RAND CAPITAL CORP
Form 10-K
March 26, 2009

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

FORM 10-K

þ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended December 31, 2008
o **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: 814-00235

Rand Capital Corporation
(Exact Name of Registrant as specified in its Charter)

New York	**16-0961359**
(State or Other Jurisdiction of Incorporation or organization)	*(IRS Employer Identification No.)*
2200 Rand Building, Buffalo, NY	**14203**
(Address of Principal executive offices)	*(Zip Code)*

(716) 853-0802
(Registrant s Telephone No. Including Area Code)

Securities registered pursuant to Section 12(b) of the Act:
None

Securities registered pursuant to Section 12(g) of the Act:
Common Stock, $.10 par value

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

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

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 þ No o

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

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

Large accelerated filer o Accelerated filer o Non-accelerated filer þ Smaller reporting company o
(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 Act). Yes o No þ

The aggregate market value of the registrant s outstanding common stock held by non-affiliates of the registrant as of June 30, 2008 was approximately $13,325,039 based upon the last sale price as quoted by NASDAQ Capital Market on such date.

As of March 6, 2009 there were 5,718,934 shares of the registrant s common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Corporation s definitive proxy statement for the Annual Meeting of Stockholders to be held on April 30, 2009 are incorporated by reference into certain sections of Part III herein.

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PART I

Item 1. *Business*

Corporation Formation

Rand Capital Corporation (Rand) was incorporated under the laws of New York on February 24, 1969. Beginning in 1971, Rand operated as a publicly traded, closed-end, diversified management company that was registered under Section 8 of the Investment Company Act of 1940 (the 1940 Act). On August 16, 2001, Rand elected to be treated as a business development company (BDC) under the 1940 Act. In 2002, Rand formed a wholly-owned subsidiary for the purpose of operating it as a small business investment company (SBIC) licensed by the U.S. Small Business Investment Administration (SBA). The subsidiary received an SBA license to operate as an SBIC in August 2002. The subsidiary, which had been organized as a Delaware limited partnership, was converted into a New York corporation on December 31, 2008, at which time its operations as a licensed small business investment company was continued by a newly formed corporation under the name of Rand Capital SBIC, Inc. (Rand SBIC). The following discussion will describe the operations of Rand, its wholly-owned subsidiary Rand SBIC, and the predecessor wholly-owned limited partnership (collectively, the Corporation).

Throughout the Corporation s history, its principal business has been to make venture capital investments in small to medium sized companies that are engaged in the exploitation of new or unique products or services with a sustainable competitive advantage, typically in New York and its surrounding states. The Corporation s principal investment objective is to achieve long-term capital appreciation while maintaining a current cash flow from its debenture instruments. The Corporation invests in a mixture of debenture and equity instruments. The debt securities most often have an equity piece attached to the debenture in the form of stock, warrants or options to acquire stock or the right to convert the debt securities into stock. Rand SBIC was the primary investment vehicle in 2007 and 2008 and it is anticipated that will continue to be the case in 2009. Consistent with its status as a BDC and the purposes of the regulatory framework for BDC s under the 1940 Act, the Corporation provides managerial assistance, often in the form of a board of director s seat, to the portfolio companies in which it invests.

The Corporation operates as an internally managed investment company whereby its officers and employees conduct its operations under the general supervision of its Board of Directors. It has not elected to qualify to be taxed as a regulated investment company as defined under Subchapter M of the Internal Revenue Code.

The Corporation is listed on the NASDAQ Small Capital Market under the symbol Rand .

The Corporation s website is www.randcapital.com. The Corporation s annual report on Form 10-K and its Proxy Statement are available at the following web address: http://materials.proxyvote.com/752185. In addition, the annual report on Form 10-K, the quarterly reports on Form 10-Q, current reports on Form 8-K, charters for the Corporation s committees and other reports filed with the Securities and Exchange Commission (SEC) are available through the Corporation s website.

Regulation as a Business Development Company

Although the 1940 Act exempts a BDC from registration under that Act, it contains significant limitations on the operations of BDCs. Among other things, the 1940 Act contains prohibitions and restrictions relating to transactions between a BDC and its affiliates, principal underwriters and affiliates of its affiliates or underwriters, and it requires that a majority of the BDC s directors be persons other than interested persons, as defined under the 1940 Act. The

1940 Act also prohibits a BDC from changing the nature of its business so as to cease to be, or to withdraw its election as, a BDC unless so authorized by a vote of the holders of a majority of its outstanding voting securities. BDC s are not required to maintain fundamental investment policies relating to diversification and concentration of investments within a single industry. More specifically, in order to qualify as a BDC, a company must:

(1) be a domestic company;

(2) have registered a class of its equity securities or have filed a registration statement with the SEC pursuant to Section 12 of the Securities Exchange Act of 1934;

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(3) operate for the purpose of investing in the securities of certain types of portfolio companies, namely immature or emerging companies and businesses suffering or just recovering from financial distress;

(4) extend significant managerial assistance to such portfolio companies; and

(5) have a majority of disinterested directors (as defined in the 1940 Act). Generally, a BDC must be primarily engaged in the business of furnishing capital and providing managerial expertise to companies that do not have ready access to capital through conventional financial channels. Such portfolio companies are termed eligible portfolio companies.

An eligible portfolio company is, generally, a private domestic operating company, or a public domestic operating company whose securities are not listed on a national securities exchange. In addition, any small business investment company that is licensed by the SBA and that is a wholly owned subsidiary of a BDC is an eligible portfolio company.

The 1940 Act prohibits or restricts companies subject to the 1940 Act from investing in certain types of companies, such as brokerage firms, insurance companies, investment banking firms and investment companies. Moreover, the 1940 Act limits the type of assets that BDCs may acquire to qualifying assets and certain assets necessary for its operations (such as office furniture, equipment and facilities) if, at the time of acquisition, less than 70% of the value of the BDC s assets consist of qualifying assets. Qualifying assets include: (1) securities of companies that were eligible portfolio companies at the time the BDC acquired their securities; (2) securities of bankrupt or insolvent companies that were eligible at the time of the BDC s initial acquisition of their securities but are no longer eligible, provided that the BDC has maintained a substantial portion of its initial investment in those companies; (3) securities received in exchange for or distributed in or with respect to any of the foregoing; and (4) cash items, government securities and high-quality short-term debt. The 1940 Act also places restrictions on the nature of the transactions in which, and the persons from whom, securities can be purchased in order for the securities to be considered qualifying assets. These restrictions include limiting purchases to transactions not involving a public offering and acquiring securities from the portfolio company or its officers, directors, or affiliates.

A BDC is permitted to invest in the securities of public companies and other investments that are not qualifying assets, but those kinds of investments may not exceed 30% of the BDC s total asset value at the time of the investment.

A BDC must make significant managerial assistance available to the issuers of eligible portfolio securities in which it invests. Making available significant managerial assistance means, among other things, any arrangement whereby the BDC, through its directors, officers or employees, offers to provide, and, if accepted does provide, significant guidance and counsel concerning the management, operations or business objectives and policies of a portfolio company.

SBIC Subsidiary

Since 2002, Rand has operated a wholly-owned SBIC subsidiary in order to have access to the various forms of leverage provided by the SBA to SBICs. Rand operates Rand SBIC, and Rand formerly operated the limited partnership SBIC predecessor of Rand SBIC, for the same investment purposes and with investments in the same kinds of securities as Rand. The operations of the SBIC predecessor were, and the operations of Rand SBIC are, consolidated with those of Rand for both financial reporting and tax purposes.

On May 28, 2002, Rand and the predecessor SBIC subsidiary filed an Exemption Application with the SEC seeking an order for a number of operating exemptions that the SEC has commonly granted from certain restrictions under the 1940 Act that would otherwise limit the operations of the wholly-owned subsidiary. After the filing of the Exemption Application, the Corporation had extended discussions with the staff of the Division of Investment

Management of the SEC concerning the application. The principal substantive issue in these discussions was the structure of the predecessor of Rand SBIC as a limited partnership.

Rand formed the predecessor SBIC in 2002 as a limited partnership because that was the organizational form that the SBA strongly encouraged for all new entities seeking licenses as SBICs. Rand organized the SBIC subsidiary in a manner that was consistent with the SBA s model limited partnership forms for licensed SBICs. In that structure, the general partner of Rand SBIC was a limited liability company whose managers were the principal executive officers of Rand.

