

Horizon Technology Finance Corp  
Form 10-Q  
May 11, 2011

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**  
**Form 10-Q**

(Mark One)

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

**FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2011 OR  
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: 814-00802\_**  
**HORIZON TECHNOLOGY FINANCE CORPORATION**  
*(Exact name of registrant as specified in its charter)*

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

**27-2114934**  
*(I.R.S. Employer Identification No.)*

**312 Farmington Avenue**  
**Farmington, CT**  
*(Address of principal executive offices)*

**06032**  
*(Zip Code)*

**Registrant's telephone number, including area code (860) 676-8654**  
**Securities registered pursuant to Section 12(b) of the Act:**

**Title of Each Class**

**Name of Each Exchange on Which Registered**

Common Stock, par value \$0.001 per share

The NASDAQ Global Market

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer" and "large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller Reporting Company

(Do not check if a 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

Edgar Filing: Horizon Technology Finance Corp - Form 10-Q

As of May 10, 2011, the Registrant had 7,593,421 shares of common stock, \$0.001 par value, outstanding.

---

**HORIZON TECHNOLOGY FINANCE CORPORATION  
FORM 10-Q  
TABLE OF CONTENTS**

|  | <b>Page</b> |
|--|-------------|
| <b><u>PART I</u></b>   |             |
| <u>Financial Statements</u>  |             |
| <u>Item 1.</u>   |             |
| <u>Consolidated Statements of Assets and Liabilities as of March 31, 2011 and December 31, 2010 (unaudited)</u>        | 5           |
| <u>Consolidated Statements of Operations for the three months ended March 31, 2011 and 2010 (unaudited)</u>            | 6           |
| <u>Consolidated Statements of Changes in Net Assets for the three months ended March 31, 2011 and 2010 (unaudited)</u> | 7           |
| <u>Consolidated Statements of Cash Flows for the three months ended March 31, 2011 and 2010 (unaudited)</u>            | 8           |
| <u>Consolidated Schedules of Investments as of March 31, 2011 and December 31, 2010 (unaudited)</u>                    | 9           |
| <u>Notes to the Consolidated Financial Statements (unaudited)</u>  | 15          |
| <u>Item 2.</u>   |             |
| <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>                           | 27          |
| <u>Item 3.</u>   |             |
| <u>Quantitative And Qualitative Disclosures About Market Risk</u>  | 36          |
| <u>Item 4.</u>   |             |
| <u>Controls and Procedures</u>   | 36          |
| <b><u>PART II</u></b>  |             |
| <u>Item 1.</u>   |             |
| <u>Legal Proceedings</u>   | 36          |
| <u>Item 1A.</u>  |             |
| <u>Risk Factors</u>  | 37          |
| <u>Item 2.</u>   |             |
| <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>   | 37          |
| <u>Item 3.</u>   |             |
| <u>Defaults Upon Senior Securities</u>   | 37          |
| <u>Item 4.</u>   |             |
| <u>Removed and Reserved</u>  | 37          |
| <u>Item 5.</u>   |             |
| <u>Other Information</u>   | 37          |
| <u>Item 6.</u>   |             |
| <u>Exhibits</u>  | 37          |
| <u>Signatures</u>  | 38          |
| <u>EX-31.1</u>   |             |
| <u>EX-31.2</u>   |             |
| <u>EX-32.1</u>   |             |
| <u>EX-32.2</u>   |             |

### **Forward-Looking Statements**

This quarterly report on Form 10-Q, including the Management's Discussion and Analysis of Financial Condition and Results of Operations, contains statements that constitute forward-looking statements, which relate to future events or our future performance or financial condition. These forward-looking statements are not historical facts, but rather are based on current expectations, estimates and projections about our industry, our beliefs and our assumptions. The forward-looking statements contained in this quarterly report on Form 10-Q involve risks and uncertainties, including statements as to:

our future operating results, including the performance of our existing loans and warrants;

the introduction, withdrawal, success and timing of business initiatives and strategies;

changes in political, economic or industry conditions, the interest rate environment or financial and capital markets, which could result in changes in the value of our assets;

the relative and absolute investment performance and operations of our Advisor;

the impact of increased competition;

the impact of investments we intend to make and future acquisitions and divestitures;

the unfavorable resolution of legal proceedings;

our business prospects and the prospects of our portfolio companies;

the impact, extent and timing of technological changes and the adequacy of intellectual property protection;

our regulatory structure and tax status;

the adequacy of our cash resources and working capital;

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

the impact of interest rate volatility on our results, particularly if we use leverage as part of our investment strategy;

the ability of our portfolio companies to achieve their objective;

our ability to cause a subsidiary to become a licensed SBIC;

the impact of legislative and regulatory actions and reforms and regulatory supervisory or enforcement actions of government agencies relating to us or our Advisor;

our contractual arrangements and relationships with third parties;

our ability to access capital and any future financings by us;

the ability of our Advisor to attract and retain highly talented professionals; and

the impact of changes to tax legislation and, generally, our tax position.

We use words such as anticipates, believes, expects, intends, seeks and similar expressions to identify forward-looking statements. Undue influence should not be placed on the forward looking statements as our actual results could differ materially from those projected in the forward-looking statements for any reason, including the factors in Risk Factors in our annual report on Form 10-K for the year ended December 31, 2010 and elsewhere in this quarterly report on Form 10-Q.

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

**Horizon Technology Finance Corporation and Subsidiaries**  
**Consolidated Statements of Assets and Liabilities (Unaudited)**  
(In thousands, except share data)

|   | <b>March 31,<br/>2011</b> | <b>December 31,<br/>2010</b> |
|---|---------------------------|------------------------------|
| <b>ASSETS</b>   |                           |                              |
| Non-affiliate investments at fair value (cost of \$148,783 and \$133,494, respectively)   | \$ 153,216                | \$ 136,810                   |
| Cash and cash equivalents   | 69,503                    | 76,793                       |
| Interest receivable   | 2,281                     | 1,938                        |
| Other assets  | 444                       | 664                          |
| <b>Total assets</b>   | <b>\$ 225,444</b>         | <b>\$ 216,205</b>            |
| <b>LIABILITIES</b>  |                           |                              |
| Borrowings (Note 6)   | \$ 92,712                 | \$ 87,425                    |
| Base management fee payable (Note 3)  | 376                       | 360                          |
| Incentive fee payable (Note 3)  | 529                       | 414                          |
| Interest rate swap liability (Note 9)   | 180                       | 258                          |
| Other accrued expenses  | 824                       | 553                          |
| <b>Total liabilities</b>  | <b>94,621</b>             | <b>89,010</b>                |
| <b>Net assets</b>   |                           |                              |
| Common stock, par value \$0.001 per share, 100,000,000 shares authorized, 7,593,421 shares outstanding as of March 31, 2011 and December 31, 2010 | 8                         | 8                            |
| Paid-in capital in excess of par  | 123,836                   | 123,836                      |
| Accumulated undistributed (distribution in excess of) net investment income   | 2,085                     | (143)                        |
| Net unrealized appreciation on investments  | 4,237                     | 3,043                        |
| Net realized gains on investments   | 657                       | 451                          |
| <b>Total net assets</b>   | <b>130,823</b>            | <b>127,195</b>               |
| <b>Total liabilities and net assets</b>   | <b>\$ 225,444</b>         | <b>\$ 216,205</b>            |
| <b>Net asset value per common share</b>   | <b>\$ 17.23</b>           | <b>\$ 16.75</b>              |

See Notes to Consolidated Financial Statements

**Horizon Technology Finance Corporation and Subsidiaries**  
**Consolidated Statements of Operations (Unaudited)**  
(In thousands, except share data)

|   | <b>Post-IPO as a<br/>Business<br/>Development<br/>Company<br/>Three Months<br/>Ended<br/>March 31, 2011</b> | <b>Pre-IPO Prior to<br/>becoming a<br/>Business<br/>Development<br/>Company<br/>Three Months<br/>Ended<br/>March 31, 2010</b> |
|---|---|---|
| <b>Investment income</b>                                    |   |   |
| Interest income on non-affiliate investments                | \$ 4,893  | \$ 3,745  |
| Interest income on cash and cash equivalents                | 65  | 9   |
| Fee income on non-affiliate investments                     | 502   | 39  |
| <b>Total investment income</b>                              | <b>5,460</b>  | <b>3,793</b>  |
| <b>Expenses</b>   |   |   |
| Interest expense  | 810   | 1,003   |
| Base management fee (Note 3)                                | 1,075   | 547   |
| Performance based incentive fee (Note 3)                    | 529   |   |
| Administrative fee (Note 3)                                 | 295   |   |
| Professional fees   | 318   | 73  |
| General and administrative                                  | 205   | 57  |
| <b>Total expenses</b>                                       | <b>3,232</b>  | <b>1,680</b>  |
| <b>Net investment income</b>                                | <b>2,228</b>  | <b>2,113</b>  |
| Credit for loan losses                                      |   | 303   |
| <b>Net realized and unrealized gain on investments</b>      |   |   |
| Net realized gain on investments                            | 206   |   |
| Net change in unrealized appreciation on investments        | 1,194   | 202   |
| <b>Net realized and unrealized gain on investments</b>      | <b>1,400</b>  | <b>202</b>  |
| <b>Net increase in net assets resulting from operations</b> | <b>\$ 3,628</b>   | <b>\$ 2,618</b>   |
| Net investment income per common share <sup>(1)</sup>       | \$ 0.29   | N/A   |
| Change in net assets per common share <sup>(1)</sup>        | \$ 0.48   | N/A   |
| Weighted average shares outstanding <sup>(1)</sup>          | 7,593,421   | N/A   |

(1)

Edgar Filing: Horizon Technology Finance Corp - Form 10-Q

For the three months ended March 31, 2010, the Company did not have common shares outstanding or an equivalent and, therefore, earnings per share and weighted average shares outstanding information for this period is not provided.

See Notes to Consolidated Financial Statements

6

---



**Horizon Technology Finance Corporation and Subsidiaries**  
**Consolidated Statements of Changes in Net Assets (Unaudited)**  
(In thousands, except share data)

|  | Accumulated<br>Other<br>Comprehensive<br>Income | Common Stock<br>Shares | Common Stock<br>Amount | Paid-In<br>Capital in<br>Excess of<br>Par | Accumulated<br>Undistributed<br>(distribution<br>in<br>excess<br>of)<br>Net<br>Investment<br>Income | Net<br>Unrealized<br>Appreciation<br>on<br>Investments | Net<br>Realized<br>Gains<br>on<br>Investments | Total<br>Net<br>Assets |            |
|--|---|------------------------|------------------------|---|---|--|---|------------------------|------------|
| <b>Balance at<br/>December 31,<br/>2009</b>      | \$ 60,260                                       | \$ (768)               | \$                     | \$  | \$  | \$   | \$  | \$ 59,492              |            |
| Comprehensive<br>income:                         |   |                        |                        |   |   |  |   |                        |            |
| Net income                                       | 2,618   |                        |                        |   |   |  |   | 2,618                  |            |
| Unrealized loss<br>on interest rate<br>swaps     |   | 100                    |                        |   |   |  |   | 100                    |            |
| Total<br>comprehensive<br>income                 |   |                        |                        |   |   |  |   | 2,718                  |            |
| <b>Balance at<br/>March 31, 2010</b>             | \$ 62,878                                       | \$ (668)               | \$                     | \$  | \$  | \$   | \$  | \$ 62,210              |            |
| <b>Balance at<br/>December 31,<br/>2010</b>      | \$  | \$                     | 7,593,421              | \$ 8                                      | \$ 123,836  | \$ (143)   | \$ 3,043                                      | \$ 451                 | \$ 127,195 |
| Net increase in<br>net assets from<br>operations |   |                        |                        |   | 2,228   | 1,194  | 206   | 3,628                  |            |
| <b>Balance at<br/>March 31, 2011</b>             | \$  | \$                     | 7,593,421              | \$ 8                                      | \$ 123,836  | \$ 2,085   | \$ 4,237                                      | \$ 657                 | \$ 130,823 |

See Notes to Consolidated Financial Statements



**Horizon Technology Finance Corporation and Subsidiaries**  
**Consolidated Statements of Cash Flows (Unaudited)**  
(In thousands)

|   | <b>Post-IPO as a<br/>Business<br/>Development<br/>Company<br/>Three Months<br/>Ended<br/>March 31, 2011</b> | <b>Pre-IPO Prior to<br/>becoming a<br/>Business<br/>Company<br/>Three Months<br/>Ended<br/>March 31, 2010</b> |
|---|---|---|
| <b>Cash flows from operating activities:</b>  |   |   |
| Net increase in net assets resulting from operations  | \$ 3,628  | \$ 2,618  |
| Adjustments to reconcile net increase in net assets resulting from operations to net cash used in operating activities: |   |   |
| Credit for loan losses  |   | (303)   |
| Amortization of debt issuance costs   | 194   | 290   |
| Net realized gain on investments  | (206)   |   |
| Net change in unrealized appreciation on investments  | (1,194)   | (202)   |
| Purchase of investments   | (26,063)  | (12,025)  |
| Principal payments received on investments  | 11,106  | 8,289   |
| Proceeds from sale of investments   | 321   |   |
| Stock received in settlement of fee income  | (482)   |   |
| Changes in assets and liabilities:  |   |   |
| Increase in interest receivable   | (343)   | (264)   |
| Increase (decrease) in unearned loan income   | 34  | (105)   |
| Decrease (increase) in other assets   | 26  | (145)   |
| Increase in other accrued expenses  | 271   | 39  |
| Increase in base management fee payable   | 16  | 1   |
| Increase in incentive fee payable   | 115   |   |
| Net cash used in operating activities   | (12,577)  | (1,807)   |
| <b>Cash flows from financing activities:</b>  |   |   |
| Net increase in revolving borrowings  | 5,287   | 11,064  |
| Net cash provided by financing activities   | 5,287   | 11,064  |
| Net (decrease) increase in cash and cash equivalents  | (7,290)   | 9,258   |
| <b>Cash and cash equivalents:</b>   |   |   |
| Beginning of period   | 76,793  | 9,892   |
| End of period   | \$ 69,503   | \$ 19,149   |
| Cash paid for interest  | \$ 532  | \$ 713  |
| Supplemental non-cash investing and financing activities:   |   |   |
| Warrant investments received & recorded as unearned loan income   | \$ 395  | \$ 275  |

|  |    |      |    |      |
|--|----|------|----|------|
| Decrease in interest rate swap liability | \$ | (78) | \$ | (99) |
|--|----|------|----|------|

