10-Q, including Management's Discussion and Analysis of Financial Condition and Results of Operations, contains forward-looking statements that involve substantial risks and uncertainties. These forward-looking statements are not historical facts, but rather are based on current expectations, estimates, forecasts, projections, intentions, goals, strategies, plans, prospects and the beliefs and assumptions of our management including, without limitation: our expectations regarding our results of operations, including revenues, net operating income, distributable net operating income, net investment losses and general and administrative expenses and the factors that may affect such results; our expectations regarding the full use before expiration of certain financial instruments, including loans, participations in loans, guarantees, letters of credit and other financial commitments; our intentions regarding the use of independent valuation firms to provide additional support for our internal analyses; our expectations regarding a second SBIC license; our belief that our restructuring plan reflects our focus on originating high-yielding debt securities, aligns the size of our organization with our asset base and establishes an efficient framework that we believe is scalable with our assets; the aggregate charges associated with our corporate restructuring and the estimated savings related to such restructuring; our belief that our inability to access the equity and debt markets has impacted our growth; the sufficiency of liquidity to meet 2011 operating requirements, as well as new origination opportunities and potential dividend distributions; the reduction of investments in equity securities to no more than 10% to 20% of the fair value of our portfolio over the next few years; our expectations regarding the origination of higher-yielding investments that meet our risk and underwriting standards; the cause of unrealized losses; the performance of our current and former portfolio companies; our decision to make dividend distributions during 2011 based on the minimum statutorily required level of distributions, gains and losses recognized for tax purposes, portfolio transactional events, our liquidity, cash earnings and our BDC asset coverage ratio; the limitation of future investing activities principally to debt investments; our level of investments in control companies beyond those that are currently in our portfolio; the timing of, and our ability to, repurchase equity, additional debt securities and make stockholder distributions; our expectations regarding the repayment of outstanding debt; general market conditions; the state of the economy and the potential for future growth and other factors. Forward-looking statements can be identified by terminology such as "anticipate," "believe," "could," "could increase the likelihood," "hope," "target," "project," "goals," "potential," "predict," "might," "estimate," "expect," "intend," "is planned," "may," "should," "will," "will enable," "would be expected," "look forward," "may provide," "would" or similar terms, variations of such terms or the negative of those terms. These statements are not guarantees of future performance and are subject to risks, uncertainties, and other factors, some of which are beyond our control and difficult to predict. Important factors could cause our actual results to differ materially from those indicated or implied by forward-looking statements. Such factors that could cause or contribute to such differences include those risk factors discussed in Item IA of Part II of this Quarterly Report on Form 10-Q.*

*Although we believe that the assumptions on which these forward-looking statements are based are reasonable, any of those assumptions could prove to be inaccurate, and as a result, the forward-looking statements based on those assumptions also could be incorrect. In light of these and other uncertainties, the inclusion of a projection or forward-looking statement in this Quarterly Report on Form 10-Q should not be regarded as a representation by us that our plans and objectives will be achieved. You should not place undue reliance on these forward-looking statements, which apply only as of the date of this Quarterly Report on Form 10-Q. We undertake no obligation to update or revise any forward-looking statements for any reason, even if new information becomes available or other events occur in the future.*

### DESCRIPTION OF BUSINESS

We are a solutions-focused commercial finance company providing capital and advisory services to middle-market companies throughout the United States. For our core portfolio, we make debt and equity investments primarily in companies with annual revenue of \$20 million to \$200 million and earnings before interest, taxes, depreciation and amortization, or EBITDA, of \$3 million to \$25 million, which we refer to as "middle-market" companies. Generally, our portfolio companies use our capital investment to finance acquisitions, recapitalizations, buyouts, organic growth and working capital. We identify and source new portfolio companies through multiple channels, including private equity sponsors, investment bankers, brokers, fund-less sponsors, institutional syndication partners, other club lenders and owner operators.

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Currently, we use borrowings under Solutions Capital I L.P., our wholly owned subsidiary, licensed as a small business investment company, or SBIC, under the Small Business Investment Act of 1958, as amended, or SBIC Act, to fund unitranche, second lien and subordinated debt investments. Historically, we have also purchased rated syndicated private debt in larger companies through our on-balance sheet securitization trust—Commercial Loan Trust 2006-1. This securitized trust included a five-year reinvestment period, during which the trust was permitted to use principal collections received from repayments of the underlying collateral to purchase new collateral from us. The reinvestment period ended on July 20, 2011 and all future principal collections received will be used to repay the securitized debt. On October 20, 2011, the next payment date for this facility, we used \$80.2 million of securitized cash in that facility (primarily representing previous principal collections) to repay a portion of this facility.

We are an internally managed, non-diversified, closed-end investment company that has elected to be regulated as a business development company, or BDC, under the *Investment Company Act of 1940, as amended*, or the 1940 Act. As a BDC we must meet various regulatory tests, which include investing at least 70% of our total assets in private or thinly traded public U.S.-based companies and meeting a 200% asset coverage ratio of total net assets to total senior securities, which include most of our borrowings (including accrued interest payable) and any preferred stock we may issue in the future. In addition, we have elected to be treated for federal income tax purposes as a regulated investment company, or RIC, under Subchapter M of the Internal Revenue Code. In order to continue to qualify as a RIC for federal income tax purposes and obtain favorable RIC tax treatment, we must meet certain requirements, including certain minimum distribution requirements. If we satisfy these requirements, we generally will not have to pay corporate-level taxes on any income we distribute to our stockholders as distributions, allowing us to substantially reduce or eliminate our corporate-level tax liability. From time to time, our wholly owned subsidiaries may execute transactions that trigger corporate-level tax liabilities. In such cases, we recognize a tax provision in the period when it becomes more likely than not that the taxable event will occur.

### **R E C E N T D E V E L O P M E N T S**

#### *O V E R V I E W O F R E S U L T S O F O P E R A T I O N S*

There were a number of indicators of modest growth in the United States' economy during the first nine months of 2011. However, certain leading and lagging indicators suggest near-term volatility and a slowdown of the United States' economy. Our financial and operating results, including those of a number of our portfolio companies, continue to be affected by the stagnation of the economy.

During the three months ended September 30, 2011, we reported a net loss of \$25.1 million, or \$0.33 per diluted share, compared to a net loss of \$0.5 million, or \$0.01 per diluted share, during the three months ended September 30, 2010. This increase in net loss resulted primarily from a \$21.3 million increase in net investment loss and a \$5.4 million decrease in our net operating income, partially offset by a \$1.7 million decrease in income tax provision.

Our net operating income during the three months ended September 30, 2011 was \$6.0 million, or \$0.08 per diluted share, compared to \$11.4 million, or \$0.15 per diluted share, during the three months ended September 30, 2010. This \$5.4 million, or 47.8%, decrease in our operating income from the comparable period in 2010 reflects a \$3.6 million, or 32.1%, increase in total operating expense and a decrease in total revenue by \$1.9 million, or 8.2%. The increase in total operating expense resulted primarily from \$4.1 million in restructuring expense and a \$1.4 million, or 58.7%, increase in general and administrative expense due to higher professional fees related to portfolio litigation and other corporate initiatives, partially offset by a decrease in compensation expense by \$1.5 million, or 33.2%, primarily due to a decrease in employee compensation and the timing of the recognition of certain stock-based compensation. In addition, interest expense decreased by \$0.4 million, or 8.5%, due to a narrowing of the interest rate spread and a decrease in the average LIBOR from the third quarter of 2010 compared to the third quarter of 2011. The decrease in total revenue primarily resulted from a \$2.4 million, or 12.2%, decrease in interest income reflecting a 161 basis-point decrease in our spread to LIBOR offset by increases in our loan fee income and advisory fee income.

During the quarter ended September 30, 2011, we recorded net investment losses of \$31.1 million, which primarily resulted from a \$24.7 million decrease in the fair value of our investment in Broadview Networks Holdings, Inc., or Broadview. Broadview is a publicly traded commercial local exchange carrier, or CLEC. We recorded \$24.7 million of unrealized depreciation on our Broadview investment primarily to reflect, among other factors, continuing challenges in the bond market, a recent downgrade of Broadview's corporate credit rating, delays by Broadview in refinancing its debt, as well as the near-term maturities of Broadview's debt facilities. As of June 30, 2011, Broadview had \$17.1 million of borrowings outstanding under its revolving credit facility, which

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becomes payable on February 23, 2012. In addition, as of June 30, 2011, Broadview had \$301.4 million of outstanding senior secured notes, which will mature on September 1, 2012. If Broadview is unable to refinance these debt facilities by their respective maturity dates, the value of our portfolio investment in Broadview could decline by up to the remaining fair value at September 30, 2011, and we may be required to recognize additional unrealized depreciation on this investment. During the quarter ended September 30, 2011, we also recorded \$5.6 million of unrealized depreciation on our investment in Jet Plastica Investors, LLC, or Jet Plastica, to reflect a decrease in the multiple that we use to value the company and in that company's operating performance.

A more detailed discussion of our results of operations for the quarter ended September 30, 2011 begins on page 57.

### *A CCESS TO C APITAL AND L IQUIDITY*

The availability of debt and equity capital continues to be constrained. We believe that we will continue to be constrained by the limited access we have to debt and equity capital. Because our stock continues to trade below net asset value and we do not have stockholder approval to sell equity below our net asset value, we effectively lack access to the equity markets. Lenders, in general, may be reluctant to extend credit to us without such equity capital markets access.

As of September 30, 2011, we had \$70.9 million of cash and cash equivalents and cash in restricted accounts that we could use to fund our new investments, operating requirements and dividend distributions. In addition, we had \$99.4 million of cash in securitization accounts, including \$13.1 million in our Commercial Loan Funding Trust which could be used to fund our new investments or make interest and principal payments on our securitized borrowings and \$86.3 million in our Commercial Loan Trust 2006-1 that may only be used to make interest and principal payments on our securitized borrowings or distributions to MCG as in accordance with the indenture agreement. The reinvestment period for Commercial Loan Trust 2006-1 ended on July 20, 2011 and all subsequent principal collections received will be used to repay the securitized debt. On October 20, 2011, the next payment date for this facility, we used \$80.2 million of securitized cash (primarily representing previous principal collections) to repay a portion of this facility.

In January 2011, the United States Small Business Administration, or SBA, increased its total commitment for potential borrowings from \$130.0 million to \$150.0 million. As of September 30, 2011, \$108.6 million of SBA borrowings were outstanding. In addition, as of September 30, 2011, we had \$41.4 million of funded borrowing capacity to originate new investments in our wholly owned subsidiary, Solutions Capital I, L.P., or Solutions Capital, subject to approval by the SBA. In January 2011, we also obtained a liquidity renewal from SunTrust Bank for our warehouse financing facility, or SunTrust Warehouse, and amended this facility to provide for a final legal maturity of January 2014.

In March 2011, we formed Solutions Capital II, L.P., and in May 2011, we submitted a license application to the SBA for a second SBIC license under Solutions Capital II, L.P. After discussions with the SBA, we elected to withdraw our application for a second license until the SBA has an opportunity to evaluate, among other things, the organizational impact of our recent restructuring and changes in management. We may seek to re-file our application for a second license within six months. There is no assurance that, if filed, the SBA will grant the additional license.

### *D EPARTURE A ND A PPOINTMENT OF C ERTAIN O FFICERS*

Effective October 31, 2011, or the Effective Date, Mr. Steven F. Tunney, Sr. resigned in order to pursue other interests and will no longer serve as Chief Executive Officer or President of the Company or as a member of our board of directors. In connection with Mr. Tunney's departure, on the Effective Date, we entered in to a letter agreement, or Letter Agreement, with Mr. Tunney, which sets forth the terms of his separation from the Company in accordance with his pre-existing employment agreement. Under the terms of the Letter Agreement, Mr. Tunney's resignation will be treated as a "termination without cause" for purposes of his employment agreement. Mr. Tunney will receive: (i) his accrued and unpaid base salary and paid time off and unreimbursed business expenses, in each case accrued through the Effective Date; (ii) full and immediate vesting and/or lapsing of forfeiture conditions of 67,135 shares of time-vesting restricted stock; (iii) his accrued balance under the Company's tax-qualified savings plan and Supplemental Non-Qualified Retirement Plan; and (iv) immediate payout of \$154,333.33 of long-term incentive cash awards. Mr. Tunney will also receive a severance amount of \$2,244,600, representing an amount equal to two times the sum of his current base salary and his target annual bonus, payable in installments over the 24-month period following the Effective Date. We will also pay the employer's portion of the insurance benefits for continuation of Mr. Tunney's participation in our group medical, dental and hospitalization plans for a period following the Effective Date. In addition, we will reimburse

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Mr. Tunney's attorney's fees in connection with the negotiation of the Letter Agreement. Receipt of certain separation benefits is subject to Mr. Tunney's execution and non-revocation of a release of claims against us and his continued compliance with certain non-competition and other obligations. During the quarter ending December 31, 2011, we expect to record a liability and recognize as a general and administrative expense of approximately \$2.5 million for severance and other obligations payable under the terms of Mr. Tunney's Letter Agreement.

Also on October 31, 2011, our board of directors appointed Mr. Richard W. Neu, 55, the chairman of our board of directors, as the Chief Executive Officer of the Company, and B. Hagen Saville, 50, our Executive Vice President of Business Development and a member of our board of directors, as our President and Chief Operating Officer. Concurrently, Mr. Neu stepped down from each of the audit committee and nominating and corporate governance committee of our board of directors, but will continue to serve on the investment and valuation committee. As of the date of this report, new compensation and benefit arrangements with Mr. Neu and Mr. Saville have not been determined.

Our SunTrust Warehouse also contains a provision that if either Steven F. Tunney or B. Hagen Saville ceases to be involved actively in the management of MCG and is not replaced by a person reasonably acceptable to SunTrust within 90 consecutive calendar days of such occurrence, we would be in default under such facility. Mr. Tunney resigned from MCG effective October 31, 2011 and Richard W. Neu was appointed as the Chief Executive Officer. If SunTrust does not accept Mr. Neu as a reasonably acceptable replacement or if we lose the services of Mr. Saville and are unable to identify and hire a suitably qualified replacement, it could provide SunTrust with the right to accelerate the termination date of that facility and entitle the administrative agent thereunder to exercise available remedies, including selling the collateral securing this facility and applying the proceeds to reduce outstanding borrowings thereunder.

### *CORPORATE RESTRUCTURING*

We are restructuring our business to simplify our organizational structure, refine operations and reduce annual operating expenses. On August 1, 2011, our board of directors approved a plan to reduce our workforce by 42%, including 22 current employees and 5 recent resignations. As of September 30, 2011, we had 39 employees, which we expect to decline to 37 employees after the corporate restructuring is completed. We believe this plan, which includes a cost reduction initiative, reflects our focus on originating high-yielding debt securities to the extent funds are available, aligns the size of our organization with our asset base and establishes an efficient framework that is scalable with our assets. The workforce reduction sizes the organization at a level appropriate for our expected near-term objectives. Affected employees are eligible to receive severance pay, continuation of benefits and, for employees who previously had been awarded restricted stock, additional lapsing of restrictions associated with restricted stock awards.

We estimate that the aggregate charges associated with the plan will total \$4.3 million to \$4.4 million. These estimated costs primarily reflect severance pay and related obligations. During the nine-months ended September 30, 2011, we incurred \$4.2 million of restructuring expenses, which we reported as a separate line item on our *Consolidated Statements of Operations*. We expect we will incur approximately \$115,000 to \$120,000 of additional restructuring charges during the remainder of 2011. During 2012 and 2013, we expect to record restructuring charges of \$65,000 and \$14,000, respectively, which represent the accretion costs of severance benefits. We will account for these costs in accordance with *ASC 420-10—Exit or Disposal Cost Obligations*. We expect these actions, when combined with the closure of one of our offices and other planned reductions in our general and administrative expense will result in approximately \$6.7 million to \$7.0 million of expected savings through the five quarters ending December 31, 2012.

In addition to the reduction in our workforce, we will also close our Richmond, Virginia office, which houses certain of our accounting operations, prior to the December 2011 expiration of the lease for that office. We are also seeking to sublet a portion of our office in Arlington, Virginia. As of September 30, 2011, we continued to use the Richmond and Arlington offices and did not have a firm expectation if, or when, we would cease to use these offices. As a result, no restructuring charges have been reflected for either a sublease of a portion of our Arlington office or the closure of our Richmond office.

### *2011 RETENTION PROGRAM*

On August 1, 2011, our board of directors approved the *MCG Capital Corporation 2011 Retention Program*, or the Retention Program, for the benefit of our employees, including one of our named executive officers, but excluding our: i) President and Chief Executive Officer; ii) Executive Vice President and Chief Financial Officer; iii)

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Executive Vice President of Business Development; and iv) Senior Vice President, General Counsel and Chief Compliance Officer. We designed the Retention Program to provide eligible employees with certain incentives related to their past service and continuing employment with MCG. The Retention Program consists of an aggregate of \$1.3 million in cash and up to 114,750 shares of restricted common stock.

Under the Retention Program, we awarded a cash bonus to eligible employees, representing a specified percentage of each eligible employee's respective annual cash bonus target for the fiscal year ending December 31, 2011. We will pay the incentive bonus to eligible employees in two equal installments on each of March 31, 2012 and September 30, 2012, subject to continued employment with MCG. Certain employees also received shares of restricted common stock under the *MCG Capital Corporation 2006 Employee Restricted Stock Plan*, as amended, or the 2006 Plan. The forfeiture provisions with respect to 50% of the shares of restricted common stock subject to each retention stock award will lapse on each of March 31, 2012 and September 30, 2012.

### PORTFOLIO COMPOSITION AND INVESTMENT ACTIVITY

As of September 30, 2011, the fair value of our investment portfolio was \$824.2 million, which represents a \$185.5 million, or 18.4%, decrease from the \$1,009.7 million fair value as of December 31, 2010. The following sections describe the composition of our investment portfolio as of September 30, 2011 and describe key changes in our portfolio during the nine months ended September 30, 2011.

#### PORTFOLIO COMPOSITION

The following table summarizes the composition of our investment portfolio *at fair value* :

<i>(dollars in thousands)</i>	September 30, 2011		December 31, 2010	
	Investments at Fair Value	Percent of Total Portfolio	Investments at Fair Value	Percent of Total Portfolio
<b>Debt investments</b>				
Senior secured debt	\$ 535,247	64.9%	\$ 555,667	55.0%
Subordinated debt				
Secured	124,203	15.1	190,309	18.9
Unsecured	14,411	1.8	12,321	1.2
<b>Total debt investments</b>	<b>673,861</b>	<b>81.8</b>	<b>758,297</b>	<b>75.1</b>
<b>Equity investments</b>				
Preferred equity	116,310	14.1	218,690	21.7
Common/common equivalents equity	34,002	4.1	32,718	3.2
<b>Total equity investments</b>	<b>150,312</b>	<b>18.2</b>	<b>251,408</b>	<b>24.9</b>
<b>Total investments</b>	<b>\$ 824,173</b>	<b>100.0%</b>	<b>\$ 1,009,705</b>	<b>100.0%</b>

Our debt instruments bear contractual interest rates ranging from 2.5% to 17.5%, a portion of which may be in the form of paid in kind interest. As of September 30, 2011, approximately 88.6% of the fair value of our loan portfolio had variable interest rates, based on a LIBOR benchmark or prime rate, and 11.4% of the fair value of our loan portfolio had fixed interest rates. As of September 30, 2011, approximately 76.8% of our loan portfolio, at fair value, had LIBOR floors between 1.0% and 3.0% on the LIBOR base index and prime floors between 1.75% and 6.0%. At origination, our loans generally have four- to eight-year stated maturities. Borrowers typically pay an origination fee based on a percentage of the total commitment and a fee on undrawn commitments.

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The following table summarizes our investment portfolio by industry at *fair value* :

<i>(dollars in thousands)</i>	September 30, 2011		December 31, 2010	
	Investments	Percent of	Investments at	Percent of
	at Fair Value	Total Portfolio	Fair Value	Total Portfolio
Healthcare	\$ 86,703	10.5%	\$ 76,358	7.6%
Business services	81,021	9.8	87,897	8.7
Manufacturing	79,959	9.7	54,178	5.4
Education	69,065	8.4	43,704	4.3
Communications	53,767	6.5	150,907	14.9
Plastic products	43,884	5.3	33,633	3.3
Cable	41,630	5.1	92,467	9.2
Technology	36,274	4.4	35,327	3.5
Information services	35,427	4.3	17,940	1.8
Logistics	34,260	4.2	28,036	2.8
Electronics	32,391	3.9	30,409	3.0
Broadcasting	31,521	3.8	53,996	5.3
Publishing	30,682	3.7	22,543	2.2
Food services	29,147	3.5	73,407	7.3
Insurance	24,637	3.0	24,993	2.5
Repair services	20,175	2.4	—	—
Auto parts	19,641	2.4	16,959	1.7
Entertainment	13,793	1.7	11,782	1.2
Home furnishings	13,400	1.6	17,151	1.7
Restaurants	9,893	1.2	11,150	1.1
Agriculture	9,539	1.2	8,418	0.8
Cosmetics	8,408	1.0	—	—
Consumer products	4,692	0.6	9,016	0.9
Other media	2,474	0.3	7,430	0.7
Diversified financial services	2,154	0.3	12,489	1.2
Leisure activities	—	—	32,216	3.2
Sporting goods	—	—	42,886	4.2
Other <sup>(a)</sup>	9,636	1.2	14,413	1.5
<b>Total</b>	<b>\$ 824,173</b>	<b>100.0%</b>	<b>\$ 1,009,705</b>	<b>100.0%</b>

<sup>(a)</sup> No individual industry within this category exceeds 1%.

As of September 30, 2011, our ten largest portfolio companies represented approximately 39.5% of the total fair value of our investments. These ten companies accounted for 30.2% of our total revenue during the nine months ended September 30, 2011. In addition, we have concentrations in the healthcare, business services and communications industries.

During the nine months ended September 30, 2011, we had concentrations in certain industries, including the healthcare, business services and communications industries. The following table summarizes, our fair value and revenue concentrations in each of those industries:

<i>(dollars in thousands)</i>	Investments at Fair Value				Revenue for the nine months ended			
	September 30, 2011		December 31, 2010		September 30, 2011		September 30, 2010	
	Amount	% of Total Portfolio	Amount	% of Total Portfolio	Amount	% of Total Revenue	Amount	% of Total Revenue
<b>Industry</b>								
Healthcare	\$86,703	10.5%	\$ 76,358	7.6%	\$8,287	12.5%	\$8,586	13.0%
Business services	81,021	9.8	87,897	8.7	7,295	11.0	3,150	4.8
Communications <sup>(a)</sup>	53,767	6.5	150,907	14.9	2,379	3.6	2,781	4.2

<sup>(b)</sup> Includes Broadview, which represented \$29.2 million, or 3.5%, and \$103.0 million, or 10.2%, of the fair value of our investment portfolio as of September 30, 2011 and December 31, 2010, respectively.