Under the rules and interpretations of the SEC applicable to BDCs (which the subsidiary SBIC intended to become), if a BDC is structured in limited partnership form, then it must have general partners who serve as a board of directors, or a general partner with very limited authority and a separate board of directors, all of the persons who serve on the board of directors must be natural persons, and a majority of the directors must not be interested persons of the BDC. Since the managers of the limited liability company general partner of the SBIC subsidiary were the principal executive officers of Rand, and since both the limited liability company general partner and the subsidiary SBIC were wholly-owned by Rand, Rand believed that the board of directors of Rand was the functional equivalent of a board of directors for both the general partner limited liability company and for the SBIC limited partnership. Nevertheless, the staff of the Division of Investment Management of the SEC maintained the view that if the limited partnership subsidiary was to be operated as a limited partnership BDC in compliance with the 1940 Act, then the organizational documents of the limited partnership would have to specifically provide that it would have a board of directors consisting of natural persons, a majority of whom would not be interested persons.

After lengthy discussions between Rand and the SBA, in December 2008 the SBA indicated that if Rand SBIC were reorganized as a corporation whose directors were the directors of Rand, it would license the corporation as an SBIC that would continue the operations of the limited partnership predecessor. Accordingly, Rand merged the limited partnership subsidiary and its limited liability company general partner into Rand SBIC, effective on December 31, 2008. As a result of the merger, Rand SBIC is a wholly-owned corporate subsidiary of Rand whose board of directors is comprised of directors of Rand, a majority of whom are not interested persons of Rand or Rand SBIC.

On February 26, 2009, the Corporation filed an Exemption Application with the SEC seeking an order under Sections 6(c), 12(d)(1)(J), 57(c), and 57(i) of, and Rule 17d-1 under, the 1940 Act for exemptions from the application of Sections 12(d)(1), 18(a), 21(b), 57(a)(1), (2), (3), and (4), and 61(a) of the 1940 Act to certain aspects of its operations. The application also seeks an order under Section 12(h) of the Securities Exchange Act of 1934 Act (the Exchange Act) for an exemption from separate reporting requirements for Rand SBIC under Section 13(a) of the Exchange Act. In general, the Corporation s application seeks exemptions that would permit:

- Rand and Rand SBIC to engage in certain related party transactions that the Corporation would otherwise be permitted to engage in as a BDC if its component parts were organized as a single corporation;

- Rand, as a BDC, and Rand SBIC, as its BDC/SBIC subsidiary, to meet asset coverage requirements for senior securities on a consolidated basis; and

- Rand SBIC, as a BDC/SBIC subsidiary of Rand as a BDC, to file Exchange Act reports on a consolidated basis as part of Rand s Exchange Act reports.

The SEC has recently granted exemptions in response to applications that reflected similar issues and factual circumstances, and Rand believes that it will receive the exemptions it has requested for the operation of Rand SBIC as a BDC subsidiary of Rand.

Regulation of the SBIC Subsidiary

SBA Lending Restrictions

The SBA licenses SBICs as part of a program designed to stimulate the flow of private debt and/or equity capital to small businesses. SBICs use funds borrowed from the SBA, together with their own capital, to provide loans to, and make equity investments in, concerns that (a) do not have a net worth in excess of $18 million and do not have average net income after U.S. federal income taxes for the two years preceding any date of determination of more than $6 million, or (b) meet size standards set by the SBA that are measured by either annual receipts or number of employees, depending on the industry in which the concerns are primarily engaged. The types and dollar amounts of the loans and other investments an SBIC that is a BDC may make are limited by the 1940 Act, the SBA

Act and SBA regulations. The SBA is authorized to examine the operations of SBICs, and an SBIC s ability to obtain funds from the SBA is also governed by SBA regulations.

In addition, at the end of each fiscal year, an SBIC must have at least 20% (in total dollars) invested in Smaller Enterprises . The SBA defines Smaller Enterprises as concerns that (a) do not have a net worth in excess of $6 million and have average net income after U.S. federal income taxes for the preceding two years no greater than $2 million, or (b) meet size standards set by the SBA that are measured by either annual receipts or number of employees, depending on the industry in which the concerns are primarily engaged. The Corporation has maintained compliance with this requirement since inception of the SBIC subsidiary.

SBICs may invest directly in the equity of their portfolio companies, but they may not become a general partner of a non-incorporated entity or otherwise become jointly or severally liable for the general obligations of a non-incorporated entity. An SBIC may acquire options or warrants in its portfolio companies, and the options or warrants may have redemption provisions, subject to certain restrictions.

SBA Leverage

The SBA raises capital to enable it to provide funds to SBICs by guaranteeing certificates or bonds that are pooled and sold to purchasers of the government guaranteed securities. The amount of funds that the SBA may lend to SBICs is determined by annual Congressional appropriations.

In order to obtain SBA borrowings, also known as leverage, an SBIC must demonstrate its need to the SBA. To demonstrate need, an SBIC must invest 50% of its Leverageable Capital (defined as Regulatory Capital less unfunded commitments and federal funds) and any outstanding SBA leverage. Other requirements include compliance with SBA regulations, adequacy of capital, and meeting liquidity standards. An SBIC s license entitles an SBIC to apply for SBA leverage, but does not assure that it will be available, or if available, that it will be available at the level of the relevant matching ratio. Availability depends on the SBIC s continued regulatory compliance and sufficient SBA funds being available when the SBIC applies to draw down SBA leverage. Under the provisions of the SBIC regulations, the Corporation may apply for the SBA s conditional commitment to reserve a specific amount of leverage for future use. The Corporation may then apply to draw down leverage against the commitment. All SBICs must obtain a leverage commitment in order to draw leverage from the SBA. Commitments expire on September 30 of the fourth full fiscal year following issuance and require the payment of a fee equal to 1 percent of the total commitment at the time of issuance. An additional fee equal to 2 percent of the amount drawn is deducted at the time of each draw.

The Corporation paid $100,000 to the SBA to reserve $10,000,000 of its approved debenture leverage as a partial prepayment of the SBA s nonrefundable 3% leverage fee. As of December 31, 2008, Rand SBIC had drawn $8,100,000 in leverage from the SBA. The remaining leverage commitment expired on September 30, 2008 and $1,900,000 of approved leverage expired. The remaining unamortized prepaid leverage fee of $19,000 was expensed during 2008.

SBA debentures are issued with 10-year maturities. Interest only is payable semi-annually until maturity. Ten-year SBA debentures may be prepaid with a penalty during the first 5 years, and then are pre-payable without penalty. Rand initially capitalized Rand SBIC with $5 million in Regulatory Capital. The Corporation expects to use Rand SBIC as its primary investment vehicle.

Employees

As of December 31, 2008, the Corporation had four employees.

Item 1A. ***Risk Factors***

The Corporation is Subject to Risks Created by the Valuation of its Portfolio Investments

There is typically no public market for equity securities of the small privately held companies in which the Corporation invests. As a result, the valuations of the equity securities in the Corporation s portfolio are stated at fair value as determined by the good faith estimate of the Corporation s Board of Directors. In the absence of a readily

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ascertainable market value, the estimated value of the Corporation s portfolio of securities may differ significantly, favorably or unfavorably, from the values that would be placed on the portfolio if a ready market for the equity securities existed. Any changes in estimated value are recorded in the statement of operations as Net increase in unrealized appreciation.

The Corporation s Portfolio Investments are Illiquid

Most of the investments of the Corporation are or will be either equity securities acquired directly from small companies or subordinated debt securities. The Corporation s portfolio of equity and debt securities is, and will usually be, subject to restrictions on resale or otherwise has no established trading market. The illiquidity of most of the Corporation s portfolio may adversely affect the ability of the Corporation to dispose of the securities at times when it may be advantageous for the Corporation to liquidate investments.

Investing in Private Companies involves a High Degree of Risk

The Corporation typically invests a substantial portion of its assets in small and medium sized private companies. These private businesses may be thinly capitalized, unproven companies with risky technologies, may lack management depth, and may not have attained profitability. Because of the speculative nature and the lack of a public market for these investments, there is significantly greater risk of loss than is the case with traditional investment securities. The Corporation expects that some of its venture capital investments will be a complete loss or will be unprofitable and that some will appear to be likely to become successful but never realize their potential. The Corporation has been risk seeking rather than risk averse in its approach to venture capital and other investments.

Even if the Corporation s portfolio companies are able to develop commercially viable products, the market for new products and services is highly competitive and rapidly changing. Commercial success is difficult to predict and the marketing efforts of the portfolio companies may not be successful.

Investing in the Corporation s Shares May be Inappropriate for the Investor s Risk Tolerance

The Corporation s investments, in accordance with its investment objective and principal strategies, result in a greater than average amount of risk and volatility and may well result in loss of principal. Its investments in portfolio companies are highly speculative and aggressive and, therefore, an investment in its shares may not be suitable for investors for whom such risk is inappropriate. Neither the Corporation s investments nor an investment in the Corporation is intended to constitute a balanced investment program.