See Notes to Consolidated Financial Statements

8

---

**Horizon Technology Finance Corporation and Subsidiaries**  
**Consolidated Schedule of Investments**  
**March 31, 2011**  
(In thousands)

| Portfolio Company                  | Sector         | Type<br>of<br>Investment(2) | Interest<br>Rate(3) | Maturity  | Cost of<br>Investment(5) | Fair<br>Value |
|------------------------------------|----------------|-----------------------------|---------------------|-----------|--------------------------|---------------|
| <b>Debt Investments(1)</b>         |                |                             |                     |           |                          |               |
| <b>Debt Investments</b>            | <b>Life</b>    |                             |                     |           |                          |               |
| <b>Science 42.2%</b>               |                |                             |                     |           |                          |               |
| ACT Biotech, Inc.                  | Biotechnology  | Term<br>Loan                | 12.10%              | 6/1/2013  | \$ 902                   | \$ 902        |
|                                    |                | Term<br>Loan                | 12.01%              | 6/1/2013  | 901                      | 901           |
|                                    |                | Term<br>Loan                | 12.01%              | 6/1/2013  | 1,392                    | 1,392         |
| Ambit Biosciences, Inc.            | Biotechnology  | Term<br>Loan                | 12.25%              | 10/1/2013 | 5,913                    | 5,913         |
| Anacor Pharmaceuticals,<br>Inc.(4) | Biotechnology  | Term<br>Loan                | 9.41%               | 4/1/2015  | 3,191                    | 3,191         |
| GenturaDX, Inc.                    | Biotechnology  | Term<br>Loan                | 11.25%              | 4/1/2014  | 1,893                    | 1,893         |
| N30 Pharmaceuticals,<br>LLC,       | Biotechnology  | Term<br>Loan                | 11.25%              | 9/1/2014  | 2,394                    | 2,394         |
| Pharmasset, Inc.(4)                | Biotechnology  | Term<br>Loan                | 12.00%              | 8/1/2011  | 504                      | 504           |
|                                    |                | Term<br>Loan                | 12.00%              | 1/1/2012  | 1,103                    | 1,103         |
|                                    |                | Term<br>Loan                | 12.50%              | 10/1/2012 | 2,110                    | 2,110         |
| Revanche Therapeutics,<br>Inc.     | Biotechnology  | Term<br>Loan                | 10.50%              | 12/1/2011 | 1,102                    | 1,102         |
|                                    |                | Term<br>Loan                | 10.50%              | 3/1/2013  | 3,137                    | 3,137         |
| Supernus Pharmaceuticals,<br>Inc.  | Biotechnology  | Term<br>Loan                | 11.00%              | 8/1/2014  | 2,937                    | 2,937         |
| Tranzyme, Inc.                     | Biotechnology  | Term<br>Loan                | 10.75%              | 1/1/2014  | 4,971                    | 4,971         |
| Xcovery Holding<br>Company, LLC    | Biotechnology  | Term<br>Loan                | 12.00%              | 10/1/2013 | 1,491                    | 1,491         |
| Concentric Medical, Inc.           | Medical Device | Term<br>Loan                | 12.04%              | 9/1/2013  | 6,903                    | 6,903         |
| OraMetrix, Inc.                    | Medical Device | Term<br>Loan                | 11.50%              | 4/1/2014  | 4,901                    | 4,901         |
| PixelOptics, Inc.                  | Medical Device | Term<br>Loan                | 13.00%              | 1/1/2013  | 3,779                    | 3,779         |
| Tengion, Inc.(4)                   | Medical Device | Term<br>Loan                | 11.75%              | 1/1/2014  | 4,928                    | 4,928         |

Edgar Filing: Horizon Technology Finance Corp - Form 10-Q

|  |                                  |              |        |           |        |        |
|--|----------------------------------|--------------|--------|-----------|--------|--------|
| ViOptix, Inc.                                | Medical Device                   | Term<br>Loan | 13.55% | 11/1/2011 | 810    | 750    |
| Total Debt Investments<br>Life Science       |                                  |              |        |           | 55,262 | 55,202 |
| <b>Debt Investments<br/>Technology 25.8%</b> |                                  |              |        |           |        |        |
| OpenPeak, Inc.                               | Communications                   | Term<br>Loan | 11.86% | 12/1/2013 | 6,566  | 6,566  |
| Starcite, Inc.                               | Consumer-related<br>technologies | Term<br>Loan | 12.05% | 9/1/2012  | 2,332  | 2,332  |
| Tagged, Inc.                                 | Consumer-related<br>technologies | Term<br>Loan | 12.78% | 5/1/2012  | 1,060  | 1,060  |
|  |                                  | Term<br>Loan | 11.46% | 8/1/2012  | 425    | 425    |
| Vette Corp.                                  | Data Storage                     | Term<br>Loan | 11.75% | 7/1/2014  | 4,910  | 4,910  |
| XIOtech, Inc.                                | Data Storage                     | Term<br>Loan | 14.00% | 5/1/2012  | 2,511  | 2,511  |
| IntelePeer, Inc.                             | Networking                       | Term<br>Loan | 12.43% | 4/1/2012  | 426    | 426    |
|  |                                  | Term<br>Loan | 12.33% | 6/1/2012  | 507    | 507    |
|  |                                  | Term<br>Loan | 12.33% | 10/1/2012 | 1,029  | 1,029  |
| Clarabridge, Inc.                            | Software                         | Term<br>Loan | 12.50% | 1/1/2013  | 1,001  | 1,001  |
|  |                                  | Term<br>Loan | 12.50% | 6/1/2013  | 608    | 608    |
|  |                                  | Term<br>Loan | 12.50% | 5/1/2014  | 744    | 744    |
| Courion Corporation                          | Software                         | Term<br>Loan | 11.45% | 9/1/2014  | 6,857  | 6,857  |
| Netuitive, Inc.                              | Software                         | Term<br>Loan | 12.90% | 4/1/2011  | 39     | 39     |
| StreamBase Systems, Inc.                     | Software                         | Term<br>Loan | 12.51% | 11/1/2013 | 3,739  | 3,739  |
|  |                                  | Term<br>Loan | 12.50% | 6/1/2014  | 980    | 980    |
| Total Debt Investments<br>Technology         |                                  |              |        |           | 33,734 | 33,734 |
| <b>Debt Investments<br/>Cleantech 20.4%</b>  |                                  |              |        |           |        |        |
| Cereplast, Inc.(4)                           | Waste Removal                    | Term<br>Loan | 12.00% | 4/1/2014  | 2,429  | 2,429  |
|  | Waste Removal                    |              | 12.00% | 6/1/2014  | 2,422  | 2,422  |

Edgar Filing: Horizon Technology Finance Corp - Form 10-Q

|                                     |                      |              |        |           |        |        |
|-------------------------------------|----------------------|--------------|--------|-----------|--------|--------|
|                                     |                      | Term<br>Loan |        |           |        |        |
| Enphase Energy, Inc.                | Energy<br>Efficiency | Term<br>Loan | 12.60% | 10/1/2013 | 6,890  | 6,890  |
|                                     | Energy<br>Efficiency | Term<br>Loan | 10.75% | 4/1/2015  | 1,897  | 1,897  |
| Satcon Technology<br>Corporation(4) | Energy<br>Efficiency | Term<br>Loan | 12.58% | 1/1/2014  | 9,743  | 9,743  |
| Tigo Energy, Inc.                   | Energy<br>Efficiency | Term<br>Loan | 11.00% | 8/1/2014  | 3,337  | 3,337  |
| Total Debt Investments<br>Cleantech |                      |              |        |           | 26,718 | 26,718 |

See Notes to Consolidated Financial Statements

**Horizon Technology Finance Corporation and Subsidiaries**  
**Consolidated Schedule of Investments**  
**March 31, 2011 (Continued)**  
(In thousands)

| Portfolio Company                         | Sector                              | Type of Investment(2)                      | Interest Rate(3) | Maturity  | Cost of Investment(5) | Fair Value     |  |
|---|-------------------------------------|--|------------------|-----------|-----------------------|----------------|--|
| <b>Debt Investments</b>                   |                                     | <b>Healthcare information and services</b> |                  |           |                       |                |  |
| <b>22.2%</b>                              |                                     |  |                  |           |                       |                |  |
| BioScale, Inc.                            | Diagnosics                          | Term Loan                                  | 12.00%           | 8/1/2012  | 2,098                 | 2,098          |  |
|   |                                     | Term Loan                                  | 11.51%           | 1/1/2014  | 4,919                 | 4,919          |  |
| Precision Therapeutics, Inc.              | Diagnosics                          | Term Loan                                  | 13.00%           | 3/1/2012  | 2,649                 | 2,649          |  |
| Radisphere National Radiology Group, Inc. | Diagnosics                          | Term Loan                                  | 12.75%           | 1/1/2014  | 9,874                 | 9,874          |  |
|   | Other                               |  |                  |           |                       |                |  |
| Singulex, Inc.                            | Healthcare                          | Term Loan                                  | 11.00%           | 3/1/2014  | 2,955                 | 2,955          |  |
|   |                                     | Term Loan                                  | 11.00%           | 3/1/2014  | 1,969                 | 1,969          |  |
|   | Other                               |  |                  |           |                       |                |  |
| Talyst, Inc.                              | Healthcare                          | Term Loan                                  | 12.10%           | 12/1/2013 | 2,276                 | 2,276          |  |
|   |                                     | Term Loan                                  | 12.05%           | 12/1/2013 | 2,272                 | 2,272          |  |
| Total Debt Investment                     | Healthcare information and services |  |                  |           | 29,012                | 29,012         |  |
| <b>Total Debt Investments</b>             |                                     |  |                  |           | <b>144,726</b>        | <b>144,666</b> |  |
| <b>Warrant Investments(1)</b>             |                                     |  |                  |           |                       |                |  |
| <b>Warrants</b>                           |                                     | <b>Life Science</b>                        |                  |           |                       |                |  |
| <b>2.0%</b>                               |                                     |  |                  |           |                       |                |  |
| ACT Biotech, Inc.                         | Biotechnology                       | Preferred Stock Warrants                   |                  |           | 23                    | 32             |  |
| Ambit Biosciences, Inc.                   | Biotechnology                       | Preferred Stock Warrants                   |                  |           | 143                   | 148            |  |
| Anacor Pharmaceuticals, Inc.(4)           | Biotechnology                       | Common Stock Warrants                      |                  |           | 42                    | 42             |  |
| Anesiva, Inc.(4)                          | Biotechnology                       | Common Stock Warrants                      |                  |           | 18                    |                |  |
| GenturaDX, Inc.                           | Biotechnology                       | Preferred Stock Warrants                   |                  |           | 63                    | 64             |  |
| N30 Pharmaceuticals, LLC,                 | Biotechnology                       | Preferred Stock Warrants                   |                  |           | 60                    | 60             |  |
|   | Biotechnology                       | Warrants                                   |                  |           | 69                    |                |  |



Edgar Filing: Horizon Technology Finance Corp - Form 10-Q

|                                    |  |                          |       |       |
|------------------------------------|--|--------------------------|-------|-------|
| Novalar Pharmaceuticals, Inc.      |  | Preferred Stock Warrants |       |       |
| Revanche Therapeutics, Inc.        | Biotechnology                                | Preferred Stock Warrants | 224   | 122   |
| Supernus Pharmaceuticals, Inc.     | Biotechnology                                | Preferred Stock Warrants | 16    | 16    |
| Tranzyme, Inc.                     | Biotechnology                                | Preferred Stock Warrants | 1     |       |
| Advanced BioHealing, Inc.          | Medical Device                               | Preferred Stock Warrants | 9     | 1,848 |
| Calypso Medical Technologies, Inc. | Medical Device                               | Preferred Stock Warrants | 17    | 76    |
| Concentric Medical, Inc.           | Medical Device                               | Preferred Stock Warrants | 84    | 90    |
| EnteroMedics, Inc.(4)              | Medical Device                               | Preferred Stock Warrants | 347   | 9     |
| OraMetrix, Inc.                    | Medical Device                               | Preferred Stock Warrants | 78    | 84    |
| PixelOptics, Inc.                  | Medical Device                               | Preferred Stock Warrants | 61    | 13    |
| Tengion, Inc.(4)                   | Medical Device                               | Preferred Stock Warrants | 62    | 47    |
| ViOptix, Inc.                      | Medical Device                               | Preferred Stock Warrants | 13    |       |
| Total Warrants Life Science        |  |                          | 1,330 | 2,651 |
| <b>Warrants Technology</b>         |  |                          |       |       |
| <b>1.4%</b>                        |  |                          |       |       |
| OpenPeak, Inc.                     | Communications Consumer related technologies | Preferred Stock Warrants | 89    | 93    |
| Everyday Health, Inc.              | Consumer-related technologies                | Preferred Stock Warrants | 69    | 139   |
| SnagAJob.com, Inc.                 | Consumer-related technologies                | Preferred Stock Warrants | 23    | 273   |

Edgar Filing: Horizon Technology Finance Corp - Form 10-Q

|                |  |    |    |
|----------------|--|----|----|
| Starcite, Inc. | Preferred<br>Consumer-related Stock<br>technologies Warrants | 23 | 28 |
| Tagged, Inc.   | Preferred<br>Consumer-related Stock<br>technologies Warrants | 17 | 27 |
|                | See Notes to Consolidated Financial Statements               |    |    |

**Horizon Technology Finance Corporation and Subsidiaries**  
**Consolidated Schedule of Investments**  
**March 31, 2011 (Continued)**  
(In thousands)

| Portfolio Company        | Sector             | Type of Investment(2) | Interest Rate(3) | Maturity Investment(5) | Cost of Investment(5) | Fair Value |
|--------------------------|--------------------|-----------------------|------------------|------------------------|-----------------------|------------|
| Vette Corp.              | Data Storage       | Preferred Stock       |                  |                        | 75                    | 49         |
|                          |                    | Warrants              |                  |                        |                       |            |
| XIOtech, Inc.            | Data Storage       | Preferred Stock       |                  |                        | 22                    | 81         |
|                          |                    | Warrants              |                  |                        |                       |            |
| Cartera Commerce, Inc.   | Internet and media | Preferred Stock       |                  |                        | 16                    | 38         |
|                          |                    | Warrants              |                  |                        |                       |            |
| Grab Networks, Inc.      | Networking         | Preferred Stock       |                  |                        | 74                    |            |
|                          |                    | Warrants              |                  |                        |                       |            |
| IntelePeer, Inc.         | Networking         | Preferred Stock       |                  |                        | 40                    | 561        |
|                          |                    | Warrants              |                  |                        |                       |            |
| Motion Computing, Inc.   | Networking         | Preferred Stock       |                  |                        | 7                     | 292        |
|                          |                    | Warrants              |                  |                        |                       |            |
| Impinj, Inc.             | Semi-conductor     | Preferred Stock       |                  |                        | 7                     |            |
|                          |                    | Warrants              |                  |                        |                       |            |
| Clarabridge, Inc.        | Software           | Warrants              |                  |                        | 28                    | 25         |
|                          |                    | Preferred Stock       |                  |                        |                       |            |
| Courion Corporation      | Software           | Preferred Stock       |                  |                        | 85                    | 102        |
|                          |                    | Warrants              |                  |                        |                       |            |
| DriveCam, Inc.           | Software           | Preferred Stock       |                  |                        | 19                    | 8          |
|                          |                    | Warrants              |                  |                        |                       |            |
| Netuitive, Inc.          | Software           | Preferred Stock       |                  |                        | 27                    | 22         |
|                          |                    | Warrants              |                  |                        |                       |            |
| Plateau Systems, Ltd.    | Software           | Preferred Stock       |                  |                        | 7                     | 35         |
|                          |                    | Warrants              |                  |                        |                       |            |
| StreamBase Systems, Inc. | Software           | Warrants              |                  |                        | 67                    | 70         |

|  |                      |                                |              |              |
|--|----------------------|--------------------------------|--------------|--------------|
| Total Warrants<br>Technology                                     |                      |                                | 695          | 1,843        |
| <b>Warrants Cleantech<br/>0.9%</b>                               |                      |                                |              |              |
| Cereplast, Inc.(4)   | Waste<br>Removal     | Common<br>Stock<br>Warrants    | 112          | 229          |
| Enphase Energy, Inc.   | Energy<br>Efficiency | Preferred<br>Stock<br>Warrants | 175          | 177          |
| Satcon Technology<br>Corporation(4)                              | Energy<br>Efficiency | Common<br>Stock<br>Warrants    | 286          | 720          |
| Tigo Energy, Inc.  | Energy<br>Efficiency | Preferred<br>Stock<br>Warrants | 100          | 100          |
| Total Warrants<br>Cleantech                                      |                      |                                | 673          | 1,226        |
| <b>Warrants Healthcare<br/>information and<br/>services 0.6%</b> |                      |                                |              |              |
| BioScale, Inc.   | Diagnostics          | Preferred<br>Stock<br>Warrants | 54           | 62           |
| Precision Therapeutics,<br>Inc.                                  | Diagnostics          | Preferred<br>Stock<br>Warrants | 52           | 140          |
| Radisphere National<br>Radiology Group, Inc.                     | Diagnostics          | Preferred<br>Stock<br>Warrants | 167          | 388          |
| Singulex, Inc.   | Other<br>Healthcare  | Preferred<br>Stock<br>Warrants | 39           | 39           |
| Talyst, Inc.   | Other<br>Healthcare  | Preferred<br>Stock<br>Warrants | 101          | 106          |
| Total Warrants<br>Healthcare information<br>and services         |                      |                                | 413          | 735          |
| <b>Total Warrants</b>  |                      |                                | <b>3,111</b> | <b>6,455</b> |
| <b>Equity (1) 1.6%</b>   |                      |                                |              |              |
| AFS Technologies, Inc.   |                      | Common<br>Stock                | 142          | 142          |
| Insmmed Incorporated(4)  |                      | Common<br>Stock                | 227          | 224          |

|   |   |       |                   |                   |
|---|---|-------|-------------------|-------------------|
| Overture Networks Inc.                  | Preferred<br>Stock  |       | 482               | 526               |
| Pharmasset, Inc.(4)                     | Common<br>Stock   |       | 95                | 1,203             |
| Total equity                            |   |       | <b>946</b>        | <b>2,095</b>      |
| <b>Total investments assets</b>         |   |       | <b>\$ 148,783</b> | <b>\$ 153,216</b> |
| <b>Investment Liabilities</b>           |   |       |                   |                   |
| <b>Derivative Agreement</b>             |   |       |                   |                   |
| WestLB, AG                              | Interest rate<br>swap pay<br>fixed/receive<br>floating,<br>Notional<br>Amount \$10<br>million | 3.58% | 10/14/2011        | 180               |
| <b>Total investment<br/>liabilities</b> |   |       | <b>\$</b>         | <b>180</b>        |

- (1) Substantially all debt, warrant and equity investments have been pledged as collateral under the Credit Facility.
- (2) All investments are less than 5% ownership of the class and ownership of the portfolio company.
- (3) All interest is payable in cash due monthly in arrears, unless otherwise indicated and applies only to the Company's debt investments. Amount is the annual interest rate on the debt investment and does not include any additional fees related to the investment, such as deferred interest, commitment fees or prepayment fees. The majority of the debt investments are at fixed rates for the term of the loan. For each debt investment, we have provided the current interest rate in effect as of March 31, 2011.
- (4) Portfolio company is a public company.
- (5) For debt investments, represents principal balance.