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### *C HANGES IN I NVESTMENT P ORTFOLIO*

During the nine months ended September 30, 2011, we completed \$270.5 million of originations and advances, including \$158.1 million of originations to 15 new portfolio companies and \$112.4 million of originations and advances to existing portfolio companies, compared to \$160.2 million of originations and advances during the nine months ended September 30, 2010. The following table summarizes our total portfolio investment activity during the nine months ended September 30, 2011 and 2010:

<i>(in thousands)</i>	Nine months ended September 30,	
	2011	2010
Beginning investment portfolio	\$1,009,705	\$ 986,346
Originations and advances	270,505	160,169
Gross payments, reductions and sales of securities	(368,937)	(196,965)
Net realized (loss) gain	(73,348)	1,988
Unrealized depreciation	(69,332)	(23,193)
Reversals of unrealized depreciation (appreciation)	69,231	(4,147)
Origination fees and amortization of unearned income	(13,651)	55
<b>Ending investment portfolio</b>	<b>\$ 824,173</b>	<b>\$ 924,253</b>

### *Originations and Advances*

The following table shows our originations and advances during the nine months ended September 30, 2011 and 2010 by security type:

<i>(dollars in thousands)</i>	Nine months ended September 30,			
	2011		2010	
	Amount	% of Total	Amount	% of Total
<b>Debt investments</b>				
Senior secured debt	\$224,300	82.9%	\$114,102	71.3%
Subordinated debt				
Secured	31,368	11.6	28,374	17.7
Unsecured	1,884	0.7	13,165	8.2
<b>Total debt investments</b>	<b>257,552</b>	<b>95.2</b>	<b>155,641</b>	<b>97.2</b>
<b>Equity investments</b>				
Preferred equity	12,444	4.6	4,527	2.8
Common/common equivalents equity	509	0.2	1	—
<b>Total equity investments</b>	<b>12,953</b>	<b>4.8</b>	<b>4,528</b>	<b>2.8</b>
<b>Total originations and advances</b>	<b>\$270,505</b>	<b>100.0%</b>	<b>\$160,169</b>	<b>100.0%</b>

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The following table shows our significant originations and advances.

(in thousands)

Company	Nine months ended September 30, 2011			
	Originations	Draws/ Advances	PIK Advances/ Dividends	Total
<b>Debt</b>				
Education Management, Inc.	\$ 25,000	\$ —	\$ —	\$ 25,000
Industrial Safety Technologies, LLC	22,747	—	—	22,747
Qualawash Holdings, LLC	20,000	—	—	20,000
Jet Plastica Investors, LLC	12,000	4,250	995	17,245
NPS Holding, LLC	15,273	500	—	15,773
Virtual Radiologic Corp.	14,000	—	—	14,000
West World Media, LLC	11,250	—	28	11,278
Focus Brands, Inc.	11,000	—	—	11,000
Bentley Systems, Inc.	10,000	—	—	10,000
Sally Holdings, LLC	10,000	—	—	10,000
Data Based Systems International, Inc.	9,000	—	220	9,220
Capstone Logistics, LLC	—	8,260	201	8,461
BarBri, Inc.	7,000	—	—	7,000
Chase Doors Holdings, Inc.	—	6,652	—	6,652
Georgia-Pacific Corporation	6,300	—	—	6,300
Tank Intermediate Holding Corp.	6,000	—	—	6,000
Harron Communications, LP	6,000	—	—	6,000
Scotsman Industries, Inc.	5,500	—	—	5,500
Visant Corporation	5,125	—	—	5,125
Savvis Communications Corporation	4,993	—	—	4,993
Excelitas Technologies Corp.	3,990	—	—	3,990
Orbitel Holdings, LLC	3,775	—	—	3,775
GSDM Holdings, Corp.	2,754	—	373	3,127
Goodman Global, Inc.	3,000	—	—	3,000
ShowPlex Cinemas, Inc.	—	2,993	—	2,993
Stratford School Holdings, Inc.	—	2,500	—	2,500
Rural/Metro Operating Company, LLC	2,000	—	—	2,000
Service Champ, Inc.	—	1,693	191	1,884
Advanced Sleep Concepts, Inc.	—	1,450	247	1,697
The Gavilon Group, LLC	1,500	—	—	1,500
Miles Media Group, LLC	—	1,500	—	1,500
Intran Media, LLC	—	1,000	229	1,229
Restaurant Technologies, Inc.	—	—	1,141	1,141
Getty Images, Inc.	1,000	—	—	1,000
Other (< \$1 million)	—	500	3,422	3,922
<b>Total debt</b>	<b>219,207</b>	<b>31,298</b>	<b>7,047</b>	<b>257,552</b>
<b>Equity</b>				
Orbitel Holdings, LLC	3,000	—	348	3,348
NDSSI Holdings, LLC	2,000	—	—	2,000
Intra Media, LLC	1,250	—	—	1,250
RadioPharmacy Investors, LLC	—	—	1,199	1,199
Equity (< \$1 million)	862	—	4,294	5,156
<b>Total equity</b>	<b>7,112</b>	<b>—</b>	<b>5,841</b>	<b>12,953</b>
<b>Total originations and advances</b>	<b>\$ 226,319</b>	<b>\$31,298</b>	<b>\$12,888</b>	<b>\$270,505</b>

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### *Repayments, Sales and Other Reductions of Investment Portfolio*

The following table shows our gross payments, reductions and sales of securities during the nine months ended September 30, 2011 and 2010 by security type:

	Nine months ended September 30,			
	2011		2010	
	Amount	% of Total	Amount	% of Total
<i>(dollars in thousands)</i>				
<b>Debt investments</b>				
Senior secured debt	\$224,375	60.8%	\$ 63,481	32.2%
Subordinated debt				
Secured	86,186	23.4	63,724	32.3
Unsecured	142	—	31,618	16.1
<b>Total debt investments</b>	<b>310,703</b>	<b>84.2</b>	<b>158,823</b>	<b>80.6</b>
<b>Equity investments</b>				
Preferred equity	56,045	15.2	25,423	12.9
Common/common equivalents equity	2,189	0.6	12,719	6.5
<b>Total equity investments</b>	<b>58,234</b>	<b>15.8</b>	<b>38,142</b>	<b>19.4</b>
Total gross payments, reductions and sales of securities	<u>\$368,937</u>	<u>100.0%</u>	<u>\$196,965</u>	<u>100.0%</u>

During the nine months ended September 30, 2011 and 2010, our gross payments, reductions and sales of securities by transaction type included:

	Nine months ended September 30,	
	2011	2010
<i>(in thousands)</i>		
Principal repayments, reductions and loan sales	\$ 251,817	\$ 110,998
Sale of equity investments	45,879	36,040
Scheduled principal amortization	38,764	30,302
Collection of accrued paid-in-kind interest and dividends	32,477	19,625
<b>Total gross payments, reductions and sales of securities</b>	<b>\$ 368,937</b>	<b>\$ 196,965</b>

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As shown in the following table, during the nine months ended September 30, 2011, we monetized all, or part of, 28 portfolio investments with proceeds totaling \$320.2 million:

<i>(in thousands)</i>	Nine months ended September 30, 2011			
	Principal Repayments, Amortization, and Loan Sales	Sale of Equity Investments	PIK Interest and Dividend Prepayments	Total
<b>Monetizations</b>				
Avenue Broadband LLC	\$ 12,864	\$ 29,153	\$ 9,182	\$ 51,199
Restaurant Technologies, Inc.	35,701	1,879	8,182	45,762
Superior Industries Investors, LLC	19,333	13,528	8,903	41,764
Teleguam Holdings, LLC	20,000	—	—	20,000
Savvis Communications Corporation	14,947	—	—	14,947
Equibrand Holding Corporation	13,080	—	1,348	14,428
The Telx Group, Inc.	13,860	—	—	13,860
Maverick Healthcare Equity, LLC	12,500	—	888	13,388
Focus Brands, Inc.	10,909	—	—	10,909
Chase Doors Holdings, Inc.	10,206	—	—	10,206
Massage Envy, LLC	10,054	—	—	10,054
Interactive Data Corporation	9,950	—	—	9,950
Visant Corporation	6,983	—	—	6,983
Allen's T.V Cable Service, Inc.	6,853	65	—	6,918
Provo Craft & Novelty, Inc.	6,704	—	—	6,704
Georgia-Pacific Corporation	6,283	—	—	6,283
Knology, Inc.	6,090	—	—	6,090
Rural/Metro Operating Company, LLC	5,985	—	—	5,985
Vox Communications Group Holdings, LLC	4,100	—	—	4,100
Excelitas Technologies Corporation	3,999	—	—	3,999
Wireco Worldgroup, Inc.	3,840	—	—	3,840
Empower IT Holdings, Inc.	3,387	—	—	3,387
The SI Organization, Inc.	3,000	—	—	3,000
Stratford School Holdings, Inc.	2,500	—	—	2,500
Active Brands International, Inc.	2,062	—	—	2,062
Getty Images, Inc.	1,015	—	—	1,015
Lambeau Telecom Company, LLC	612	—	1	613
Sunshine Media Delaware, LLC	—	228	—	228
<b>Total monetizations</b>	<b>246,817</b>	<b>44,853</b>	<b>28,504</b>	<b>320,174</b>
Other scheduled payments	43,764	1,026	3,973	48,763
<b>Total gross payments, sales and other reductions of investment portfolio</b>	<b>\$ 290,581</b>	<b>\$ 45,879</b>	<b>\$ 32,477</b>	<b>\$368,937</b>

The proceeds from these monetizations correlated closely with the most recently reported fair value of the associated investments.

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### A SSET Q UALITY

Asset quality is generally a function of portfolio company performance and economic conditions, as well as our underwriting and ongoing management of our investment portfolio. In addition to various risk management and monitoring tools, we use the following investment rating system to characterize and monitor our expected level of returns on each investment in our portfolio:

Investment Rating	Summary Description
1	Capital gain expected or realized
2	Full return of principal and interest or dividend expected with customer performing in accordance with plan
3	Full return of principal and interest or dividend expected, but customer requires closer monitoring
4	Some loss of interest or dividend expected, but still expect an overall positive internal rate of return on the investment
5	Loss of interest or dividend and some loss of principal investment expected, which would result in an overall negative internal rate of return on the investment

The following table shows the distribution of our investments on our 1 to 5 investment rating scale *at fair value* as of September 30, 2011 and December 31, 2010:

Investment Rating	September 30, 2011		December 31, 2010	
	Investments at	% of Total	Investments at	% of Total
	Fair Value	Portfolio	Fair Value	Portfolio
1	\$ 315,725 <sup>(a)</sup>	38.3%	\$ 330,605 <sup>(a)</sup>	32.7%
2	298,957	36.3	370,694	36.7
3	173,391	21.0	173,447	17.2
4 <sup>(b)</sup>	2,535	0.3	112,811	11.2
5 <sup>(c)</sup>	33,565	4.1	22,148	2.2
<b>Total</b>	<b>\$ 824,173</b>	<b>100.0%</b>	<b>\$ 1,009,705</b>	<b>100.0%</b>

<sup>(a)</sup> As of September 30, 2011 and December 31, 2010, Investment Rating "1" included \$118.0 million and \$112.2 million, respectively, of loans to companies in which we also hold equity securities.

<sup>(b)</sup> During the nine months ended September 30, 2011, approximately \$103.0 million of the reduction in Investment Rating 4 assets resulted from the reclassification of our investment in Broadview Networks Holdings, Inc. from Investment Rating 4 to Investment Rating 5.

<sup>(c)</sup> Approximately \$103.0 million of the increase in Investment Rating 5 assets resulted from the reclassification of our investment in Broadview Networks Holdings, Inc. from Investment Rating 4 to Investment Rating 5. This increase was partially offset by a \$73.8 million decrease in the fair value of Broadview Networks Holdings, Inc. from December 31, 2010 to September 30, 2011.

When one of our loans becomes more than 90 days past due, or if we otherwise do not expect the customer to be able to service its debt and other obligations, we will, as a general matter, place the loan on non-accrual status and generally will cease recognizing interest income on that loan until all principal and interest have been brought current through payment or due to a restructuring such that the interest income is deemed to be collectible. However, we may make exceptions to this policy if the loan has sufficient collateral value and is in the process of collection. If the fair value of a loan is below cost, we may cease recognizing paid-in-kind, or PIK, interest and/or the accretion of a discount on the debt investment until such time that the fair value equals or exceeds cost.

The following table summarizes loans on non-accrual status and loans greater than 90 days past due, *at cost*, as of September 30, 2011 and December 31, 2010:

(dollars in thousands)	September 30, 2011		December 31, 2010	
	Investments	% of Loan	Investments	% of Loan
	at Cost	Portfolio	at Cost	Portfolio
<b>Loans greater than 90 days past due</b>				
On non-accrual status	\$ 23,461	3.18%	\$ 10,388	1.18%
Not on non-accrual status	—	—	—	—
<b>Total loans greater than 90 days past due</b>	<b>\$ 23,461</b>	<b>3.18%</b>	<b>\$ 10,388</b>	<b>1.18%</b>
<b>Loans on non-accrual status</b>				
0 to 90 days past due	\$ 63,910	8.67%	\$ 128,989	14.69%
Greater than 90 days past due	23,461	3.18	10,388	1.18
<b>Total loans on non-accrual status</b>	<b>\$ 87,371</b>	<b>11.85%</b>	<b>\$ 139,377</b>	<b>15.87%</b>



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The following table summarizes loans on non-accrual status and loans greater than 90 days past due, *at fair value*, as of September 30, 2011 and December 31, 2010:

<i>(dollars in thousands)</i>	September 30, 2011		December 31, 2010	
	Investments at Fair Value	% of Loan Portfolio	Investments at Fair Value	% of Loan Portfolio
<b>Loans greater than 90 days past due</b>				
On non-accrual status	\$ 10,714	1.59%	\$ 6,157	0.81%
Not on non-accrual status	—	—	—	—
<b>Total loans greater than 90 days past due</b>	<u>\$ 10,714</u>	<u>1.59%</u>	<u>\$ 6,157</u>	<u>0.81%</u>
<b>Loans on non-accrual status</b>				
0 to 90 days past due	\$ 19,230	2.85%	\$ 19,835	2.62%
Greater than 90 days past due	10,714	1.59	6,157	0.81
<b>Total loans on non-accrual status</b>	<u>\$ 29,944</u>	<u>4.44%</u>	<u>\$ 25,992</u>	<u>3.43%</u>

The following table summarizes the changes in the cost and fair value of the loans on non-accrual status from December 31, 2010 through September 30, 2011:

<i>(In thousands)</i>	Nine months ended September 30, 2011	
	Cost	Fair Value
<b>Non-accrual loan balance as of December 31, 2010</b>	<u>\$139,377</u>	<u>\$ 25,992</u>
Additional loans on non-accrual status—other media	9,247	4,235
Advances to companies on non-accrual status	9,543	9,543
Loans converted to equity	(5,904)	(5,904)
Payments received on loans on non-accrual status	(7,458)	(7,458)
Change in valuation of loans on non-accrual status	—	(256)
Reversal of previously recognized unrealized loss on non-accrual loans	—	61,226 <sup>(a)</sup>
Realized loss on non-accrual loans	(57,434) <sup>(a)</sup>	(57,434) <sup>(a)</sup>
<b>Total change in non-accrual loans</b>	<u>(52,006)</u>	<u>3,952</u>
<b>Non-accrual loan balance as of September 30, 2011</b>	<u>\$ 87,371</u>	<u>\$ 29,944</u>

- (a) Primarily reflects our sales of Active Brands International, Inc. and Vox Communications Group Holdings, LLC, as well as the write-off of our investment in Total Sleep Holdings, Inc. during the nine months ended September 30, 2011. Our investments in the debt issued by these portfolio companies were on non-accrual status as of December 31, 2010. Upon the sales and write-off of these investments, we reversed the previously unrealized depreciation and recorded realized losses.

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### Results of Operations

The following section compares our results of operations for the three months ended September 30, 2011 to the three months ended September 30, 2010.

#### C O M P A R I S O N O F T H E T H R E E M O N T H S E N D E D S E P T E M B E R 3 0, 2 0 1 1 A N D 2 0 1 0

The following table summarizes the components of our net loss for the three months ended September 30, 2011 and 2010:

<i>(dollars in thousands)</i>	Three months ended September 30,		Variance	
	2011	2010	\$	Percentage
<b>Revenue</b>				
Interest and dividend income				
Interest income	\$ 17,128	\$19,519	\$ (2,391)	(12.2)%
Dividend income	1,226	1,561	(335)	(21.5)
Loan fees	1,426	810	616	76.0
Total interest and dividend income	19,780	21,890	(2,110)	(9.6)
Advisory fees and other income	930	681	249	36.6
<b>Total revenue</b>	<b>20,710</b>	<b>22,571</b>	<b>(1,861)</b>	<b>(8.2)</b>
<b>Operating expense</b>				
Interest expense	3,960	4,326	(366)	(8.5)
Employee compensation				
Salaries and benefits	2,683	3,527	(844)	(23.9)
Amortization of employee restricted stock awards	348	1,013	(665)	(65.6)
<b>Total employee compensation</b>	<b>3,031</b>	<b>4,540</b>	<b>(1,509)</b>	<b>(33.2)</b>
General and administrative expense	3,657	2,305	1,352	58.7
Restructuring expense	4,109	—	4,109	NM
<b>Total operating expense</b>	<b>14,757</b>	<b>11,171</b>	<b>3,586</b>	<b>32.1</b>
<b>Net operating income before net investment loss, loss on extinguishment of debt and income tax provision</b>	<b>5,953</b>	<b>11,400</b>	<b>(5,447)</b>	<b>(47.8)</b>
<b>Net investment loss before income tax provision</b>	<b>(31,052)</b>	<b>(9,800)</b>	<b>(21,252)</b>	<b>216.9</b>
<b>Loss on extinguishment of debt before income tax provision</b>	<b>—</b>	<b>(449)</b>	<b>449</b>	<b>(100.0)</b>
<b>Income tax provision</b>	<b>10</b>	<b>1,680</b>	<b>(1,670)</b>	<b>(99.4)</b>
<b>Net loss</b>	<b>\$(25,109)</b>	<b>\$ (529)</b>	<b>\$(24,580)</b>	<b>NM</b>

NM=Not Meaningful

#### T O T A L R E V E N U E

Total revenue includes interest and dividend income and advisory fees and other income. During the three months ended September 30, 2011, our total revenue was \$20.7 million, which represents a \$1.9 million, or 8.2%, decrease from the three months ended September 30, 2010. This decrease resulted from a \$2.4 million, or 12.2%, decrease in interest income and a \$0.3 million, or 21.5%, decrease in dividend income, which was partially offset by a \$0.6 million, or 76.0%, increase in loan fees and a \$0.2 million, or 36.6%, increase in advisory fees and other income. The following sections describe the reasons for the variances in each major component of our revenue during the three months ended September 30, 2011 from the three months ended September 30, 2010.

#### I N T E R E S T I N C O M E

The level of interest income that we earn depends upon the level of interest-bearing investments outstanding during the period, as well as the weighted-average yield on these investments. During the three months ended September 30, 2011, the total yield on our average debt portfolio at fair value was 10.9% compared to 12.0% during the three months ended September 30, 2010. The weighted-average yield varies each period because of changes in the composition of our portfolio of debt investments, changes in stated interest rates, fee accelerations of unearned fees on paid/restructured loans and the balance of loans on non-accrual status for which we are not accruing interest.

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The following table shows the various components of the total yield on our average debt portfolio at fair value for the three months ended September 30, 2011 and 2010:

	Three months ended September 30,	
	2011	2010
Average 90-day LIBOR	0.3%	0.4%
Spread to average LIBOR on average loan portfolio	10.8	12.4
Impact of fee accelerations of unearned fees on paid/restructured loans	0.6	0.2
Impact of non-accrual loans	(0.8)	(1.0)
<b>Total yield on average loan portfolio</b>	<b>10.9%</b>	<b>12.0%</b>

During the three months ended September 30, 2011, interest income was \$17.1 million, compared to \$19.5 million during the three months ended September 30, 2010, which represented a \$2.4 million, or 12.2%, decrease. This decrease reflected a \$2.6 million decrease in interest income resulting from a 161 basis-point decrease in our spread to LIBOR and a \$0.2 million decrease related to the change in LIBOR. These decreases were partially offset by a \$0.4 million increase in interest income resulting from the impact of interest rate floors.

### PIK Income

Interest income includes certain amounts that we have not received in cash, such as PIK interest. PIK interest represents contractually deferred interest that is added to the principal balance of the loan and compounded if not paid on a current basis. PIK may be prepaid by either contract or the portfolio company's choice, but generally is paid at the end of the loan term. The following table shows the PIK-related activity for the three months ended September 30, 2011 and 2010, *at cost* :

<i>(in thousands)</i>	Three months ended September 30,	
	2011	2010
Beginning PIK loan balance	\$15,279	\$ 35,862
PIK interest earned during the period	2,365	3,021
Interest receivable converted to PIK	230	3,083
Payments received on PIK loans	(2,366)	(12,704)
<b>Ending PIK loan balance</b>	<b>\$15,508</b>	<b>\$ 29,262</b>

As of September 30, 2011 and 2010, we were not accruing interest on \$6.2 million and \$7.9 million, respectively, of the PIK loans, at cost, shown in the preceding table. The payments received on PIK loans during the three months ended September 30, 2011, include \$1.7 million collected in conjunction with the partial repayment of our investment in Sagamore Hill Broadcasting, LLC, as well as PIK collected from seven other portfolio investments.

### DIVIDEND INCOME

We accrete dividends on equity investments with stated dividend rates as they are earned, to the extent that we believe the dividends will be paid ultimately and the associated portfolio company has sufficient value to support the accretion. We recognize dividends on our other equity investments when we receive the dividend payment. Our dividend income varies from period to period because of changes in the size and composition of our equity investments, the yield from the investments in our equity portfolio and the ability of the portfolio companies to declare and pay dividends.

The following table summarizes our dividend activity, at cost, for the three months ended September 30, 2011 and 2010:

<i>(in thousands)</i>	Three months ended September 30,	
	2011	2010
Beginning accrued dividend balance	\$83,541	\$90,386
Dividend income earned during the period	1,226	1,561
Dividend collections	(301)	(1,147)
Realized loss	(92)	(936)
<b>Ending accrued dividend balance</b>	<b>\$84,374</b>	<b>\$89,864</b>

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During the three months ended September 30, 2011, our dividend income was \$1.2 million, which represented a \$0.3 million, or 21.5%, decrease from the three months ended September 30, 2010. The decrease in dividend income resulted from a \$0.9 million decrease as a result of the sale of four dividend-producing investments and a \$0.4 million decrease because the fair value of two existing portfolio companies was not sufficient to support the accretion of dividends. Dividend income increased \$1.0 million primarily because the fair value of six existing portfolio companies improved sufficiently to support the accretion of dividends.