The Corporation is Subject to Risks Created by its Regulated Environment

The Corporation is regulated by the SBA and the SEC. Changes in the laws or regulations that govern SBICs and BDCs could significantly affect the Corporation s business. Regulations and laws may be changed periodically, and the interpretations of the relevant regulations and laws are also subject to change. Any change in the regulations and laws governing the Corporation s business could have a material impact on its financial condition or its results of operations. Moreover, the laws and regulations that govern BDCs and SBICs may place conflicting demands on the manner in which the Corporation operates, and the resolution of those conflicts may restrict or otherwise adversely affect the operations of the Corporation.

The Corporation is Subject to Risks Created by Borrowing Funds from the SBA

The Corporation s Leverageable Capital may include large amounts of debt securities issued through the SBA, and all of the debentures will have fixed interest rates. Until and unless the Corporation is able to invest substantially all of the proceeds from debentures at annualized interest or other rates of return that substantially exceed annualized interest rates that Rand SBIC must pay the SBA, the Corporation s operating results may be adversely affected which may, in turn, depress the market price of the Corporation s common stock.

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The Corporation is Dependent Upon Key Management Personnel for Future Success

The Corporation is dependent on the diligence and skill of its two senior officers, Allen F. Grum and Daniel P. Penberthy, for the selection, structuring, closing and monitoring of its investments. The future success of the Corporation depends to a significant extent on the continued service and coordination of its senior management team. The departure of either of its executive officers could materially adversely affect its ability to implement its business strategy. The Corporation does not maintain key man life insurance on any of its officers or employees.

The Corporation Operates in a Competitive Market for Investment Opportunities

The Corporation faces competition in its investing activities from many entities including other SBICs, private venture capital funds, investment affiliates of large companies, wealthy individuals and other domestic or foreign investors. The competition is not limited to entities that operate in the same geographical area as the Corporation. As a regulated BDC, the Corporation is required to disclose quarterly and annually the name and business description of portfolio companies and the value of its portfolio securities. Most of its competitors are not subject to this disclosure requirement. The Corporation s obligation to disclose this information could hinder its ability to invest in certain portfolio companies. Additionally, other regulations, current and future, may make the Corporation less attractive as a potential investor to a given portfolio company than a private venture capital fund.

The Corporation May be Negatively Affected by Adverse Changes in the General Economic Conditions of the Domestic and Global Markets

The continued economic crisis and related turmoil in the global financial markets has had and may continue to have an impact on the Corporation s portfolio companies and the overall financial condition of the Corporation. If the current market conditions continue to deteriorate, the Corporation may suffer further losses on its investment portfolio, which could have a material adverse effect on Net Asset Value.

Fluctuations of Quarterly Results

The Corporation s quarterly operating results could fluctuate significantly as a result of a number of factors. These factors include, among others, variations in and the timing of the recognition of realized and unrealized gains or losses, the degree to which portfolio companies encounter competition in their markets, and general economic conditions. As a result of these factors, results for any one quarter should not be relied upon as being indicative of performance in future quarters.

Item 1B. ***Unresolved Staff Comments***

Not Applicable

Item 2. ***Properties***

The Corporation maintains its offices at 2200 Rand Building, Buffalo, New York 14203, where it leases approximately 1,300 square feet of office space pursuant to a lease agreement that expires December 31, 2010. The Corporation believes that its leased facilities are adequate to support its current staff and expected future needs.

Item 3. ***Legal Proceedings***

None

Item 4. ***Submission of Matters to a Vote of Security Holders***

None

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Part II

Item 5. ***Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities***

The Corporation s common stock, par value $0.10 per share (Common Stock), is traded on the NASDAQ Small Cap Market (NASDAQ) under the symbol RAND. The following table sets forth, for the periods indicated, the range of high and low closing sales prices per share as reported by NASDAQ:

2008 Quarter ending:	**High**	**Low**
March 31st	$ 4.78	$ 3.55
June 30th	$ 4.29	$ 3.25
September 30th	$ 4.00	$ 3.25
December 31st	$ 4.00	$ 3.11

2007 Quarter ending:	**High**	**Low**
March 31st	$ 5.04	$ 3.26
June 30th	$ 3.94	$ 3.26
September 30th	$ 4.62	$ 3.35
December 31st	$ 4.72	$ 3.50

The Corporation did not sell any securities during the period covered by this report that were not registered under the Securities Act. The Corporation has not paid any cash dividends in its most recent two fiscal years, and it has no intention of paying cash dividends in the coming fiscal year.

Profit Sharing and Stock Option Plans

In July 2001, the stockholders of the Corporation authorized the establishment of an Employee Stock Option Plan (the Plan). The Plan provides for the award of options to purchase up to 200,000 common shares to eligible employees. In 2002, the Corporation placed the Plan on inactive status as it developed a new profit sharing plan for the Corporation s employees in connection with the establishment of its SBIC subsidiary. As of December 31, 2008 no stock options had been awarded under the Plan. Because Section 57(n) of the 1940 Act prohibits maintenance of a profit sharing plan for the officers and employees of a BDC where any option, warrant or right is outstanding under an executive compensation plan, no options will be granted under the Plan while any profit sharing plan is in effect with respect to the Corporation.

In 2002, the Corporation established a non-equity incentive Profit Sharing Plan for its executive officers in accordance with Section 57(n) of the Investment Company Act of 1940 (the 1940 Act). The profit sharing plan provides for incentive compensation to the named executive officers based on a stated percentage of net realized capital gains and after reduction for realized and unrealized losses on the Rand SBIC investment portfolio. Any profit sharing paid cannot exceed 20% of the Corporation s net income, as defined. There have been no accruals for, or contributions to, the Profit Sharing Plan since its inception in 2002.

Shareholders of Record

On March 6, 2009 the Corporation had a total of 820 shareholders, which included 97 record holders of its common stock, and an estimated 723 shareholders with shares beneficially owned in nominee name or under clearinghouse positions of brokerage firms or banks.

Stock Repurchase Plan

The Board of Directors has authorized the repurchase of up to 285,947 shares of the Corporation s outstanding Common Stock on the open market at prices that are no greater than current net asset value through October 23, 2009. During 2003 and 2002 the Corporation purchased 44,100 shares of its Common Stock for a total cost of $47,206. No additional shares have been repurchased since 2003.

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Company Performance Graph

The following graph shows a five-year comparison of cumulative total shareholder returns for the Company s Common Stock, the NASDAQ Market Index, and a New Peer Group and the Old Peer Group, assuming a base index of $100 at the end of 2003. The cumulative total return for each annual period within the five years presented is measured by dividing (1) the sum of (A) the cumulative amount of dividends for the measurement period, assuming dividend investment, and (B) the difference between share prices at the end and at the beginning of the measurement period by (2) the share price at the beginning of the measurement period.

COMPARISON OF 5-YEAR CUMULATIVE TOTAL RETURN
AMONG RAND CAPITAL CORP.,
NASDAQ MARKET INDEX AND PEER GROUP INDEX

ASSUMES $100 INVESTED ON DEC. 31, 2003
ASSUMES DIVIDEND REINVESTED
FISCAL YEAR ENDING DEC. 31, 2008

COMPARISON OF CUMULATIVE TOTAL RETURN OF ONE OR MORE COMPANIES, PEER GROUPS, INDUSTRY INDEXES AND/OR BROAD MARKETS

FISCAL YEAR ENDING

COMPANY/INDEX/MARKET	12/31/2003	12/31/2004	12/30/2005	12/29/2006	12/31/2007	12/31/2008
Rand Capital Corporation	100.00	107.59	92.41	241.38	248.14	241.38
Old Peer Group Index	100.00	101.62	95.36	132.43	87.47	18.67
New Peer Group Index	100.00	108.41	110.79	122.16	134.29	79.25
NASDAQ Market Index	100.00	101.62	95.36	130.52	91.89	34.03

The Old Peer Group was made up of the following securities:
Ameritrans Capital Corp (NasdaqCM:AMTC)
Brantley Capital Corp (OTC:BBDC.pk)
Capital Southwest Corp (NasdaqGM:CSWC)

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Equus Total Return Inc (NYSE:EQS)
Gladstone Investment CP (NasdaqGS:GAIN)
Harris & Harris Group (NasdaqGM:TINY)
Macc Private Equities Inc (NasdaqCM:MACC)
MCG Capital Corporation (NasdaqGS:MCGC)
MVC Capital Inc (NYSE:MVC)

The New Peer Group is made up of the following securities:
Ameritrans Capital Corp (NasdaqCM:AMTC)
Equus Total Return Inc (NYSE:EQS)
Gladstone Investment CP (NasdaqGS:GAIN)
Harris & Harris Group (NasdaqGM:TINY)
Hercules Tech Growth Cap (NasdaqGS: HTGC)
Main Street Capital Corp (NasdaqGS: MAIN)
MCG Capital Corporation (NasdaqGS:MCGC)
Patriot Capital Funding (NasdaqGS: PCAP)
Triangle Capital Corp (NasdaqGM: TCAP)

The New Peer Group was selected in good faith by the Corporation and contains nine business development companies or other funds believed by the Corporation to be of similar size and have similar investment objectives to those of the Corporation.