See Notes to Consolidated Financial Statements

**Horizon Technology Finance Corporation and Subsidiaries**  
**Consolidated Schedule of Investments**  
**December 31, 2010**  
(In thousands)

| Portfolio Company                          | Sector         | Type<br>of   | Investment(2)<br>Rate(3) | Maturity  | Cost of<br>Investment(5) | Fair<br>Value |
|--|----------------|--------------|--------------------------|-----------|--------------------------|---------------|
| <b>Debt Investments(1)</b>                 |                |              |                          |           |                          |               |
| <b>Debt Investments Life Science 39.3%</b> |                |              |                          |           |                          |               |
| ACT Biotech, Inc.                          | Biotechnology  | Term<br>Loan | 12.10%                   | 6/1/2013  | \$ 958                   | \$ 958        |
|  |                | Term<br>Loan | 12.01%                   | 6/1/2013  | 957                      | 957           |
|  |                | Term<br>Loan | 12.01%                   | 6/1/2013  | 1,478                    | 1,478         |
| Ambit Biosciences, Inc.                    | Biotechnology  | Term<br>Loan | 12.25%                   | 10/1/2013 | 5,898                    | 5,898         |
| GenturaDX, Inc.                            | Biotechnology  | Term<br>Loan | 11.25%                   | 4/1/2014  | 1,917                    | 1,917         |
| Novalar Pharmaceuticals, Inc.              | Biotechnology  | Term<br>Loan | 12.00%                   | 6/1/2012  | 3,146                    | 3,146         |
| Pharmasset, Inc.(4)                        | Biotechnology  | Term<br>Loan | 12.00%                   | 8/1/2011  | 868                      | 868           |
|  |                | Term<br>Loan | 12.00%                   | 1/1/2012  | 1,448                    | 1,448         |
|  |                | Term<br>Loan | 12.50%                   | 10/1/2012 | 2,422                    | 2,422         |
| Revanche Therapeutics, Inc.                | Biotechnology  | Term<br>Loan | 10.50%                   | 12/1/2011 | 1,445                    | 1,445         |
|  |                | Term<br>Loan | 10.50%                   | 3/1/2013  | 3,478                    | 3,478         |
| Tranzyme, Inc.                             | Biotechnology  | Term<br>Loan | 10.75%                   | 1/1/2014  | 4,966                    | 4,966         |
| Xcovery Holding Company, LLC               | Biotechnology  | Term<br>Loan | 12.00%                   | 10/1/2013 | 1,490                    | 1,490         |
| Concentric Medical, Inc.                   | Medical Device | Term<br>Loan | 12.04%                   | 9/1/2013  | 6,887                    | 6,887         |
| OraMetrix, Inc.                            | Medical Device | Term<br>Loan | 11.50%                   | 4/1/2014  | 4,887                    | 4,887         |
| PixelOptics, Inc.                          | Medical Device | Term<br>Loan | 13.00%                   | 1/1/2013  | 4,221                    | 4,221         |
| Tengion, Inc.(4)                           | Medical Device | Term<br>Loan | 12.26%                   | 9/1/2011  | 2,740                    | 2,740         |
| ViOptix, Inc.                              | Medical Device | Term<br>Loan | 13.55%                   | 11/1/2011 | 885                      | 837           |

Edgar Filing: Horizon Technology Finance Corp - Form 10-Q

|                        |  |  |  |  |        |        |
|------------------------|--|--|--|--|--------|--------|
| Total Debt Investments |  |  |  |  |        |        |
| Life Science           |  |  |  |  | 50,091 | 50,043 |

**Debt Investments**  
**Technology 24.4%**

|                          |                                  |              |        |           |        |        |
|--------------------------|----------------------------------|--------------|--------|-----------|--------|--------|
| Hatteras Networks, Inc.  | Communications                   | Term<br>Loan | 12.40% | 2/1/2011  | 1,042  | 1,042  |
| OpenPeak, Inc.           | Communications                   | Term<br>Loan | 11.86% | 12/1/2013 | 6,549  | 6,549  |
| Starcite, Inc.           | Consumer-related<br>technologies | Term<br>Loan | 12.05% | 9/1/2012  | 2,679  | 2,679  |
| Tagged, Inc.             | Consumer-related<br>technologies | Term<br>Loan | 12.78% | 5/1/2012  | 1,284  | 1,284  |
|                          |                                  | Term<br>Loan | 11.46% | 8/1/2012  | 498    | 498    |
| Vette Corp.              | Data Storage                     | Term<br>Loan | 11.75% | 7/1/2014  | 4,916  | 4,916  |
| XIOtech, Inc.            | Data Storage                     | Term<br>Loan | 14.00% | 5/1/2012  | 2,997  | 2,997  |
| IntelePeer, Inc.         | Networking                       | Term<br>Loan | 12.43% | 4/1/2012  | 515    | 515    |
|                          |                                  | Term<br>Loan | 12.33% | 6/1/2012  | 598    | 598    |
|                          |                                  | Term<br>Loan | 12.33% | 10/1/2012 | 1,171  | 1,171  |
| Clarabridge, Inc.        | Software                         | Term<br>Loan | 12.50% | 1/1/2013  | 1,166  | 1,166  |
|                          |                                  | Term<br>Loan | 12.50% | 6/1/2013  | 688    | 688    |
|                          |                                  | Term<br>Loan | 12.50% | 5/1/2014  | 743    | 743    |
| Courion Corporation      | Software                         | Term<br>Loan | 11.45% | 12/1/2011 | 1,083  | 1,083  |
| Netuitive, Inc.          | Software                         | Term<br>Loan | 12.90% | 4/1/2011  | 152    | 152    |
| StreamBase Systems, Inc. | Software                         | Term<br>Loan | 12.51% | 11/1/2013 | 3,934  | 3,934  |
|                          |                                  | Term<br>Loan | 12.50% | 6/1/2014  | 977    | 977    |
| Total Debt Investments   |                                  |              |        |           |        |        |
| Technology               |                                  |              |        |           | 30,992 | 30,992 |

**Debt Investments**  
**Cleantech 14.9%**

|                                  |               |              |        |           |       |       |
|----------------------------------|---------------|--------------|--------|-----------|-------|-------|
| Cereplast, Inc.(4)               | Waste Removal | Term<br>Loan | 12.00% | 4/1/2014  | 2,363 | 2,363 |
| Enphase Energy, Inc.             | Energy        | Term<br>Loan | 12.60% | 10/1/2013 | 6,869 | 6,869 |
| Satcon Technology Corporation(4) | Energy        | Term<br>Loan | 12.58% | 1/1/2014  | 9,701 | 9,701 |

|                        |        |        |
|------------------------|--------|--------|
| Total Debt Investments |        |        |
| Cleantech              | 18,933 | 18,933 |

See Notes to Consolidated Financial Statements

12

---



**Horizon Technology Finance Corporation and Subsidiaries**  
**Consolidated Schedule of Investments**  
**December 31, 2010 (Continued)**  
(In thousands)

| Portfolio Company                         | Sector                              | Type of Investment(2)                      | Interest Rate(3) | Maturity  | Cost of Investment(5) | Fair Value     |
|---|-------------------------------------|--|------------------|-----------|-----------------------|----------------|
| <b>Debt Investments</b>                   |                                     | <b>Healthcare information and services</b> |                  |           |                       |                |
| <b>23.8%</b>                              |                                     |  |                  |           |                       |                |
| BioScale, Inc.                            | Diagnosics                          | Term Loan                                  | 12.00%           | 8/1/2012  | 2,454                 | 2,454          |
|   |                                     | Term Loan                                  | 11.51%           | 1/1/2014  | 4,908                 | 4,908          |
| Precision Therapeutics, Inc.              | Diagnosics                          | Term Loan                                  | 13.00%           | 3/1/2012  | 3,255                 | 3,255          |
| Radisphere National Radiology Group, Inc. | Diagnosics                          | Term Loan                                  | 12.75%           | 1/1/2014  | 9,855                 | 9,855          |
|   | Other                               |  |                  |           |                       |                |
| Singulex, Inc.                            | Healthcare                          | Term Loan                                  | 11.00%           | 3/1/2014  | 2,949                 | 2,949          |
|   |                                     | Term Loan                                  | 11.00%           | 3/1/2014  | 1,964                 | 1,964          |
|   | Other                               |  |                  |           |                       |                |
| Talyst, Inc.                              | Healthcare                          | Term Loan                                  | 12.10%           | 12/1/2013 | 2,443                 | 2,443          |
|   |                                     | Term Loan                                  | 12.05%           | 12/1/2013 | 2,438                 | 2,438          |
| Total Debt Investment                     | Healthcare information and services |  |                  |           | 30,266                | 30,266         |
| <b>Total Debt Investments</b>             |                                     |  |                  |           | <b>130,282</b>        | <b>130,234</b> |
| <b>Warrant Investments(1)</b>             |                                     |  |                  |           |                       |                |
| <b>Warrants</b>                           |                                     | <b>Life Science</b>                        |                  |           |                       |                |
| <b>2.1%</b>                               |                                     |  |                  |           |                       |                |
| ACT Biotech, Inc.                         | Biotechnology                       | Preferred Stock Warrants                   |                  |           | 23                    | 23             |
| Ambit Biosciences, Inc.                   | Biotechnology                       | Preferred Stock Warrants                   |                  |           | 143                   | 147            |
| Anesiva, Inc.(4)                          | Biotechnology                       | Common Stock Warrants                      |                  |           | 18                    |                |
| GenturaDX, Inc.                           | Biotechnology                       | Preferred Stock Warrants                   |                  |           | 63                    | 63             |
| Novalar Pharmaceuticals, Inc.             | Biotechnology                       | Preferred Stock Warrants                   |                  |           | 69                    |                |
| Pharmasset, Inc.(4)                       | Biotechnology                       | Common Stock Warrants                      |                  |           | 126                   | 789            |
|   | Biotechnology                       |  |                  |           | 224                   | 121            |

Edgar Filing: Horizon Technology Finance Corp - Form 10-Q

|                                    |                |                          |       |       |
|------------------------------------|----------------|--------------------------|-------|-------|
| Revanche Therapeutics, Inc.        |                | Preferred Stock Warrants |       |       |
|                                    |                | Preferred Stock          |       |       |
| Tranzyme, Inc.                     | Biotechnology  | Warrants                 | 1     | 1     |
|                                    |                | Preferred Stock          |       |       |
| Advanced BioHealing, Inc.          | Medical Device | Warrants                 | 9     | 1,209 |
|                                    |                | Preferred Stock          |       |       |
| Calypso Medical Technologies, Inc. | Medical Device | Warrants                 | 17    | 76    |
|                                    |                | Preferred Stock          |       |       |
| Concentric Medical, Inc.           | Medical Device | Warrants                 | 85    | 89    |
|                                    |                | Common Stock             |       |       |
| EnteroMedics, Inc.(4)              | Medical Device | Warrants                 | 347   | 18    |
|                                    |                | Preferred Stock          |       |       |
| OraMetrix, Inc.                    | Medical Device | Warrants                 | 78    | 83    |
|                                    |                | Preferred Stock          |       |       |
| PixelOptics, Inc.                  | Medical Device | Warrants                 | 61    | 61    |
|                                    |                | Common Stock             |       |       |
| Tengion, Inc.(4)                   | Medical Device | Warrants                 | 15    |       |
|                                    |                | Preferred Stock          |       |       |
| ViOptix, Inc.                      | Medical Device | Warrants                 | 13    |       |
|                                    |                | Preferred Stock          |       |       |
| Total Warrants                     | Life Science   |                          | 1,292 | 2,680 |

**Warrants Technology**  
**1.2%**

|                         |                               |                 |    |     |
|-------------------------|-------------------------------|-----------------|----|-----|
|                         |                               | Preferred Stock |    |     |
| Hatteras Networks, Inc. | Communications                | Warrants        |    | 35  |
|                         |                               | Preferred Stock |    |     |
| OpenPeak, Inc.          | Communications                | Warrants        | 89 | 92  |
|                         |                               | Preferred Stock |    |     |
| Everyday Health, Inc.   | Consumer related technologies | Warrants        | 69 | 137 |
|                         |                               | Preferred Stock |    |     |
| SnagAJob.com, Inc.      | Consumer-related technologies | Warrants        | 23 | 39  |
|                         |                               | Preferred Stock |    |     |
| Starcite, Inc.          | Consumer-related technologies | Warrants        | 24 | 28  |
|                         |                               | Preferred Stock |    |     |

Edgar Filing: Horizon Technology Finance Corp - Form 10-Q

|                        |                               |                             |    |     |
|------------------------|-------------------------------|-----------------------------|----|-----|
| Tagged, Inc.           | Consumer-related technologies | Preferred Stock<br>Warrants | 17 | 27  |
| Vette Corp.            | Data Storage                  | Preferred Stock<br>Warrants | 75 | 49  |
| XIOtech, Inc.          | Data Storage                  | Preferred Stock<br>Warrants | 22 | 81  |
| Cartera Commerce, Inc. | Internet and media            | Preferred Stock<br>Warrants | 16 | 38  |
| Grab Networks, Inc.    | Networking                    | Preferred Stock<br>Warrants | 74 |     |
| IntelePeer, Inc.       | Networking                    | Preferred Stock<br>Warrants | 39 | 544 |
| Motion Computing, Inc. | Networking                    | Preferred Stock<br>Warrants | 7  | 292 |
| Impinj, Inc.           | Semi-conductor                | Preferred Stock<br>Warrants | 7  |     |