### *LOAN FEES*

Loan fees include origination fees on loans that we defer and amortize into interest income over the life of the loan. When repayments or restructurings with major modifications occur, we accelerate the recognition of previously unamortized loan origination fees into loan income. These accelerations have the effect of increasing current period income and may reduce future amortizable income. Because the repayments and restructurings may vary from period to period, the level of loan origination fees included in interest income may also vary. During the three months ended September 30, 2011, our loan fees increased \$0.6 million, or 76.0%, compared to the same period in 2010 due to higher repayments in the third quarter of 2011.

### *ADVISORY FEES AND OTHER INCOME*

Advisory fees and other income primarily include fees related to advisory and management services, equity structuring fees, syndication fees, prepayment fees, bank interest and other income. Generally, advisory fees and other income relate to specific transactions or services and, therefore, may vary from period to period depending on the level and types of services provided. During the three months ended September 30, 2011, we earned \$0.9 million of advisory fees and other income, which represented a \$0.2 million, or 36.6%, increase from the three months ended September 30, 2010. This increase was attributable primarily to advisory fees earned in conjunction with the origination of four investments during the three months ended September 30, 2011 compared with two new investments during the three months ended September 30, 2010.

### *TOTAL OPERATING EXPENSE*

Total operating expense includes interest, employee compensation, general and administrative expense, and restructuring expense. During the three months ended September 30, 2011, we incurred \$14.8 million of operating expense, representing a \$3.6 million, or 32.1%, increase from the same quarter in the prior year. This increase was primarily the result of \$4.1 million of expenses related to our corporate restructuring that were incurred during the quarter ended September 30, 2011 and a \$1.4 million increase in general and administrative expense from the three months ended September 30, 2010. These increases were partially offset by a \$1.5 million decrease in employee compensation expense and a \$0.4 million decrease in interest expense. The reasons for these variances are discussed in more detail below. See *Recent Developments* for a discussion of our corporate restructuring and retention programs and the impact that we estimate that the implementation of these programs will have on our future operating expense.

### *INTEREST EXPENSE*

During the three months ended September 30, 2011, we incurred \$4.0 million of interest expense, which represented a \$0.4 million, or 8.5%, decrease from the same period in 2010. A narrowing of the interest rate spread from 2.31% during the three months ended September 30, 2010 to 2.12% during the three months ended September 30, 2011 caused interest expense to decrease by \$0.3 million. In addition, a reduction in average LIBOR from 0.39% in the third quarter of 2010 to 0.30% in the third quarter of 2011 reduced interest expense by \$0.1 million, and a decrease in average borrowing balance in the third quarter of 2011 from the third quarter of 2010 further reduced interest expense by \$0.2 million. These decreases were offset by a \$0.2 million increase in our amortization of debt issuance costs.

### *EMPLOYEE COMPENSATION*

Employee compensation expense includes base salaries and benefits, variable annual incentive compensation and amortization of employee stock awards. During the three months ended September 30, 2011, our employee compensation expense was \$3.0 million, which represented a \$1.5 million, or 33.2%, decrease from the same period in 2010. Our salaries and benefits decreased by \$0.8 million, or 23.9%, primarily due to a \$0.3 million decrease in salaries, a \$0.3 million decrease in incentive compensation, and a \$0.2 million decrease in payroll taxes and benefits, which primarily resulted from a 42% reduction in our workforce that occurred as part of our

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corporate restructuring that we implemented during the three months ended September 30, 2011. See *Recent Developments* for a discussion of our corporate restructuring and retention programs and the impact that we estimate that the implementation of these programs will have on our future employee compensation expense.

During the three months ended September 30, 2011, we recognized \$0.3 million of compensation expense related to restricted stock awards, compared to \$1.0 million for the three months ended September 30, 2010, which represented a \$0.7 million, or 65.6%, decrease. The lapsing of forfeiture provisions for previously awarded restricted stock accounted for the reduction in amortization of employee restricted stock. This lapsing of forfeiture provisions more than offset the amortization of restricted stock awarded during the three months ended September 30, 2011.

### *GENERAL AND ADMINISTRATIVE*

During the three months ended September 30, 2011, general and administrative expense was \$3.7 million, which represented a \$1.4 million, or 58.7%, increase from the same period in 2010. This increase was primarily the result of professional fees paid for portfolio related litigation and other corporate initiatives undertaken during the third quarter of 2011. See *Recent Developments* for a discussion of our corporate restructuring and retention programs and the impact that we estimate that the implementation of these programs will have on our future general and administrative expenses.

### *RESTRUCTURING*

During the nine months ended September 30, 2011, we incurred \$4.1 million of restructuring expense, related to the corporate restructuring approved by our board of directors on August 1, 2011. Virtually all of these expenses represent severance-related obligations to our former employees. We anticipate that during the quarter ending December 2011, we will incur approximately \$115,000 to \$120,000 of additional restructuring expenses related to the closure of our Richmond office by December 31, 2011. During the twelve months ending December 31, 2012 and 2013, we expect to record restructuring charges of \$65,000 and \$14,000, respectively, which represent the accretion costs associated with the severance benefits for employees. See *Recent Developments* for a discussion of our corporate restructuring and the impact that we estimate that the implementation of the restructuring will have on our future expenses.

### *NET OPERATING INCOME BEFORE NET INVESTMENT LOSS, LOSS ON EXTINGUISHMENT OF DEBT AND INCOME TAX PROVISION*

Net operating income before net investment loss, loss on extinguishment of debt and income tax provision for the three months ended September 30, 2011 totaled \$6.0 million, compared with \$11.4 million for the three months ended September 30, 2010. This decrease was due to the items discussed above.

### *DISTRIBUTABLE NET OPERATING INCOME*

Distributable net operating income, or DNOI, is net operating income before net investment loss, (loss) gain on extinguishment of debt and income tax provision, as determined in accordance with accounting principles generally accepted in the United States, or GAAP, adjusted for amortization of employee restricted stock awards. We view DNOI and the related per share measures as useful and appropriate supplements to net operating income, net (loss) income, earnings (loss) per share and cash flows from operating activities. These measures serve as an additional measure of MCG's operating performance exclusive of employee restricted stock amortization, which represents an expense of the company, but does not require settlement in cash. DNOI does include PIK interest and dividend income, which generally are not payable in cash on a regular basis, but rather at investment maturity or when declared. DNOI should not be considered as an alternative to net operating income, net income (loss), earnings (loss) per share or cash flows from operating activities (each computed in accordance with GAAP). Instead, DNOI should be reviewed in connection with net operating income, net income (loss), earnings (loss) per share and cash flows from operating activities in MCG's consolidated financial statements, to help analyze how MCG's business is performing.

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During the three months ended September 30, 2011, DNOI was \$6.7 million, or \$0.09 per share, compared to \$12.4 million, or \$0.16 per share for the three months ended September 30, 2010. The following table shows a reconciliation of our reported net operating income before net investment loss, loss on extinguishment of debt and income tax provision to DNOI for the quarters ended September 30, 2011 and 2010:

	Three months ended September 30,	
	2011	2010
<i>(in thousands, except per share data)</i>		
Net operating income before net investment loss, loss on extinguishment of debt and income tax provision	\$ 5,953	\$11,400
Amortization of employee restricted stock awards <sup>(a)</sup>	779	1,013
<b>DNOI</b>	<b>\$ 6,732</b>	<b>\$12,413</b>
<b>Per common share data (basic and diluted)</b>		
Weighted-average common shares outstanding	76,404	75,486
Loss per common share	\$ (0.33)	\$ (0.01)
Net operating income before net investment loss, loss on extinguishment of debt and income tax provision per common share	\$ 0.08	\$ 0.15
DNOI per common share	\$ 0.09	\$ 0.16

<sup>(a)</sup> Results for the three months ended September 30, 2011, include \$431 of amortization of employee restricted stock awards associated with our corporate restructuring. These amortization expenses are included in restructuring expense on our *Consolidated Statements of Operations*. See *Recent Developments* for a discussion of our corporate restructuring and the impact that we estimate that the implementation of the restructuring will have on our future expenses.

### NET INVESTMENT LOSS BEFORE INCOME TAX PROVISION

During the three months ended September 30, 2011, we incurred \$31.1 million of net investment losses before income tax provision, compared to \$9.8 million of net investment losses during the same period in 2010. These amounts represent the total of net realized gains and losses, net unrealized appreciation (depreciation), and reversals of unrealized (appreciation) depreciation. We reverse unrealized (appreciation) depreciation at the time that we realize the gain or loss. The following table summarizes our realized and unrealized gain and loss on investments and changes in our unrealized appreciation and depreciation on investments for the three months ended September 30, 2011:

Portfolio Company	Industry	Type	Three months ended September 30, 2011			
			Realized Gain/(Loss)	Unrealized (Depreciation)/Appreciation	Reversal of Unrealized Depreciation/(Appreciation)	Net (Loss)/Gain
Broadview Networks Holdings, Inc.	Communications	Control	\$ —	\$ (24,697)	\$ —	\$(24,697)
Jet Plastica Investors, LLC	Plastic Products	Control	—	(5,637)	—	(5,637)
Intran Media, LLC	Other Media	Control	—	(1,959)	—	(1,959)
Total Sleep Holdings, Inc.	Healthcare	Control	(38,081)	—	38,054	(27)
Stratford School Holdings, Inc.	Education	Affiliate	—	2,217	—	2,217
GSDM Holdings, Corp.	Healthcare	Non-Affiliate	—	1,857	—	1,857
NDSSI Holdings, LLC	Electronics	Non-Affiliate	—	1,277	—	1,277
Other (< \$1 million net gain (loss))			254	(3,685)	(652)	(4,083)
<b>Total</b>			<b>\$(37,827)</b>	<b>\$ (30,627)</b>	<b>\$ 37,402</b>	<b>\$(31,052)</b>

The following bulleted items summarize the reasons for significant changes in realized and unrealized (loss) and gain on investments and changes in unrealized appreciation depreciation on investment for the three months ended September 30, 2011:

- We recorded \$24.7 million of unrealized depreciation on our Broadview investment primarily to reflect, among other factors, continuing challenges in the bond market, a recent downgrade of Broadview's corporate credit rating, delays by Broadview in refinancing its debt, as well as the near-term maturities of Broadview's debt facilities. As of June 30, 2011, Broadview had \$17.1 million of borrowings outstanding under its revolving credit facility, which becomes payable on February 23, 2012. In addition, as of June 30, 2011, Broadview had \$301.4 million of outstanding senior secured notes, which will mature on September 1, 2012. The fair value of Broadview, which we used as the foundation for determining the fair value our investment in Broadview, is consistent with an independent third-party valuation. If Broadview is unable to refinance these debt facilities by their respective maturity dates, the value of our portfolio

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investment in Broadview could decline by up to the remaining fair value at September 30, 2011, and we may be required to recognize additional unrealized depreciation on this investment.

- We recorded \$5.6 million of unrealized depreciation on our investment in Jet Plastica, to reflect a decrease in that company's operating performance and the multiple that we use to value the company.
- We also wrote off our remaining investment in Total Sleep Holdings, Inc., or Total Sleep, during the quarter ended September 30, 2011, which resulted in the reversal of \$38.1 million of previously unrealized depreciation and the realization of a \$38.1 million loss.
- The remaining unrealized depreciation and appreciation shown in the above table resulted predominantly from a change in the performance of certain of our portfolio companies and the multiples used to value certain of our investments.

The following table summarizes our realized gain and (loss) on our investments and changes in unrealized appreciation and depreciation on our investments during the three months ended September 30, 2010:

(in thousands)

Portfolio Company	Industry	Type	Three months ended September 30, 2010			
			Realized Gain/(Loss)	Unrealized (Depreciation)/Appreciation	Reversal of Unrealized Depreciation/(Appreciation)	Net (Loss)/Gain
Active Brands International, Inc.		Non-Affiliate	\$ —	\$ (11,194)	\$ —	\$(11,194)
	Consumer Products					
Jet Plastica Investors, LLC	Plastic Products	Control	—	(8,577)	—	(8,577)
PremierGarage Holdings LLC	Home Furnishings	Control	—	(3,089)	—	(3,089)
JetBroadband Holdings, LLC	Cable	Control	(3,911)	—	1,386	(2,525)
Total Sleep Holdings, Inc.	Healthcare	Control	—	(2,020)	—	(2,020)
Intran Media, LLC	Other Media	Control	—	(1,238)	—	(1,238)
MCI Holdings LLC		Non-Affiliate	9,531	—	(9,663)	(132)
	Healthcare					
RadioPharmacy Investors, LLC	Healthcare	Control	—	4,819	—	4,819
GSDM Holdings, LLC		Non-Affiliate	—	3,933	—	3,933
	Healthcare					
Metropolitan Telecommunications Holding Company	Communications	Non-Affiliate	—	1,645	—	1,645
Coastal Sunbelt Real Estate, Inc.	Real Estate Investments	Non-Affiliate	—	1,521	—	1,521
Jenzabar, Inc.	Technology	Non-Affiliate	—	1,397	—	1,397
Superior Industries Investors, Inc.	Sporting goods	Control	—	1,094	—	1,094
Avenue Broadband LLC	Cable	Control	—	1,025	—	1,025
Quantum Medical Holdings, LLC	Laboratory Instruments	Non-Affiliate	1,359	—	(1,074)	285
Home Interiors & Gifts, Inc.	Home Furnishings	Non-Affiliate	(3,467)	—	3,645	178
Other (< \$1 million net gain (loss))			(40)	3,078	40	3,078
<b>Total</b>			<b>\$ 3,472</b>	<b>\$ (7,606)</b>	<b>\$ (5,666)</b>	<b>\$ (9,800)</b>

During the quarter ended September 30, 2010, we received proceeds from the sales of MCI Holdings LLC and Quantum Medical Holdings, LLC, for approximately the fair value of those investments reported as of June 30, 2010. During the quarter ended September 30, 2010, we also sold our remaining investment in JetBroadband Holdings, LLC. As a result of this sale, we reversed \$1.4 million of previously unrealized depreciation and realized a \$3.9 million loss, including \$2.5 million of transaction costs that we recorded at the time of sale. During the quarter ended September 30, 2010, we received a payment of \$200,000, as our portion of the liquidation of Home Interiors & Gifts, Inc., which resulted in a net gain of \$178,000. During the quarter ended September 30, 2010, we recorded unrealized depreciation primarily related to Active Brands, Jet Plastica and PremierGarage Holdings LLC, or PremierGarage. The decreases in the fair value of Active Brands, Jet Plastica and PremierGarage were attributable to a decrease in the performance of those companies, as well as reductions in valuation multiples. The remaining unrealized depreciation and appreciation shown in the above table resulted predominantly from a change in the performance of certain of our portfolio companies and the multiples used to value certain of our investments.

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### GAIN ON EXTINGUISHMENT OF DEBT

We incurred a \$0.4 million premium when we repurchased \$22.4 million of our private placement notes during the third quarter of 2010. This premium represents 102% of the principal amount required to be purchased with monetization proceeds by our agreement with the holders of these unsecured notes.

### INCOME TAX PROVISION

During the three months ended September 30, 2011, we incurred a \$10,000 income tax provision compared to a \$1.7 million income tax provision during the three months ended September 30, 2010. Approximately \$1.6 million of the income tax expense accrued for the three months ended September 30, 2010 was attributable to the sale of JetBroadband in July 2010. The income tax expense for the three months ended September 30, 2011, and the remaining tax expense for the three months ended September 30, 2010 were primarily attributable to unrealized depreciation or appreciation and flow-through taxable income on certain investments held by our subsidiaries.

### NET LOSS

During the three months ended September 30, 2011, we recorded a net loss of \$25.1 million, compared to a net loss of \$0.5 million during the three months ended September 30, 2010. This change is attributable to the items discussed above.

### COMPARISON OF THE NINE MONTHS ENDED SEPTEMBER 30, 2011 AND 2010

The following table summarizes the components of our net (loss) income for the nine months ended September 30, 2011 and 2010:

<i>(dollars in thousands)</i>	Nine months ended September 30,		Variance	
	2011	2010	\$	Percentage
<b>Revenue</b>				
Interest and dividend income				
Interest income	\$ 54,439	\$ 58,166	\$ (3,727)	(6.4)%
Dividend income	5,840	4,384	1,456	33.2
Loan fees	3,125	2,104	1,021	48.5
Total interest and dividend income	63,404	64,654	(1,250)	(1.9)
Advisory fees and other income	2,817	1,431	1,386	96.9
<b>Total revenue</b>	<b>66,221</b>	<b>66,085</b>	<b>136</b>	<b>0.2</b>
<b>Operating expense</b>				
Interest expense	11,778	13,182	(1,404)	(10.7)
Employee compensation				
Salaries and benefits	9,567	12,065	(2,498)	(20.7)
Amortization of employee restricted stock awards	1,378	3,363	(1,985)	(59.0)
<b>Total employee compensation</b>	<b>10,945</b>	<b>15,428</b>	<b>(4,483)</b>	<b>(29.1)</b>
General and administrative expense	9,130	8,785	345	3.9
Restructuring expense	4,174	1	4,173	NM
<b>Total operating expense</b>	<b>36,027</b>	<b>37,396</b>	<b>(1,369)</b>	<b>(3.7)</b>
<b>Net operating income before net investment loss, (loss) gain on extinguishment of debt and income tax provision</b>	<b>30,194</b>	<b>28,689</b>	<b>1,505</b>	<b>5.2</b>
<b>Net investment loss before income tax provision</b>	<b>(73,444)</b>	<b>(25,130)</b>	<b>(48,314)</b>	<b>192.3</b>
<b>(Loss) gain on extinguishment of debt before income tax provision</b>	<b>(863)</b>	<b>2,983</b>	<b>(3,846)</b>	<b>NM</b>
<b>Income tax provision</b>	<b>29</b>	<b>1,866</b>	<b>(1,837)</b>	<b>(98.4)</b>
<b>Net (loss) income</b>	<b><u>\$(44,142)</u></b>	<b><u>\$ 4,676</u></b>	<b><u>\$(48,818)</u></b>	<b>NM</b>

NM=Not Meaningful

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### TOTAL REVENUE

Total revenue includes interest and dividend income and advisory fees and other income. During the nine months ended September 30, 2011, our total revenue was \$66.2 million, which represents a \$0.1 million, or 0.2%, increase from the nine months ended September 30, 2010. This increase resulted from a \$1.5 million, or 33.2%, increase in dividend income, a \$1.3 million, or 96.9%, increase in advisory fees and other income and a \$1.0 million, or 48.5%, increase in loan fees partially offset by a \$3.7 million, or 6.4%, decrease in interest. The following sections describe the reasons for the variances in each major component of our revenue during the nine months ended September 30, 2011 from the nine months ended September 30, 2010.

### INTEREST INCOME

The level of interest income that we earn depends upon the level of interest-bearing investments outstanding during the period, as well as the weighted-average yield on these investments. During the nine months ended September 30, 2011, the total yield on our average debt portfolio at fair value was 10.8% compared to 11.8% during the nine months ended September 30, 2010.

The following table shows the various components of the total yield on our average debt portfolio at fair value for the nine months ended September 30, 2011 and 2010:

	Nine months ended September 30,	
	2011	2010
Average 90-day LIBOR	0.3%	0.4%
Spread to average LIBOR on average loan portfolio	10.8	12.2
Impact of fee accelerations of unearned fees on paid/restructured loans	0.3	0.1
Impact of non-accrual loans	(0.6)	(0.9)
<b>Total yield on average loan portfolio</b>	<b>10.8%</b>	<b>11.8%</b>

During the nine months ended September 30, 2011, interest income was \$54.4 million, compared to \$58.2 million during the nine months ended September 30, 2010, which represented a \$3.7 million, or 6.4%, decrease. This decrease reflected a \$5.3 million decrease in interest income resulting from a 140 basis-point decrease in our spread to LIBOR, a \$0.8 million decrease resulting from the net impact of loans that were on non-accrual status during the nine months ended September 30, 2011 that were accruing interest during the nine months ended September 30, 2010 and a \$0.3 million decrease related to the change in LIBOR. These decreases were partially offset by a \$1.6 million increase resulting from a 4.3% rise in our average loan balance and a \$1.1 million increase in interest income resulting from the impact of interest rate floors.

### PIK Income

The following table shows the PIK-related activity for the nine months ended September 30, 2011 and 2010, at cost :

<i>(in thousands)</i>	Nine months ended September 30,	
	2011	2010
Beginning PIK loan balance	\$ 30,923	\$ 33,436
PIK interest earned during the period	6,458	9,928
Interest receivable converted to PIK	590	3,420
Payments received from PIK loans	(20,410)	(17,522)
PIK converted to other securities	(876)	—
Realized loss	(1,177)	—
<b>Ending PIK loan balance</b>	<b>\$ 15,508</b>	<b>\$ 29,262</b>

The payments received from PIK loans during the nine months ended September 30, 2011, includes \$8.2 million and \$4.7 million of PIK collected in conjunction with the respective sales of our investments in Restaurant Technologies, Inc. and Avenue Broadband LLC, as well as \$1.7 million collected in conjunction with the partial repayment of our investments in Sagamore Hill Broadcasting, LLC.

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### DIVIDEND INCOME

The following table summarizes our dividend activity, at cost, for the nine months ended September 30, 2011 and 2010:

<i>(in thousands)</i>	Nine months ended September 30,	
	2011	2010
Beginning accrued dividend balance	\$ 90,981	\$88,898
Dividend income earned during the period	5,840	4,384
Dividend collections	(12,355)	(2,103)
Realized loss	(92)	(1,315)
<b>Ending accrued dividend balance</b>	<b>\$ 84,374</b>	<b>\$89,864</b>

During the nine months ended September 30, 2011, our dividend income was \$5.8 million, which represented a \$1.5 million, or 33.2%, increase from the nine months ended September 30, 2010. Dividend income increased \$3.5 million primarily because the fair value of eight existing portfolio companies improved sufficiently to support the accretion of dividends partially offset by a \$1.9 million decrease resulting from the sale of five dividend-producing investments. The sale of our equity investment in Avenue Broadband, LLC resulted in the collection of \$6.8 million of dividends, and the sale of our equity investment in Superior Industries Investors, Inc. resulted in the collection of \$4.2 million of dividends.

### LOAN FEES

During the nine months ended September 30, 2011, our loan fees increased \$1.0 million, or 48.5%, compared to the same period in 2010. This increase was primarily attributable to the acceleration of previously unamortized loan origination fees into loan income as a result of higher loan repayments during the nine months ended September 30, 2011 compared to the same period of 2010.

### ADVISORY FEES AND OTHER INCOME

During the nine months ended September 30, 2011, we earned \$2.8 million of advisory fees and other income, which represented a \$1.4 million, or 96.9%, increase from the nine months ended September 30, 2010. Approximately \$1.2 million of this increase was attributable to advisory fees earned in conjunction with the origination of eight investments during the nine months ended September 30, 2011, compared to four investments originated during the nine months ended September 30, 2010. The remainder of the increase was attributable primarily to higher prepayment penalty fees collected on six investments during the nine months ended September 30, 2011 compared with prepayment penalty fees collected on one investment during the nine months ended September 30, 2010.