The performance graph information provided above will not be deemed to be soliciting material or filed with the SEC or subject to Regulations 14A or 14C, or to the liabilities of section 18 of the Securities Exchange Act, unless in the future the Corporation specifically requests that the information be treated as soliciting material or specifically incorporates it by reference into any filing under the Securities Act or the Securities Exchange Act.

Item 6. ***Selected Financial Data***

The following table provides selected consolidated financial data of the Corporation for the periods indicated. You should read the selected financial data set forth below in conjunction with Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, and with our consolidated financial statements and related notes appearing elsewhere in this report.

Balance Sheet Data as of December 31:

	2008	2007	2006	2005	2004
Total assets	$ 32,228,797	$ 32,722,151	$ 29,463,944	$ 16,063,605	$ 12,743,109
Total liabilities	$ 12,001,831	$ 12,904,328	$ 12,681,539	$ 7,447,671	$ 3,716,055
Net assets	$ 20,226,966	$ 19,817,823	$ 16,782,405	$ 8,615,934	$ 9,027,054
Net asset value per outstanding share	$ 3.54	$ 3.47	$ 2.93	$ 1.51	$ 1.58
Common stock shares outstanding	5,718,934	5,718,934	5,718,934	5,718,934	5,718,934

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Operating Data for the year ended December 31:

	2008	2007	2006	2005	2004
Investment income	$ 1,757,003	$ 2,302,870	$ 1,326,962	$ 736,573	$ 757,704
Total expenses	$ 1,721,555	$ 1,650,947	$ 1,519,184	$ 1,265,846	$ 900,812
Net investment gain (loss)	$ 135,689	$ 425,406	$ (1,264,802)	$ (175,179)	$ (112,384)
Net realized (loss) gain on sales and dispositions of investments		$ (68,748)	$ 3,456,441	$ (382,353)	$ 26,727
Net increase (decrease) in unrealized appreciation	$ 273,454	$ 2,362,507	$ 5,974,832	$ 146,412	$ (125,777)
Net increase (decrease) in net assets from operations	$ 409,143	$ 2,719,165	$ 8,166,471	$ (411,120)	$ (211,434)

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Item 7. ***Management s Discussion and Analysis of Financial Condition and Results of Operations***

You should read the following discussion and analysis of our financial condition and results of operations in conjunction with our financial statements and related notes included elsewhere in this report.

Forward Looking Statements

Statements included in this Management s Discussion and Analysis of Financial Condition and Results of Operations and elsewhere in this document that do not relate to present or historical conditions are forward-looking statements within the meaning of that term in Section 27A of the Securities Act of 1933, and in Section 21F of the Securities Exchange Act of 1934. Additional oral or written forward-looking statements may be made by the Corporation from time to time, and those statements may be included in documents that are filed with the Securities and Exchange Commission. Such forward-looking statements involve risks and uncertainties that could cause results or outcomes to differ materially from those expressed in the forward-looking statements. Forward-looking statements may include, without limitation, statements relating to the Corporation s plans, strategies, objectives, expectations and intentions and are intended to be made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Words such as believes, forecasts, intends, possible, expects, estimates, anticipates, or plans and similar expressions are intended to identify forward-looking statements. Among the important factors on which such statements are based are assumptions concerning the state of the national economy and the local markets in which the Corporation s portfolio companies operate, the state of the securities markets in which the securities of the Corporation s portfolio company trade or could be traded, liquidity within the national financial markets, and inflation. Forward-looking statements are also subject to the risks and uncertainties described under the caption Risk Factors contained in Part I, Item 1A, which is incorporated herein by reference.

There may be other factors that we have not identified that affect the likelihood that the forward-looking statements may prove to be accurate. Further, any forward-looking statement speaks only as of the date it is made and, except as required by law, we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which it is made or to reflect the occurrence of anticipated or unanticipated events or circumstances. New factors emerge from time to time that may cause our business not to develop as we expect, and we cannot predict all of them.

Business Overview

Rand Capital Corporation (Rand) was incorporated under the law of New York on February 24, 1969. Beginning in 1971, Rand operated as a publicly traded, closed-end, diversified management company that was registered under Section 8 of the Investment Company Act of 1940 (the 1940 Act). On August 16, 2001, Rand elected to be treated as a business development company (BDC) under the 1940 Act. In 2002, Rand formed a wholly-owned subsidiary for the purpose of operating it as a small business investment company (SBIC) licensed by the U.S. Small Business Investment Administration (SBA). The subsidiary received an SBA license to operate as an SBIC in August 2002. The subsidiary, which had been organized as a Delaware limited partnership, was converted into a New York corporation on December 31, 2008, at which time its operations as a licensed small business investment company were continued by a newly formed corporation under the name of Rand Capital SBIC, Inc. (Rand SBIC). The following discussion will describe the operations of Rand, its wholly-owned subsidiary Rand SBIC, and the predecessor wholly-owned limited partnership (collectively, the Corporation).

The Corporation anticipates that most, if not all, of its investments in the next year will be originated through the SBIC subsidiary.

The Corporation s primary business is making investments in companies, usually in the form of subordinated debt, membership interests, or preferred and common stock. The investment focus is usually on small and medium-sized companies that meet certain criteria, including:

1) a qualified and experienced management team

2) a new or unique product or service with a sustainable competitive advantage

3) a potential for growth in revenue and cash flow

4) a potential to realize appreciation in an equity position, if any.

The Corporation makes investments in portfolio companies that typically range from $500,000 to $1,000,000 and it invest either directly in the equity of a company through equity shares or in a debt instrument. The debt instruments generally have a maturity of not more than five years and usually have detachable equity warrants. Interest is either paid currently or deferred.

The Corporation s management team identifies investment opportunities. Throughout the Corporation s history it has established a large network of investment referral relationships. Investment proposals may, however, come to the Corporation from many other sources, and may include unsolicited proposals from the public and referrals from banks, lawyers, financial accountants and other members of the financial community. The Corporation believes that its reputation in the community and experience provide a competitive advantage in originating qualified new investments.

In a typical private financing, the management team of the Corporation will review, analyze, and confirm, through due diligence, the business plan and operations of the potential portfolio company. Additionally, the Corporation will become familiar with the portfolio company s industry and competitive landscape and may conduct additional reference checks with customers and suppliers of the portfolio company.

Following an initial investment in a portfolio company, the Corporation may be requested to make follow-on investments in the company. Follow-on investments may be made to take advantage of warrants or other preferential rights granted to the Corporation or otherwise to increase or maintain the Corporation s position in a promising portfolio company. The Corporation may also be called upon to provide an additional investment to a portfolio company in order for that company to fully implement its business plans, to develop a new line of business or to recover from unexpected business problems. Follow-on investments in a portfolio company are evaluated individually and may be subject to regulatory restrictions.

The Corporation will exit its investments generally through the maturation of the debt security or when a liquidity event takes place, such as the sale, recapitalization, or initial public offering of a portfolio company. The method and timing of the disposition of the Corporation s portfolio investments can be critical to the realization of maximum total return. The Corporation generally expects to dispose of its equity securities through the private sales of securities to other investors or through an outright sale of the company or a merger. The Corporation anticipates its debentures will be repaid with interest and hopes to realize further appreciation from the warrants or other equity type instruments it receives in connection with the origination of the debenture. The Corporation anticipates generating cash for new investments and operating expenses through SBA leverage draw downs, and interest and principal payments from its portfolio concerns.

2008 Highlights and Outlook

The Corporation s net asset value increased $0.07, or 2% during 2008, closing the year at $3.54 per share up from $3.47 at December 31, 2007. At December 31, 2008, the Corporation s total investment portfolio was valued at $28.1 million, which exceeds its cost basis of $14.4 million, reflecting $13.7 million in net unrealized appreciation.

Although the Corporation s stock traded at a premium to its net asset value during 2007, during 2008 its common stock traded in a range that was above and below the current net asset value per share. The year closed with the stock trading at $3.50 which represented a slight discount to the net asset value of $3.54.

During 2008 the Corporation recognized $1,757,003 in total investment income, a decrease of ($545,867) from $2,302,870 of investment income in 2007. The 23.7% decrease is attributable to the decrease in dividends and interest from portfolio companies. Dividends from portfolio companies that are limited liability companies can fluctuate based on the portfolio companies profitability and the timing of distributions. In addition, lower cash balances in the current year caused the interest income to decrease.

Also during 2008 certain portfolio companies repaid some or all of their outstanding debenture instruments, including: Contract Staffing, Gemcor and New Monarch Machine Tool, Inc. These repayments may impact future earnings by reducing interest income in 2009 and future periods.