See Notes to Consolidated Financial Statements

**Horizon Technology Finance Corporation and Subsidiaries**  
**Consolidated Schedule of Investments**  
**December 31, 2010 (Continued)**  
(In thousands)

| Portfolio Company                                       | Sector               | Type of Investment(2) | Interest Rate(3) | Maturity | Cost of Investment(5) | Fair Value |
|---|----------------------|-----------------------|------------------|----------|-----------------------|------------|
| Clarabridge, Inc.                                       | Software             | Preferred Stock       |                  |          |                       |            |
|   |                      | Warrants              |                  |          | 28                    | 25         |
| Courion Corporation                                     | Software             | Preferred Stock       |                  |          |                       |            |
|   |                      | Warrants              |                  |          | 7                     | 17         |
| DriveCam, Inc.  | Software             | Preferred Stock       |                  |          |                       |            |
|   |                      | Warrants              |                  |          | 20                    | 8          |
| Netuitive, Inc.   | Software             | Preferred Stock       |                  |          |                       |            |
|   |                      | Warrants              |                  |          | 27                    | 22         |
| Plateau Systems, Ltd.                                   | Software             | Preferred Stock       |                  |          |                       |            |
|   |                      | Warrants              |                  |          | 7                     | 35         |
| StreamBase Systems, Inc.                                | Software             | Preferred Stock       |                  |          |                       |            |
|   |                      | Warrants              |                  |          | 67                    | 69         |
| Total Warrants<br>Technology                            |                      |                       |                  |          | 618                   | 1,538      |
| <b>Warrants Cleantech</b>                               |                      |                       |                  |          |                       |            |
| <b>1.0%</b>   |                      |                       |                  |          |                       |            |
| Cereplast, Inc.(4)                                      | Waste<br>Removal     | Common Stock          |                  |          |                       |            |
|   |                      | Warrants              |                  |          | 112                   | 112        |
| Enphase Energy, Inc.                                    | Energy<br>Efficiency | Preferred Stock       |                  |          |                       |            |
|   |                      | Warrants              |                  |          | 122                   | 122        |
| Satcon Technology<br>Corporation(4)                     | Energy<br>Efficiency | Common Stock          |                  |          |                       |            |
|   |                      | Warrants              |                  |          | 286                   | 1,057      |
| Total Warrants Cleantech                                |                      |                       |                  |          | 520                   | 1,291      |
| <b>Warrants Healthcare<br/>information and services</b> |                      |                       |                  |          |                       |            |
| <b>0.6%</b>   |                      |                       |                  |          |                       |            |
| BioScale, Inc.  | Diagnosics           | Preferred Stock       |                  |          |                       |            |
|   |                      | Warrants              |                  |          | 55                    | 49         |
| Precision Therapeutics,<br>Inc.                         | Diagnosics           | Preferred Stock       |                  |          |                       |            |
|   |                      | Warrants              |                  |          | 52                    | 139        |
| Radisphere National<br>Radiology Group, Inc.            | Diagnosics           | Preferred Stock       |                  |          |                       |            |
|   |                      | Warrants              |                  |          | 167                   | 384        |
| Singulex, Inc.  | Other<br>Healthcare  | Preferred Stock       |                  |          |                       |            |
|   |                      | Warrants              |                  |          | 39                    | 39         |
| Talyst, Inc.  | Other<br>Healthcare  | Preferred Stock       |                  |          |                       |            |
|   |                      | Warrants              |                  |          | 100                   | 105        |

|                                     |   |       |        |         |  |                   |                   |
|-------------------------------------|---|-------|--------|---------|--|-------------------|-------------------|
| Total Warrants                      |   |       |        |         |  |                   |                   |
| Healthcare information and services |   |       |        |         |  | 413               | 716               |
| <b>Total Warrants</b>               |   |       |        |         |  | <b>2,843</b>      | <b>6,225</b>      |
| <b>Equity 0.3%</b>                  |   |       |        |         |  |                   |                   |
| AFS Technologies, Inc               | Common Stock  |       |        |         |  | 142               | 142               |
| Insmmed Incorporated(4)             | Common Stock and Convertible Preferred Stock                                |       |        |         |  | 227               | 209               |
| Total equity                        |   |       |        |         |  | 369               | 351               |
| <b>Total investments assets</b>     |   |       |        |         |  | <b>\$ 133,494</b> | <b>\$ 136,810</b> |
| <b>Investment Liabilities</b>       |   |       |        |         |  |                   |                   |
| <b>Derivative Agreement</b>         |   |       |        |         |  |                   |                   |
|                                     | Interest rate swap pay fixed/receive floating, Notional Amount \$10 million |       |        |         |  |                   |                   |
| WestLB, AG                          |   | 3.58% | 10/14/ | 2011 -- |  |                   | 258               |
| <b>Total investment liabilities</b> |   |       |        |         |  | <b>\$</b>         | <b>258</b>        |

- (1) Substantially all debt, equity and warrant investments have been pledged as collateral under the Credit Facility.
- (2) All investments are less than 5% ownership of the class and ownership of the portfolio company.
- (3) All interest is payable in cash due monthly in arrears, unless otherwise indicated and applies only to the Company's debt investments. Amount is the annual interest rate on the debt investment and does not include any additional fees related to the investment, such as deferred interest, commitment fees or prepayment fees. The majority of the debt investments are at fixed rates for the term of the loan. For each debt investment, we have provided the current interest rate in effect as of December 31, 2010.
- (4) Portfolio company is a public company.
- (5) For debt investments, represents principal balance.

See Notes to Consolidated Financial Statements

**Horizon Technology Finance Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**(In thousands, except shares and per share data)**

**Note 1. Organization**

Horizon Technology Finance Corporation (the Company) was organized as a Delaware corporation on March 16, 2010 and is an externally managed, non-diversified, closed end investment company. The Company has elected to be regulated as a business development company (BDC) under the Investment Company Act of 1940, as amended (1940 Act). In addition, for tax purposes, the Company has elected to be treated as a regulated investment company (RIC) as defined in Subtitle A, Chapter 1, under Subchapter M of the Internal Revenue Code of 1986, as amended (the Code). As a RIC, the Company will not be subject to federal income tax on the portion of its taxable income and capital gains the Company distributes to the stockholders. The Company primarily makes secured loans to development-stage companies in the technology, life science, healthcare information and services and cleantech industries.

On October 28, 2010 the Company completed an initial public offering (IPO) and its common stock trades on the NASDAQ Global Market under the symbol HRZN. The Company was formed to continue and expand the business of Compass Horizon Funding Company LLC (CHF), a Delaware limited liability company, which commenced operations in March 2008 and became the Company's wholly owned subsidiary with the completion of the IPO.

Horizon Credit I LLC (Credit I) was formed as a Delaware limited liability company on January 23, 2008, with CHF as the sole equity member. Credit I is a special purpose bankruptcy remote entity and is reported herein as a wholly owned subsidiary of the Company. CHF sold certain portfolio transactions to Credit I (Purchased Assets). Credit I is a separate legal entity from CHF and the Purchased Assets conveyed to Credit I are not available to creditors of CHF or any other entity other than Credit I's lenders.

The Company's investment strategy is to maximize the investment portfolio's return by generating current income from the loans made and the capital appreciation from the warrants received when making such loans. The Company has entered into an investment management agreement (the Investment Management Agreement) with Horizon Technology Finance Management LLC (HTFM or the Advisor), under which the Advisor will manage the day-to-day operations of, and provide investment advisory services to, the Company.

On February 11, 2011, the Company formed, as wholly owned subsidiaries, Longview SBIC GP LLC and Longview SBIC LP (collectively, Horizon SBIC) in anticipation of receiving a license to operate a small business investment company (SBIC) from the Small Business Administration (SBA). If licensed, Longview SBIC LP may issue SBA-guaranteed debentures at long-term fixed rates. On March 1, 2011, the Company applied for exemptive relief from the Securities and Exchange Commission to permit the Company to exclude the debt of the Longview SBIC LP from the consolidated asset coverage ratio.

**Note 2. Basis of Presentation and Significant Accounting Policies**

***Election to become a Business Development Company and Basis of Financial Statement Presentation***

The results of operations for the three months ended March 31, 2011 reflect the Company's results as a BDC under the 1940 Act, whereas the operating results for the three months ended March 31, 2010 reflect the Company's results prior to operating as a BDC under the 1940 Act. Accounting principles used in the preparation of these two periods are different and, therefore, the financial position and results of operations of these periods are not directly comparable. The primary differences in accounting principles relate to the carrying value of loan investments and classification of hedging activity—see corresponding sections below for further discussion.

The consolidated financial statements of the Company have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) and pursuant to the requirements for reporting on Form 10-Q and Articles 6 or 10 of Regulation S-X. In the opinion of management, the consolidated financial statements reflect all adjustments and reclassifications that are necessary for the fair presentation of financial results as of and for the periods presented. All intercompany balances and transactions have been eliminated. Certain prior period amounts have been reclassified to conform to the current period presentation.

**Horizon Technology Finance Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**(In thousands, except shares and per share data)**

***Principles of Consolidation***

As permitted under Regulation S-X and the AICPA Audit and Accounting Guide for Investment Companies, the Company will generally not consolidate its investment in a company other than an investment company subsidiary or a controlled operating company whose business consists of providing services to the Company. Accordingly, the Company consolidated the results of the Company's subsidiaries in its consolidated financial statements.

***Use of Estimates***

In preparing the consolidated financial statements in accordance with GAAP, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosures of contingent assets and liabilities, as of the date of the balance sheet and income and expenses for the period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the valuation of loans, equity investments and warrants.

***Fair Value***

The Company applies fair value to substantially all of its investments in accordance with relevant GAAP, which establishes a framework used to measure fair value and requires disclosures for fair value measurements. The Company has categorized its investments carried at fair value, based on the priority of the valuation technique, into a three-level fair value hierarchy as more fully described in Note 5. Fair value is a market-based measure considered from the perspective of the market participant who holds the financial instrument rather than an entity specific measure. Therefore, when market assumptions are not readily available, the Company's own assumptions are set to reflect those that management believes market participants would use in pricing the financial instrument at the measurement date.

The availability of observable inputs can vary depending on the financial instrument and is affected by a wide variety of factors, including, for example, the type of product, whether the product is new, whether the product is traded on an active exchange or in the secondary market and the current market conditions. To the extent that the valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires more judgment. Accordingly, the degree of judgment exercised by the Company in determining fair value is greatest for financial instruments classified as Level 3.

In January 2010, the FASB issued Accounting Standards Update 2010-06, Fair Value Measurements and Disclosure—Improving Disclosures about Fair Value Measurements, which amends the existing guidance related to fair value measurements and disclosures. The amendments require the following new fair value disclosures:

Separate disclosure of the significant transfers in and out of Level 1 and Level 2 fair value measurements, and a description of the reasons for the transfers.

In the roll forward of activity for Level 3 fair value measurements (significant unobservable inputs), purchases, sales, issuances, and settlements should be presented separately (on a gross basis rather than as one net number).

In addition, the amendments clarify existing disclosure requirements, as follows:

Fair value measurements and disclosures should be presented for each class of assets and liabilities within a line item in the balance sheet.

Reporting entities should provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements that fall in either Level 2 or Level 3.

The new disclosures and clarifications of existing disclosures were effective for the Company's interim and annual reporting periods beginning after December 15, 2009, except for the disclosures included in the roll forward of activity for Level 3 fair value measurements, for which the effective date is for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years.

See Note 5 for additional information regarding fair value.

**Horizon Technology Finance Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**(In thousands, except shares and per share data)**

***Segments***

The Company has determined that it has a single reporting segment and operating unit structure. The Company lends to and invests in portfolio companies in various technology, life science, healthcare information and services and cleantech industries. The Company separately evaluates the performance of each of its lending and investment relationships. However, because each of these loan and investment relationships has similar business and economic characteristics, they have been aggregated into a single lending and investment segment.

***Cash and Cash Equivalents***

Cash and cash equivalents as presented in the consolidated balance sheets and the consolidated statements of cash flows include bank checking accounts and money market funds with an original maturity of less than 90 days.

***Investments***

Investments are recorded at fair value. The Company's board of directors ( Board ) determines the fair value of its portfolio investments. Prior to the Company's election to become a BDC, debt investments were stated at current unpaid principal balances adjusted for the allowance for loan losses, unearned income and any unamortized deferred fees or costs.

The Company has the intent to hold its loans for the foreseeable future or until maturity or payoff.

Interest on debt investments is accrued and included in income based on contractual rates applied to principal amounts outstanding. Interest income is determined using a method that results in a level rate of return on principal amounts outstanding. When a loan becomes 90 days or more past due, or if the Company otherwise does not expect to receive interest and principal repayments, the loan is placed on non-accrual status and the recognition of interest income is discontinued. Interest payments received on loans that are on non-accrual status are treated as reductions of principal until the principal is repaid. No loans were on non-accrual status as of March 31, 2011 and December 31, 2010.

The Company receives a variety of fees from borrowers in the ordinary course of conducting its business, including advisory fees, commitment fees, amendment fees, non-utilization fees and prepayment fees (collectively, the Fees ). In a limited number of cases, the Company may also receive a non-refundable deposit earned upon the termination of a transaction. Loan origination fees, net of certain direct origination costs, are deferred, and, along with unearned income, are amortized as a level yield adjustment over the respective term of the loan. Fees for counterparty loan commitments with multiple loans are allocated to each loan based upon each loan's relative fair value. When a loan is placed on non-accrual status, the amortization of the related fees and unearned income is discontinued until the loan is returned to accrual status.

Certain loan agreements also require the borrower to make an end-of-term payment that is accrued into income over the life of the loan to the extent such amounts are expected to be collected. The Company will generally cease accruing the income if there is insufficient value to support the accrual or the Company does not expect the borrower to be able to pay all principal and interest due.

In connection with substantially all lending arrangements, the Company receives warrants to purchase shares of stock from the borrower. The warrants are recorded as assets at estimated fair value on the grant date using the Black-Scholes valuation model. The warrants are considered loan fees and are also recorded as unearned loan income on the grant date. The unearned income is recognized as interest income over the contractual life of the related loan in accordance with the Company's income recognition policy. Subsequent to loan origination, the warrants are also measured at fair value using the Black-Scholes valuation model. Any adjustment to fair value is recorded through earnings as net unrealized gain or loss on investments. Gains from the disposition of the warrants or stock acquired from the exercise of warrants are recognized as realized gains on investments.

See Note 5 for additional information regarding fair value.

***Allowance for Loan Losses***

Prior to the Company's election to become a BDC, the allowance for loan losses represented management's estimate of probable loan losses inherent in the loan portfolio as of the balance sheet date. The estimation of the allowance was



based on a variety of

**Horizon Technology Finance Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**(In thousands, except shares and per share data)**

factors, including past loan loss experience, the current credit profile of the Company's borrowers, adverse situations that had occurred that may affect individual borrowers' ability to repay, the estimated value of underlying collateral and general economic conditions. The loan portfolio is comprised of large balance loans that are evaluated individually for impairment and are risk-rated based upon a borrower's individual situation, current economic conditions, collateral and industry-specific information that management believes is relevant in determining the potential occurrence of a loss event and in measuring impairment. The allowance for loan losses was sensitive to the risk rating assigned to each of the loans and to corresponding qualitative loss factors that the Company used to estimate the allowance. Those factors were applied to the outstanding loan balances in estimating the allowance for loan losses. If necessary, based on performance factors related to specific loans, specific allowances for loan losses were established for individual impaired loans. Increases or decreases to the allowance for loan losses were charged or credited to current period earnings through the provision (credit) for loan losses. Amounts determined to be uncollectible were charged against the allowance for loan losses, while amounts recovered on previously charged-off loans increased the allowance for loan losses.

A loan was considered impaired when, based on current information and events, it was probable that the Company was unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment included payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experienced insignificant payment delays and payment shortfalls generally were not classified as impaired. Management determined the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed. Impairment was measured on a loan by loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's observable market price or the fair value of the collateral, if the loan was collateral dependent.

Impaired loans also included loans modified in troubled debt restructurings where concessions had been granted to borrowers experiencing financial difficulties. These concessions could include a reduction in the interest rate on the loan, payment extensions, forgiveness of principal, forbearance or other actions intended to maximize collection.

***Debt Issuance Costs***

Debt issuance costs are fees and other direct incremental costs incurred by the Company in obtaining debt financing from its lender and are recognized as assets and are amortized as interest expense over the term of the related Credit Facility. The unamortized balance of debt issuance costs as of March 31, 2011 and December 31, 2010, included in other assets, was \$0 and \$194, respectively. The amortization expense for the three months ended March 31, 2011 and March 31, 2010 relating to debt issuance costs was \$194 and \$290, respectively.