### TOTAL OPERATING EXPENSE

During the nine months ended September 30, 2011, we incurred \$36.0 million of operating expense, representing a \$1.4 million, or 3.7%, decrease from the same period in the prior year. This decrease was composed of a \$4.5 million decrease in employee compensation expense and a \$1.4 million decrease in interest expense offset by a \$4.2 million increase in restructure expense and a \$0.3 million increase in general and administrative expense. The reasons for these variances are discussed in more detail below. See *Recent Developments* for a discussion of our corporate restructuring and retention programs and the impact that we estimate that the implementation of these programs will have on our future operating expense.

### INTEREST EXPENSE

During the nine months ended September 30, 2011, we incurred \$11.8 million of interest expense, which represented a \$1.4 million, or 10.7%, decrease from the same period in 2010. A narrowing of the interest rate spread from 2.39% during the nine months ended September 30, 2010 to 2.16% during the nine months ended September 30, 2011 caused interest expense to decrease by \$0.9 million. Interest expense also decreased \$0.3 million as a result of a reduction in average LIBOR from 0.36% in the nine months ended September 30, 2010 to 0.29% in the nine months ended September 30, 2011 and \$0.2 million as a result of a reduction in average borrowing balance in the nine months ended September 30, 2011 from the nine months ended September 30, 2010.

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### *E M P L O Y E E C O M P E N S A T I O N*

Employee compensation expense includes base salaries and benefits, variable annual incentive compensation and amortization of employee stock awards. During the nine months ended September 30, 2011, our employee compensation expense was \$10.9 million, which represented a \$4.5 million, or 29.1%, decrease from the same period in 2010. Our salaries and benefits decreased by \$2.5 million, or 20.7%, primarily due to a \$2.1 million decrease in incentive compensation and a \$0.3 million decrease in salaries, which primarily resulted from a 42% reduction in our workforce that occurred as part of the corporate restructuring that we implemented during the three months ended September 30, 2011. See *Recent Developments* for a discussion of our corporate restructuring and retention programs and the impact that we estimate that the implementation of these programs will have on our future employee compensation expense.

During the nine months ended September 30, 2011, we recognized \$1.4 million of compensation expense related to restricted stock awards, compared to \$3.4 million for the nine months ended September 30, 2010, which represented a \$2.0 million, or 59.0%, decrease. The lapsing of forfeiture provisions for previously awarded restricted stock accounted for the reduction in amortization of employee restricted stock. Issuance of restricted stock under the *2009 Long-Term Incentive Plan*, or LTIP, was contingent upon the closing price of MCG's stock meeting certain price thresholds and the approval of the Compensation Committee of our board of directors. We achieved the final price threshold under which restricted stock could be issued during the nine months ended September 30, 2011, resulting in the issuance of 86,500 shares of restricted common stock and the award of \$1.0 million to LTIP participants.

### *G E N E R A L A N D A D M I N I S T R A T I V E*

During the nine months ended September 30, 2011, general and administrative expense was \$9.1 million, which represented a \$0.3 million, or 3.9%, increase from the same period in 2010. This increase was primarily the result of a \$1.1 million increase in professional fees paid for portfolio-related litigation and other corporate initiatives in the third quarter of 2011 offset by \$0.9 million of fees paid in the second quarter of 2010 related to the contested election of directors to our board of directors at our 2010 Annual Meeting. See *Recent Developments* for a discussion of our corporate restructuring and retention programs and the impact that we estimate that the implementation of these programs will have on our future general and administrative expenses.

### *R E S T R U C T U R I N G*

During the nine months ended September 30, 2011, we incurred \$4.2 million of restructuring expense, related to our corporate restructuring that was approved by our board of directors on August 1, 2011. Virtually all of these expenses represent severance-related obligations to our former employees. We anticipate that during the quarter ending December 2011, we will incur approximately \$115,000 to \$120,000 of additional restructuring expenses related to the closure of our Richmond office by December 31, 2011. During the twelve months ending December 31, 2012 and 2013, we expect that we will record restructuring charges of \$65,000 and \$14,000, respectively, which represent the accretion costs associated with the severance benefits. See *Recent Developments* for a discussion of our corporate restructuring and the impact that we estimate that the implementation of the restructuring will have on our future expenses.

### *N E T O P E R A T I N G I N C O M E B E F O R E N E T I N V E S T M E N T L O S S , ( L O S S ) G A I N O N E X T I N G U I S H M E N T O F D E B T A N D I N C O M E T A X P R O V I S I O N*

Net operating income before net investment loss, (loss) gain on extinguishment of debt and income tax provision for the nine months ended September 30, 2011 totaled \$30.2 million, compared with \$28.7 million for the nine months ended September 30, 2010. This increase was due to the items discussed above.

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### D ISTRIBUTABLE N ET O PERATING I NCOME

During the nine months ended September 30, 2011, DNOI was \$32.0 million, or \$0.42 per share, compared to \$32.1 million, or \$0.42 per share for the nine months ended September 30, 2010. The following table shows a reconciliation of our reported net operating income before net investment loss, (loss) gain on extinguishment of debt and income tax provision to DNOI for the nine months ended September 30, 2011 and 2010:

	Nine months ended September 30,	
	2011	2010
<i>(in thousands, except per share data)</i>		
Net operating income before net investment loss, (loss) gain on extinguishment of debt and income tax provision	\$30,194	\$28,689
Amortization of employee restricted stock awards <sup>(a)</sup>	1,809	3,363
<b>DNOI</b>	<b>\$32,003</b>	<b>\$32,052</b>
<b>Per common share data (basic and diluted)</b>		
Weighted-average common shares outstanding	76,173	76,469
(Loss) earnings per common share	\$ (0.58)	\$ 0.06
Net operating income before net investment loss, (loss) gain on extinguishment of debt and income tax provision per common share	\$ 0.40	\$ 0.38
DNOI per common share	\$ 0.42	\$ 0.42

<sup>(a)</sup> Results for the nine months ended September 30, 2011, include \$431 of amortization of employee restricted stock awards associated with our corporate restructuring. These amortization expenses are included in restructuring expense on our *Consolidated Statements of Operations*. See *Recent Developments* for a discussion of our corporate restructuring and the impact that we estimate that the implementation of the restructuring will have on our future expenses.

### N ET I NVESTMENT L OSS B EFORE I NCOME T AX P ROVISION

The following table summarizes our realized and unrealized (loss) and gain on investments and changes in our unrealized appreciation and depreciation on investments for the nine months ended September 30, 2011:

Portfolio Company	Industry	Type	Nine months ended September 30, 2011			
			Realized Gain/ (Loss)	Unrealized (Depreciation)/ Appreciation	Reversal of Unrealized Depreciation/ (Appreciation)	Net (Loss)/ Gain
Broadview Networks Holdings, Inc.	Communications	Control	\$ —	\$ (73,815)	\$ —	\$(73,815)
Jet Plastica Investors, LLC	Plastic Products	Control	—	(6,911)	—	(6,911)
PremierGarage Holdings, LLC	Home Furnishings	Control	—	(5,381)	—	(5,381)
Intran Media, LLC	Other Media	Control	—	(6,487)	—	(6,487)
VOX Communications	Broadcasting	Non-Affiliate	(7,688)	—	5,645	(2,043)
Superior Industries Investors, Inc.	Sporting Goods	Control	988	—	(2,788)	(1,800)
Provo Craft & Novelty, Inc.	Leisure Activities	Non-Affiliate	(1,152)	(1,160)	1,151	(1,161)
G & L Investment Holdings, LLC	Insurance	Non-Affiliate	—	(1,116)	—	(1,116)
Avenue Broadband LLC	Cable	Control	11,977	(325)	(11,895)	(243)
Total Sleep Holdings, Inc.	Healthcare	Control	(38,081)	—	38,054	(27)
RadioPharmacy Investors, LLC	Healthcare	Control	—	8,029	—	8,029
GSDM Holdings, Corp.	Healthcare	Non-Affiliate	—	4,411	—	4,411
NPS Holding Group, LLC	Business Services	Control	—	3,921	—	3,921
Coastal Sunbelt Real Estate, Inc.	Real Estate Investments	Non-Affiliate	—	2,252	—	2,252
Stratford School Holdings, Inc.	Education	Affiliate	—	1,867	—	1,867
Cruz Bay Publishing, Inc.	Publishing	Non-Affiliate	—	1,583	—	1,583
Restaurant Technologies, Inc.	Food Services	Non-Affiliate	1,527	1,429	(1,842)	1,114
GMC Television Broadcasting, LLC	Broadcasting	Control	(1,000)	730	1,000	730
Active Brands International, Inc.	Consumer Products	Non-Affiliate	(39,706)	—	39,829	123
Other (< \$1 million net gain (loss))			(825)	1,448	887	1,510
<b>Total</b>			<b>\$(73,960)</b>	<b>\$ (69,525)</b>	<b>\$ 70,041</b>	<b>\$(73,444)</b>

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A summary of the reasons for significant changes in realized and unrealized (loss) and gain on investments and changes in unrealized appreciation and depreciation on investments for the nine months ended September 30, 2011 are summarized below.

- During the nine months ended September 30, 2011, we recorded a \$73.8 million decrease in the fair value of our investment in Broadview. On June 21, 2011, Broadview withdrew its tender offer for \$300 million of its 11 <sup>3</sup>/<sub>8</sub>% Senior Secured Notes, due in 2012, following Broadview's review of market conditions. As of June 30, 2011, Broadview had \$17.1 million of borrowings outstanding under its revolving credit facility, which becomes payable on February 23, 2012. In addition, as of June 30, 2011, Broadview had \$301.4 million of outstanding senior secured notes, which will mature on September 1, 2012. The \$73.8 million decrease in fair value that we recorded during the nine months ended September 30, 2011, reflects, among other factors, the impact of continuing challenges in the bond market, a recent downgrade of Broadview's corporate credit rating, continuing delays by Broadview in refinancing its debt, as well as the near-term maturities of its debt. The fair value of Broadview, which we used as the foundation for determining the fair value of our investment in Broadview, is consistent with an independent third-party valuation. If Broadview is unable to refinance these debt facilities by their respective maturity dates, the value of our portfolio investment in Broadview could decline by up to the remaining fair value at September 30, 2011, and we may be required to recognize additional unrealized depreciation on this investment.
- We recorded \$6.9 million of unrealized depreciation on our investment in Jet Plastica, to reflect a decrease in that company's operating performance and the multiple that we use to value the company. In addition, we also recorded unrealized depreciation on our investment in Jet Plastica to reflect an incremental investment that we made in this investment in this portfolio company during the nine months ended September 30, 2011, that we subsequently wrote down to zero.
- During the nine months ended September 30, 2011, we recorded \$5.4 million of unrealized depreciation on our investment in PremierGarage and \$6.5 million of unrealized depreciation on our investment in Intran Media, LLC, to reflect our portion of the estimated liquidation value of those companies.
- We wrote off our remaining subordinated debt and equity investment in Total Sleep resulting in the reversal of \$38.1 million of previously unrealized depreciation and the realization of a \$38.1 million loss.
- We received payments of \$2.1 million on the sale of Active Brands' senior debt and wrote off our subordinated debt and equity investment in that portfolio company, which resulted in the reversal of \$39.8 million of previously unrealized depreciation and the realization of a \$39.7 million loss.
- We received payments of \$4.1 million in satisfaction of our \$11.8 million debt investment in VOX and wrote off our remaining investment in that portfolio company, which resulted in the reversal of \$5.6 million of previously unrealized depreciation and the realization of a \$7.7 million loss.
- We sold our investment in Avenue Broadband, which resulted in the reversal of \$11.9 million of previously unrealized appreciation and the realization of an \$11.9 million gain.
- We sold our investment in Superior, which resulted in the reversal of \$2.8 million of previously unrealized appreciation and the realization of a \$1.0 million gain, including \$1.8 million of transaction costs that we recorded at the time of sale.

The remaining unrealized depreciation and appreciation shown in the above table resulted predominantly from a change in the performance of certain of our portfolio companies and the multiples used to value certain of our investments.

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The following table summarizes our realized gain and (loss) on our investments and changes in unrealized appreciation and depreciation on our investments during the nine months ended September 30, 2010:

(in thousands)

Portfolio Company	Industry	Type	Nine months ended September 30, 2010			
			Realized (Loss)/ Gain	Unrealized (Depreciation) /Appreciation	Reversal of Unrealized Depreciation/ (Appreciation)	Net (Loss)/ Gain
Jet Plastica Investors, LLC	Plastic Products	Control	\$ —	\$ (24,737)	\$ —	\$(24,737)
Active Brands International, Inc.	Consumer Products	Non-affiliate	—	(16,703)	—	(16,703)
Broadview Network Holdings, Inc.	Communications	Control	—	(11,625)	—	(11,625)
JetBroadband Holdings, LLC	Cable	Control	(5,943)	(1,756)	3,418	(4,281)
Total Sleep Holdings, Inc.	Healthcare	Control	—	(4,082)	—	(4,082)
PremierGarage Holdings, LLC	Home Furnishings	Control	—	(3,670)	—	(3,670)
Intran Media, LLC	Other Media	Control	—	(2,877)	—	(2,877)
Superior Industries Investors, LLC	Sporting Goods	Control	—	(1,332)	—	(1,332)
B&H Education, Inc.	Education	Non-affiliate	3,665	(72)	(3,642)	(49)
Avenue Broadband LLC	Cable	Control	—	10,288	—	10,288
GSDM Holdings, LLC	Healthcare	Non-affiliate	—	5,560	—	5,560
RadioPharmacy Investors, LLC	Healthcare	Control	—	4,577	—	4,577
Jenzabar, Inc.	Technology	Non-affiliate	—	3,950	—	3,950
Metropolitan Telecommunications Holding Company	Communications	Non-affiliate	—	3,610	—	3,610
MCI Holdings LLC	Healthcare	Non-affiliate	9,531	3,486	(9,663)	3,354
Coastal Holdings, LLC	Real Estate Investments	Non-Affiliate	—	1,791	—	1,791
Orbitel Holdings, LLC	Cable	Control	—	1,745	—	1,745
Stratford School Holdings, Inc.	Education	Affiliate	—	1,386	—	1,386
Sagamore Hill Broadcasting, LLC	Broadcasting	Non-affiliate	—	1,232	—	1,232
Quantum Medical Holdings, LLC	Laboratory Instruments	Non-affiliate	1,359	357	(1,074)	642
Home Interiors & Gifts, Inc.	Home Furnishings	Control	(3,467)	1	3,645	179
WebMediaBrands Inc.	Information Systems	Non-affiliate	(1,981)	—	1,984	3
Other (< \$1 million net gain (loss))			(1,216)	5,900	1,225	5,909
<b>Total</b>			<b>\$ 1,948</b>	<b>\$ (22,971)</b>	<b>\$ (4,107)</b>	<b>\$(25,130)</b>

During the nine months ended September 30, 2010, we sold our investments in WebMediaBrands Inc., B&H Education Inc., MCI Holdings LLC and Quantum Medical Holdings, LLC, for approximately the most recently reported fair values of those investments. During the nine months ended September 30, 2010, we sold our investment in JetBroadband. As a result of the sale of JetBroadband, we reversed \$3.4 million of previously unrealized depreciation and realized a \$5.9 million loss, including \$2.5 million of transaction costs that we recognized at the time of sale.

During the first nine months of 2010, we recorded unrealized depreciation primarily related to Jet Plastica, Active Brands and Broadview. The decrease in the fair value of Jet Plastica and Active Brands was attributable to a decrease in the performance of those companies, as well as a reduction in valuation multiples. The decrease in the fair value of Broadview was attributable principally to an adjustment to our estimate of the fair value of this investment, which was based on, among other things, merger and acquisition comparables, private market transactions, public company comparables, a discounted cash flow analysis and an independent third-party valuation. The remaining unrealized depreciation and appreciation shown in the above table resulted predominantly from a change in the performance of certain of our portfolio companies and the multiples used to value certain of our investments.

### GAIN (LOSS) ON EXTINGUISHMENT OF DEBT

We incurred a \$0.9 million premium when we repurchased \$17.4 million of our private placement notes during the first nine months of 2011. In the first nine months of 2010, we repurchased \$8.0 million of collateralized loan obligations for \$4.4 million that previously had been issued by our Commercial Loan Trust 2006-1, which resulted in the recognition of a \$3.6 million gain on extinguishment of debt, excluding the effect of the amortization of the

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acceleration of \$0.1 million in deferred debt costs. Additionally, in the first nine months of 2010, we incurred a \$0.5 million premium when we repurchased \$25.3 million of our private placement notes. This premium represents 102% of the principal amount to be purchased with monetization proceeds as required by our agreement with the holders of these unsecured notes.

### INCOME TAX PROVISION

During the nine months ended September 30, 2011, we incurred a \$29,000 income tax provision compared to a \$1.9 million income tax provision during the nine months ended September 30, 2010. Approximately \$1.6 million of the income tax expense accrued for the nine months ended September 30, 2010 was attributable to the sale of JetBroadband in July 2010. The income tax expense for the nine months ended September 30, 2011, and the remaining tax expense for the nine months ended September 30, 2010 were primarily attributable to unrealized depreciation or appreciation and flow-through taxable income on certain investments held by our subsidiaries.

### NET (LOSS) INCOME

During the nine months ended September 30, 2011, we recorded a \$44.1 million net loss, compared to net income of \$4.7 million during the nine months ended September 30, 2010. This change is attributable to the items discussed above.

### FINANCIAL CONDITION, LIQUIDITY AND CAPITAL RESOURCES

#### CASH AND CASH EQUIVALENTS, CASH, SECURITIZATION ACCOUNTS, AND CASH, RESTRICTED

Our *Consolidated Balance Sheets* and our *Consolidated Statements of Cash Flows* reflect three categories of cash: cash and cash equivalents; cash, securitization accounts; and cash, restricted. Each of these categories is described more fully below:

- *Cash and cash equivalents* represents unrestricted cash, including checking accounts, interest bearing deposits collateralized by marketable debt securities and highly liquid investments with original maturities of 90 days or less. As of September 30, 2011 and December 31, 2010, we had \$53.9 million and \$45.0 million, respectively, in cash and cash equivalents. As of September 30, 2011, \$44.4 million was held in interest-bearing accounts.
- *Cash, securitization accounts* include principal and interest payments received on securitized loans, which, in certain cases, are held in designated bank accounts until monthly or quarterly disbursements are made from the securitization trusts. In certain cases, we are required to use a portion of these amounts to pay interest expense, reduce borrowings or pay other amounts in accordance with the related securitization agreements. In other cases, we are permitted to use these amounts to acquire new loans into the securitization trusts. Cash in securitization accounts has a negative impact on our earnings since the interest we pay on borrowings typically exceeds the rate of return that we are able to earn on temporary cash investments. Our objective is to maintain sufficient cash-on-hand and availability under our debt facilities to cover current funding requirements. As of September 30, 2011 and December 31, 2010, we had \$99.4 million and \$42.2 million, respectively, in cash, securitization accounts. On October 20, 2011, the next reporting date for our Commercial Loan Trust 2006-1 facility, we used \$80.2 million of securitized cash in that facility (primarily representing previous principal collections) to repay a portion of that facility. Subsequent collections of principal that we receive from collateral held by Commercial Loan Trust 2006-1 will be used to repay that facility.
- *Cash, restricted* includes cash held for regulatory purposes and cash held in escrow. The largest component of restricted cash was represented by cash held by Solutions Capital I, L.P., our SBIC, which generally is restricted to the origination of new loans from our SBIC. As of September 30, 2011 and December 31, 2010, we had \$17.0 million and \$29.4 million respectively, of restricted cash.

During the nine months ended September 30, 2011, our operating activities provided \$147.9 million of cash and cash equivalents, compared to \$70.4 million used during the nine months ended September 30, 2010. The \$77.5 million increase in cash provided by operating activities resulted primarily from increased monetizations partially offset by increased investments in portfolio companies. During the nine months ended September 30, 2011, our financing activities used \$138.9 million of cash, compared to \$53.9 million during the nine months

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ended September 30, 2010. This \$85.0 million increase in cash used by financing activities was due primarily to a \$45.3 million net increase in cash held in securitization and restricted cash accounts, a \$27.0 million increase in payments of dividends, a \$10.7 million increase in payments on borrowings, and a \$22.5 million decrease in proceeds from our borrowings.

Although there can be no assurance, we believe we have sufficient liquidity to meet our operating requirements for the remainder of 2011, as well as liquidity for new origination opportunities and potential dividend distributions.

### ***L IQUIDITY AND C APITAL R ESOURCES***

The availability of debt and equity capital continues to be constrained. We believe that we will continue to be constrained by the limited access we have to debt and equity capital. Because our stock continues to trade below net asset value and we do not have stockholder approval to sell equity below our net asset value, we effectively lack access to the equity markets. Lenders, in general, may be reluctant to extend credit to us without such equity capital markets access.

We expect to continue to monetize our equity investments to reduce them to no more than 10% to 20% of the fair value of our portfolio over the next few years. We generally expect to limit our future investing activities principally to debt investments and do not intend to make significant investments in control companies beyond those that are currently in our portfolio for the foreseeable future. We also expect to continue to originate higher-yield investments to the extent funding is available, and expect to underwrite credit in a manner consistent with our expectation that macro-economic conditions will be under pressure for an extended period of time. Over time, if we meet our goals with respect to leverage levels and unrestricted cash balances, we potentially may, depending on stock price and debt pricing levels, seek to repurchase our equity and additional debt securities, including our collateralized loan obligations, subject to the limitations set forth in our private placement borrowing agreements and any regulatory limits. To help provide sustainable stockholder value, we expect to make future distributions to stockholders based upon a quarterly assessment of the minimum statutorily required level of distributions, gains and losses recognized for tax purposes, portfolio transactional events, our liquidity, cash earnings and our asset coverage ratio at the time of such decision.

As discussed in *Liquidity and Capital Resources—Borrowings*, the reinvestment period for the MCG Commercial Loan Funding Trust facility ended on July 20, 2011 and all future principal collections from collateral in the facility will be used to repay the securitized debt. On October 20, 2011, the next payment date for this facility, we used \$80.2 million of securitized cash in that facility (primarily representing previous principal collections) to repay that facility. Following the October 20, 2011 repayment, we had \$237.1 million of securitized debt outstanding under this facility.

As discussed in *Recent Developments*, we have incurred \$4.1 million of restructuring expenses during the nine-months ended September 30, 2011 and expect to incur approximately \$115,000 to \$120,000 of additional restructuring charges through the remainder of 2012. Excluding these severance and severance-related costs, we believe that the implementation of this restructuring plan, which will include the closure of one of our offices and other planned reductions in our general and administrative expense, will result in approximately \$6.7 million to \$7.0 million of savings through December 31, 2012.

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### LIQUIDITY AND CAPITAL RESOURCES — BORROWINGS

As of September 30, 2011, we reported \$490.0 million of borrowings on our Consolidated Balance Sheets at cost. We estimate that the fair value of these borrowings as of September 30, 2011 was approximately \$472.7 million, based on market data and current interest rates. As of September 30, 2011, the weighted-average annual interest rate on all of our outstanding borrowings was 2.3%, excluding the amortization of deferred debt issuance costs. The following table summarizes our borrowing facilities and the potential borrowing capacity of those facilities and contingent borrowing eligibility of Solutions Capital I, L.P., a wholly owned subsidiary, as an SBIC, under the SBIC Act.