The cash balance at December 31, 2008 was $2.8 million which was approximately $1.6 million lower than at the end of 2007. The Corporation was unable to draw the remaining $1.9 million of outstanding leverage available from the Small Business Administration (SBA), due to Rand SBIC s excess cash position, and the leverage expired in September 2008. Given that the Corporation has used up much of its available SBA leverage, in order for the Corporation to raise substantial amounts of capital in the short term, it will need to rely on Rand s ability to sell additional shares of its common stock through public or private offerings. Although Rand currently has no specific plans concerning the timing or amount of any common stock offering it might make, it is considering the possibility of making an offering at some time in the next year in order to have more capital available with which to pursue favorable investment opportunities. See Liquidity and Capital Resources, below.

While the business of some of our portfolio companies is strengthening, in terms of employee growth, increase in revenue, and strengthening net income position, it remains difficult to forecast when future exits will happen, or if the portfolio companies will have sufficient capital to remain viable while their respective markets mature.

Critical Accounting Policies

The Corporation prepares its financial statements in accordance with United States generally accepted accounting principles (GAAP), which requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities. For a summary of all significant accounting policies, including critical accounting policies, see Note 1 to the consolidated financial statements in Item 8.

The increasing complexity of the business environment and applicable authoritative accounting guidance require the Corporation to closely monitor its accounting policies and procedures. The Corporation has identified two critical accounting policies that require significant judgment. The following summary of critical accounting policies is intended to enhance your ability to assess the Corporation s financial condition and results of operations and the potential volatility due to changes in estimates.

Valuation of Investments

The most important estimate inherent in the preparation of the Corporation s consolidated financial statements is the valuation of its investments and the resulting unrealized appreciation or depreciation.

Investments are valued at fair value as determined in good faith by the management of the Corporation and submitted to the Board of Directors for approval. There is no single standard for determining fair value in good faith. As a result, determining fair value requires that judgment be applied to the specific facts and circumstances of each portfolio investment while employing a consistently applied valuation process for investments. The Corporation analyzes and values each investment on a quarterly basis, and records unrealized depreciation for an investment that it believes has become impaired, including where collection of a loan or realization of the recorded value of an equity security is doubtful. Conversely, the Corporation will record unrealized appreciation if it believes that the underlying portfolio company has appreciated in value and, therefore, its equity security has also appreciated in value. These estimated fair values may differ from the values that would have been used had a ready market for the investments existed and these differences could be material if our assumptions and judgments differ from results of actual liquidation events.

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) 157, Fair Value Measurements. This statement defines fair value, establishes a framework for measuring fair value in GAAP, and expands disclosures about fair value measurements. This statement was effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those years. On January 1, 2008, the Corporation adopted SFAS 157.

SFAS No. 157 classifies the inputs used to measure fair value into the following hierarchy:

Level 1: Quoted prices in active markets for identical assets or liabilities, used in the Corporation s valuation at the measurement date.

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

Level 3: Unobservable and significant inputs to determining the fair value.

Most of the Corporation s investments are classified in Level 3 due to their privately held restricted nature.

In the valuation process, the Corporation uses financial information received monthly, quarterly, and annually from its portfolio companies, which includes both audited and unaudited financial statements, annual projections and budgets prepared by the portfolio company and other financial and non-financial business information supplied by the portfolio companies management. This information is used to determine financial condition, performance, and valuation of the portfolio investments. The valuation may be reduced if a company s performance and potential have significantly deteriorated. If the factors which led to the reduction in valuation are overcome, the valuation may be restored.

Another key factor used in valuing equity investments is recent arms-length equity transactions with unrelated new investors entered into by the portfolio company that the Corporation utilizes to form a basis for its underlying value. Many times the terms of these equity transactions may not be identical to the equity transactions between the portfolio company and the Corporation, and the impact of the discrepancy in transaction terms on the market value of the portfolio company may be difficult or impossible to quantify.

Any changes in estimated fair value are recorded in our statement of operations as Net increase in unrealized appreciation.

Revenue Recognition (Interest Income)

Interest income generally is recognized on the accrual basis except where the investment is in default or otherwise presumed to be in doubt. In such cases, interest is recognized at the time of receipt. A reserve for possible losses on interest receivable is maintained when appropriate. Certain investments of the Corporation are structured to provide a deferred interest period when interest is not currently due.

Rand SBIC s interest accrual is also regulated by the SBA s Accounting Standards and Financial Reporting Requirements for Small Business Investment Companies . Under these rules interest income cannot be recognized if collection is doubtful, and a 100% reserve must be established. The collection of interest is presumed to be in doubt when there is substantial doubt about a portfolio company s ability to continue as a going concern or the loan is in default more than 120 days. Management also utilizes other qualitative and quantitative measures to determine the value of a portfolio investment and the collectability of any accrued interest.

Recent Accounting Pronouncements

In September 2006, the FASB issued Statement No. 157 (SFAS 157), Fair Value Measurements. This statement defines fair value, establishes guidelines for measuring fair value and expands disclosures regarding fair value measurements. SFAS 157 does not require any new fair value measurements but rather eliminates inconsistencies in guidance found in various prior accounting pronouncements. SFAS 157 is effective for fiscal years beginning after November 15, 2007. The Corporation adopted the enhanced disclosure provisions of SFAS 157 during 2008.

Management does not believe that any other recently issued, but not yet effective, accounting standards, if currently adopted, would have a material effect on the accompanying consolidated financial statements.

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Financial Condition

Overview:

	12/31/08	12/31/07	(Decrease) Increase	% (Decrease) Increase
Total assets	$ 32,228,797	$ 32,722,151	$ (493,354)	(1.5)%
Total liabilities	12,001,831	12,904,328	(902,497)	(7.0)%
Net assets	$ 20,226,966	$ 19,817,823	$ 409,143	2.1%

Net asset value per share (NAV) was $3.54 per share at December 31, 2008 versus $3.47 per share at December 31, 2007.

The Corporation did not draw down on any of the SBA leverage during the year ended December 31, 2008 and the total owed to the SBA at December 31, 2008 was $8,100,000. These debentures bear a fixed interest rate and an annual fee, averaging 5.9%, payable semi-annually. The debenture principal is repayable in full 10 years from issuance beginning in 2014.

Cash and cash equivalents approximated 14% of net assets at December 31, 2008 compared to 22% at December 31, 2007.

The effect of investment income, realized losses and the change in unrealized appreciation on investments resulted in a net decrease in the net deferred tax liability from $3,955,000 at December 31, 2007 to $3,490,000 at December 31, 2008.

Composition of the Corporation s Portfolio

The Corporation s financial condition is dependent on the success of its portfolio holdings. It has invested a substantial portion of its assets in small to medium-sized companies. The following summarizes the Corporation s investment portfolio at the year-ends indicated.

	12/31/08	12/31/07	Increase	% Increase
Investments, at cost	$ 14,386,451	$ 13,390,644	$ 995,807	7.4%
Unrealized appreciation, net	13,739,831	13,137,846	601,985	4.6%
Investments, at fair value	$ 28,126,282	$ 26,528,490	$ 1,597,792	6.0%

The Corporation s total investments at fair value, as estimated by the Board of Directors, approximated 139% of net assets at December 31, 2008 and 134% of net assets at December 31, 2007.

The change in investments, at cost, is comprised of the following:

New Investments:	**Amount**
GridApp Systems, Inc. (GridApp)	$ 666,667
Niagara Dispensing Technologies, Inc. (Niagara Dispensing)	374,990
SOMS Technologies, LLC (SOMS)	250,000
Associates Interactive, LLC (Associates)	200,000
Mezmeriz, Inc. (Mezmeriz)	100,000
Rocket Broadband Networks, Inc. (Rocket Broadband)	35,000
Total of investments made during the year ended December 31, 2008	$ 1,626,657
Other Changes to investments:	
APF Group, Inc. (APF) interest conversion	40,832
Niagara Dispensing interest conversion	41,783
Total of new investments and changes to investments during the year ended December 31, 2008	$ 1,709,272

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Sales/Investment Repayments	Amount
New Monarch Machine Tool, Inc. (Monarch)	(520,147)
Contract Staffing	(131,066)
Gemcor II, LLC (Gemcor)	(62,252)
Total of sales and investment repayments during the year ended December 31, 2008	(713,465)
Total change in investment balance, at cost, during the year ended December 31, 2008	$ 995,807

The Corporation s top five portfolio companies represented 68% of total assets at December 31, 2008:

Company	Industry	Fair Value at December 31, 2008	% of Total Assets at December 31, 2008
Innov-X Systems, Inc. (Innov-X)	Manufacturing Metals Testing Equipment	$ 8,761,700	27%
Gemcor	Manufacturing Aerospace Machinery	$ 5,803,201	18%
Synacor Inc. (Synacor)	Software	$ 4,168,001	13%
Kionix, Inc . (Kionix)	Manufacturing Silicon Chips	$ 2,000,000	6%
Ultra-Scan Corporation (Ultra-Scan)	Electronics Hardware/Software	$ 1,203,000	4%