***Income Taxes***

The Company elected to be treated as a RIC under subchapter M of the Code and operates in a manner so as to qualify for the tax treatment applicable to RICs. In order to qualify as a RIC, among other things, the Company is required to meet certain source of income and asset diversification requirements and timely distribute to its stockholders at least 90% of investment company taxable income, as defined by the Code, for each year. The Company, among other things, has made and intends to continue to make the requisite distributions to its stockholders, which will generally relieve the Company from U.S. federal income taxes.

Depending on the level of taxable income earned in a tax year, the Company may choose to carry forward taxable income in excess of current year dividend distributions into the next tax year and pay a 4% excise tax on such income, as required. To the extent that the Company determines that its estimated current year annual taxable income will be in excess of estimated current year dividend distributions, the Company accrues excise tax, if any, on estimated excess taxable income as taxable income is earned. For the three months ended March 31, 2011 no amount was recorded for U.S. federal excise tax.

The Company evaluates tax positions taken in the course of preparing the Company's tax returns to determine whether the tax positions are more-likely-than-not to be sustained by the applicable tax authority. Tax benefits of positions not deemed to meet the more-likely-than-not threshold, or uncertain tax positions, would be recorded as a tax expense in the current year. It is the Company's policy to recognize accrued interest and penalties related to uncertain tax benefits in income tax expense. There were no material uncertain tax positions at March 31, 2011 and December 31, 2010. The 2008 and 2009 tax years remain subject to examination by U.S. federal and state tax authorities.

**Horizon Technology Finance Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**(In thousands, except shares and per share data)**

Prior to the Company's election to become a BDC, the Company was a limited liability company treated as a partnership for U.S. federal income tax purposes and, as a result, all items of income and expense were passed through to, and are generally reportable on, the tax returns of the respective members of the limited liability company. Therefore, no federal or state income tax provision has been recorded for the three months ended March 31, 2010.

***Dividends***

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

The Company has adopted a dividend reinvestment plan that provides for reinvestment of cash distributions and other distributions on behalf of its stockholders, unless a stockholder elects to receive cash. As a result, if the Board authorizes, and the Company declares, a cash dividend, then stockholders who have not opted out of the dividend reinvestment plan will have their cash dividends automatically reinvested in additional shares of the Company's common stock, rather than receiving the cash dividend. The Company may use newly issued shares to implement the plan (especially if the Company's shares are trading at a premium to net asset value), or the Company may purchase shares in the open market in connection with the obligations under the plan.

***Interest Rate Swaps and Hedging Activities***

The Company entered into interest rate swap agreements to manage interest rate risk. The Company does not hold or issue interest rate swap agreements or other derivative financial instruments for speculative purposes.

Subsequent to the Company's election to become a BDC, the interest rate swaps are recorded at fair value with changes in fair value reflected in net unrealized appreciation or depreciation of investments during the reporting period. The Company records the accrual of periodic interest settlements of interest rate swap agreements in net unrealized appreciation or depreciation of investments and subsequently records the amount as a net realized gain or loss on investments on the interest settlement date. Cash payments received or paid for the termination of an interest rate swap agreement would be recorded as a realized gain or loss upon termination in the consolidated statements of operations.

Prior to the Company's election to become a BDC, the Company recognized its interest rate swap derivatives on the balance sheet as either an asset or liability measured at fair value. Changes in the derivatives' fair value were recognized in income unless specific hedge accounting criteria were met. Special accounting for qualifying hedges allows a derivative's gains and losses to offset related results on the hedged item in the statement of operations and required the Company to formally document, designate and assess effectiveness of transactions that receive hedge accounting. Derivatives that are not hedges are adjusted to fair value through earnings. If the derivative qualifies as a hedge, depending on the nature of the hedge, changes in the fair value of derivatives are either offset against the change in fair value of hedged assets, liabilities or firm commitments through earnings, or recognized in other comprehensive income until the hedged item is recognized in earnings. The ineffective portion of a derivative's change in fair value, if any, would have been recognized as interest expense.

***Transfers of Financial Assets***

Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company's put presumptively beyond the reach of the transferor and its creditors, even in bankruptcy or other receivership, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets and (3) the transferor does not maintain effective control over the transferred assets through either (a) an agreement that both entitles and obligates the transferor to repurchase or redeem the assets before maturity or (b) the ability to unilaterally cause the holder to return specific assets, other than through a cleanup call.

**Horizon Technology Finance Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**(In thousands, except shares and per share data)**

**Note 3. Related Party Transactions**

***Investment Management Agreement***

On October 28, 2010, the Company entered into the Investment Management Agreement with the Advisor, under which the Advisor manages the day-to-day operations of, and provides investment advisory services to, the Company. Under the terms of the Investment Management Agreement, the Advisor determines the composition of the Company's investment portfolio, the nature and timing of the changes to the investment portfolio and the manner of implementing such changes; identifies, evaluates and negotiates the structure of the investments the Company makes (including performing due diligence on the Company's prospective portfolio companies); and closes, monitors and administers the investments the Company makes, including the exercise of any voting or consent rights.

The Advisor's services under the Investment Management Agreement are not exclusive to the Company, and the Advisor is free to furnish similar services to other entities so long as its services to the Company are not impaired. The Advisor is a registered investment advisor with the SEC. The Advisor receives fees for providing services, consisting of two components, a base management fee and an incentive fee.

The base management fee is calculated at an annual rate of 2.00% of the Company's gross assets, payable monthly in arrears. For purposes of calculating the base management fee, the term "gross assets" includes any assets acquired with the proceeds of leverage.

The incentive fee has two parts, as follows:

The first part is calculated and payable quarterly in arrears based on the Company's pre-incentive fee net investment income for the immediately preceding calendar quarter. For this purpose, pre-incentive fee net investment income means interest income, dividend income and any other income (including any other fees (other than fees for providing managerial assistance), such as commitment, origination, structuring, diligence and consulting fees or other fees received from portfolio companies) accrued during the calendar quarter, minus operating expenses for the quarter (including the base management fee, expenses payable under the administration agreement (as defined below) and any interest expense and any dividends paid on any issued and outstanding preferred stock, but excluding the incentive fee). Pre-incentive fee net investment income includes, in the case of investments with a deferred interest feature (such as original issue discount, debt instruments with payment-in-kind interest and zero coupon securities), accrued income that we have not yet received in cash. The incentive fee with respect to the pre-incentive fee net income is 20.00% of the amount, if any, by which the pre-incentive fee net investment income for the immediately preceding calendar quarter exceeds a 1.75% (which is 7.00% annualized) hurdle rate and a "catch-up" provision measured as of the end of each calendar quarter. Under this provision, in any calendar quarter, the Advisor receives no incentive fee until the net investment income equals the hurdle rate of 1.75%, but then receives, as a "catch-up," 100.00% of the pre-incentive fee net investment income with respect to that portion of such pre-incentive fee net investment income, if any, that exceeds the hurdle rate but is less than 2.1875%. The effect of this provision is that, if pre-incentive fee net investment income exceeds 2.1875% in any calendar quarter, the Advisor will receive 20.00% of the pre-incentive fee net investment income as if a hurdle rate did not apply.

Pre-incentive fee net investment income does not include any realized capital gains, realized capital losses or unrealized capital appreciation or depreciation. Because of the structure of the incentive fee, it is possible that the Company may pay an incentive fee in a quarter in which the Company incurs a loss. For example, if the Company receives pre-incentive fee net investment income in excess of the quarterly minimum hurdle rate, the Company will pay the applicable incentive fee even if the Company has incurred a loss in that quarter due to realized and unrealized capital losses. The Company's net investment income used to calculate this part of the incentive fee is also included in the amount of the Company's gross assets used to calculate the 2.00% base management fee. These calculations are appropriately prorated for any period of less than three months and adjusted for any share issuances or repurchases during the current quarter. The base management fee expense was \$1,075 for the three months ended March 31, 2011 and the accrued management fee as of March 31, 2011 and December 31, 2010 was \$376 and \$360, respectively.

The second part of the incentive fee is determined and payable in arrears as of the end of each calendar year (or upon termination of the Investment Management Agreement, as of the termination date), and equals 20.00% of the Company's aggregate realized capital gains, if any, on a cumulative basis from the date of the election to be a BDC through the end of each calendar year, computed net of all realized capital losses and unrealized capital depreciation through the end of such year, less all previous amounts paid in respect of the capital gain incentive fee. The incentive fee expense was \$529 for the three months ended March 31, 2011 and the incentive fee payable as of March 31, 2011 and December 31, 2010 was \$529 and \$414, respectively.

**Horizon Technology Finance Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
(In thousands, except shares and per share data)

Prior to the Company's election to become a BDC, the Advisor served as the Advisor for CHF under a Management and Services Agreement which provided for management fees to be paid monthly at a rate of 2.0% per annum of the gross investment assets of CHF. Total management fee expense was \$547 for the three months ended March 31, 2010.

**Administration Agreement**

The Company entered into an administration agreement with the Advisor to provide administrative services to the Company. For providing these services, facilities and personnel, the Company will reimburse the Advisor for the Company's allocable portion of overhead and other expenses incurred by the Advisor in performing its obligations under the administration agreement, including rent, the fees and expenses associated with performing compliance functions and the Company's allocable portion of the costs of compensation and related expenses of the Company's chief compliance officer and chief financial officer and their respective staffs. For the three months ended March 31, 2011, \$295 was charged to operations under this agreement.

From time to time, the Advisor may pay amounts owed by the Company to third-party providers of goods or services. The Company will subsequently reimburse the Advisor for such amounts paid on the Company's behalf.

**Note 4. Investments**

Investments, all of which are with portfolio companies in the United States, consisted of the following:

|              | <b>March 31, 2011</b> |                   | <b>December 31, 2010</b> |                   |
|--------------|-----------------------|-------------------|--------------------------|-------------------|
|              | <b>Cost</b>           | <b>Fair Value</b> | <b>Cost</b>              | <b>Fair Value</b> |
| Debt         | \$ 144,726            | \$ 144,666        | \$ 130,282               | \$ 130,234        |
| Warrants     | 3,111                 | 6,455             | 2,843                    | 6,225             |
| Equity       | 946                   | 2,095             | 369                      | 351               |
| <b>Total</b> | <b>\$ 148,783</b>     | <b>\$ 153,216</b> | <b>\$ 133,494</b>        | <b>\$ 136,810</b> |

The following table shows the Company's investments by industry sector.

|                                       | <b>March 31, 2011</b> |                   | <b>December 31, 2010</b> |                   |
|---------------------------------------|-----------------------|-------------------|--------------------------|-------------------|
|                                       | <b>Cost</b>           | <b>Fair Value</b> | <b>Cost</b>              | <b>Fair Value</b> |
| Life Science                          |                       |                   |                          |                   |
| Biotechnology                         | \$ 34,922             | \$ 35,852         | \$ 31,138                | \$ 31,614         |
| Medical Device                        | 21,992                | 23,428            | 20,472                   | 21,317            |
| Technology                            |                       |                   |                          |                   |
| Consumer-related Technologies         | 3,949                 | 4,284             | 4,592                    | 4,692             |
| Networking                            | 2,083                 | 2,815             | 2,405                    | 3,120             |
| Software                              | 14,343                | 14,372            | 9,042                    | 9,062             |
| Data Storage                          | 7,518                 | 7,551             | 8,010                    | 8,042             |
| Internet and Media                    | 16                    | 38                | 16                       | 38                |
| Communications                        | 7,137                 | 7,185             | 7,681                    | 7,719             |
| Semiconductors                        | 7                     |                   | 7                        |                   |
| Healthcare Information and Services   |                       |                   |                          |                   |
| Diagnostics                           | 19,813                | 20,130            | 20,745                   | 21,044            |
| Other Healthcare Related Services and |                       |                   |                          |                   |
| Technologies                          | 9,612                 | 9,617             | 9,934                    | 9,938             |
| Cleantech                             |                       |                   |                          |                   |
| Energy Efficiency                     | 22,428                | 22,864            | 16,977                   | 17,749            |
| Waste Recycling                       | 4,963                 | 5,080             | 2,475                    | 2,475             |

|              |            |            |            |            |
|--------------|------------|------------|------------|------------|
| <b>Total</b> | \$ 148,783 | \$ 153,216 | \$ 133,494 | \$ 136,810 |
|--------------|------------|------------|------------|------------|

21

---



**Horizon Technology Finance Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**(In thousands, except shares and per share data)**

**Note 5. Fair Value**

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Fair value is 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. Fair value is best determined based upon quoted market prices. However, in certain instances, there are no quoted market prices for certain assets or liabilities. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the asset or liability.

Fair value measurements focus on exit prices in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. If there has been a significant decrease in the volume and level of activity for the asset or liability, a change in valuation technique or the use of multiple valuation techniques may be appropriate. In such instances, determining the price at which willing market participants would transact at the measurement date under current market conditions depends on the facts and circumstances and requires the use of significant judgment.

The Company's fair value measurements are classified into a fair value hierarchy based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. The three categories within the hierarchy are as follows:

- Level 1** Quoted prices in active markets for identical assets and liabilities.
- Level 2** Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities in active markets, quoted prices in markets that are not active and model-based valuation techniques for which all significant inputs are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3** Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

*Cash and cash equivalents and interest receivable:* The carrying amount is a reasonable estimate of fair value. These financial instruments are not recorded at fair value on a recurring basis.

*Loans:* For variable rate loans that re-price frequently and have no significant change in credit risk, carrying values are a reasonable estimate of fair values, adjusted for credit losses inherent in the portfolio. The fair value of fixed rate loans is estimated by discounting the future cash flows using the year end rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities, adjusted for credit losses inherent in the portfolio. Therefore, the Company has categorized loan investments as Level 3 within the fair value hierarchy described above. These financial instruments are recorded at fair value on a recurring basis.

*Warrants:* The Company values its warrants using the Black-Scholes valuation model incorporating the following material assumptions:

Underlying asset value of the issuer is estimated based on information available, including any information regarding the most recent rounds of borrower funding.

Volatility, or the amount of uncertainty or risk about the size of the changes in the warrant price, is based on guideline publicly traded companies within indices similar in nature to the underlying company issuing the warrant. A total of seven such indices were used. The weighted average volatility assumptions used for the warrant valuation at March 31, 2011 and December 31, 2010 was 30%.

The risk-free interest rates are derived from the U.S. Treasury yield curve. The risk-free interest rates are calculated based on a weighted average of the risk-free interest rates that correspond closest to the expected

remaining life of the warrant.

**Horizon Technology Finance Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
(In thousands, except shares and per share data)

Other adjustments, including a marketability discount on private company warrants, are estimated based on management's judgment about the general industry environment. The marketability discount used for the warrant valuation at March 31, 2011 and December 31, 2010 was 20%.

The fair value of the Company's warrants held in publicly traded companies is determined based on inputs that are readily available in public markets or can be derived from information available in public markets. Therefore, the Company has categorized these warrants as Level 2 within the fair value hierarchy described in Note 2. The fair value of the Company's warrants held in private companies is determined using both observable and unobservable inputs and represents management's best estimate of what market participants would use in pricing the warrants at the measurement date. Therefore, the Company has categorized these warrants as Level 3 within the fair value hierarchy described above. These financial instruments are recorded at fair value on a recurring basis.

*Borrowings:* The carrying amount of borrowings under the revolving credit facility approximates its fair value due to the short duration and variable interest rate of this debt. Additionally, the Company considers its creditworthiness in determining the fair value of such borrowings. These financial instruments are not recorded at fair value on a recurring basis.

*Interest rate swap derivatives:* The fair value of the Company's interest rate swap derivative instruments is estimated as the amount the Company would pay to terminate its swaps at the balance sheet date, taking into account current interest rates and the creditworthiness of the counterparty for assets and the creditworthiness of the Company for liabilities. The Company has categorized these derivative instruments as Level 2 within the fair value hierarchy described above. These financial instruments are recorded at fair value on a recurring basis.

*Off-balance-sheet instruments:* Fair values for off-balance-sheet lending commitments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standings. Off-balance-sheet instruments are not recorded at fair value on a recurring basis.