<i>(dollars in thousands)</i>	Maturity Date	September 30, 2011		December 31, 2010	
		Total Facility/Program	Amount Outstanding	Total Facility/Program	Amount Outstanding
<i>Private Placement Notes</i>					
Series 2005-A	October 2011	\$ —	\$ —	\$ 17,434	\$ 17,434
Series 2007-A	October 2012	8,717	8,717	8,717	8,717
<i>Commercial Loan Funding Trust</i>					
Variable Funding Note	January 2014 <sup>(a)</sup>	150,000	55,822	150,000	100,251
<i>Commercial Loan Trust 2006-1</i>					
Series 2006-1 Class A-1 Notes	April 2018 <sup>(b)</sup>	106,250	106,250	106,250	106,250
Series 2006-1 Class A-2 Notes	April 2018 <sup>(b)</sup>	5,000	5,000	50,000	—
Series 2006-1 Class A-3 Notes	April 2018 <sup>(b)</sup>	85,000	85,000	85,000	85,000
Series 2006-1 Class B Notes	April 2018 <sup>(b)</sup>	58,750	58,750	58,750	58,750
Series 2006-1 Class C Notes <sup>(c)</sup>	April 2018 <sup>(b)</sup>	45,000	32,000	45,000	32,000
Series 2006-1 Class D Notes <sup>(d)</sup>	April 2018 <sup>(b)</sup>	47,500	29,880	47,500	29,880
<i>SBIC (Maximum borrowing potential) <sup>(e)</sup></i>	<sup>(f)</sup>	150,000	108,600	130,000	108,600
Total borrowings		<u>\$656,217</u>	<u>\$ 490,019</u>	<u>\$ 698,651</u>	<u>\$ 546,882</u>

- <sup>(a)</sup> In January 2011, the lender renewed this facility through January 2013 and the legal final maturity date was extended to January 2014.
- <sup>(b)</sup> Borrowings under the MCG Commercial Loan Trust 2006-1 facility are listed based on the contractual maturity date. The reinvestment period for this facility ended on July 20, 2011 and we will use all future principal collections from collateral in the facility to repay the securitized debt. On October 20, 2011, the next payment date for this facility, we used \$80.2 million of securitized cash in that facility (primarily representing previous principal collections of collateral in the facility) to repay a portion of the facility.
- <sup>(c)</sup> Amount outstanding excludes \$5.0 million of notes that we repurchased in December 2008 for \$1.6 million and \$8.0 million of notes that we repurchased in April 2010 for \$4.4 million. As part of the consolidation process, we eliminated the notes that MCG, the parent company, purchased.
- <sup>(d)</sup> Amount outstanding excludes \$10.1 million of notes that we repurchased in December 2008 for \$2.4 million and \$7.5 million of notes that we repurchased in January 2009 for \$2.1 million. As part of the consolidation process, we eliminated the notes that MCG, the parent company, purchased.
- <sup>(e)</sup> As of September 30, 2011, we had the potential to borrow up to \$150.0 million of SBA-guaranteed debentures under the SBIC program. As of September 30, 2011, the SBA had approved and committed up to \$150.0 million in borrowings to the SBIC. As of September 30, 2011, we have funded \$75.0 million, which allows us to utilize the full \$150.0 million borrowing potential approved and committed by the SBA under this program. Based on our funded capital as of September 30, 2011, Solutions Capital I, L.P., subject to the SBA's approval, may borrow up to an additional \$41.4 million to originate investments.
- <sup>(f)</sup> As of September 30, 2011, we could originate new borrowings under the \$150.0 million commitment made by the SBA through September 2015. We must repay borrowings under the SBIC program within ten years after the borrowing date, which will occur between September 2018 and September 2025.

Each of our credit facilities has certain collateral requirements and/or financial covenants. As of September 30, 2011, the net worth covenant of our SunTrust Warehouse requires that we maintain a consolidated tangible net worth of not less than \$450.0 million, plus 50% of any equity raised after February 26, 2009. Under these covenants, we must also maintain an asset coverage ratio of at least 180%.

As of September 30, 2011, our asset coverage ratio was 230% and we had \$41.4 million of unused, currently available borrowing capacity remaining in our SBIC subsidiary (subject to the SBA's approval) that is exempt from the asset coverage ratio requirements under the SEC exemptive order issued to us in October 2008.

As of September 30, 2011, we were in compliance with all key financial covenants under each of our borrowing facilities, although there can be no assurance regarding compliance in future periods. On our website, we have provided a list of hyperlinks to each of our borrowing agreements where these covenant requirements can be reviewed. You may view this list at <http://www.mcgcapiatal.com/>. We are not including the information contained on our website as a part of, or incorporating it by reference into, this *Quarterly Report on Form 10-Q*.

Our access to current and future liquidity from our borrowing facilities depends on several factors, including, but not limited to: the credit quality of our investment portfolio, including those investments used to collateralize borrowing facilities; the magnitude of our investments in individual companies and the industries in which they operate; our compliance with specific covenants in each borrowing agreement; and the specific provisions of our borrowing facilities.



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Certain of our borrowing facilities contain provisions that require that we apply a portion of the proceeds we receive from monetizations to pay down a portion of the outstanding balances. In addition, as each of our borrowing facilities mature, it is important that we have sufficient liquidity available to repay our borrowing obligations. We may obtain the liquidity for repayment of our borrowing facilities from a number of sources, including cash on-hand, the maturity or monetization of our investment portfolio, other borrowing facilities and equity issuances, and from other borrowing arrangements.

We fund all of our current debt facilities, except our private placement notes, through our bankruptcy remote, special-purpose, wholly owned subsidiaries. Therefore, these subsidiaries' assets may not be available to our creditors. In some cases, advances under our debt facilities are subject to certain collateral levels, collateral quality, leverage and other restrictive covenants. We continue to service those portfolio investments that we use as collateral in our secured borrowing facilities.

### *P R I V A T E P L A C E M E N T N O T E S*

As of September 30, 2011, we had one outstanding series of fixed-term, unsecured notes, or the Series 2007-A unsecured notes, with a total balance of \$8.7 million and an interest rate of 8.96%. Under the terms of the most recent amended agreement for the Series 2007-A unsecured notes, we are required to offer to repurchase such notes with a portion of certain monetization proceeds at a purchase price of 102% of the principal amount to be purchased. We are required to offer to repurchase these notes with 45% of the cash net proceeds of any sale of unencumbered assets to reduce amounts outstanding under the Series 2007-A unsecured notes as, and when, such sales occur in the event of proceeds of \$5.0 million or more or otherwise on a semi-annual basis, unless an event of default under one of the financing subsidiary debt facilities has occurred and is continuing, in which case the percentage of net proceeds increases to 60%. When the Series 2007-A unsecured notes mature, we expect to repay these notes with the proceeds from monetizations of our unencumbered investments and unrestricted cash and cash equivalents. As of September 30, 2011, the consolidated stockholders' equity covenant of the Private Placement Notes required that we maintain a consolidated stockholders' equity of not less than \$425.0 million.

In March 2011, we prepaid in full the Series 2005-A unsecured notes. In connection with the prepayment of the Series 2005-A unsecured notes and pursuant to the terms set forth in the Series 2005-A unsecured notes note purchase agreement, we paid to the noteholders \$17.4 million of principal, \$0.8 million in accrued interest and \$0.9 million in prepayment fees. Prior to the repayment, the Series 2005-A unsecured notes had an interest rate of 9.98%. We initially issued \$50.0 million of the Series 2005-A unsecured notes in October 2005 and, prior to the March 2011 prepayment, had repurchased or prepaid in the aggregate \$32.6 million in principal.

### *C O M M E R C I A L L O A N F U N D I N G T R U S T*

As of September 30, 2011, we had a \$55.8 million balance outstanding under the SunTrust Warehouse, an asset-backed commercial paper conduit administered by SunTrust Robinson Humphrey, Inc. Structured to operate like a revolving credit facility, the SunTrust Warehouse is secured primarily by MCG Commercial Loan Funding Trust's assets, including commercial loans that MCG Capital Corporation, the parent, sold to the trust. The SunTrust Warehouse is funded by third parties through the commercial paper market with SunTrust Bank providing a liquidity backstop through January 2013. The pool of commercial loans in the trust must meet certain requirements, such as term, average life, investment rating, agency rating and industry diversity requirements. The pool of commercial loans must also meet certain requirements related to portfolio performance, including required minimum portfolio yield and limitations on delinquencies and charge-offs.

In January 2011, SunTrust Bank renewed this liquidity facility through January 2013. The legal final maturity date of the SunTrust Warehouse is January 2014 and the scheduled termination date is January 2013. If a new agreement or extension is not executed by January 2013, the SunTrust Warehouse enters a 12-month amortization period during which principal under the facility is paid down through orderly monetizations of portfolio company assets that are financed in the facility. Any remaining balance must be repaid by the January 2014 legal maturity date, otherwise all or part of the associated collateral may be forfeited. Prior to the commencement of any amortization period, net proceeds from monetizations of collateral financed in the SunTrust Warehouse must be reinvested in additional collateral or used to repay the outstanding borrowings. Under the terms of the renewal, investments in new collateral are limited to senior secured loans.

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Under the SunTrust Warehouse, we are required to comply with various covenants, reporting requirements and other customary requirements for similar revolving credit facilities, including, without limitation, 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 a certain minimum stockholders' equity; e) maintaining a ratio of total assets (less total liabilities and indebtedness not represented by senior securities) to total indebtedness represented by senior securities, of the Company and its subsidiaries, of not less than 1.8:1.0; and f) maintaining minimum liquidity.

In addition to the asset coverage ratio described above, borrowings under the SunTrust Warehouse will be subject to compliance with a borrowing base that will apply different advance rates to different types of assets in MCG Commercial Loan Funding Trust's portfolio.

Our SunTrust Warehouse also contains a provision that if either Steven F. Tunney or B. Hagen Saville ceases to be involved actively in the management of MCG and is not replaced by a person reasonably acceptable to SunTrust within 90 consecutive calendar days of such occurrence, we would be in default under such facility. Mr. Tunney resigned from MCG effective October 31, 2011 and Richard W. Neu was appointed as the Chief Executive Officer. If SunTrust does not accept Mr. Neu as a reasonably acceptable replacement or if we lose the services of Mr. Saville and are unable to identify and hire a suitably qualified replacement, it could provide SunTrust with the right to accelerate the termination date of that facility and entitle the administrative agent thereunder to exercise available remedies, including selling the collateral securing this facility and applying the proceeds to reduce outstanding borrowings thereunder.

The following table sets forth the maturity of the SunTrust Warehouse, as well as the maturity of the securitized assets and the September 30, 2011 balance of securitized cash in this borrowing facility.

(in thousands)	Maturities				
	Total	Less than			After 5 years
		1 year	1-3 years	4-5 years	
<b>Borrowings</b>	<u>\$ 55,822</u>	<u>\$ —</u>	<u>\$55,822</u>	<u>\$ —</u>	<u>\$ —</u>
<b>Collateral</b>					
Securitized investments	123,949	4,551	58,511	54,676	6,211
Cash, securitization accounts	13,099	13,099	—	—	—
<b>Total collateral</b>	<u>\$137,048</u>	<u>\$17,650</u>	<u>\$58,511</u>	<u>\$54,676</u>	<u>\$6,211</u>

### COMMERCIAL LOAN TRUST 2006-1

As of September 30, 2011, we had \$316.9 million of securitized debt outstanding under the Commercial Loan Trust 2006-1, which matures in April 2018. We retain all of the equity in the securitization. The pool of commercial loans in the trust must meet certain requirements, such as asset mix and concentration, collateral coverage, term, agency rating, minimum coupon, minimum spread and sector diversity requirements. The securitization included a five-year reinvestment period, during which the trust was permitted to use principal collections received on the underlying collateral to purchase new collateral from us.

The following table sets forth the maturity of this facility, as well as the maturity of the securitized assets and the current balance of securitized cash in this borrowing facility.

(in thousands)	Maturities				
	Total	Less than			After 5 years
		1 year	1-3 years	4-5 years	
<b>Borrowings</b> <sup>(a)</sup>	<u>\$316,880</u>	<u>\$80,173</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$236,707</u>
<b>Collateral</b>					
Fair value of securitized investments	334,847	892	117,518	91,771	124,666
Fair value of equity investments	205	—	—	—	205 <sup>(b)</sup>
Cash, securitization account	86,317	86,317	—	—	—
<b>Total collateral</b>	<u>\$421,369</u>	<u>\$87,209</u>	<u>\$117,518</u>	<u>\$91,771</u>	<u>\$124,871</u>

<sup>(a)</sup> Borrowings under the MCG Commercial Loan Trust 2006-1 facility are listed based on the contractual maturity date. The reinvestment period for this facility ended on July 20, 2011 and all future principal collections from collateral in the facility will be used to repay the securitized debt. On October 20, 2011, the next payment date for this facility, we used \$80.2 million of securitized cash in that facility (primarily representing previous principal collections to repay a portion of the facility).

<sup>(b)</sup> Equity investments do not have a stated maturity date.

We were able to use the cash in the securitized account, as well as proceeds from principal collections of securitized investments, to originate new loans until July 20, 2011. The reinvestment period ended on July 20, 2011 and all

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subsequent principal collections received will be used to repay the securitized debt. On October 20, 2011, the next payment date for this facility, we used \$80.2 million of securitized cash in that facility (primarily representing previous principal collections) to repay a portion of this facility. Any additional principal collections or monetization proceeds that we receive from collateral used to securitize this Commercial Loan Trust 2006-1 must be applied to the outstanding balance of that facility. Upon maturity of this facility, any remaining balance must be repaid, otherwise all or part of the associated collateral may be forfeited. As shown in the above table, repayments of principal of the collateral held by this facility are expected to permit the repayment of Commercial Loan Trust 2006-1 prior to its April 2018 maturity.

### SBIC DEBENTURES

In December 2004, we formed a wholly owned subsidiary, Solutions Capital I, L.P. Solutions Capital I, L.P. has a license from the SBA to operate as an SBIC under the SBIC Act. As of September 30, 2011, the license gave Solutions Capital I, L.P. the potential to borrow up to \$150.0 million, which is the maximum amount of outstanding leverage available to single-license SBIC companies. The maximum amount of outstanding leverage available to SBIC companies with multiple licenses is \$225.0 million on an aggregate basis.

In total, the SBA has approved and committed \$150.0 million in borrowings to Solutions Capital I, L.P., subject to certain capital requirements and customary procedures. We may use these funds to provide debt and equity capital to qualifying small businesses. We may use the borrowings from the SBA to fund new originations; however, we may not use these borrowings to originate debt to certain companies that are currently in our portfolio without SBA approval. In addition, we may not use these funds for MCG's, the parent company's, working capital.

To realize the full \$150.0 million potential borrowing for which we have received approval under this program, we needed to fund a total of \$75.0 million to Solutions Capital I, L.P., which we have done as of September 30, 2011. As of September 30, 2011, \$108.6 million of SBA borrowings were outstanding, and Solutions Capital I, L.P. may borrow, subject to the SBA's approval, up to an additional \$41.4 million to originate new investments.

SBICs are subject to regulation and oversight by the SBA, including requirements with respect to maintaining certain minimum financial ratios and other covenants. Receipt of an SBIC license does not assure that an SBIC will receive SBA-guaranteed debenture funding, which is dependent upon continued compliance with SBA regulations and policies. The SBA, as a creditor, will have superior claim to Solutions Capital I, L.P.'s assets over our stockholders in the event we liquidate Solutions Capital I, L.P. or the SBA exercises its remedies under the SBA-guaranteed debentures issued by Solutions Capital I, L.P. upon an event of default.

In March 2011, we formed Solutions Capital II, L.P., and in May 2011, we submitted a license application to the SBA for a second SBIC license under Solutions Capital II, L.P. After discussions with the SBA, we elected to withdraw our application for a second license until such time as the SBA has an opportunity to evaluate, among other things, the organizational impact of our recent restructuring and any changes in management. We may seek to re-file our application for a second license within six months. There is no assurance that, if filed, the SBA will grant the additional license.

The following table sets forth the maturity of Solutions Capital I, L.P. debentures, as well as the maturity of the investments and the current balance of restricted cash in Solutions Capital I, L.P. as of September 30, 2011.

	Maturities				
	Total	Less than 1 year	1- 3 years	4-5 years	After 5 years
<i>(in thousands)</i>					
<b>Borrowings</b>	<u>\$108,600</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$108,600</u>
<b>Collateral</b>					
Fair value of debt investments	175,640	—	3,775	159,956	11,909
Fair value of equity investments	9,724	—	—	—	9,724 <sup>(a)</sup>
Cash, restricted account	10,074	10,074	—	—	—
Total collateral	<u>\$195,438</u>	<u>\$10,074</u>	<u>\$3,775</u>	<u>\$159,956</u>	<u>\$ 21,633</u>

<sup>(a)</sup> Equity investments do not have a stated maturity date.

As shown in the above table, the collateral in this facility exceeds the outstanding balance.

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### WEIGHTED-AVERAGE BORROWINGS AND COST OF FUNDS

The following table shows our weighted-average borrowings, the weighted-average interest rate on all of our borrowings, including amortization of deferred debt issuance costs and commitment fees, the average LIBOR, and the average spread to LIBOR for 2011 and 2010:

<i>(dollars in thousands)</i>	For the nine months ended	
	September 30, 2011	September 30, 2010
Weighted-average borrowings	\$ 521,652	\$ 533,264
Average LIBOR	0.29%	0.36%
Average spread to LIBOR, excluding amortization of deferred debt issuance costs	2.16	2.39
Impact of amortization of deferred debt issuance costs	0.53	0.51
<b>Total cost of funds</b>	<b>2.98%</b>	<b>3.26%</b>

The 2.98% weighted-average cost of funds for 2011 was 28 basis points less than the same period in 2010. This decrease resulted from a 23 basis-point decrease in the average spread to LIBOR and a 7 basis-point decrease in average LIBOR, partially offset by 2 basis-point increase in the impact of amortization of deferred debt issuance costs.

### LIQUIDITY AND CAPITAL RESOURCES — COMMON STOCK

We are a closed-end investment company that has elected to be regulated as a BDC under the 1940 Act. The 1940 Act prohibits us from selling shares of our common stock at a price below the current NAV of such stock, except in limited circumstances, including approval by our stockholders of such a sale and certain determinations by our board of directors.

### OFF-BALANCE SHEET ARRANGEMENTS

#### FINANCIAL INSTRUMENTS

We are party to financial instruments with off-balance sheet risk in the normal course of business to meet the financial needs of our customers. These instruments include commitments to extend credit and involve, to varying degrees, elements of credit risk in excess of the amount recognized in the balance sheet. We attempt to limit our credit risk by conducting extensive due diligence and obtaining collateral where appropriate.

Commitments to extend credit include the unused portions of commitments that obligate us to extend credit in the form of loans, participations in loans, guarantees, letters of credit and other financial commitments. Commitments to extend credit would also include loan proceeds we are obligated to advance, such as loan draws, rotating or revolving credit arrangements, or similar transactions. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee by the counterparty. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

We do not report the unused portions of these commitments on our *Consolidated Balance Sheets*. As of September 30, 2011, we had \$23.1 million of outstanding unused loan commitments, as shown in the table below. We believe that our operations, monetizations and unrestricted cash will provide sufficient liquidity to fund, as necessary, requests to draw on these unfunded commitments. We estimate that the fair value of these commitments was \$0.1 million based on the fees that we currently charge to enter into similar arrangements, taking into account the creditworthiness of the counterparties. From time to time, we provide guarantees or standby letters of credit on behalf of our portfolio companies. As of September 30, 2011, we had no outstanding guarantees or standby letters of credit.

<i>(in thousands)</i>	As of September 30, 2011			
	Non-Affiliate Investments	Affiliate Investments	Control Investments	Total
Unused commitments to portfolio companies				
Revolving credit facilities	\$ 7,344	\$ 6,200	\$ 3,294	\$16,838
Other	4,003	484	1,750	6,237
<b>Total unused commitments to portfolio companies</b>	<b>\$ 11,347</b>	<b>\$ 6,684</b>	<b>\$ 5,044</b>	<b>\$23,075</b>

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### CONTRACTUAL OBLIGATIONS

The following table shows our contractual obligations as of September 30, 2011:

(in thousands)

Contractual Obligations <sup>(a)</sup>	Payments Due by Period				
	Total	Less than 1 year	1-3 years	4-5 years	After 5 years
<b>Borrowings</b>					
Term securitizations <sup>(b)</sup>	\$316,880	\$80,173	\$ —	\$ —	\$236,707
Warehouse facility	55,822	—	55,822	—	—
Unsecured notes	8,717	—	8,717	—	—
SBIC	108,600	—	—	—	108,600
Total borrowings	490,019	80,173	64,539	—	345,307
Interest payments on borrowings <sup>(c)</sup>	72,475	11,189	20,158	15,790	25,338
Operating and capital leases	3,098	2,169	929	—	—
Severance obligations remaining from 2011 restructuring <sup>(d)</sup>	4,031	3,113	918	—	—
Total contractual obligations	<u>\$569,623</u>	<u>\$96,644</u>	<u>\$86,544</u>	<u>\$15,790</u>	<u>\$370,645</u>

<sup>(a)</sup> Excludes the unused commitments to extend credit to our customers of \$23.1 million as discussed above.

<sup>(b)</sup> Borrowings under the MCG Commercial Loan Trust 2006-1 facility are listed based on the contractual maturity date. The reinvestment period for this facility ended on July 20, 2011 and all future principal collections from collateral in the facility will be used to repay the securitized debt. On October 20, 2011, the next payment date for this facility, we used \$80.2 million of securitized cash in that facility (primarily representing previous principal collections to repay a portion of the facility).

<sup>(c)</sup> Interest payments are based on contractual maturity and the current outstanding principal balance of our borrowings and assume no changes in interest rate benchmarks.

<sup>(d)</sup> Represents remaining severance payments, benefits, deferred compensation, employer taxes that we are obligated to pay to employees who were terminated as a result of the corporate restructuring that we undertook in August 2011. See *Recent Developments* for a discussion of our corporate restructuring and the impact that we estimate that the implementation of the restructuring will have on our future expenses.

In addition to the contractual obligations set forth in the preceding table, effective October 31, 2011, we entered into a Letter Agreement with Mr. Steven Tunney in conjunction with his resignation from our company. In conjunction with the Letter Agreement, we are required to pay Mr. Tunney specified severance payments, benefits, deferred compensation, and employer taxes totaling \$2.7 million, of which \$1.4 million is payable in less than one year and \$1.3 million is payable in one to three years. See *Recent Developments* for a discussion of Mr. Tunney's resignation and other related management changes.