The Corporation s top five portfolio companies represented 61% of total assets at December 31, 2007:

Company	Industry	Fair Value at December 31, 2007	% of Total Assets at December 31, 2007
Innov-X	Manufacturing Metals Testing Equipment	$ 8,761,700	27%
Synacor	Software	$ 4,168,001	13%
Gemcor	Manufacturing Aerospace Machinery	$ 4,165,451	13%
Carolina Skiff LLC (Carolina Skiff)	Manufacturing Boating	$ 1,227,000	4%
Kionix	Manufacturing Silicon Chips	$ 1,221,568	4%

Below is the Geographic breakdown of the Corporation s investments, at fair value, to the net asset value as of December 31, 2008 and 2007:

Geographic Region	% of Net Asset Value at December 31, 2008	% of Net Asset Value at December 31, 2007
USA East	95%	94%
USA South	5%	6%
	100%	100%

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As of December 31, 2008 and 2007, the Corporation s investment portfolio consisted of the following investments:

	Cost	Percentage of Total Portfolio	Fair Value	Percentage of Total Portfolio
December 31, 2008:				
Subordinated Debt and Promissory Notes	$ 3,240,266	23%	$ 2,111,013	8%
Convertible Debt	356,667	2%	356,667	1%
Equity and Partnership Interests	10,721,519	75%	25,525,261	91%
Equity Warrants	68,000		133,341	
Total	$ 14,386,452	100%	$ 28,126,282	100%
December 31, 2007:				
Subordinated Debt and Promissory Notes	$ 3,992,927	30%	$ 3,071,009	11%
Convertible Debt	50,000		50,000	
Equity and Partnership Interests	9,279,717	69%	23,274,140	88%
Equity Warrants	68,000	1%	133,341	1%
Total	$ 13,390,644	100%	$ 26,528,490	100%

Results of Operations

Investment Income

The Corporation s investment objective is to achieve long-term capital appreciation on its equity investments while maintaining a current cash flow from its debenture and pass through equity instruments. Therefore, the Corporation invests in a mixture of debenture and equity instruments, which will provide a current return on a portion of the investment portfolio. The equity features contained in our investment portfolio are structured to realize capital appreciation over the long-term and may not generate current income in the form of dividends or interest. In addition, the Corporation earns interest income from investing its idle funds in money market instruments held at high grade financial institutions.

Comparison of the years ended December 31, 2008 and 2007

	December 31, 2008	December 31, 2007	(Decrease)	% (Decrease)
Interest from portfolio companies	$ 608,180	$ 618,430	$ (10,250)	(1.7)%
Interest from other investments	90,660	173,664	(83,004)	(47.8)%
Dividend and other investment income	1,027,377	1,469,864	(442,487)	(30.1)%
Other income	30,786	40,912	(10,126)	(24.8)%

Total investment income	$	1,757,003	$	2,302,870	$	(545,867)	(23.7)%

Interest from portfolio companies The portfolio interest income decrease is a result of several factors. Two portfolio companies (Contract Staffing and Monarch) repaid their debt instruments during the last twelve months and one portfolio company (Niagara Dispensing) converted its debenture instrument into equity during 2008. During the year ended December 31, 2007 the Corporation recognized Original Issue Discount (OID) income on its Adampluseve, Inc (Adampluseve) investment in the amount of $62,333. Adampluseve paid off its debenture instrument early and therefore the remaining unamortized OID was accreted into income during 2007. OID is created when the Corporation invests in a debenture instrument that has a warrant attached to the instrument. This requires an allocation of a portion of the investment cost to the warrant and reduces the debt instrument by an equal amount in the form of a note discount or OID. The note is then reported net of the discount and the discount is accreted into income over the life of the debenture instrument

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These aforementioned decreases in the current year portfolio interest income are offset by several revenue items that increased portfolio income. The Corporation began to recognize dividends on the Series A Convertible Preferred Stock of Innov-X during the year ended December 31, 2008. These dividends resulted from the re-negotiation of the preferred stock terms and provided for an 8% cumulative deferred return while the investment is outstanding. The amount recognized during the year ended December 31, 2008 was $162,413. This dividend is classified as portfolio interest income and this revenue classification is consistent with other interest bearing instruments in the portfolio. Interest of $43,067 was recognized on the escrow from Innov-X during 2008. The Innov-X escrow of $711,249 and the earned interest of $43,067 were received in the second quarter of 2008.

After reviewing the portfolio companies performance and the circumstances surrounding the investments, the Corporation has ceased accruing interest income on the following investment instruments:

Company	**Interest Rate**	**Investment Cost**	**Year that Interest Accrual Ceased**
G-Tec	8%	$ 400,000	2004
Rocket Broadband	11.25%	35,000	2008
UStec	5%	100,000	2006
WineIsIt.com (Wineisit)	10%	801,918	2005

Interest from other investments The decrease in interest income is due to lower cash balances coupled with lower yields on these cash balances.

Dividend and other investment income Dividend income is comprised of distributions from Limited Liability Companies (LLC s) in which the Corporation has invested. The Corporation s investment agreements with certain LLC companies require the entities to distribute funds to the Corporation for payment of income taxes on its allocable share of the entities profits. These dividends will fluctuate based upon the profitability of the entities and the timing of the distributions.

Dividend income for the year ended December 31, 2008 consisted of distributions from Gemcor for $974,287, Carolina Skiff for $19,838 and Somerset Gas Transmission Company (Somerset) for $33,252.

Dividend income for the year ended December 31, 2007 consisted of distributions from Gemcor for $1,372,407, Carolina Skiff for $40,464, Somerset for $36,788, Topps Meat Company LLC (Topps) for $19,524, and Vanguard Modular Building Systems (Vanguard) for $681.

Other income Other income consists of the revenue associated with the amortization of financing fees charged to the portfolio companies upon successful closing of Rand SBIC financing. The SBA regulations limit the amount of fees that can be charged to a portfolio company, and the Corporation typically charges 1% to 3% to the portfolio concerns. These fees are amortized ratably over the life of the instrument associated with the fees. The unamortized fees are carried on the balance sheet under Deferred revenue . In addition, other income includes fees charged by the Corporation to its portfolio companies for attendance at the portfolio companies board meetings.

Other income decreased due to the fact that the Corporation has not charged any of its new portfolio companies financing fees in the last two years. The annualized financing fee income based on the existing portfolio will be approximately $6,700 in 2009 and $2,700 in 2010. In addition board attendance income amounted to $14,000 for the year ended December 31, 2008 and $13,000 for year ended December 31, 2007.

Comparison of the years ended December 31, 2007 and 2006

	December 31, 2007	December 31, 2006	(Decrease) Increase	% (Decrease) Increase
Interest from portfolio companies	$ 618,430	$ 757,824	$ (139,394)	(18.4)%
Interest from other investments	173,664	53,104	120,560	227.0%
Dividend and other investment income	1,469,864	432,296	1,037,568	240.0%
Other income	40,912	83,738	(42,826)	(51.1)%
Total investment income	$ 2,302,870	$ 1,326,962	$ 975,908	73.5%

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Interest from portfolio companies The portfolio interest income decrease can be attributed to the fact that five debenture instruments Concentrix Corporation (Concentrix), Innov-X, Ramsco, UStec, Inc. (UStec) and Synacor that contributed to portfolio interest income for the year ended December 31, 2006 were either repaid or converted into equity instruments during the last six months of 2006 and throughout 2007, thereby reducing portfolio interest income earned during the year ended December 31, 2007.

This decrease is offset by the recognition of the Adampluseve OID income. This portfolio company, Adampluseve, paid off its debenture instrument early and therefore the remaining $62,333 in unamortized OID was accreted into income during the year ended December 31, 2007.

After reviewing the portfolio companies performance and the circumstances surrounding the investments, the Corporation ceased accruing interest income on the following investment instruments:

Company	Interest Rate	Investment Cost	Year that Interest Accrual Ceased
G-Tec	8%	$ 400,000	2004
UStec	5%	100,000	2006
WineIsIt.com	10%	801,918	2005

Interest from other investments The increase in interest income was primarily due to higher cash balances and higher yields on these cash balances. The higher cash balances were a result of portfolio investment repayments and sales of portfolio companies equity instruments.

Dividend and other investment income Dividend income for the year ended December 31, 2007 consisted of distributions from Gemcor for $1,372,407, Carolina Skiff for $40,464, Somerset for $36,788, Topps for $19,524, and Vanguard for $681. Dividend income for the year ended December 31, 2006 consisted of distributions from Gemcor for $375,372, Topps for $37,334, Carolina Skiff for $18,416 and Vanguard for $1,174.