The following tables detail the financial instruments that are carried at fair value and measured at fair value on a recurring basis as of March 31, 2011 and December 31, 2010, and indicate the fair value hierarchy of the valuation techniques utilized by the Company to determine the fair value:

|                              | <b>March 31, 2011</b> |                |                |                |
|------------------------------|-----------------------|----------------|----------------|----------------|
|                              | <b>Total</b>          | <b>Level 1</b> | <b>Level 2</b> | <b>Level 3</b> |
| Loan investments             | \$ 144,666            | \$             | \$             | \$ 144,666     |
| Equity investments           | \$ 2,095              | \$ 1,427       | \$             | \$ 668         |
| Warrant investments          | \$ 6,455              | \$             | \$ 1,047       | \$ 5,408       |
| Interest rate swap liability | \$ 180                | \$             | \$ 180         | \$             |

  

|                              | <b>December 31, 2010</b> |                |                |                |
|------------------------------|--------------------------|----------------|----------------|----------------|
|                              | <b>Total</b>             | <b>Level 1</b> | <b>Level 2</b> | <b>Level 3</b> |
| Loan investments             | \$ 130,234               | \$             | \$             | \$ 130,234     |
| Equity investments           | \$ 351                   | \$ 209         | \$             | \$ 142         |
| Warrant investments          | \$ 6,225                 | \$             | \$ 1,976       | \$ 4,249       |
| Interest rate swap liability | \$ 258                   | \$             | \$ 258         | \$             |



**Horizon Technology Finance Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
(In thousands, except shares and per share data)

The following tables show a reconciliation of the beginning and ending balances for Level 3 assets for the three months ended March 31, 2011 and 2010:

|   | <b>Three months ended March 31, 2011</b> |                                |                               | <b>Total</b> |
|---|--|--------------------------------|-------------------------------|--------------|
|   | <b>Loan<br/>Investments</b>              | <b>Warrant<br/>Investments</b> | <b>Equity<br/>Investments</b> |              |
| Level 3 assets, beginning of period                         | \$ 130,234                               | \$ 4,249                       | \$ 142                        | \$ 134,625   |
| Purchase of investments                                     | 26,063                                   |                                |                               | 26,063       |
| Warrants and equity received and classified as Level 3      |  | 306                            | 482                           | 788          |
| Principal payments received on investments                  | (11,106)                                 |                                |                               | (11,106)     |
| Unrealized (depreciation) appreciation included in earnings | (12)                                     | 853                            | 44                            | 884          |
| Other   | (513)                                    |                                |                               | (513)        |
| Level 3 assets, end of period                               | \$ 144,666                               | \$ 5,408                       | \$ 668                        | \$ 150,741   |

|  | <b>The three months<br/>ended<br/>March 31, 2010</b> |       |
|--|--|-------|
| Level 3 assets, beginning of period          | \$   | 2,010 |
| Warrants received and classified as Level 3  |  | 276   |
| Unrealized depreciation included in earnings |  | (63)  |
| Level 3 assets, end of period                | \$   | 2,223 |

The total change in unrealized appreciation included in the statement of operations attributable to Level 3 investments still held at March 31, 2011 includes \$12 depreciation on loans, \$888 appreciation on warrants and \$44 appreciation on equity.

The Company discloses fair value information about financial instruments, whether or not recognized in the statement of assets and liabilities, for which it is practicable to estimate that value. Certain financial instruments are excluded from the disclosure requirements. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of the Company.

The fair value amounts have been measured as of the reporting date, and have not been reevaluated or updated for purposes of these financial statements subsequent to that date. As such, the fair values of these financial instruments subsequent to the reporting date may be different than amounts reported at year-end.

As of March 31, 2011 and December 31, 2010, the recorded book balances and fair values of the Company's financial instruments were as follows:

|                         | <b>March 31, 2011</b>                |                   | <b>December 31, 2010</b>             |                   |
|-------------------------|--------------------------------------|-------------------|--------------------------------------|-------------------|
|                         | <b>Recorded<br/>Book<br/>Balance</b> | <b>Fair Value</b> | <b>Recorded<br/>Book<br/>Balance</b> | <b>Fair Value</b> |
| Financial Assets:       |                                      |                   |                                      |                   |
| Cash & cash equivalents | \$ 69,503                            | \$ 69,503         | \$ 76,793                            | \$ 76,793         |

## Investments:

|                              |            |            |            |            |
|------------------------------|------------|------------|------------|------------|
| Debt                         | \$ 144,666 | \$ 144,666 | \$ 130,234 | \$ 130,234 |
| Warrants                     | \$ 6,455   | \$ 6,455   | \$ 6,225   | \$ 6,225   |
| Equity                       | \$ 2,095   | \$ 2,095   | \$ 351     | \$ 351     |
| Interest receivable          | \$ 2,281   | \$ 2,281   | \$ 1,938   | \$ 1,938   |
| Financial Liabilities:       |            |            |            |            |
| Borrowings                   | \$ 92,712  | \$ 92,712  | \$ 87,425  | \$ 87,425  |
| Interest rate swap liability | \$ 180     | \$ 180     | \$ 258     | \$ 258     |

***Off-balance-sheet instruments***

The Company assumes interest rate risk (the risk that general interest rate levels will change) as a result of its normal operations. As a result, the fair values of the Company's financial instruments will change when interest rate levels change and that change may be either favorable or unfavorable to the Company. Management attempts to match maturities of assets and liabilities to the extent believed necessary to minimize interest rate risk. Management monitors rates and maturities of assets and liabilities and attempts to

**Horizon Technology Finance Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**(In thousands, except shares and per share data)**

minimize interest rate risk by adjusting terms of new loans and by investing in securities with terms that mitigate the Company's overall interest rate risk.

**Note 6. Borrowings**

In accordance with the 1940 Act, with certain limited exceptions, the Company is only allowed to borrow amounts such that the asset coverage, as defined in the 1940 Act, is at least 200% after such borrowings. As of March 31, 2011, the asset coverage for borrowed amounts was 238%.

The Company entered into a Revolving Credit Facility (the Credit Facility) with WestLB, AG, New York Branch (WestLB) effective March 4, 2008. The Credit Facility had a three year initial revolving term and on March 3, 2011 the revolving term ended. The balance at the time the revolving term ended, which is the same as the balance as of March 31, 2011 of \$92,712 will be amortized based on loan investment payments received through March 3, 2015. The interest rate is based upon the one-month LIBOR plus a spread of 2.50%. The rates at March 31, 2011 and December 31, 2010 were 2.74% and 2.76%, respectively, and the average rates for the three months ended March 31, 2011 and 2010 were 2.78%, and 2.65%, respectively.

The Credit Facility is collateralized by all loans and warrants held by Credit I, the Company's subsidiary, and permits an advance rate of up to 75% of eligible loans held by Credit I. The Credit Facility contains covenants that, among other things, require the Company to maintain a minimum net worth and to restrict the loans securing the Credit Facility to certain criteria for qualified loans, and includes portfolio company concentration limits as defined in the related loan agreement. The average amounts of borrowings were approximately \$85,000 and \$67,000 for the three months ended March 31, 2011 and 2010, respectively. At March 31, 2011 and December 31, 2010, the Company had actual borrowings outstanding of \$92,712 and \$87,425, respectively, on the Credit Facility.

**Note 7. Financial Instruments with Off-Balance-Sheet Risk**

In the normal course of business, the Company is party to financial instruments with off-balance-sheet risk to meet the financing needs of its borrowers. These financial instruments include commitments to extend credit and involve, to varying degrees, elements of credit risk in excess of the amount recognized in the consolidated balance sheet. The Company attempts to limit its credit risk by conducting extensive due diligence and obtaining collateral where appropriate.

The balance of unfunded commitments to extend credit was approximately \$48,200 and \$26,500 as of March 31, 2011 and December 31, 2010, respectively. Commitments to extend credit consist principally of the unused portions of commitments that obligate the Company to extend credit, such as revolving credit arrangements or similar transactions. Commitments may also include a financial or non-financial milestone that has to be achieved before the commitment can be drawn. Commitments generally have fixed expiration dates or other termination clauses. Since commitments may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

**Note 8. Concentrations of Credit Risk**

The Company's loan portfolio consists primarily of loans to development-stage companies at various stages of development in the technology, life science, healthcare information and services and cleantech industries. Many of these companies may have relatively limited operating histories and also may experience variation in operating results. Many of these companies conduct business in regulated industries and could be affected by changes in government regulations. Most of the Company's borrowers will need additional capital to satisfy their continuing working capital needs and other requirements, and in many instances, to service the interest and principal payments on the loans.

The largest loans may vary from year to year as new loans are recorded and repaid. The Company's five largest loans represented approximately 28% and 31% of total loans outstanding as of March 31, 2011 and December 31, 2010, respectively. No single loan represents more than 10% of the total loans as of March 31, 2011 and December 31, 2010. Loan income, consisting of interest and fees, can fluctuate significantly upon repayment of large loans. Interest income from the five largest loans accounted for approximately 31% and 18% of total loan interest and

fee income for the three months ended March 31, 2011 and March 31, 2010, respectively.



**Horizon Technology Finance Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
(In thousands, except shares and per share data)

**Note 9: Interest Rate Swaps and Hedging Activities**

On October 14, 2008, the Company entered into two interest rate swap agreements (collectively, the Swap ) with WestLB, fixing the rate of \$10 million at 3.58% and \$15 million at 3.20% on the first advances of a like amount of variable rate Credit Facility borrowings. The \$15 million interest rate swap expired in October 2010 and the \$10 million interest rate swap will expire in October 2011. The objective of the Swap was to hedge the risk of changes in cash flows associated with the future interest payments on the first \$25 million of the variable rate Credit Facility debt with a combined notional amount of \$25 million.

During the three months ended March 31, 2011, approximately \$77 of net unrealized appreciation from the Swap was recorded in the statement of operations, and approximately \$83 of net realized losses from the Swap was recorded in the statement of operations.

Prior to the Company's election to become a BDC, the Swap was designated as a hedging instrument and the Company applied cash flow hedge accounting. The Swap was recorded in the statement of assets and liabilities at fair value, and any related increases or decreases in the fair value were recognized within accumulated other comprehensive income.

Prior to the Company's election to become a BDC, the Company assessed the effectiveness of the Swap on a quarterly basis. The Company had considered the impact of the current credit crisis in the United States in assessing the risk of counterparty default. As most of the critical terms of the hedging instruments and hedged items matched, the hedging relationship was considered to be highly effective. No ineffectiveness on the Swap was recognized during the three months ended March 31, 2010.

**Note 10: Subsequent Events**

On May 10, 2011, the Company declared a first quarter dividend of \$0.33 per share, payable on May 26, 2011 to stockholders of record on May 19, 2011.

**Note 11: Financial Highlights**

The financial highlights for the Company are as follows:(1)

|  | <b>Three months<br/>ended<br/>March 31, 2011</b> |
|--|--|
| <b>Per share data:</b>                               |  |
| Net asset value at beginning of period               | \$ 16.75   |
| Net investment income                                | 0.29   |
| Realized gain on investments                         | 0.03   |
| Net change in unrealized appreciation on investments | 0.16   |
| <b>Net asset value at end of period</b>              | <b>\$ 17.23</b>                                  |
| Per share market value, end of period                | \$ 16.07   |
| Total return based on average net asset value        | 11.2%  |
| Shares outstanding at end of period                  | 7,593,421  |
| Ratios to average net assets:                        |  |
| Expenses without incentive fees                      | 8.4%(3)  |
| Incentive fees                                       | 1.6%(3)  |
| Total expenses                                       | 10.0%(3)   |
| Net investment income without incentive fees         | 8.5%(3)  |
| Average net asset value                              | \$ 129,008                                       |

- (1) Periods prior to becoming a public company are not presented in the financial highlights because the Company did not record assets at fair value, therefore the information would not be meaningful.
- (2) Per share data is not provided as the Company did not have shares of common stock outstanding or an equivalent prior to the IPO on October 28, 2010.
- (3) Annualized.

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

In this section, except where the context suggests otherwise, the terms *we*, *us*, *our* and *Horizon Technology Finance* refer to *Horizon Technology Finance Corporation and its consolidated subsidiaries*. The information contained in this section should be read in conjunction with our consolidated financial statements and related notes thereto appearing elsewhere in this quarterly report on Form 10-Q. For periods prior to October 28, 2010, the consolidated financial statements and related footnotes reflect the performance of our predecessor, *Compass Horizon Funding Company LLC*, and its wholly owned subsidiary, *Horizon Credit I LLC*, both of which were formed in January 2008 and commenced operations in March 2008. Amounts are stated in thousands, except shares and per share data and where otherwise noted.

**Overview**

We are a specialty finance company that lends to and invests in development-stage companies in the technology, life science, healthcare information and services, and cleantech industries, which we refer to as our *Target Industries*. Our investment objective is to generate current income from the loans we make and capital appreciation from the warrants we receive when making such loans. We make secured loans, which we refer to as *Technology Loans*, to companies backed by established venture capital and private equity firms in our *Target Industries*, which we refer to as *Technology Lending*. We also selectively lend to publicly traded companies in our *Target Industries*.

We are an externally managed, closed-end, non-diversified management investment company that has elected to be regulated as a business development company under the Investment Company Act of 1940, or the 1940 Act. As a business development company, we are required to comply with regulatory requirements, including limitations on our use of debt. We are permitted to, and expect to, finance our investments through borrowings. However, as a business development company, we are only generally allowed to borrow amounts such that our asset coverage, as defined in the 1940 Act, equals at least 200% after such borrowing. The amount of leverage that we employ will depend on our assessment of market conditions and other factors at the time of any proposed borrowing.

Compass Horizon Funding Company LLC, which we refer to as *Compass Horizon*, our predecessor company, commenced operations in March 2008. We were formed in March 2010 for the purpose of acquiring *Compass Horizon* and continuing its business as a public entity. On October 28, 2010, we and certain selling stockholders completed an initial public offering and sold 6,250,000 shares of our common stock at a public offering price of \$16.00 per share. Our shares are listed on The NASDAQ Global Market under the symbol *HRZN*.

**Portfolio Composition and Investment Activity**

As of March 31, 2011 and December 31, 2010, our loan portfolio consisted of 34 and 32 loans, respectively, which had an aggregate fair value of \$144.7 million and \$130.2 million, respectively. Our warrant portfolio had an aggregate fair value of \$6.5 million and \$6.2 million at March 31, 2011 and December 31, 2010, respectively.

The following table shows our portfolio by asset class as of March 31, 2011 and December 31, 2010.

|                            | March 31, 2011   |            |   | December 31, 2010 |            |                      |
|----------------------------|------------------|------------|---|-------------------|------------|----------------------|
|                            | # of Investments | Fair Value | % of Total Portfolio<br>(\$ in thousands) | # of Investments  | Fair Value | % of Total Portfolio |
| Secured term loans         | 33               | \$ 142,704 | 93.1%                                     | 31                | \$ 127,949 | 93.5%                |
| Equipment loans            | 1                | 1,962      | 1.3%                                      | 1                 | 2,285      | 1.6%                 |
| Total loans                | 34               | 144,666    | 94.4%                                     | 32                | 130,234    | 95.1%                |
| Warrants to purchase stock | 45               | 6,455      | 4.2%                                      | 43                | 6,225      | 4.6%                 |
| Equity                     | 4                | 2,095      | 1.4%                                      | 2                 | 351        | 0.3%                 |
| Total                      |                  | \$ 153,216 | 100.0%                                    |                   | \$ 136,810 | 100.0%               |



Total portfolio investment activity for the periods ended March 31, 2011 and 2010 was as follows:

|  | <b>For the<br/>three<br/>Months<br/>ended<br/>March<br/>31, 2011</b> | <b>For the three<br/>Months ended<br/>March 31,<br/>2010</b> |
|--|--|--|
|  | (\$ in thousands)  |  |
| Beginning portfolio                                  | \$ 136,810   | \$ 113,878   |
| New loan funding                                     | 28,833   | 13,100   |
| Less refinanced balances                             | (2,770)  | (1,075)  |
| Net new loan funding                                 | 26,063   | 12,025   |
| Principal and stock payments received on investments | (7,759)  | (8,289)  |
| Early pay-offs                                       | (3,347)  |  |
| Accretion of loan fees                               | 395  | 201  |
| New loan fees  | (513)  | (95)   |
| New equity investments                               | 577  |  |
| Net appreciation on investments                      | 990  | 201  |
| Ending portfolio                                     | \$ 153,216   | \$ 117,921   |

We receive payments in our loan portfolio based on scheduled amortization of the outstanding balances. In addition, we receive repayments of some of our loans prior to their scheduled maturity date. The frequency or volume of these repayments may fluctuate significantly from period to period.