### DISTRIBUTIONS

As a BDC that has elected to be treated as a RIC, we generally must distribute at least 90% of our investment company taxable income and 90% of any ordinary pre-RIC built-in gains that we recognize in order to deduct distributions made (or deemed made) to our stockholders. In addition, for calendar years ended December 31, 2010 and earlier, we were subject to a 4% excise tax to the extent that we did not distribute (actually or on a deemed basis): 98% of our ordinary income for each calendar year; 98% of our capital gain net income for each calendar year; and any income realized, but not distributed, in prior calendar years. Beginning in 2011, we are subject to the 4% excise tax to the extent that we do not distribute (actually or on a deemed basis): 98% of our ordinary income for each calendar year; 98.2% of our capital gain net income for each calendar year; and any income realized but not distributed in prior calendar years.

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. In addition, we may be limited in our ability to make distributions due to the BDC asset coverage test for borrowings applicable to us as a BDC under the 1940 Act and due to provisions in our credit facilities and SBA regulations. 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. We cannot assure stockholders that they will receive any distributions or distributions at a particular level. We may make distributions to our stockholders of certain net capital gains. From December 2001 through September 30, 2011, we have declared distributions of \$12.64 per share.

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The following table summarizes the distributions that we declared since January 1, 2010:

<u>Date Declared</u>	<u>Record Date</u>	<u>Payable Date</u>	<u>Dividends per Share</u>
October 31, 2011	December 15, 2011	January 13, 2012	\$ 0.17
August 1, 2011	September 14, 2011	October 14, 2011	\$ 0.17
May 5, 2011	June 15, 2011	July 15, 2011	\$ 0.17
March 1, 2011	March 15, 2011	April 15, 2011	\$ 0.15
November 2, 2010	December 9, 2010	January 6, 2011	\$ 0.14
August 3, 2010	September 7, 2010	October 4, 2010	\$ 0.12
April 29, 2010	June 2, 2010	July 2, 2010	\$ 0.11

If we determined the tax attributes of our 2011 distributions as of September 30, 2011, 26% would be from ordinary income and 74% would be a return of capital. However, actual determinations of the tax attributes of our distributions, including determinations of return of capital, are made annually as of the end of our fiscal year based upon our taxable income and distributions paid for the full year and will be reported to each stockholder on a Form 1099. Future distributions will take into account the requirements for us to distribute the majority of our taxable income to fulfill our distribution requirements as a RIC, together with an assessment of our current and forecasted gains and losses recognized or to be recognized for tax purposes, portfolio transactional events, liquidity, cash earnings and our asset coverage ratio at the time of such decision.

Each year, we mail statements on Form 1099-DIV to our stockholders, which identify the source of the distribution, such as paid from ordinary income, paid from net capital gains on the sale of securities and/or a return of paid-in-capital surplus, which is a nontaxable distribution. To the extent our taxable earnings fall below the total amount of our distributions for that fiscal year, a portion of those distributions may be deemed a return of capital to our stockholders for tax purposes. A portion of the distributions that we paid to stockholders during fiscal years 2008, 2006, 2005, 2004 and 2003 represented a return of capital. We determine the tax attributes of our distributions as of the end of our fiscal year based upon our taxable income for the full year and distributions paid during the full year. Therefore, a determination of tax attributes made on a quarterly basis may not be representative of the actual tax attributes of distributions for a full year.

The following table reconciles GAAP net loss to taxable income before deductions for distributions for the nine months ended September 30, 2011 and the year ended December 31, 2010:

<i>(in thousands)</i>	Nine months ended	
	September 30, 2011	Year ended December 31, 2010
Net loss	\$ (44,142)	\$ (13,072)
Difference between book and tax losses on investments	48,950	(52,865)
Net change in unrealized (appreciation) depreciation on investments not taxable until realized	(516)	66,674
Capital losses in excess of capital gains	12,638	4,861
Timing difference related to deductibility of long-term incentive compensation	(6,085)	1,594
Taxable interest income on non-accrual loans <sup>(a)</sup>	(838)	14,857
Dividend income accrued for GAAP purposes that is not yet taxable	(5,840)	(7,368)
Distributions from taxable subsidiaries	1,828	3,529
Federal tax provision	29	1,801
Other, net	1,975	24
<b>Taxable income before deductions for distributions</b>	<b>\$ 7,999</b>	<b>\$ 20,035</b>

<sup>(a)</sup> Results for the period ended September 30, 2011 reflect the reversal of interest we previously recognized on non-accrual loans of portfolio investments that we monetized. In accordance with the Internal Revenue Service's Code, we are required to recognize as taxable interest income all interest that is owed to us by portfolio companies, including interest on those debt investments that are on non-accrual status for GAAP reporting purposes.

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### C RITICAL A CCOUNTING P OLICIES

These *Condensed Consolidated Financial Statements* are based on the selection and application of critical accounting policies, which require management to make significant estimates and assumptions. The following section describes our accounting policies associated with the valuation of our portfolio of investments. For a full discussion of our other critical accounting policies and estimates, see *Management's Discussion and Analysis of Financial Condition and Results of Operations* in our Annual Report on Form 10-K for the year ended December 31, 2010.

#### V ALUATION OF I NVESTMENTS

##### F AIR V ALUE M EASUREMENTS AND D ISCLOSURES

We account for our investments at fair value in accordance with Accounting Standard Codification Topic 820—Fair Value Measurements and Disclosures, or ASC 820. ASC 820 defines fair value, establishes a framework for measuring fair value, and expands disclosures about assets and liabilities measured at fair value. ASC 820 defines “fair value” as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This fair value definition focuses on exit price in the principal, or most advantageous, market and prioritizes, within a measurement of fair value, the use of market-based inputs over entity-specific inputs.

ASC 820 establishes the following three-level hierarchy, based upon the transparency of inputs to the fair value measurement of an asset or liability as of the measurement date:

<u>ASC 820 Fair Value Hierarchy</u>	<u>Inputs to Fair Value Methodology</u>
<b>Level 1</b>	Quoted prices in active markets for identical assets or liabilities
<b>Level 2</b>	Quoted prices for similar assets or liabilities; quoted markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the financial instrument; inputs other than quoted prices that are observable for the asset or liability; or inputs that are derived principally from, or corroborated by, observable market information
<b>Level 3</b>	Pricing models, discounted cash flow methodologies or similar techniques and at least one significant model assumption is unobservable or when the estimation of fair value requires significant management judgment

We categorize a financial instrument in the fair value hierarchy based on the lowest level of input that is significant to its fair value measurement. In the event that transfers between these levels were to occur in the future, we would recognize those transfers as of the ending balance sheet date, based on changes in the use of observable and unobservable inputs utilized to perform the valuation for the period.

Our investment portfolio is not composed of homogeneous debt and equity securities that can be valued with a small number of inputs. Instead, the majority of our investment portfolio is composed of complex debt and equity securities with unique contract terms and conditions. As such, our valuation of each investment in our portfolio is unique and complex, often factoring in numerous unique inputs, including the historical and forecasted financial and operational performance of the portfolio company, projected cash flows, market multiples, comparable market transactions, the priority of our securities compared with those of other investors, credit risk, interest rates, independent valuations and reviews and other inputs too numerous to list quantitatively herein.

##### D ETERMINATION OF F AIR V ALUE IN G OOD F AITH

As a BDC, we invest primarily in illiquid securities, including debt and equity securities of private companies. To protect our investments and maximize our returns, we negotiate the structure of each equity security and the majority of the debt securities in our investment portfolio. Our contracts with our portfolio companies generally include many terms governing interest rate, repayment terms, prepayment penalties, financial covenants, operating covenants, ownership and corporate governance parameters, dilution parameters, liquidation preferences, voting rights, and put or call rights. In some cases, our loan agreements also allow for increases in the spread to the base index rate, if the portfolio company's financial or operational performance deteriorates or

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shows negative variances from its business plan and, in some cases, allow for decreases in the spread if financial or operational performance improves or exceeds the portfolio company's plan. Generally, our investments are subject to some restrictions on resale and have no established trading market. Because of the type of investments that we make and the nature of our business, our valuation processes require analyses of numerous market, industry and company-specific factors, including the performance of the underlying investment; the financial condition of the portfolio company; changing market events; market prices, when available; and other factors relevant to the individual security.

There is no single approach for determining fair value in good faith. Unlike banks, we are not permitted to provide a general reserve for anticipated loan losses. As a result, for portfolio investments that do not have an active market, we must apply judgment to the specific facts and circumstances associated with each security to determine fair value.

Generally, we value securities that are traded in the over-the-counter market or on a stock exchange at the average of the prevailing bid and ask prices on the date of the relevant period end. When such market prices are not available, we use several valuation methodologies to estimate the fair value of our investment portfolio, which generally results in a range of fair values from which we derive a single estimate of the portfolio company's fair value. To determine a portfolio company's fair value, we analyze its historical and projected financial results, as well as key market value factors. In determining a security's fair value, we assume we would exchange it in an orderly transaction at the measurement date. We use the following methods to determine the fair value of investments in our portfolio that are not traded actively:

- *Majority-Owned Control Investments*—Majority-owned control investments comprise 18.5% of our investment portfolio. Market quotations are not readily available for these investments; therefore, we use a combination of market and income approaches to determine their fair value. Typically, private companies are bought and sold based on multiples of EBITDA, cash flows, net income, revenues or, in limited cases, book value. Generally, we apply multiples that we observe for other comparable companies to relevant financial data for the portfolio company. Also, in a limited number of cases, we use income approaches to determine the fair value of these securities, based on our projections of the discounted future free cash flows that the portfolio company will likely generate, as well as industry derived capital costs. Our valuation approaches for majority-owned investments estimate the value were we to sell or exit the investment. These valuation approaches assume the highest and best use of the investment by market participants and consider the value of our ability to control the portfolio company's capital structure and the timing of a potential exit.
- *Non-Majority-Owned Control Investments*—Non-majority owned control investments comprise 1.2% of our investment portfolio. For our non-majority owned control equity investments, we use the same market and income valuation approaches used to value our majority-owned control investments. For non-majority-owned control debt investments, we estimate fair value using the market yield approach based on the expected future cash flows discounted at the loans' effective interest rates, based on our estimate of current market rates. We may adjust discounted cash flow calculations to reflect other market conditions or the perceived credit risk of the borrower.
- *Non-Control Investments*—Non-control investments comprise 80.3% of our investment portfolio. Quoted prices are not available for 81.0% of our non-control investments. For our non-control equity investments, we use the same market and income approaches used to value our control investments. For non-control debt investments, we estimate fair value using a market-yield approach based on the expected future cash flows discounted at the loans' effective interest rates, based on our estimate of current market rates. We may adjust discounted cash flow calculations to reflect other market conditions or the perceived credit risk of the borrower.
- *Thinly Traded and Over-the-Counter Securities*—Generally, we value securities that are traded in the over-the-counter market or on a stock exchange at the average of the prevailing bid and ask prices on the date of the relevant period end. However, we may apply a discount to the market value of restricted or thinly traded public securities to reflect the impact that these restrictions have on the value of these securities. We review factors including the trading volume, total securities outstanding and our percentage ownership of securities to determine whether the trading levels are active (Level 1) or inactive (Level 2). As of September 30, 2011, these securities represented 15.3% of our investment portfolio.

Our valuation analyses incorporate the impact that key events could have on the securities' values, including public and private mergers and acquisitions, purchase transactions, public offerings, letters of intent and subsequent debt or equity sales. Our valuation analyses also include key external data, such as market changes and industry valuation benchmarks. We also use independent valuation firms to provide additional data points for

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our quarterly valuation analyses. Our general practice is to obtain an independent valuation or review of valuation at least once per year for each portfolio investment that had a fair value in excess of \$5.0 million, unless the fair value has otherwise been derived through a sale of some or all of our investment in the portfolio company or is a new investment made within the last twelve months. As set forth in more detail in the following table, in total, either we obtained a valuation or review from an independent firm, considered new investments made or used market quotes in the preceding twelve month period for 99.2% of the fair value of our investment portfolio as of September 30, 2011.

	September 30, 2011					
	Investments at Fair Value			Percent of		
	Debt	Equity	Total	Debt Portfolio	Equity Portfolio	Total Portfolio
<i>(dollars in thousands)</i>						
<b>Independent valuations/reviews, recent transactions or market quotes</b>						
<b>Independent valuation/review prepared</b>						
Third quarter 2011	\$152,917	\$ 39,336	\$192,253	22.7%	26.2%	23.3%
Second quarter 2011	56,809	16,833	73,642	8.4	11.2	8.9
First quarter 2011	104,997	3,830	108,827	15.6	2.5	13.2
Fourth quarter 2010	116,748	69,061	185,809	17.3	45.9	22.5
<b>Total independent valuations/reviews</b>	<b>431,471</b>	<b>129,060</b>	<b>560,531</b>	<b>64.0</b>	<b>85.8</b>	<b>67.9</b>
<b>Fair value from</b>						
Market quotes (Level 2)	116,958	2,154	119,112	17.4	1.4	14.5
Pending sales of investments or letters of intent	28,378	14,644	43,022	4.2	9.8	5.2
<b>Fair value from market quotes and pending sales</b>	<b>145,336</b>	<b>16,798</b>	<b>162,134</b>	<b>21.6</b>	<b>11.2</b>	<b>19.7</b>
<b>New investments made during the 12 months ended September 30, 2011</b>	<b>94,051</b>	<b>1,195</b>	<b>95,246</b>	<b>14.0</b>	<b>0.8</b>	<b>11.6</b>
<b>Total portfolio evaluated</b>	<b>670,858</b>	<b>147,053</b>	<b>817,911</b>	<b>99.6</b>	<b>97.8</b>	<b>99.2</b>
<b>Not evaluated during the 12 months ended September 30, 2011</b>	<b>3,003</b>	<b>3,259</b>	<b>6,262</b>	<b>0.4</b>	<b>2.2</b>	<b>0.8</b>
<b>Total investment portfolio</b>	<b>\$673,861</b>	<b>\$150,312</b>	<b>\$824,173</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

The majority of the valuations performed by the independent valuation firms utilize proprietary models and inputs. We have used, and intend to continue to use, independent valuation firms to provide additional support for our internal analyses. Our board of directors considers our valuations, as well as the independent valuations and reviews, in its determination of the fair value of our investments. The fair value of our interest rate swaps is based on a binding broker quote, which is based on the estimated net present value of the future cash flows using a forward interest rate yield-curve in effect as of the measurement period.

Due to the uncertainty inherent in the valuation process, such fair value estimates may differ significantly from the values that would have been used had a ready market for the securities existed, and the differences could be material. In addition, changes in the market environment and other events that may occur over the life of the investments may cause the gains or losses that we ultimately realize on these investments to differ from the valuations currently assigned.

### RECENT ACCOUNTING PRONOUNCEMENTS

#### TROUBLED DEBT RESTRUCTURING

In April 2011, Financial Accounting Standards Board, or FASB, issued *Accounting Standards Update 2011-02—A Creditor's Determination of Whether a Restructuring is a Troubled Debt Restructuring*, or ASU 2011-02. This standard amends previous guidance provided in *Accounting Standards Codification 310-40—Receivables—Troubled Debt Restructurings by Creditors*. ASU 2011-02 provides additional guidance and criteria on how companies should determine whether a restructuring or refinancing of an existing financial receivable represents a troubled debt restructuring. Companies must assess whether the restructuring or refinancing of an existing financial receivable is a troubled debt restructuring in order to determine how to account for the remaining unamortized portion of certain fees, such as origination fees, associated with the original debt investment. ASU 2011-02 is effective for the first interim period beginning on or after June 15, 2011. We adopted this standard beginning with the quarter ended September 30, 2011. Our adoption of this update did not have a material impact on our financial position or results of operations.

#### FAIR VALUE

In May 2011, the FASB issued *Accounting Standards Update No. 2011-04—Fair Value Measurement: Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and*

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*IFRSs*, or ASU 2011-04. ASU 2011-04 clarifies the application of existing fair value measurement and disclosure requirements, changes the application of some requirements for measuring fair value and requires additional disclosure for fair value measurements. The disclosure requirements are expanded to include for fair value measurements categorized in Level 3 of the fair value hierarchy: 1) a quantitative disclosure of the unobservable inputs and assumptions used in the measurement; 2) a description of the valuation processes in place; and 3) a narrative description of the sensitivity of the fair value to changes in unobservable inputs and interrelationships between those inputs. ASU 2011-04 is effective for interim and annual periods beginning after December 15, 2011, for public entities. We will adopt this standard beginning on January 1, 2012. We are evaluating the impact, if any, that our adoption of this update may have on our financial position or results of operations. However, since this accounting standards update primarily requires expanded disclosure related to Category 3 financial assets and liabilities, we do not anticipate that the implementation of this standard will have a significant impact on our process for measuring fair values, our financial position or results of operations.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There were a number of indicators of modest growth in the United States' economy during the first nine months of 2011. However, certain leading and lagging indicators suggest rising risk and volatility and increasing concerns about the continuing expansion of the United States' economy. In the event of renewed financial turmoil affecting the banking system and financial markets, the financial position and results of operations of certain of the middle-market companies in our portfolio could be affected adversely, which ultimately could lead to difficulty in their meeting debt service requirements and an increase in defaults.

Interest rate sensitivity refers to the change in earnings that may result from changes in the level of interest rates. Our net interest income is affected by changes in various interest rates, including LIBOR, prime rates and commercial paper rates. As of September 30, 2011, approximately 88.6% of our loan portfolio, at fair value, bore interest at a spread to LIBOR or prime rate, and 11.4% at a fixed interest rate. As of September 30, 2011, approximately 76.8% of our loan portfolio, at fair value, had LIBOR floors between 1.0% and 3.0% on the LIBOR base index and prime floors between 1.75% and 6.0%. The three-month weighted-average LIBOR interest rate was 0.30% as of September 30, 2011. Thus, the LIBOR floors in these loan investments lessen the impact of such historically low LIBOR rates.

We regularly measure exposure to interest rate risk. We assess interest rate risk and we manage our interest rate exposure on an ongoing basis by comparing our interest rate sensitive assets to our interest rate sensitive liabilities. Based on this review, we determine whether or not any hedging transactions are necessary to mitigate exposure to changes in interest rates. We also enter into derivative transactions in connection with our financing vehicles. During the quarter ended March 31, 2009, in connection with our financing vehicle requirements, we entered into two interest rate swaps, having notional amounts of \$8.7 million and \$12.5 million at interest rates of 9.0% and 13.0%, respectively. These swap agreements expired in August 2011.

The following table shows a comparison of the interest rate base for our interest-bearing cash, outstanding commercial loans, at cost, and our outstanding borrowings as of September 30, 2011 and December 31, 2010:

<i>(in thousands)</i>	September 30, 2011		December 31, 2010	
	Interest Bearing Cash and Commercial Loans	Borrowings	Interest Bearing Cash and Commercial Loans	Borrowings
Money market rate	\$ 52,442	\$ —	\$ 23,244	\$ —
Prime rate	28,089	—	49,227	—
<b>LIBOR</b>				
30-day	61,391	—	92,787	—
60-day	240	—	—	—
90-day	517,836	316,880	478,896	311,880
180-day	18,924	—	—	—
Commercial paper	—	55,822	—	100,251
Fixed rate	110,790	117,317	257,536	134,751
<b>Total</b>	<b>\$ 789,712</b>	<b>\$490,019</b>	<b>\$ 901,690</b>	<b>\$546,882</b>

Based on our September 30, 2011 balance sheet, the following table shows the impact to net income of hypothetical base rate increases in interest rates, assuming no changes in our investment and borrowing structure. The impact to net income of hypothetical base rate decreases in interest rates is not shown in the

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following table because as of September 30, 2011, the quarterly average LIBOR was 0.30% and a 100-basis point decrease could not occur:

*(dollars in thousands)*

<u>Basis Point Change</u>	<u>Interest Income</u>	<u>Interest Expense</u>	<u>Net Income (Loss)</u>
100	\$ 1,891	\$ 3,727	\$ (1,836)
200	7,603	7,454	149
300	15,486	11,181	4,305

We maintain a portion of our excess cash in secure interest-bearing accounts. As we redeploy additional cash into interest-bearing accounts and we originate new investments, our sensitivity to interest rate fluctuations and our net loss from a hypothetical increase in interest rates should decrease. As of September 30, 2011, we had a total of \$170.4 million of unrestricted cash, restricted cash and cash in securitization accounts of which \$117.9 million was in non-interest bearing accounts. On October 20, 2011, the next payment date for our Commercial Loan Trust 2006-1 facility, we used \$80.2 million of securitized cash in that facility (primarily representing previous principal collections) to repay a portion of that facility. Subsequent collections of principal that we receive from collateral held by Commercial Loan Trust 2006-1 will be used to repay that facility.

For each \$10.0 million of cash in non-interest bearing accounts that we redeploy into variable interest rate investments, the net loss from our sensitivity to interest rate fluctuations will decrease by approximately \$100,000 for each 100 basis point increase in interest rates.

### **ITEM 4. CONTROLS AND PROCEDURES**

#### ***DISCLOSURE CONTROLS AND PROCEDURES***

Our management, with the participation of our Chief Executive Officer, Chief Financial Officer and Chief Accounting Officer, evaluated the effectiveness of our disclosure controls and procedures as of September 30, 2011. The term “disclosure controls and procedures” (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in 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 a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company’s management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the foregoing evaluation of our disclosure controls and procedures as of September 30, 2011, our Chief Executive Officer, our Chief Financial Officer and our Chief Accounting Officer concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

#### ***INTERNAL CONTROL OVER FINANCIAL REPORTING***

No change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act), occurred during the fiscal quarter ended September 30, 2011 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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### PART II. OTHER INFORMATION

#### ITEM 1. LEGAL PROCEEDINGS.

From time to time, we are 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 condition or results of operations. During the quarter ended September 30, 2011, there were no new or material developments in legal proceedings.

#### ITEM 1A. RISK FACTORS.

*Investing in our common stock may be speculative and involves a high degree of risk. You should consider carefully the risks described below and all other information contained in this Quarterly Report on Form 10-Q, including our financial statements and the related notes and the schedules and exhibits to this Quarterly Report on Form 10-Q.*

*Set forth below and elsewhere in this Quarterly Report on Form 10-Q and in other documents that we file with the SEC are descriptions of the risks and uncertainties that could cause our actual results to differ materially from the results contemplated by the forward-looking statements contained in this Quarterly Report on Form 10-Q. The description below includes any material changes to, and supersedes the description of, the risk factors affecting our business previously disclosed in "Part I, Item 1A. Risk Factors" of our Annual Report on Form 10-K for the fiscal year ended December 31, 2010.*

**Substantially all of our portfolio investments are not publicly traded and, as a result, there is uncertainty as to the value of our portfolio investments. If our determinations regarding the fair value of our investments were materially higher than the values that we ultimately realize upon the disposition of such investments, our NAV could be affected adversely.**

In accordance with the 1940 Act and accounting principles generally accepted in the United States, we carry substantially all of our portfolio investments at fair value as determined in good faith by our board of directors. Typically, there is no public market for the securities of the privately held companies in which we have invested and generally will continue to invest. As a result, we value these securities quarterly at fair value as determined in good faith by our board of directors.