Other income The decrease in other income from December 31, 2006 to December 31, 2007 was due to the fact that the Corporation only charged two portfolio companies closing fees in 2006 and no closing fees were charged in 2007. The Corporation also charged Concentrix an $18,000 prepayment penalty fee that was included in other income during 2006. In addition board attendance income amounted to $13,000 for the year ended December 31, 2007 and $9,000 for year ended December 31, 2006.

Operating Expenses

Comparison of the years ended December 31, 2008 and 2007

	December 31, 2008	December 31, 2007	Increase	% Increase
Total expenses	$ 1,721,555	$ 1,650,947	$ 70,608	4.3%

Operating expenses predominately consist of interest expense on SBA obligations, employee compensation and benefits, directors fees, shareholder related costs, office expenses, professional fees, and expenses related to identifying and reviewing investment opportunities.

The increase in operating expenses during the year ended December 31, 2008 can be attributed to an increase of 17%, or $35,845, in professional fees. A portion of the increase in this expense can be attributed to the escalating legal, audit and tax costs due to the increasingly more complex regulatory environment in which the Corporation operates. In addition, in order to comply with the SEC rules regarding the Corporation s operating structure the Corporation has incurred additional legal fees associated with the corporate reorganization of the SBIC subsidiary.

The increase is also due to the 63%, or $32,583, increase in other operating expenses. Other operating expenses in the current year included a write off of an escrow receivable in the amount of $69,421 for UStec. Management has deemed the collection of this escrow receivable doubtful based on the ongoing negotiations with UStec. Other operating expenses also include a one-time $5,000 reorganization fee charged by the SBA to review the corporate reorganization of Rand SBIC.

The SBA interest expense increased 4%, or $19,000, during the current year. Total SBA interest expense was $522,062 and $503,062 for the years ended December 31, 2008 and 2007, respectively. The Corporation has borrowed $8,100,000 from the SBA as of December 31, 2008 at an average borrowing rate, including surcharges, of approximately 5.9%. This interest is paid on a semi-annual basis.

Comparison of the years ended December 31, 2007 and 2006

	December 31, 2007	**December 31, 2006**	**Increase**	**% Increase**
Total expenses	$ 1,650,947	$ 1,519,184	$ 131,763	8.7%

The increase in operating expenses during the year ended December 31, 2007 can be primarily attributed to the 83% or $96,754 increase in professional fees. Some of the increase in this expense can be attributed to the escalating legal, audit and tax costs due to the increasingly more complex regulatory environment in which the Corporation operates. In addition, in order to comply with the SEC rules regarding the Corporation s operating structure the Corporation has incurred legal fees associated with the proposed corporate reorganization of its SBIC subsidiary.

Net Realized Gains and Losses on Investments

Comparison of the years ended December 31, 2008 and 2007

	December 31, 2008	**December 31, 2007**	**Change**
Net Realized (Loss)		$ (68,748)	$ 68,748

There were no realized gains or losses during the year ended December 31, 2008.

During the year ended December 31, 2007, the Corporation recognized a net realized loss of $68,748, comprised of a gain on the sale of Ramsco warrants for $555,000, a gain of $140,048 on its investment in Allworx Corp. (Allworx), a loss on the Topps investment of ($595,000), a loss of ($130,000) on Takeform, Inc. (Takeform), a loss on UStec of ($39,236) and a minor gain of $440 on a public security.

In the second quarter of 2007 Ramsco completed a refinancing of its commercial debt. As part of this restructuring Ramsco was able to pay off the outstanding debenture instrument owed to the Corporation and repurchase half of the Corporation s outstanding warrants. The Corporation recognized a $555,000 gain on the transaction.

The Corporation made an investment in the capital stock of Allworx in the second quarter of 2007 and the portfolio company merged with PAETEC Holding, Inc. in the fourth quarter of 2007. In conjunction with the merger, Allworx repaid its debenture instrument and purchased the outstanding equity held by the Corporation for $640,048, resulting in a $140,048 realized gain.

During 2007 the Corporation recognized a realized loss of $595,000 on its investment in Topps when the plant that produces its frozen meat products was forced to recall its frozen hamburger products. Topps announced in October 2007 that due to the economic impact of the recall it would close the Elizabeth, NJ plant and file for bankruptcy.

The Corporation reclassed its $130,000 loss in Takeform from unrealized to realized in the fourth quarter of 2007 following the repayment of its obligation. The portfolio company had agreed to pay $20,000 of its $150,000 debenture instruments and it satisfied this obligation to the Corporation.

UStec satisfied its $350,000 debenture instrument obligation by a payment of $310,764, which gave rise to a $39,236 realized loss

Comparison of the years ended December 31, 2007 and 2006

	December 31, 2007	December 31, 2006	Change
Net Realized (Loss) Gain	$ (68,748)	$ 3,456,441	$ (3,525,189)

During the year ended December 31, 2007, the Corporation recognized a net realized loss of ($68,748), comprised of a gain on the sale of Ramsco warrants for $555,000, a gain of $140,048 on its investment in Allworx, a loss on the Topps investment of ($595,000), a loss of ($130,000) on Takeform, a loss on UStec of ($39,236) and a minor gain of $440 on a public security.

During the year ended December 31, 2006, the Corporation sold a portion of its shares in Innov-X and recognized a realized gain of $2,280,682 on the sale.

Furthermore, the Corporation sold its remaining 677,981 shares of Minrad during 2006 and recognized a gain of $1,256,759. The average sales price of Minrad was $3.26/share and the basis of the stock was $1.36/share. The Corporation incurred $33,899 in broker transaction fees that were netted against the realized gain. In addition, the Corporation sold its interest in Vanguard during 2006 and recognized an ($81,000) loss on the disposition.

Net Change in Unrealized Appreciation of Investments

For the years ended December 31, 2008 and 2007

	December 31, 2008	December 31, 2007	Decrease	% Decrease
Net Change in Unrealized Appreciation	$ 601,985	$ 3,521,821	$ (2,919,836)	(82.9)%

The increase in unrealized appreciation on investments of $601,985 is due to the following valuation changes made by the Corporation:

	December 31, 2008
Gemcor	$ 1,700,000
Kionix	778,432
Bioworks, Inc. (Bioworks)	(28,000)
Wineisit	(100,000)
Niagara Dispensing	(111,000)
Photonics Products Group, Inc (Photonics)	(150,700)
Carolina Skiff	(227,000)
Golden Goal, LLC (Golden Goal)	(237,413)
APF	(307,334)
Rocket Broadband	(715,000)
Total Change in net Unrealized Appreciation during the year ended December 31, 2008	$ 601,985

The Corporation recognized appreciation on its equity investment in Gemcor based on the improved financial condition of the portfolio company since the Corporation made its first investment.

Kionix was written up in accordance with FAS 157 due to overall improvement in the revenues, customer base and the market acceptance of its products.

The Corporation s investment in Bioworks was valued at zero at December 31, 2008 based on an analysis of the liquidation preferences of senior securities in the portfolio company.

The Wineisit investment was revalued to zero during the year ended December 31, 2008 after a review by management indicated a further deterioration of the portfolio company s business. Wineisit remains in operation and is developing a new business strategy.

The Corporation converted its debt instruments in Niagara Dispensing to equity during the second quarter of 2008 and revalued its investment in based on the valuation of equity shares at conversion.

Photonics is a publicly traded stock (NASDAQ symbol: PHPG.OB) and is marked to market at the end of each quarter.

The Corporation s investment in Carolina Skiff was written down to cost based on a review of the company s financials and an overall economic downturn in the boating sector.

Rocket Broadband continued to have inadequate cash flow to sustain its operations throughout 2008. This resulted in the resignation of its Chief Executive Officer during the fourth quarter of 2008. While Rocket Broadband has been able to continue operations and maintain its base of customers it is seeking additional strategic opportunities, which may include a merger or sale of the company. Based on a review of the financial restructuring necessary to maintain the portfolio company s operations, the Corporation has recognized unrealized depreciation on its investment in Rocket Broadband and valued its investment at zero. The Corporation s valuation, if any, may be adjusted as it obtains more information about the ultimate structure and amount of the financing that Rocket Broadband is able to secure.

The Corporation s investment in Golden Goal and APF were written down during 2008 based on a review of the companies financials, their weak financial performance as compared to plan, and an overall economic downturn in their respective industries.

Synacor filed an S-1 registration statement on August 2, 2007 with the SEC and also filed an amended S-1 in April 2008. An S-1 is a registration document that a company files with the SEC regarding the proposed sale of its securities to the public. In October 2008 Synacor withdrew its S-1 plans for a public offering in a notification filed with the SEC. No valuation change has occurred with respect to the Synacor filings, but the Corporation has previously written up its investment in Synacor based on new investor financing. The company s actual financial performance continues to support the valuation.