The following table shows our debt investments by industry sector as of March 31, 2011 and December 31, 2010:

|                                     | <b>March 31, 2011</b>              |  | <b>December 31, 2010</b>           |  |
|-------------------------------------|------------------------------------|--|------------------------------------|--|
|                                     | <b>Loans at<br/>Fair<br/>Value</b> | <b>Percentage<br/>of Total<br/>Portfolio</b> | <b>Loans at<br/>Fair<br/>Value</b> | <b>Percentage<br/>of Total<br/>Portfolio</b> |
|                                     | (\$ in thousands)                  |  |                                    |  |
| Life Science                        |                                    |  |                                    |  |
| Biotechnology                       | \$ 33,941                          | 23.5%  | \$ 30,470                          | 23.4%  |
| Medical Device                      | 21,261                             | 14.7%  | 19,572                             | 15.0%  |
| Technology                          |                                    |  |                                    |  |
| Consumer-related Technologies       | 3,817                              | 2.6%   | 4,460                              | 3.4%   |
| Networking                          | 1,962                              | 1.4%   | 2,285                              | 1.8%   |
| Software                            | 13,968                             | 9.7%   | 8,745                              | 6.7%   |
| Data Storage                        | 7,421                              | 5.1%   | 7,912                              | 6.1%   |
| Communications                      | 6,566                              | 4.5%   | 7,591                              | 5.9%   |
| Cleantech                           |                                    |  |                                    |  |
| Energy Efficiency                   | 21,867                             | 15.1%  | 16,570                             | 12.7%  |
| Waste Recycling                     | 4,851                              | 3.4%   | 2,363                              | 1.8%   |
| Healthcare Information and Services |                                    |  |                                    |  |
| Diagnostics                         | 19,540                             | 13.5%  | 20,472                             | 14.5%  |
|                                     | 9,472                              | 6.5%   | 9,794                              | 7.5%   |

## Other Healthcare Related Services and Technologies

|       |            |        |            |        |
|-------|------------|--------|------------|--------|
| Total | \$ 144,666 | 100.0% | \$ 130,234 | 100.0% |
|-------|------------|--------|------------|--------|

The largest loans may vary from year to year as new loans are recorded and repaid. Our five largest loans represented approximately 28% and 31% of total loans outstanding as of March 31, 2011 and December 31, 2010, respectively. No single loan represented more than 10% of our total loans as of March 31, 2011 and December 31, 2010.

As of March 31, 2011 and December 31, 2010, interest receivable was \$2.3 million and \$1.9 million, respectively, which represents one month of accrued interest income on our loans. The increase in 2011 was due to a larger loan portfolio relative to 2010.

**Loan Portfolio Asset Quality**

We use a credit rating system which rates each loan on a scale of 4 to 1, with 4 being the highest credit quality rating and 3 being the rating for a standard level of risk. A rating of 2 or 1 represents a deteriorating credit quality and increased risk. The following table shows the classification of our loan portfolio by credit rating as of March 31, 2011 and December 31, 2010:

| Credit Rating | March 31, 2011                        |                              | December 31, 2010                     |                              |
|---------------|---------------------------------------|------------------------------|---------------------------------------|------------------------------|
|               | Loans at Fair Value (\$ in thousands) | Percentage of Loan Portfolio | Loans at Fair Value (\$ in thousands) | Percentage of Loan Portfolio |
| 4             | \$ 26,149                             | 18.1%                        | \$ 29,054                             | 22.3%                        |
| 3             | 115,256                               | 79.7%                        | \$ 94,200                             | 72.3%                        |
| 2             | 3,261                                 | 2.2%                         | \$ 6,980                              | 5.4%                         |
| 1             |                                       |                              |                                       |                              |
| Total         | \$ 144,666                            | 100.0%                       | \$ 130,234                            | 100.0%                       |

As of both March 31, 2011 and December 31, 2010, our loan portfolio had a weighted average credit rating of 3.2. As of March 31, 2011 and December 31, 2010, no investments were on non-accrual status.

**Consolidated Results of Operations**

The consolidated results of operations set forth below include historical financial information of our predecessor, Compass Horizon, prior to our election to become a business development company and our election to be treated as a RIC. As a business development company and a RIC for U.S. federal income tax purposes, we are also subject to certain constraints on our operations, including limitations imposed by the 1940 Act and the Code. Also, the management fee that we pay to our Advisor under the Investment Management Agreement is determined by reference to a formula that differs materially from the management fee paid by Compass Horizon in prior periods. For these and other reasons, the results of operations described below may not be indicative of the results we report in future periods.

Consolidated operating results for the three months ended March 31, 2011 and 2010 are as follows:

|   | <b>For the three months ended<br/>March,</b> |             |
|---|--|-------------|
|   | <b>2011</b>                                  | <b>2010</b> |
|   | <b>(\$ in thousands)</b>                     |             |
| Total investment income                 | \$ 5,460                                     | \$ 3,793    |
| Total expenses                          | 3,232  | 1,680       |
| Net investment income                   | 2,228  | 2,113       |
| Net realized gains                      | 206  |             |
| Net unrealized appreciation             | 1,194  | 202         |
| Credit for loan losses                  |  | 303         |
| Net income                              | \$ 3,628                                     | \$ 2,618    |
| Average debt investments, at fair value | \$ 140,216                                   | \$ 111,354  |
| Average borrowings outstanding          | \$ 85,075                                    | \$ 66,932   |

Net income can vary substantially from period to period for various reasons, including the recognition of realized gains and losses and unrealized appreciation and depreciation. As a result, quarterly comparisons of net income may not be meaningful.

**Investment Income**

Investment income increased by \$1.7 million, or 44.0%, for the three months ended March 31, 2011 as compared to the three months ended March 31, 2010. For the three months ended March 31, 2011, total investment income consisted primarily of \$4.9 million in interest income from investments, which included \$0.4 million in income from the amortization of discounts and origination fees on investments. Interest income on investments and other investment income increased primarily due to the increased average size of the loan portfolio. Other investment income was primarily comprised of a one-time success fee received upon the completion of an acquisition of one of our portfolio companies. For the three months ended March 31, 2010, total investment income consisted primarily of \$3.7 million in interest income from investments, which included \$0.3 million in income from the amortization of discounts and origination fees on investments.

For the three months ended March 31, 2011 and 2010, our dollar-weighted average annualized yield on average loans was approximately 15.4% and 13.6%, respectively. We compute the yield on average loans as (i) total investment interest and other investment income divided by (ii) average gross loans receivable. We used month end loan balances during the period to compute average loans receivable.

Investment income, consisting of interest income and fees on loans, can fluctuate significantly upon repayment of large loans. Interest income from the five largest loans accounted for approximately 31% and 18% of investment income for the three months ended March 31, 2011 and 2010, respectively.





### ***Expenses***

Total expenses increased by \$1.6 million, or 92.4%, to \$3.2 million for the three months ended March 31, 2011 as compared to the three months ended March 31, 2010. Total operating expenses for each period consisted principally of management fees, incentive and administrative fees and interest expense and, to a lesser degree, professional fees and general and administrative expenses. Interest expense, which includes the amortization of debt issuance costs, decreased for the three months ended March 31, 2011 and 2010 primarily resulting from the expiration of fees associated with the revolving term of the Credit Facility ending and the change in classification to realized loss of our interest payments made on our swap agreement. This decrease was partially offset by a higher average outstanding balance on the Credit Facility.

Effective with the completion of our initial public offering in October 2010, we now pay management and incentive fees under the Investment Management Agreement, which provides a higher management fee base as compared to amounts previously paid by Compass Horizon. Management fee expense for the three months ended March 31, 2011 increased compared to the three months ended March 31, 2010 primarily due to the higher management fee base. Incentive fees for the three months ended March 31, 2011 totaled approximately \$529 compared to no incentives fees for the three months ended March 31, 2010.

In connection with the Administrative Agreement, we have incurred \$295 for the three months ended March 31, 2011. We did not pay an administrative servicing fee for the three months ended March 31, 2010.

Professional fees and general and administrative expenses include legal, accounting fees, insurance premiums, and miscellaneous other expenses. These expenses increased for the three months ended March 31, 2011 compared to the three months ended March 31, 2010 primarily from the increased cost of being a public company.

### ***Net Realized Gains and Net Unrealized Appreciation and Depreciation***

During the three months ended March 31, 2011, we had \$0.2 million in net realized gain on investments and we did not realize any gains during the three months ended March 31, 2010. During the same periods, we had \$1.2 million and \$0.2 million in unrealized appreciation on investments, respectively. Net realized gain on investments resulted from the sale of stock through the exercise of warrants in portfolio companies. For both periods, the net increase in unrealized appreciation on investments was primarily from our warrant and equity investments. Net unrealized appreciation on warrants and equity investments is the difference between the net changes in warrant and equity investments fair values from the prior determination date and the reversal of previously recorded unrealized appreciation or depreciation when gains or losses are realized. The increase in net unrealized appreciation on investments for three months ended March 31, 2011 and 2010 is primarily due to an increase in the enterprise value of a number of private companies for which we hold warrants and an increase in the share value of public company for which we hold warrants and common stock.

### ***Credit for Loan Losses***

For the three months ended March 31, 2010, the credit for loan losses was \$303. The loan portfolio had a weighted average credit rating of 3.1 as of March 31, 2010. See *Loan Portfolio Asset Quality*. As of the date of our election to be treated as a business development company on October 28, 2010, we no longer record a credit or provision for loan losses. We record each individual loan and investment on a quarterly basis at fair value. Changes in fair value are recorded through our statement of operations.

### ***Liquidity and Capital Resources***

As of March 31, 2011 and December 31, 2010, we had cash and cash equivalents of \$69.5 million and \$76.8 million, respectively. Cash and cash equivalents are available to fund new investments, pay operating expenses and pay dividends. To date, our primary sources of capital have been from our IPO, use of our Credit Facility and from the private placement for \$50 million of equity capital we completed on March 4, 2008.

The Credit Facility had a three year initial revolving term and on March 3, 2011 the revolving term ended. The balance as of March 31, 2011 of \$92,712 will be amortized based on loan investment payments received through March 3, 2015.

Our operating activities used cash of \$13 million for the three months ended March 31, 2011 and our financing activities provided net cash proceeds of \$5 million for the same period. Our operating activities used cash primarily for investing in portfolio companies. Such cash was provided primarily from proceeds from our initial public offering

and draws under the Credit Facility.

Our operating activities used cash of \$2 million for the three months ended March 31, 2010 and our financing activities provided net cash proceeds of \$11 million for the same period. Our operating activities used cash primarily for investing in portfolio companies that was provided primarily from our availability on our Credit Facility.

Our primary use of available funds will be investments in portfolio companies and cash distributions to holders of our common stock. After we have used our current capital resources, including the net proceeds from our initial public offering, we expect to opportunistically raise additional capital as needed, and subject to market conditions, to support our future growth through future equity offerings, issuances of senior securities and/or future borrowings, to the extent permitted by the 1940 Act. To the extent we determine to raise additional equity through an offering of our common stock at a price below net asset value, existing investors will experience dilution.

In order to satisfy the Code requirements applicable to a RIC, we intend to distribute to our stockholders all or substantially all of our income except for certain net capital gains. In addition, as a business development company, we generally will be required to meet a coverage ratio of 200%. This requirement will limit the amount that we may borrow.

We are currently seeking qualification as a small business investment company ( SBIC ) for Longview SBIC LP ( Longview SBIC ), a subsidiary, which will be licensed, leveraged and regulated by the U. S. Small Business Administration ( SBA ). The Company, on behalf of Longview SBIC, submitted an application to the SBA on December 6, 2010 for a license to operate as an SBIC (the SBIC Application ) and the SBA accepted the SBIC Application for processing on December 21, 2010. On April 21, 2011, the SBA advised us that it required additional information in order to process the SBIC Application and provided the Company up to 90 days to provide the information. During the period of time that the Company takes to provide the requested information the application process is suspended. We cannot be certain that the license to operate as an SBIC will be granted, and the failure to receive the license and SBA leverage could have a materially adverse impact on our business, results of operations and financial results.

If we receive approval to license an SBIC, we will have the ability to issue debentures guaranteed by the SBA at favorable interest rates. Under the Small Business Investment Act and the SBA rules applicable to SBICs, an SBIC can have outstanding at any time debentures guaranteed by the SBA generally in an amount up to twice its regulatory capital, which generally is the amount raised from private investors. The maximum statutory limit on the dollar amount of outstanding debentures guaranteed by the SBA issued by a single SBIC or group of SBICs under common control as of March 31, 2011, was \$150 million (which amount is subject to increase on an annual basis based on cost of living index increases).

#### ***Current Borrowings***

We, through our wholly owned subsidiary, Credit I, entered into the Credit Facility. Per this agreement, base rate borrowings bear interest at one-month LIBOR plus 2.50%. The rates were 2.74% and 2.76% as of March 31, 2011 and December 31, 2010, respectively.

We were able to request advances under the Credit Facility through March 4, 2011. We may not request new advances and we must repay the outstanding advances under the Credit Facility as of such date at such times and in such amounts as are necessary to maintain compliance with the terms and conditions of the Credit Facility, particularly the condition that the principal balance of the Credit Facility does not exceed seventy-five percent (75%) of the aggregate principal balance of our eligible loans to our portfolio companies. All outstanding advances under the Credit Facility are due and payable on March 4, 2015 ( Maturity Date ), unless such date is extended upon Credit I s request and upon mutual agreement of WestLB and Credit I.

The Credit Facility is collateralized by loans held by Credit I and permitted an advance rate of up to 75% of eligible loans. The Credit Facility contains certain customary affirmative and negative covenants, including covenants that restrict certain of our subsidiaries ability to make loans to, or investments in, third parties (other than technology loans and warrants or other equity participation rights), pay dividends and distributions, incur additional indebtedness and engage in mergers or consolidations. The Credit Facility also restricts certain of our subsidiaries and our Advisor s ability to create liens on the collateral securing the Credit Facility, permit additional negative pledges on such collateral and change the business currently conducted by them. The Credit Facility contains events of default, including upon the occurrence of a change of control, and contains certain financial covenants that among other

things, require Compass Horizon to maintain a minimum net worth, for the year 2010 and after, equal to the minimum net worth amount for 2009 plus 50% of Compass Horizon's cumulative positive net income for the year 2010 on and after December 31, 2010, and require our Advisor to maintain a minimum net worth, for the year 2010 and after, equal to the greater of (i) \$1 million or (ii) the 2009 minimum net worth amount plus 50% of the cumulative positive net income for each fiscal year. The Credit Facility also includes borrower concentration limits which include limitations on the amount of loans to companies in particular industries sectors and also restrict certain terms of the loans.

**Future Borrowings**

Our ability to make loans in the future is dependent upon our SBIC qualification, or if such approval is not granted in due course, our ability to arrange for a credit facility in the lending markets. We can give no assurances of either such event.

**Interest Rate Swaps and Hedging Activities**

In 2008, we entered into two interest rate swap agreements with WestLB, fixing the rate of \$10 million at 3.58% and \$15 million at 3.2% on the first advances of a like amount of variable rate Credit Facility borrowings. As of March 31, 2011, only the \$10 million interest rate swap was still outstanding and expires in October 2011.