Whenever possible, we value securities at market value; however, only a small percentage of our investment portfolio is traded publicly. We value the investments that are not publicly traded based on various factors during our valuation process and our investment and valuation committee reviews and approves these valuations. The types of factors that may be considered in the determination of the fair value of these investments include public and private mergers and acquisitions transactions, comparisons to publicly traded comparable companies, third-party assessments of valuation, discounted cash flow analyses, the nature and realizable value of any collateral, the portfolio company's earnings and its ability to make payments, the markets in which the portfolio company does business, market-based pricing and other relevant factors. In determining fair value in good faith, we generally obtain financial and other information from portfolio companies, which may include unaudited, projected or pro forma financial information. Our board of directors also uses several independent valuation firms to aid it in determining the fair value of these investments. Because our valuations, and particularly the valuations of private securities and private companies, are inherently uncertain, they may fluctuate over short periods of time and may be based on estimates. Our determinations of fair value may differ materially from the values that would have been used if a readily available market for these investments existed and from the amounts we may realize on any disposition of such investments. If our determinations regarding the fair value of our investments were materially higher than the values that we ultimately realize upon the disposition of such investments, our NAV could be affected adversely.

**Economic downturns or lingering effects of a capital market disruption and recession could impair our portfolio companies' financial positions and operating results, which, in turn, could harm our operating results.**

Many of the companies in which we have made, or may make, investments are, and may continue to be, susceptible to economic downturns or recessions. During the recession that occurred from late 2007 through

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mid-2009, the stock market declined and has not recovered to pre-recession levels. The U.S. government has acted to restore liquidity and stability to business, taxpayers and the financial system, but there can be no assurance these regulatory programs, stimulus initiatives and tax reductions either will continue or will have a long-term beneficial impact. In addition, equity and credit markets were characterized by increasing asset prices, lower volatility and improved liquidity beginning in mid-2009. In the event of renewed financial turmoil affecting the banking system and financial markets, additional consolidation of the financial services industry or significant financial service institution failures, there could be a new or incremental tightening in the credit markets, low liquidity and extreme volatility in fixed-income, credit, currency and equity markets. To the extent that recessionary conditions recur, the economy remains stagnant or the economy fails to return to pre-recession levels, the financial results of middle-market companies, like those in which we invest, may experience deterioration, which ultimately could lead to difficulty in meeting debt service requirements and an increase in defaults.

Adverse economic conditions have decreased the value of some of our loans and equity investments and lingering after-effects of these economic conditions, may further decrease such value. These conditions have contributed to, and could continue to contribute to, additional losses of value in our portfolio and decreases in our revenues, net income and net assets. If prolonged, unfavorable or uncertain economic and market conditions could affect the ability of our portfolio companies to repay our loans or engage in a liquidity event, such as a sale, merger, recapitalization or initial public offering. Therefore, the number of non-performing assets may increase and the value of one or more of our portfolio companies may decrease during such periods. Adverse economic conditions also may decrease the value of collateral securing some of our loans and the value of our equity investments.

**Economic recessions or downturns could impair the ability of our portfolio companies to refinance or repay loans, which, in turn, could increase our non-performing assets, decrease the value of our portfolio, reduce our volume of new loans and have an adverse effect on our operating results.**

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

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

The economic recession in the United States resulted in a reduction in the availability of debt and equity capital for the market as a whole, and financial services firms in particular. The effects of the recession continue to constrain us and other companies in the financial services sector, limiting or completely preventing access to markets for debt and equity capital needed to maintain operations, continue investment originations and to grow. On September 30, 2011, we withdrew our application for a second license from the SBA to operate an additional subsidiary (Solutions Capital II, L.P.) as an SBIC until such time as the SBA has an opportunity to evaluate, among other things, the organizational impact of our recent restructuring and changes in management. We will not be able to utilize SBA leverage beyond that available through Solutions Capital I, L.P. unless we receive a second license from the SBA. In addition, the available debt capital may be at a higher cost and/or less favorable terms and conditions. Equity capital is, and may continue to be, difficult to raise because we generally are not able to issue and sell our common stock at a price below NAV per share without stockholder approval. These economic and market conditions and inability to raise capital have had a negative effect on our origination process, curtailed our ability to grow and had a negative impact on our liquidity and operating results. The prolonged inability to raise additional capital could further constrain our liquidity, negatively impact our business prospects, cause the departure of key employees and have an adverse impact on our operating results.

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

Even though we have structured some of our investments as senior loans, if one of our portfolio companies were to go bankrupt, depending on the facts and circumstances, including the extent to which we provided managerial assistance to that portfolio company, a bankruptcy court might re-characterize our debt investments and subordinate all, or a portion, of our claims to those of other creditors. Holders of debt instruments ranking senior to our investments typically would be entitled to receive payment in full before we receive any distributions. After

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repaying such senior creditors, such portfolio company may not have any remaining assets to use to repay its obligation to us. We may also be subject to lender liability claims for actions taken by us with respect to a borrower's business or in instances in which we exercised control over the borrower. It is possible that we could become subject to a lender's liability claim, including claims associated with significant managerial assistance that we may have provided to our portfolio companies

**Investing in 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.**

Our portfolio consists primarily of debt and equity investments in privately owned middle-market companies. Investing in middle-market companies involves a number of significant risks. Typically, the debt in which we invest may be rated below investment grade by one or more rating agency. Compared to larger publicly traded companies, these middle-market companies may be in a weaker financial position and experience wider variations in their operating results, which may make them more vulnerable to economic downturns. Typically, these companies need more capital to compete; however, their access to capital is limited and their cost of capital is often higher than that of their competitors. Our portfolio companies face intense competition from larger companies with greater financial, technical and marketing resources and their success typically depends on the managerial talents and efforts of an individual or a small group of persons. Therefore, the loss of any of its key employees could affect a portfolio company's ability to compete effectively and harm its financial condition. Further, some of these companies conduct business in regulated industries that are susceptible to regulatory changes. These factors could impair the cash flow of our portfolio companies and result in other events, such as bankruptcy. These events could limit a portfolio company's ability to repay its obligations to us, which may have an adverse affect on the return on, or the recovery of, our investment in these businesses. Deterioration in a borrower's financial condition and prospects may be accompanied by deterioration in the value of the loan's collateral.

Some of these companies cannot obtain financing from public capital markets or from traditional credit sources, such as commercial banks. Accordingly, loans made to these types of companies pose a higher default risk than loans made to companies that have access to traditional credit sources. Generally, little, if any, public information is available about such companies. Therefore, we must rely on our employees' diligence to obtain information necessary to make well-informed investment decisions. If we do not uncover material information about these companies, we may not make a fully informed investment decision, which could, in turn, cause us to lose money on our investments.

**If we fail to invest a sufficient portion of our assets in qualifying assets, we could lose our BDC status.**

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. Thus, we may be precluded from investing in potentially attractive investments if such investments are not qualifying assets for purposes of the 1940 Act. If we fail to invest a sufficient portion of our assets in qualifying assets, we could lose our status as a BDC, which would have a material adverse effect on our business, financial condition and results of operations. In addition, there is a risk that this restriction could prevent us from making additional investments in our existing portfolio companies, which could cause our position to be diluted. We could also be forced to sell certain of our investments to comply with the 1940 Act, which may result in us receiving significantly less than the current value of such investments.

**Portfolio company litigation could result in additional costs, the diversion of management time and resources or have an adverse impact on the fair value of one or more of our portfolio companies.**

In the course of providing significant managerial assistance to certain of our portfolio companies, we may serve as directors on the boards of such companies. To the extent that litigation arises out of our investments in these companies, we may be named as a defendant in such litigation, which could result in additional costs and the diversion of management time and resources. In addition, litigation involving our portfolio companies could have an adverse impact on the fair value of one or more of our portfolio companies.

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### **Our financial position and results of operations could be affected adversely if a significant portion of our portfolio were invested in industries that experience adverse economic or business conditions.**

From time to time, we target specific industries in which to invest on a recurring basis. This practice could concentrate a significant portion of our portfolio in a specific industry. For example, as of September 30, 2011, approximately 10.5% and 9.8% of the fair value of our investment portfolio was composed of investments in the healthcare and business services industries, respectively. If an industry in which we have significant investment or revenue concentrations suffers from adverse business or economic conditions, as these industries have to varying degrees, a material portion of our investment portfolio could be affected adversely, which, in turn, could adversely affect our financial position and results of operations.

### **Our financial results could be affected adversely if a significant portfolio investment fails to perform as expected or if the value of a portfolio company decreases.**

Our total investment in companies may be significant individually or in the aggregate. As a result, if a significant investment in one or more companies fails to perform as expected, our financial results could be affected adversely and the magnitude of the loss could be more significant than if we had made smaller investments in a greater number of companies.

Broadview Network Holdings, Inc., or Broadview, a publicly traded competitive local exchange carrier, or CLEC, serving primarily business customers. As of September 30, 2011, we held preferred stock in Broadview with a \$29.2 million fair value. As of September 30, 2011, our investment in Broadview represented 3.5% of the fair value of our investment portfolio. During the nine months ended September 30, 2011, we recorded net investment losses of \$73.8 million related to our Broadview investment. In June 2011, Broadview terminated its previously announced tender offer for \$301.4 million of its 11 <sup>3</sup>/<sub>8</sub> % Senior Secured Notes, which mature in September 2012, following Broadview's review of market conditions. In addition, Broadview had \$17.1 million of borrowings outstanding under its revolving credit facility which becomes payable on February 23, 2012. We reflected these liquidity events in the fair value of our investment as of September 30, 2011. The bond market continued to be challenging during the three months ended September 30, 2011 and the Broadview's Senior Secured Notes were recently downgraded. If Broadview is unable to refinance these debt facilities by their respective maturity dates, the value of our portfolio investment in Broadview could decline by up to the remaining fair value and we may be required to recognize additional unrealized depreciation on this investment. Also, if Broadview's performance deteriorates or valuation multiples contract further in future periods, we may be required to recognize additional unrealized depreciation on this investment. Our ability to recognize income from our investment in Broadview in future periods depends on the performance and value of Broadview.

### **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 public and private funds, commercial and investment banks, commercial financing companies and, to the extent they provide an alternative form of financing, private equity funds. Additionally, because competition for investment opportunities generally has increased in recent years among alternative investment vehicles, such as hedge funds, those entities have begun to invest in areas in which traditionally they have not invested. As a result of these entrants, competition for investment opportunities has intensified in recent years and may intensify further in the future. Some of our existing and potential competitors are substantially larger and have considerably greater financial, technical and marketing resources than we do. For example, some competitors may have a lower cost of funds and access to funding sources that are not available to us. In addition, some of our competitors may have higher risk tolerances or different risk assessments, which could allow them to consider a wider variety of investments and establish more relationships than we can. Furthermore, many of our competitors are not subject to the regulatory restrictions and valuation requirements that the 1940 Act imposes on us as a BDC. 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 existing and potentially increasing competition, we may not be able to take advantage of attractive investment opportunities from time to time. We can offer no assurance that we will be able to identify and make investments that are consistent with our investment objective.

We do not seek to compete primarily based on the interest rates we offer. We believe that some of our competitors make loans with interest rates that are comparable to, or lower than, the rates we offer.

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We may lose investment opportunities if we do not match our competitors' pricing, terms and structure. If we match our competitors' pricing, terms and structure, we may experience decreased net interest income and increased risk of credit loss.

**We have experienced a period of capital markets disruption. This disruption has contributed to a decrease in our NAV and stock price, and could have an adverse impact on our business and operations.**

During the nine months ended September 30, 2011, nearly all classes of assets in the financial services industry and the securities markets continued to be constrained and liquidity continued to be extremely limited. During this period, the global markets continued to be characterized by substantially increased volatility, short-selling and an overall loss of investor confidence. While certain recent economic indicators have shown modest improvements in the capital markets, these indicators could worsen. In the event of renewed financial turmoil affecting the banking system and financial markets, additional consolidation of the financial services industry, or significant financial service institution failures, there could be a new or incremental tightening in the credit markets, low liquidity and extreme volatility in fixed-income, credit, currency and equity markets. In addition, the risk remains that there could be a number of follow-on effects from the credit crisis on our business.

We may be unable to monetize assets in a challenging market environment that may preclude buyers from making investments at the fair values established by our board of directors. We are susceptible to the risk of significant loss, if we are forced to discount the value of our investments in order to monetize assets to provide liquidity to fund operations, meet our liability maturities and maintain compliance with our debt covenants. In addition, if the fair value of our assets declines substantially, we may fail to maintain the BDC asset coverage ratios stipulated by the 1940 Act. Any such failure would affect our ability to issue senior securities, including borrowings, pay dividends and could cause us to breach certain covenants in our credit facilities, which could materially impair our business operations. Further asset value degradation may result from circumstances that we may be unable to control, such as a severe decline in the value of the U.S. dollar, a protracted economic downturn or an operational problem that affects third parties or us. Ongoing disruptive conditions could cause our stock price and NAV to decline, restrict our business operations and adversely impact our results of operations and financial condition. As of September 30, 2011, our common stock was trading at \$3.96 per share, or at 61% of NAV.

**Fluctuations in interest rates could affect our income adversely.**

Because we sometimes borrow to make investments, our net income depends, in part, on the difference between the rate at which we borrow funds and the rate at which we invest these funds. Because a significant portion of our assets and liabilities are priced using various short-term rate indices, including one-month to six-month LIBOR, commercial paper rates and the prime rate, the timing of changes in market interest rates or in the relationship between interest rate indices could affect the interest rates earned on our interest-earning assets differently than the interest rates we pay on interest-bearing liabilities. As a result, significant changes in market interest rates could have a material adverse effect on our net income.

A significant increase in market interest rates could harm our ability to attract new portfolio companies and originate new loans and investments, our non-performing assets could increase and the value of our portfolio could decrease because our floating-rate loan portfolio companies may be unable to meet higher payment obligations. As of September 30, 2011, approximately 88.6% of the fair value of our loan portfolio was at variable rates based on a LIBOR benchmark or prime rate and approximately 11.4% of the fair value of our loan portfolio was at fixed rates. The weighted-average LIBOR interest rate was 0.29% as of September 30, 2011. As of September 30, 2011, approximately 76.8% of the fair value of our loan portfolio had LIBOR floors between 1.0% and 3.0% on the LIBOR base index and prime floors between 1.75% and 6.0%. These floors minimize our exposure to significant decreases in interest rates.

**The downgrade in the U.S. credit rating could have a material adverse effect on our business, financial conditions and results of operations.**

On August 5, 2011, Standard & Poor's downgraded the U.S. credit rating to AA+ from its top rank of AAA. The current U.S. debt ceiling and budget deficit concerns have increased the possibility of other credit-rating agency downgrades and an economic slowdown. The downgrade of the U.S. credit rating could have a material adverse effect on the financial markets and economic conditions in the United States and throughout the world. Additionally, austerity measures necessary to reduce the deficit could accelerate an already slowing economy in the near term.

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Downgrading of the U.S. credit rating could negatively affect the trading market for U.S. government securities and would likely affect the credit risk associated with investments in U.S. Treasury securities. In addition, adverse market and economic conditions that could occur due to a downgrade of the U.S. credit rating on the United States' debt could result in rapidly rising interest rates, a falling dollar, shakier financial markets and slowing or negative economic growth in the near term. These events could adversely affect our business in many ways, including, but not limited to, adversely affecting our portfolio companies' ability to obtain financing, or obtaining financing but at significantly lower valuations than the preceding financing rounds. If any of these events were to occur, it could have a material adverse effect on our business, financial condition and results of operations.

### **Our shares of common stock may continue to trade at discounts from NAV, which limits our ability to raise additional equity capital.**

Shares of closed-end investment companies frequently trade at a market price that is less than the NAV attributable to those shares. This characteristic of closed-end investment companies is separate and distinct from the risk that our NAV per share may decline. It is not possible to predict whether our common stock will trade at, above, or below NAV. In the recent past, the stocks of BDCs as an industry, including shares of our common stock, have traded below NAV and at near historic lows as a result of concerns over liquidity, leverage restrictions and distribution requirements. When our common stock trades below its NAV per share, we generally are unable to issue additional shares of our common stock at the then-current market price without first obtaining approval for such issuance from our stockholders and our independent directors.

### **Stockholders may incur dilution if we sell shares of our common stock in one or more offerings at prices below the then-current NAV per share of our common stock or if we issue debt securities that are convertible into shares of our common stock.**

Since mid-2008, our common stock has traded consistently, and at times significantly, below NAV. The 1940 Act prohibits us from selling shares of our common stock at a price below the current NAV per share of our stock, subject to certain exceptions. One of these exceptions allows the sale of common stock at a price below NAV if the sale is approved by the holders of a majority of our outstanding voting securities and by holders of a majority of our outstanding voting securities who are not affiliated persons of us, and our board of directors make certain determinations prior to any such sale.

If we were to sell shares of our common stock below NAV per share, such sales would result in an immediate dilution to the NAV per share. This dilution would occur as a result of the sale of shares at a price below the then-current NAV per share of our common stock and 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. The greater the difference between the sale price and the NAV per share at the time of the offering, the more significant the dilutive impact would be. 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, if any, cannot currently be predicted.

If we raise additional funds by issuing more common stock or senior securities convertible into, or exchangeable for, our common stock, then the percentage ownership of our stockholders at that time will decrease, and investors might experience dilution.

### **We may in the future decide to issue 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.**

Because preferred stock is another form of leverage and the dividends on any preferred stock we might issue must be cumulative, preferred stock has the same risks to our common stockholders as borrowings. Payment of any such dividends and repayment of the liquidation preference of such preferred stock must take preference over any dividends or other payments to our common stockholders, and preferred stockholders are not subject to any of our expenses or losses and are not entitled to participate in any income or appreciation in excess of their stated preference. In addition, holders of any preferred stock we might issue would have the right to elect members of the board of directors and class voting rights on certain matters, including changes in fundamental investment restrictions and conversion to open-end status and, accordingly, could veto any such changes.

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

We have elected to be taxed for federal income tax purposes as a RIC, under Subchapter M of the Internal Revenue Code. To qualify as a RIC under the Internal Revenue Code, we must meet certain source-of-income, asset diversification and annual distribution requirements and maintain our status as a BDC, including:

- The annual distribution requirement for a RIC is satisfied if we distribute 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, on an annual basis. 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 these requirements, 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 Internal Revenue 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 as a RIC for any reason and become 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 our stockholders and us.

### **A failure on our part to maintain our qualification as a BDC would significantly reduce our operating flexibility.**

If we were to continuously fail to qualify as a BDC, we might be subject to regulation as a registered closed-end investment company under the 1940 Act, which would significantly decrease our operating flexibility. In addition, failure to comply with the requirements imposed on BDCs by the 1940 Act could cause the SEC to bring an enforcement action against us. For additional information on the qualification requirements of a BDC, see the disclosure under the caption *Item 1. Business—Regulation of our Annual Report on Form 10-K* for the fiscal year ended December 31, 2010.

### **We have substantial indebtedness and, if we do not service our debt arrangements adequately, our business could be harmed materially.**

As of September 30, 2011, we had \$490.0 million of outstanding borrowings under our debt facilities. As of September 30, 2011, the weighted-average annual interest rate on all of our outstanding borrowings was 2.3%, excluding the amortization of deferred debt issuance costs. Our ability to service our debt arrangements depends largely on our financial performance and will be subject to prevailing economic conditions and competitive pressures.

Under our warehouse financing facility, or SunTrust Warehouse, funded through Three Pillars Funding LLC, an asset-backed commercial paper conduit administered by SunTrust Robinson Humphrey, Inc., and our debt securitization through MCG Commercial Loan Trust 2006-1, we are subject to financial and operating covenants that restrict our business activities, including limitations that could hinder our ability to finance additional loans and investments or to make the distributions required to maintain our status as a RIC under Subchapter M of the Internal Revenue Code and impact our liquidity. In addition, these facilities include various affirmative and negative covenants, as well as certain cross-default provisions, whereby a payment default or acceleration under one of our debt facilities could, in certain circumstances, constitute a default under other debt facilities. In the event that there is a breach of one of the covenants contained in one of our debt facilities that has not been cured within any

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applicable cure period the lenders thereunder would have the ability to, in certain circumstances, accelerate the maturity of the indebtedness outstanding under that facility and exercise certain other remedies. In addition, our subsidiaries have sold some of our loans to trusts that serve as the vehicles for our securitization facilities, and these trusts, which are bankruptcy remote, hold legal title to these assets. However, in the event of a default on these loans held by the trusts, we could potentially bear losses to the extent that the fair value of our collateral exceeds our borrowings. The fair value of our excess collateral was \$200.2 million as of September 30, 2011.

Each of our SunTrust Warehouse and our debt securitization through MCG Commercial Loan Trust 2006-1 requires us to maintain credit ratings for each loan in the collateral pools of these facilities as determined by specified international independent rating agencies. We are subject to periodic review and updates of these credit estimates by these rating agencies that could cause portions of the collateral to become disqualified as eligible assets if credit estimates deteriorate. In the event that a portion of the eligible assets becomes disqualified, loan payments that inure to our benefit could be otherwise diverted to reduce outstanding debt within these facilities. Such diversions could be material in amount and could hinder our ability to finance additional loans, operate our business or make distributions to our stockholders. In addition, if credit estimates deteriorate significantly, an event of default or a termination event could be triggered under these facilities, which would entitle the trustee or administrative agent to exercise available remedies, including selling the collateral securing these facilities and applying the proceeds to reduce outstanding borrowings under these facilities.

Under the terms of our Series 2007-A unsecured notes we are also subject to financial and operating covenants that restrict our business activities, including our ability to incur certain additional indebtedness, effect debt and stock repurchases in specified circumstances or through the use of borrowings or unrestricted cash, or pay dividends above certain levels.

Decreases in the fair values of our portfolio company investments, which we record as unrealized depreciation, could affect certain covenants in our credit facilities. Our SunTrust Warehouse requires that we maintain a consolidated tangible net worth of not less than \$450.0 million plus 50% of the proceeds from any equity issuances after February 26, 2009. In the event that our investments experience a significant amount of unrealized depreciation, we could breach one or more of the covenants in our credit facilities, pursuant to which our lenders might, among other things, require full and immediate payment. The SunTrust Warehouse and MCG Commercial Loan Trust 2006-1 are non-recourse to MCG, the parent, therefore, in the event of a breach of one or more of the covenants, the lenders under these facilities may only look to the collateral in these facilities to satisfy the respective outstanding obligations under the SunTrust Warehouse and MCG Commercial Loan Trust 2006-1. The Series 2007-A unsecured notes require that we maintain a consolidated stockholders' equity of \$425.0 million for the periods ending as of and after June 30, 2011. As of September 30, 2011, our stockholders' equity was \$496.5 million.

In addition to the credit facility, Solutions Capital I, L.P. has issued SBA debentures that require our SBIC to generate sufficient cash flow to make required interest payments. Further, Solutions Capital I, L.P. must maintain a minimum capitalization that if impaired could materially and adversely affect our liquidity, financial condition and results of operations. Our borrowings under our SBA debentures are collateralized by the assets of Solutions Capital I, L.P.

As a BDC, we are not permitted to incur indebtedness or issue senior securities, including preferred stock, unless immediately after such borrowing we have an asset coverage for total borrowings (excluding borrowings by our SBIC facility) of at least 200%. In addition, we may not be permitted to declare any cash dividend or other distribution on our outstanding common stock, or purchase any such shares, unless, at the time of such declaration or purchase, we have an asset coverage of at least 200% after deducting the amount of such dividend, distribution or purchase price. If we are unable to meet this asset coverage requirement, 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 until we are in compliance with the 200% threshold requirement. As of September 30, 2011, our asset coverage ratio was 230%.

### **If we are not able to refinance or renew our debt or are not able to do so on favorable terms, our operations could be affected adversely.**

We cannot be certain that we will be able to renew our credit facilities as they mature or to establish new borrowing facilities to provide capital for normal operations, including new originations. Reflecting concern about the stability of the financial markets, many lenders and institutional investors have reduced or ceased providing funding to borrowers. Certain leading and lagging indicators suggest near-term volatility and a slowdown of the United States' economy. If we are unable to renew or refinance such facilities and establish new facilities, at a

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reasonable size, our liquidity will be reduced significantly. Even if we are able to renew or refinance these facilities or consummate new borrowing facilities, we may not be able to do so on favorable terms. If we are unable to repay amounts outstanding under such facilities and they are declared in default or if we are unable to renew or refinance these facilities, our operations could be affected adversely.

In addition to the SunTrust Warehouse, Solutions Capital I, L.P. has issued SBA debentures that require our SBIC to generate sufficient cash flow to make required interest payments. Further, Solutions Capital I, L.P. must maintain a minimum capitalization that if impaired could materially and adversely affect our liquidity, financial condition and results of operations. Our borrowings under our SBA debentures are collateralized by the assets of Solutions Capital I, L.P.

Historically, we have also purchased rated syndicated private debt in larger companies through our on-balance sheet securitization trust—Commercial Loan Trust 2006-1. This securitized trust included a five-year reinvestment period, during which the trust was permitted to use principal collections received from repayments of the underlying collateral to purchase new collateral from us. The reinvestment period ended on July 20, 2011 and all future principal collections received will be used to repay the securitized debt. On October 20, 2011, we used \$80.2 million of securitized cash in that facility (primarily representing previous principal collections) to repay a portion of this facility.

Our continued compliance with these requirements depends on many factors, some of which are beyond our control. Material net asset devaluation in connection with additional borrowings could result in an inability to comply with our obligation to restrict the level of indebtedness that we are able to incur in relation to the value of our assets or to maintain a minimum level of stockholders' equity.

**When we are a debt or minority equity investor in a portfolio company, we may not be in a position to have significant influence over the entity. The stockholders and management of the portfolio company may make decisions that could decrease the value of our portfolio holdings.**

We make both debt and minority equity investments. For these investments, we are subject to the risk that a portfolio company may make business decisions with which we disagree, and the stockholders and management of that company may take risks or otherwise act in ways that do not serve our interests. As a result, a portfolio company may make decisions that could decrease the value of our portfolio holdings and have an adverse effect on our financial position and results of operations.

**Investments in equity securities involve a substantial degree of risk.**

We have purchased and may purchase in the future common stock and other equity securities, including warrants. Although equity securities historically have generated higher average total returns than debt securities over the long term, equity securities may experience more volatility in those returns than debt securities. The equity securities we acquire may fail to appreciate, decline in value or lose all value, and our ability to recover our investment will depend on our portfolio company's success. Investments in equity securities involve a number of significant risks, including the risk of further dilution in the event of additional issuances. Investments in preferred securities involve special risks, such as the risk of deferred distributions, illiquidity and limited voting rights.

**You may not receive future distributions.**

In the event that our asset coverage ratio falls below 200%, we will be unable to make distributions until our asset coverage ratio improves. If we do not distribute at least 90% of our investment company taxable income annually, we will suffer adverse tax consequences, including the possible loss of our status as a RIC for the applicable period. We cannot assure you that you will receive any distributions or distributions at a particular level. As of September 30, 2011, our asset coverage ratio was 230%. From December 2001 through September 30, 2011, we declared distributions totaling \$12.64 per common share. Due to the market dislocation, we suspended our distributions from the third quarter of 2008 through the first quarter of 2010. We reinstated our distribution on April 29, 2010 and have continued to declare a quarterly dividend since that time; however, there can be no assurance that distributions will continue in the future.

Future distributions will take into account the requirements for us to distribute the majority of our taxable income to fulfill our distribution requirements as a RIC, together with an assessment of our current and forecasted gains and losses recognized or to be recognized for tax purposes, portfolio transactional events, liquidity, cash earnings and our asset coverage ratio at the time of such decision. We may not be able to achieve operating results or our business may not perform in a manner that will allow us to make any future distributions. In addition, we may not be

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able to make distributions at a specific level or to increase the amount of these distributions from time to time. Due to the BDC asset coverage test applicable to us as a BDC, we may be limited in our ability to make distributions.

**In the future, we may choose to pay distributions with shares of our own common stock. In that case, you may be required to pay tax in excess of the cash you receive.**

While currently it is not our intention to do so, we may in the future elect to distribute taxable dividends that are payable, in part, in shares of our common stock. Under an IRS revenue procedure, we may treat a distribution of our stock payable with respect to our taxable years ending on or before December 31, 2011, as a taxable dividend if, among other things, our stock is publicly traded on an established securities market and each stockholder may elect to receive his or her entire distribution in either cash or our stock subject to a limitation on the aggregate amount of cash to be distributed to all stockholders, which must be at least 10% of the aggregate declared distribution. Taxable stockholders receiving such distributions will be required to include the full amount of the distribution as ordinary income (or as a long-term capital gain to the extent such distribution is properly designated as a capital gain dividend). As a result, a U.S. stockholder may be required to pay tax with respect to such distribution in excess of any cash received. If a U.S. stockholder sells the stock it receives as a distribution 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. income taxes with respect to such distribution, 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 decide to sell shares of our stock in order to pay taxes owed on distributions, it may put downward pressure on the trading price of our stock.

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

In accordance with applicable tax laws and regulations, we include in taxable income certain amounts that we have not yet received in cash, such as contractual paid-in-kind, or PIK, interest, interest on loans that are on non-accrual status and original issue discount. PIK interest represents contractual interest added to the loan balance and due at the end of the loan term. We include increases in loan balances resulting from contractual PIK arrangements in taxable income, in advance of receiving cash payment. We may also recognize income for tax purposes for certain of our loans that are on non-accrual status for which we are not currently receiving payments. In addition, we hold debt instruments that have original issue discount, which may arise if we receive warrants in connection with the issuance of a debt instrument or in other circumstances. We are required to include in income each year a portion of the original issue discount that accrues over the life of the obligation, regardless of whether cash representing such income is received by us in the same taxable year. 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 maintain tax benefits as a RIC. Accordingly, we may have to sell some of our investments at times we would not consider advantageous, raise additional debt or equity capital or reduce new investment originations to meet these distribution requirements. If we are not able to obtain cash from other sources, we may fail to qualify as a RIC and, thus, be subject to corporate-level income tax.

**The disposition of our investments may result in contingent liabilities.**

Most of our investments will involve private securities. In connection with the disposition of an investment in private securities, we may be required to make representations about the business and financial affairs of the portfolio company typical of those made in connection with the sale of a business. We may also be required to indemnify the purchasers of such investment to the extent that any such representations turn out to be inaccurate or with respect to certain potential liabilities. These arrangements may result in contingent liabilities that ultimately yield funding obligations that must be satisfied through our return of certain distributions previously made to us.

**If we need to sell any of our investments, we may not be able to do so at a favorable price and, as a result, we may suffer losses.**

Our investments usually are subject to contractual or legal restrictions on resale or are otherwise illiquid because there is usually no established trading market for such investments. The illiquidity of most of our investments may make it difficult for us to dispose of them at a favorable price. As a result, we may suffer losses. In addition, if we were forced to liquidate some or all of the investments in our portfolio on an expedited basis, the proceeds of such liquidation could be significantly less than the current fair value of such investments. We may be required to

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liquidate some or all of our portfolio to meet our debt service obligations or to maintain our qualification as a BDC and as a RIC if we do not satisfy one or more of the applicable criteria under the respective regulatory frameworks.

### **Our business depends on our key personnel.**

We depend on the continued services of our executive officers and other key management personnel. The loss of any of our executive officers or key management personnel could result in inefficiencies in our operations and lost business opportunities, which could have a negative impact on our business. In addition, under our SunTrust Warehouse, if either Steven F. Tunney or B. Hagen Saville ceases to be involved actively in the management of MCG and is not replaced by a person reasonably acceptable to SunTrust within 90 consecutive calendar days of such occurrence, we would be in default under such facility. Mr. Tunney resigned from MCG effective October 31, 2011 and Richard W. Neu was appointed as the Chief Executive Officer. If SunTrust does not accept Mr. Neu as a reasonably acceptable replacement or if we lose the services of Mr. Saville and are unable to identify and hire a suitably qualified replacement, it could provide SunTrust with the right to accelerate the termination date of that facility and entitle the administrative agent thereunder to exercise available remedies, including selling the collateral securing this facility and applying the proceeds to reduce outstanding borrowings thereunder. On August 2, 2011, we announced a corporate restructuring, which included a reduction in force. As a result of this restructuring, the resignation of Mr. Tunney and related developments, retaining key employees and/or finding replacements may be more difficult.

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

We have issued debt securities and may issue additional debt securities, preferred stock and/or borrow money from banks or other financial institutions, which we refer to collectively as “senior securities,” up to the maximum amount permitted by the 1940 Act. Under the provisions of the 1940 Act, as a BDC, we are permitted to issue senior securities only in amounts such that our BDC asset coverage, as defined in the 1940 Act, equals at least 200% after each issuance of senior securities. If the value of our assets declines, we may be unable to satisfy this test. If that happens, we would be precluded from issuing senior securities and paying dividends and we may be required to sell a portion of our investments and, depending on the nature of our leverage, may be required to repay a portion of our indebtedness at a time when such sales may be disadvantageous. In addition, the 1940 Act prohibits us from selling shares of our common stock at a price below the current NAV unless our stockholders approve such a sale and our board of directors makes certain determinations.

### **Any change in the regulation of our business could have a significant adverse effect on the profitability of our operations and our cost of doing business.**

Changes in the laws, regulations or interpretations of the laws and regulations that govern BDCs, RICs, SBICs or non-depository commercial lenders could have a significant adverse effect on 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. If these laws, regulations or decisions change, or if we expand our business into jurisdictions that have adopted requirements that are more stringent than those in which we currently conduct business, we may have to incur significant expenses in order to comply or we may have to restrict our operations.

### **Our wholly owned subsidiary is licensed by the SBA and is subject to SBA regulations.**

Our wholly owned subsidiary, Solutions Capital I, L.P., is licensed to operate as an SBIC and is regulated by the SBA. The SBIC license allows our SBIC subsidiary to obtain leverage by issuing SBA-guaranteed debentures, subject to the issuance of a capital commitment by the SBA and other customary procedures. The SBA regulations require, among other things, that a licensed SBIC be examined periodically, by an SBA examiner, to determine the SBIC’s compliance with the relevant SBA regulations, and be audited by an independent auditor.

Under current SBA regulations, a licensed SBIC can provide capital to those entities that have a tangible net worth not exceeding \$18.0 million and an average net income after federal income taxes not exceeding \$6.0 million for the two most recent fiscal years. In addition, a licensed SBIC must devote 25% of its investment activity to those entities that have a tangible net worth not exceeding \$6.0 million and an average annual net income after federal income taxes not exceeding \$2.0 million for the two most recent fiscal years. The SBA regulations also provide alternative size standard criteria to determine eligibility, which depend on the industry in which the business is engaged and are based on factors such as the number of employees and gross sales. The

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SBA regulations permit licensed SBICs to make long term loans to small businesses and invest in the equity securities of such businesses. The SBA also places certain limitations on the financing terms of investments by SBICs in portfolio companies and prohibits SBICs from providing funds for certain purposes or to businesses in a few prohibited industries. Compliance with SBA requirements may cause our SBIC subsidiary to forego attractive investment opportunities that are not permitted under SBA regulations.

SBA regulations currently limit the amount that a single-license SBIC subsidiary may borrow up to a maximum of \$150.0 million when it has at least \$75.0 million in private capital, receives a capital commitment from the SBA and has been through an examination by the SBA subsequent to licensing. As of September 30, 2011, our SBIC subsidiary had investments in 15 portfolio companies with a total fair value of \$184.8 million. In January 2011, the SBA increased its total commitment for potential borrowings from \$130.0 million to \$150.0 million. As of September 30, 2011, \$108.6 million of SBA borrowings were outstanding. We had funded \$75.0 million through September 30, 2011, allowing us full access to the \$150.0 million commitment from the SBA. Based on our current funded capital as of September 30, 2011, Solutions Capital may borrow, subject to the SBA's approval, up to an additional \$41.4 million to originate new investments.

The SBA prohibits, without prior SBA approval, a "change of control" of an SBIC or transfers that would result in any person (or a group of persons acting in concert) owning 10% or more of a class of capital stock of a licensed SBIC. If our SBIC subsidiary fails to comply with applicable SBA regulations, the SBA could, depending on the severity of the violation, limit or prohibit its use of debentures, declare outstanding debentures immediately due and payable, and/or limit it from making new investments. In addition, the SBA can revoke or suspend a license for willful or repeated violation of, or willful or repeated failure to observe, any provision of the SBIC Act or any rule or regulation promulgated thereunder. These actions by the SBA would, in turn, negatively affect us because our SBIC subsidiary is our wholly owned subsidiary.

**Our wholly owned SBIC subsidiary may be unable to make distributions to us that will enable us to meet or maintain RIC status, which could result in the imposition of an entity-level tax.**

In order for us to continue to qualify for RIC tax treatment and to minimize corporate-level taxes, we will be required to distribute substantially all of our net ordinary income and net capital gain income, including income from certain of our subsidiaries, which includes the income from our SBIC subsidiary. We will be partially dependent on our SBIC subsidiary for cash distributions to enable us to meet the RIC distribution requirements. Our SBIC subsidiary may be limited by the SBIC Act and SBA regulations governing SBICs from making certain distributions to us that may be necessary to maintain our status as a RIC. If our SBIC is unable to make sufficient distributions to us to allow us to make the required annual distributions to maintain our status as a RIC, and we are not able to obtain cash from other sources, we may fail to qualify as a RIC and, thus, be subject to corporate-level income tax.

**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 Reform 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, results of operations and financial condition. Accordingly, we cannot predict the effect the Dodd-Frank Act or its implementing regulations will have on our business, results of operations or financial condition.

**Our stock price has been, and continues to be, volatile and purchasers of our common stock could incur substantial losses.**

The stock market in general and the market prices for securities of financial services companies, and BDCs in particular, have experienced extreme volatility that often have been unrelated or disproportionate to the operating performance of these companies. If current levels of market volatility continue or worsen, there can be no assurance that we will not continue to experience an adverse effect, which may be material, on our ability to access capital and on our business, financial condition and results of operations.

The trading price of our common stock following an offering may fluctuate substantially. The price of the common stock that will prevail in the market after an offering may be higher or lower than the price you paid and the liquidity of our common stock may be limited, in each case depending on many factors, some of which are beyond

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our control and may not be related directly to our operating performance. The market price and the liquidity of the market for our shares may from time to time be affected by a number of factors, which include, but are not limited to, the following:

- our quarterly results of operations;
- our origination activity, including the pace of, and competition for, new investment opportunities;
- price and volume fluctuations in the overall stock market from time to time;
- investors' general perception of our company, the economy and general market conditions;
- actual or anticipated changes in our earnings or fluctuations in our operating results or changes in the expectations of securities analysts;
- the financial performance of the specific industries in which we invest on a recurring basis, including without limitation, our investments in the communications, cable and healthcare industries;
- significant transactions or capital commitments by us or our competitors;
- significant volatility in the market price and trading volume of securities of BDCs or other financial services companies;
- volatility resulting from trading in derivative securities related to our common stock including puts, calls or short trading positions;
- potential future sales of debt securities convertible into or exchangeable or exercisable for our common stock or the conversion of such securities;
- changes in laws or regulatory policies or tax guidelines with respect to BDCs or RICs;
- loss of RIC status;
- the loss of a major funding source, including one of our lenders or access to SBA leverage;
- announcements of strategic developments, acquisitions and other material events by us or our competitors; or
- departures of key personnel.

If any of these factors causes an adverse effect on our business, our results of operations or our financial condition, the price of our common stock could fall and investors may not be able to sell their common stock at or above their respective purchase prices.

### **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 certificate of incorporation and our bylaws contain provisions that may have the effect of discouraging a third party from making an acquisition proposal for us. We have also adopted measures that may make it difficult for a third party to obtain control of us, including provisions of our certificate of incorporation dividing our board of directors into three classes with the term of one class expiring at each annual meeting of stockholders. 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.

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### ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

As part of our dividend reinvestment plan for our common stockholders, we may direct the plan administrator to purchase shares of our common stock on the open market to satisfy dividend reinvestment requests related to dividends that we pay on outstanding shares of our common stock. In addition, for certain employees, we may be deemed to have purchased through the net issuance of shares, a portion of the shares of restricted stock previously issued under our 2006 Plan, for which the forfeiture provisions have lapsed to satisfy the respective employee's income tax withholding obligations. We retire immediately all such shares of common stock that we purchase in connection with such net issuance to employees. The following table summarizes the shares of common stock that we have purchased during each of the three months ended September 30, 2011.

Period/Purpose	Total number of shares	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs
<b>July 1 – 31, 2011</b>				
Dividend reinvestment requirements <sup>(a)</sup>	14,519	\$ 6.05 <sup>(b)</sup>	n/a	n/a
<b>August 1 – 31, 2011</b>				
Restricted stock vesting <sup>(c)</sup>	4,539	\$ 5.50 <sup>(d)</sup>	n/a	n/a
<b>September 1 – 30, 2011</b>				
Restricted stock vesting <sup>(c)</sup>	28,772	\$ 3.96 <sup>(d)</sup>	n/a	n/a
<b>Total shares / weighted average price paid</b>	<b><u>47,830</u></b>	<b><u>\$ 4.74</u></b>	<b>n/a</b>	<b>n/a</b>

<sup>(a)</sup> Represents stock purchased on the open market to satisfy dividend reinvestment requests related to the dividend we paid on July 15, 2011.

<sup>(b)</sup> Represents the weighted-average purchase price per share, including commissions, for shares purchased pursuant to the terms of our dividend reinvestment plan.

<sup>(c)</sup> Represents shares repurchased from our employees in connection with the net issuance of shares to satisfy employee tax withholding obligations in connection with the vesting of restricted stock.

<sup>(d)</sup> Based on the weighted-average closing share prices of our common stock on the dates that the forfeiture restrictions lapsed.

### ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

Not Applicable.

### ITEM 4. RESERVED.

### ITEM 5. OTHER INFORMATION.

Not Applicable.

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### ITEM 6. EXHIBITS.

The following table lists exhibits filed as part of this report, according to the number assigned to them in Item 601 of Regulation S-K. All exhibits listed in the following table are incorporated by reference except for those exhibits denoted in the last column.

<u>Exhibit No.</u>	<u>Description</u>	<u>Incorporated by Reference</u>			<u>Filed with this 10-Q</u>
		<u>Form and SEC File No.</u>	<u>Filing Date with SEC</u>	<u>Exhibit No.</u>	
15.1	Letter regarding unaudited interim financial information from Ernst & Young LLP, independent registered public accounting firm				*
31.1	Certification of Chief Executive Officer pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002				*
31.2	Certification of Chief Financial Officer pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002				*
31.3	Certification of Chief Accounting Officer pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002				*
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002				†
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002				†
32.3	Certification of Chief Accounting Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002				†

\* Filed herewith.

† Furnished herewith.



November 3, 2011

The Board of Directors and Shareholders  
MCG Capital Corporation

We are aware of the incorporation by reference in the Registration Statements (Form S-8 No. 333-137565 and Form S-8 No. 333-167494) pertaining to the Third Amended and Restated 2006 Employee Restricted Stock Plan of MCG Capital Corporation and the Third Amended and Restated 2006 Non-Employee Director Restricted Stock Plan of MCG Capital Corporation of our report dated November 3, 2011 relating to the unaudited consolidated interim financial statements and schedules of MCG Capital Corporation included in its Form 10-Q for the three- and nine- month periods ended September 30, 2011.

/s/ ERNST & YOUNG LLP

I, Richard W. Neu, Chief Executive Officer of MCG Capital Corporation, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of MCG 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 officers 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 officers 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.

Dated this 3rd day of November, 2011.

By: \_\_\_\_\_  
/s/ Richard W. Neu  
**Richard W. Neu**  
**Chief Executive Officer**

I, Stephen J. Bacica, Chief Financial Officer of MCG Capital Corporation, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of MCG 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 officers 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 officers 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.

Dated this 3rd day of November, 2011.

By: \_\_\_\_\_ /s/ Stephen J. Bacica  
**Stephen J. Bacica**  
**Chief Financial Officer**



**Certification of Chief Executive Officer**

**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 Quarterly Report on Form 10-Q for the quarter ended **September 30, 2011** (the "Report") of **MCG Capital Corporation** (the "Registrant"), as filed with the Securities and Exchange Commission on the date hereof, I, **Richard W. Neu**, the Chief Executive Officer of the Registrant, hereby certify, to the best of my knowledge, pursuant to 18 U.S.C. Section 1350 that:

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

/s/ R ICHARD W. N EU

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Name: Richard W. Neu  
Title: Chief Executive Officer  
Date: November 3, 2011

**Certification of Chief Financial Officer**

**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 Quarterly Report on Form 10-Q for the quarter ended **September 30, 2011** (the "Report") of **MCG Capital Corporation** (the "Registrant"), as filed with the Securities and Exchange Commission on the date hereof, I, **Stephen J. Bacica**, the Chief Financial Officer of the Registrant, hereby certify, to the best of my knowledge, pursuant to 18 U.S.C. Section 1350 that:

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

/s/ STEPHEN J. BACICA

Name: Stephen J. Bacica

Title: Chief Financial Officer

Date: November 3, 2011

**Certification of Chief Accounting Officer****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 Quarterly Report on Form 10-Q for the quarter ended **September 30, 2011** (the "Report") of **MCG Capital Corporation** (the "Registrant"), as filed with the Securities and Exchange Commission on the date hereof, I, **Linda A. Nimmons**, the Chief Accounting Officer of the Registrant, hereby certify, to the best of my knowledge, pursuant to 18 U.S.C. Section 1350 that:

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

/s/ LINDA A. NIMMONS

Name: Linda A. Nimmons  
Title: Chief Accounting Officer  
Date: November 3, 2011