**Contractual Obligations and Off-Balance Sheet Arrangements**

A summary of our significant contractual payment obligations as of March 31, 2011 is as follows:

| <b>Contractual Obligations</b> | <b>Total</b> | <b>Payments due by period</b> |              |              |                |
|--------------------------------|--------------|-------------------------------|--------------|--------------|----------------|
|                                |              | <b>(in thousands)</b>         |              |              |                |
|                                |              | <b>Less than 1</b>            | <b>1 - 3</b> | <b>3 - 5</b> | <b>After 5</b> |
|                                |              | <b>year</b>                   | <b>years</b> | <b>years</b> | <b>years</b>   |
| Borrowings                     | \$ 92,712    | \$ 30,761                     | \$ 61,951    | \$           | \$             |
| Unfunded commitments           | 48,200       | 41,700                        | 6,500        |              |                |
| Total contractual obligations  | \$ 139,912   | \$ 71,461                     | \$ 68,451    | \$           | \$             |

In the normal course of business, we are party to financial instruments with off-balance sheet risk. These consist primarily of unfunded commitments to extend credit, in the form of loans, to our portfolio companies. Unfunded commitments to provide funds to portfolio companies are not reflected on our balance sheet. Our unfunded commitments may be significant from time to time. As of March 31, 2011, we had unfunded commitments of approximately \$48.2 million. These commitments will be subject to the same underwriting and ongoing portfolio maintenance as are the on balance sheet financial instruments that we hold. Since these commitments may expire without being drawn upon, the total commitment amount does not necessarily represent future cash requirements.

In addition to the Credit Facility, we have certain commitments pursuant to our Investment Management Agreement entered into with our Advisor. We have agreed to pay a fee for investment advisory and management services consisting of two components – a base management fee and an incentive fee. Payments under the Investment Management Agreement are equal to (1) a base management fee equal to a percentage of the value of our average gross assets and (2) a two-part incentive fee. We have also entered into a contract with our Advisor to serve as our administrator. Payments under the Administration Agreement are equal to an amount based upon our allocable portion of our Advisor's overhead in performing its obligation under the agreement, including rent, fees, and other expenses inclusive of our allocable portion of the compensation of our chief financial officer and any administrative staff. See Note 3 to our Consolidated Financial Statements for additional information regarding our Investment Management Agreement and our Administration Agreement.

**Distributions**

In order to qualify as a RIC and to avoid corporate level tax on the income we distribute to our stockholders, we are required under the Code to distribute at least 90% of our net ordinary income and net short-term capital gains in excess of net long-term capital losses, if any, to our net stockholders on an annual basis. Additionally, we must distribute at least 98% of our ordinary income and 98% (or, for our taxable years beginning in 2011, 98.2%) of our capital gain net income on an annual basis and any net ordinary income and net capital gains for preceding years that were not distributed during such years and on which we previously paid no U.S. federal income tax to avoid a U.S. federal excise tax. We intend to distribute quarterly dividends to our stockholders as determined by our Board.

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 our distributions from time to time. In addition, we may be limited in our ability to make distributions due to the asset coverage requirements applicable to us as a business development company under the 1940 Act. If we do not distribute a certain percentage of our income annually, we will suffer adverse tax

consequences, including the possible loss of our qualification as a RIC. We cannot assure stockholders that they will receive any distributions.

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 U.S. federal income tax purposes. Thus, the source of a distribution to our stockholders may be the original capital invested by the stockholder rather than our income or gains. Stockholders should read any written disclosure accompanying a dividend payment carefully and should not assume that the source of any distribution is our ordinary income or gains.

We have adopted an "opt out" dividend reinvestment plan for our common stockholders. As a result, if we declare a distribution, then stockholders' cash distributions will be automatically reinvested in additional shares of our common stock unless a stockholder specifically "opts out" of our dividend reinvestment plan. If a stockholder opts out, that stockholder will receive cash distributions. Although distributions paid in the form of additional shares of our common stock will generally be subject to U.S. federal, state and local taxes in the same manner as cash distributions, stockholders participating in our dividend reinvestment plan will not receive any corresponding cash distributions with which to pay any such applicable taxes.

### **Critical Accounting Policies**

The discussion of our financial condition and results of operation is based upon our financial statements, which have been prepared in accordance with U.S. generally accepted accounting principles, or GAAP. The preparation of these consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Changes in the economic environment, financial markets and any other parameters used in determining such estimates could cause actual results to differ. In addition to the discussion below, we describe our significant accounting policies in the notes to our consolidated financial statements.

We have identified the following items as critical accounting policies.

#### ***Valuation of Investments***

Investments are recorded at fair value. Our board of directors ( "Board" ) determines the fair value of our portfolio investments. Prior to our election to become a BDC, loan investments were stated at current unpaid principal balances adjusted for the allowance for loan losses, unearned income and any unamortized deferred fees or costs.

We apply fair value to substantially all of our investments in accordance with relevant GAAP, which establishes a framework used to measure fair value and requires disclosures for fair value measurements. We have categorized our investments carried at fair value, based on the priority of the valuation technique, into a three-level fair value hierarchy. Fair value is a market-based measure considered from the perspective of the market participant who holds the financial instrument rather than an entity specific measure. Therefore, when market assumptions are not readily available, our own assumptions are set to reflect those that management believes market participants would use in pricing the financial instrument at the measurement date.

The availability of observable inputs can vary depending on the financial instrument and is affected by a wide variety of factors, including, for example, the type of product, whether the product is new, whether the product is traded on an active exchange or in the secondary market and the current market conditions. To the extent that the valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires more judgment. The three categories within the hierarchy are as follows:

**Level 1** Quoted prices in active markets for identical assets and liabilities.

**Level 2** Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities in active markets, quoted prices in markets that are not active and model-based valuation techniques for which all significant inputs are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

**Level 3** Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

See Note 5 Fair Value to the Consolidated Financial Statements for further information regarding fair value.



### ***Income Recognition***

Interest on loan investments is accrued and included in income based on contractual rates applied to principal amounts outstanding. Interest income is determined using a method that results in a level rate of return on principal amounts outstanding. When a loan becomes 90 days or more past due, or if we otherwise do not expect to receive interest and principal repayments, the loan is placed on non-accrual status and the recognition of interest income is discontinued. Interest payments received on loans that are on non-accrual status are treated as reductions of principal until the principal is repaid. No loans were on non-accrual status as of March 31, 2011 and December 31, 2010.

We receive a variety of fees from borrowers in the ordinary course of conducting our business, including advisory fees, commitment fees, amendment fees, non-utilization fees and prepayment fees (collectively, the Fees). In a limited number of cases, we may also receive a non-refundable deposit earned upon the termination of a transaction. Loan origination fees, net of certain direct origination costs, are deferred, and along with unearned income, are amortized as a level yield adjustment over the respective term of the loan. Fees for counterparty loan commitments with multiple loans are allocated to each loan based upon each loan's relative fair value. When a loan is placed on non-accrual status, the amortization of the related fees and unearned income is discontinued until the loan is returned to accrual status.

Certain loan agreements also require the borrower to make an end-of-term payment that is accrued into income over the life of the loan to the extent such amounts are expected to be collected. We will generally cease accruing the income if there is insufficient value to support the accrual or if we do not expect the borrower to be able to pay all principal and interest due.

In connection with substantially all lending arrangements, we receive warrants to purchase shares of stock from the borrower. The warrants are recorded as assets at estimated fair value on the grant date using the Black-Scholes valuation model. The warrants are considered loan fees and are also recorded as unearned loan income on the grant date. The unearned income is recognized as interest income over the contractual life of the related loan in accordance with our income recognition policy. Subsequent to loan origination, the warrants are also measured at fair value using the Black-Scholes valuation model. Any adjustment to fair value is recorded through earnings as net unrealized gain or loss on warrants. Gains from the disposition of the warrants or stock acquired from the exercise of warrants are recognized as realized gains on warrants.

### ***Allowance for Loan Losses***

Prior to our election to become a BDC, the allowance for loan losses represented management's estimate of probable loan losses inherent in the loan portfolio as of the balance sheet date. The estimation of the allowance was based on a variety of factors, including past loan loss experience, the current credit profile of our borrowers, adverse situations that had occurred that may affect individual borrowers' ability to repay, the estimated value of underlying collateral and general economic conditions. The loan portfolio is comprised of large balance loans that are evaluated individually for impairment and are risk-rated based upon a borrower's individual situation, current economic conditions, collateral and industry-specific information that management believes is relevant in determining the potential occurrence of a loss event and in measuring impairment. The allowance for loan losses was sensitive to the risk rating assigned to each of the loans and to corresponding qualitative loss factors that we used to estimate the allowance. Those factors were applied to the outstanding loan balances in estimating the allowance for loan losses. If necessary, based on performance factors related to specific loans, specific allowances for loan losses were established for individual impaired loans. Increases or decreases to the allowance for loan losses were charged or credited to current period earnings through the provision (credit) for loan losses. Amounts determined to be uncollectible were charged against the allowance for loan losses, while amounts recovered on previously charged-off loans increased the allowance for loan losses.

A loan was considered impaired when, based on current information and events, it was probable that we were unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment included payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experienced insignificant payment delays and payment shortfalls generally were not classified as impaired. Management determined the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the

reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed. Impairment was measured on a loan by loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's observable market price or the fair value of the collateral, if the loan was collateral dependent.

Impaired loans also included loans modified in troubled debt restructurings where concessions had been granted to borrowers experiencing financial difficulties. These concessions could include a reduction in the interest rate on the loan, payment extensions, forgiveness of principal, forbearance or other actions intended to maximize collection.

#### ***Income taxes***

We have elected to be treated as a RIC under subchapter M of the Code and to operate in a manner so as to qualify for the tax treatment applicable to RICs. In order to qualify as a RIC, among other things, we are required to meet certain source of income and asset diversification requirements and we must timely distribute to our stockholders at least 90% of investment company taxable income, as defined by the Code, for each year. We, among other things, have made and intend to continue to make the requisite distributions to our stockholders, which will generally relieve us from U.S. federal income taxes.

Depending on the level of taxable income earned in a tax year, we may choose to carry forward taxable income in excess of current year dividend distributions into the next tax year and pay a 4% excise tax on such income, as required. To the extent that we determine that our estimated current year annual taxable income will be in excess of estimated current year dividend distributions, we will accrue excise tax, if any, on estimated excess taxable income as taxable income is earned. For the three months ended March 31, 2011 no amount was recorded for U.S. federal excise tax.

We evaluate tax positions taken in the course of preparing our tax returns to determine whether the tax positions are more-likely-than-not to be sustained by the applicable tax authority. Tax benefits of positions not deemed to meet the more-likely-than-not threshold, or uncertain tax positions, would be recorded as a tax expense in the current year. It is our policy to recognize accrued interest and penalties related to uncertain tax benefits in income tax expense. There were no material uncertain tax positions at March 31, 2011 and December 31, 2010.

Prior to our election to become a BDC, we were a limited liability company treated as a partnership for U.S. federal income tax purposes and, as a result, all items of income and expense were passed through to, and are generally reportable on, the tax returns of the respective members of the limited liability company. Therefore, no federal or state income tax provision has been recorded for the three months ended March 31, 2010.

#### **Recently Issued Accounting Standards**

In January 2010, the FASB issued Accounting Standards Update 2010-06, Fair Value Measurements and Disclosure—Improving Disclosures about Fair Value Measurements, which amends the existing guidance related to fair value measurements and disclosures. The amendments require the following new fair value disclosures:

Separate disclosure of the significant transfers in and out of Level 1 and Level 2 fair value measurements, and a description of the reasons for the transfers.

In the roll forward of activity for Level 3 fair value measurements (significant unobservable inputs), purchases, sales, issuances and settlements should be presented separately (on a gross basis rather than as one net number).

In addition, the amendments clarify existing disclosure requirements, as follows:

Fair value measurements and disclosures should be presented for each class of assets and liabilities within a line item in the balance sheet.

Reporting entities should provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements that fall in either Level 2 or Level 3.

The new disclosures and clarifications of existing disclosures were effective for our interim and annual reporting periods during the year ended December 31, 2010, except for the disclosures included in the roll forward of activity for Level 3 fair value measurements, for which the effective date was the three months ended March 31, 2011.

**Item 3: Quantitative and Qualitative Disclosures About Market Risk.**

We are subject to financial market risks, including changes in interest rates. During the periods covered by our financial statements, the interest rates on the loans within our portfolio were all at fixed rates and we expect that our loans in the future will also have primarily fixed interest rates. The initial commitments to lend to our portfolio companies are usually based on a floating LIBOR index and typically have interest rates that are fixed at the time of the loan funding and remain fixed for the term of the loan.

Assuming that the balance sheet as of March 31, 2011 was to remain constant and no actions were taken to alter the existing interest rate sensitivity, a hypothetical immediate 1% change in interest rates may affect net income by more than 1% over a one-year horizon. Although management believes that this measure is indicative of our sensitivity to interest rate changes, it does not adjust for potential changes in the credit market, credit quality, size and composition of the assets on the balance sheet and other business developments that could affect net increase in net assets resulting from operations, or net income. Accordingly, no assurances can be given that actual results would not differ materially from the statement above.

Our Credit Facility has a floating interest rate provision based on a LIBOR index which resets daily, and we expect that, other than any SBIC debenture program debt, any other credit facilities into which we enter in the future may have floating interest rate provisions. We have used hedging instruments in the past to protect us against interest rate fluctuations and we may use them in the future. Such instruments may include swaps, futures, options and forward contracts. While hedging activities may insulate us against adverse changes in interest rates, they may also limit our ability to participate in the benefits of lower interest rates with respect to the investments in our portfolio with fixed interest rates.

Because we currently fund, and will continue to fund, our investments with borrowings, our net income is dependent upon the difference between the rate at which we borrow funds and the rate at which we invest the funds borrowed. Accordingly, there can be no assurance that a significant change in market interest rates will not have a material adverse effect on our net income. In periods of rising interest rates, our cost of funds would increase, which could reduce our net investment income if there is not a corresponding increase in interest income generated by floating rate assets in our investment portfolio.

**Item 4: Controls and Procedures.**

***(a) Evaluation of Disclosure Controls and Procedures***

As of March 31, 2011, we, including our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) of the Exchange Act). Based on that evaluation, our management, including the Chief Executive Officer and Chief Financial Officer, concluded that our disclosure controls and procedures were effective and provided reasonable assurance that information required to be disclosed in our periodic SEC filings is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. However, in evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of such possible controls and procedures.

***(b) Changes in Internal Controls Over Financial Reporting.***

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

**Part II Other Information**

**Item 1: Legal Proceedings.**

Although we may, from time to time, be involved in litigation arising out of our operations in the normal course of business or otherwise, we are currently not a party to any pending material legal proceedings.

**Item 1A: Risk Factors.**

In addition to other information set forth in this report, you should carefully consider the Risk Factors discussed in our Annual Report on Form 10-K for the year ended December 31, 2010, which could materially affect our business, financial condition and/or operating results. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially affect our business, financial condition and/or operating results. There have been no material changes during the three months ended March 31, 2011 to the risk factors discussed in Item 1A. Risk Factors in our annual report on Form 10-K for the year ended December 31, 2010.

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

None.

**Item 3: Defaults Upon Senior Securities.**

None.

**Item 4: Removed and Reserved.**

**Item 5: Other Information.**

None.

**Item 6: Exhibits.**

**EXHIBIT INDEX**

**Number Description**

- |      |  |
|------|--|
| 31.1 | Certifications by Chief Executive Officer pursuant to Exchange Act Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002* |
| 31.2 | Certifications by Chief Financial Officer pursuant to Exchange Act Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002* |
| 32.1 | Certification of the 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 the Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002*   |

\* - Filed herewith

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this Quarterly Report on Form 10-Q to be signed on its behalf by the undersigned, thereunto duly authorized.

Horizon Technology Finance Corporation

Date: May 11, 2011

By: /s/ Robert D. Pomeroy, Jr.  
Name: Robert D. Pomeroy, Jr.  
Title: Chief Executive Officer and  
Chairman of the Board

Date: May 11, 2011

By: /s/ Christopher M. Mathieu  
Name: Christopher M. Mathieu  
Title: Chief Financial Officer and  
Treasurer