All of these value adjustments resulted from a review by management using the guidance set forth by SFAS 157 and the Corporation s established valuation policy.

For the years ended December 31, 2007 and 2006

	December 31, 2007	**December 31, 2006**	**Decrease**	**% Decrease**
Net Change in Unrealized Appreciation	$ 3,521,821	$ 9,958,053	$ (6,436,232)	(64.6)%

The increase in unrealized appreciation on investments of $3,521,821 was due to the following valuation changes made by the Corporation:

	December 31, 2007
Increase Gemcor valuation	$ 3,500,000
Reclass Takeform to a realized loss	130,000
Increase Photonics valuation	119,480
Adampluseve warrants	65,341
Reclass USTec to realized loss	39,000
Reclass Topps to realized loss	(332,000)
Total Change in net Unrealized Appreciation during the year ended December 31, 2007	$ 3,521,821

The Corporation recognized appreciation on its equity investment in Gemcor based on the improved financial condition of the portfolio company since the Corporation made its first investment. Per the Corporation s valuation policy, a portfolio company can be valued based on a conservative financial measure if the portfolio company has been self-financing and has had positive cash flow from operations for at least the past two fiscal years.

The Topps investment was valued to zero during the third quarter of 2007 when the plant that produces its frozen meat products was forced to recall its frozen hamburgers products. Topps announced on October 5, 2007 that because of the economic impact of the recall it closed its Elizabeth, NJ plant and subsequently the company filed for bankruptcy. The Corporation, therefore, realized a total loss on the investment in the fourth quarter of 2007 and removed the $332,000 of unrealized appreciation on Topps that had been previously recorded.

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The Corporation recognized appreciation on its remaining equity investment in Adampluseve which participated in a round of financing in January 2007 that enabled it to pay off the Corporation s debenture instrument prior to the maturity date. The Corporation still holds warrants in Adampluseve, the value of which was adjusted based on the pricing of this recent round of financing.

USTec and Takeform satisfied their obligations to the Corporation during 2007 and therefore any unrealized appreciation (depreciation) was reclassified to a realized gain (loss).

Photonics is a publicly traded stock (NASDAQ symbol: PHPG.OB) and is marked to market at the end of the year.

All of these value adjustments were done in accordance with the Corporation s established valuation policy.

Net Increase (Decrease) in Net Assets from Operations

The Corporation accounts for its operations using Generally Accepted Accounting Practices (GAAP) for investment companies. The principal measure of its financial performance is net increase (decrease) in net assets from operations on its consolidated statements of operations. During the year ended December 31, 2008, the net increase was $409,143, as compared to a net increase in net assets from operations of $2,719,165 in 2007 and a net increase of $8,166,471 in 2006.

The net increase in net assets from operations for the year ended December 31, 2008 is due to the net unrealized appreciation on investments of $273,454 and the net investment gain of $135,689. The net increase in net assets from operations for the year ended December 31, 2007 can be attributed to the investment gain before income taxes of $651,923 and the net unrealized gain on investments of $2,362,507. In addition, the Corporation recognized a $316,253 increase in net assets attributed to the cumulative effect adjustment upon adopting the provisions of FIN 48 Accounting for Uncertainty in Income Taxes . The net increase for the year ended December 31, 2006 is due to the $9,431,273 net realized and unrealized gain on investments.

Liquidity and Capital Resources

The Corporation s principal objective is to achieve capital appreciation. Therefore, a significant portion of the investment portfolio is structured to maximize the potential for capital appreciation and certain of the Corporation s portfolio investments may be structured to provide little or no current yield in the form of dividends or interest payments.

As of December 31, 2008, the Corporation s total liquidity, consisting of cash and cash equivalents, was $2,757,653.

Net cash used in operating activities has averaged approximately $469,000 over the last three years and management anticipates cash will continue to be utilized at similar levels. The cash flow may fluctuate based on possible expenses associated with compliance with new regulations.

The Corporation used approximately $925,000 in net cash flow from investing activities in fiscal 2008. The Corporation realized approximately $545,000 in net cash flow from investing activities of for fiscal year 2007 and approximately $2.5 million of cash for investing activities in fiscal year 2006. The Corporation will generally use cash in investing activities as it builds its portfolio utilizing its available cash and proceeds from liquidations of portfolio investments. The Corporation anticipates that it will continue to make new investments and may experience a net use of cash over the next two years. In addition, significant liquidating events within the Corporation s investment portfolio are difficult to determine with any certainty.

The Corporation had paid $100,000 to the SBA to reserve its approved $10,000,000 leverage. The Corporation has drawn down $8,100,000 of this leverage as of December 31, 2008. The remaining leverage commitment of $1.9 million expired on September 30, 2008.

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The following table summarizes the cash to be received over the next five years from portfolio companies based on contractual obligations as of December 31, 2008. These payments represent scheduled principal and interest payments that are contained in the investment documents of each portfolio company.

	Cash Receipts due by year				
	2009	**2010**	**2011**	**2012**	**2013 and beyond**
Scheduled Cash Receipts from Portfolio Companies	$ 235,500	$ 1,646,000	$ 2,700,000	$ 918,000	$ 0

The preceding table only includes debenture instruments and does not include any equity investments which may provide additional proceeds upon exit of these securities.

During late 2007 and throughout 2008, the global economy experienced severe turmoil. Therefore, the debt and equity markets in the United States have been affected by this crisis. If market conditions continue to deteriorate, the Corporation may suffer losses on its investment portfolio, which could impact cash receipts over the next couple of years.

The unfavorable change in credit market conditions also has created opportunities for capital providers, like the Corporation, because small business are selling for lower prices, and they are generally willing to pay higher interest rates and to accept more contractual terms that are more favorable to us in their investment agreements. Accordingly, for firms that continue to have access to capital, management believes that the current environment could provide investment opportunities on more favorable terms than have been available in prior periods. Because the Corporation has used its available SBA leverage, in the short term, if the Corporation requires significant additional capital to take advantage of current investment opportunities, it will need to rely primarily on its ability to make public or private offerings of Rand s common stock. Although the Corporation currently has no specific plans as to the timing or amount of any common stock offering it might make, it is considering the possibility of making such an offering during the next year in order to raise additional capital to pursue favorable investment opportunities.

Any common stock offering that the Corporation may make will be need to be based upon the market price of its currently outstanding shares. As a regulated BDC, the Corporation is generally prohibited from selling its common shares at prices that are less than the NAV of its common stock at the time of the sale. The Corporation s common stock sold in the NASDAQ market at a premium to net asset value during 2007, but during most of 2006 and 2008 its stock sold in a range that was below current per share NAV. In order to permit the Corporation to sell its common stock at prices below current net asset value if a majority of the Directors of the Corporation who are not interested persons (as defined under the Investment Company Act) make a specific determination that such a sale would be in the best interests of the Corporation, it is seeking approval by shareholder vote at its annual meeting of a one-year exemption from the provisions of the Investment Company Act that would otherwise prohibit it from making sales of its common stock at less than NAV per share.

The inability to raise capital through timely sales of common stock could also have the effect of forcing the Corporation to sell assets that it would not otherwise sell, and such sales could occur at times that are disadvantageous to sell.

Management expects that the cash and cash equivalents at December 31, 2008, coupled with the scheduled interest and dividend payments on its portfolio investments, will be sufficient to meet the Corporation s cash needs throughout

2009. The Corporation is also evaluating potential exits from portfolio companies and sale of its common stock to increase the amount of liquidity available for new investments and operating activities. The potential sale of stock or portfolio assets is subject to inherent market risks and volatility, which may affect the ability of the Corporation to complete these sales and provide cash to the Corporation over the next twelve months.

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Disclosure of Contractual Obligations

The following table shows the Corporation s contractual obligations at December 31, 2008. The Corporation does not have any capital lease obligations or other long-term liabilities reflected on its balance sheet.

		Payments due by period			
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 yrs
SBA Debentures	$ 8,100,000	$ 0	$ 0	$ 0	$ 8,100,000
Operating Lease Obligations (Rent of office space)	$ 32,520	$ 16,080	$ 16,440	$ 0	$ 0
Total	$ 8,132,520	$ 16,080	$ 16,440	$ 0	$ 8,100,000

Item 7A. *Quantitative and Qualitative Disclosures about Market Risk*

The Corporation s investment activities contain elements of risk. The portion of the Corporation s investment portfolio consisting of equity and debt securities in private companies is subject to valuation risk. Because there is typically no public market for the equity and equity-linked debt securities in which it invests, the valuation of the equity interests in the portfolio is stated at fair value as determined in good faith by the Board of Directors in accordance with the Corporation s investment valuation policy. (The discussion of valuation policy contained in the Notes to Schedule of Portfolio Investments in the consolidated financial statements contained in Item 8 of this report is hereby incorporated herein by reference.) In the absence of a readily ascertainable market value, the estimated value of the Corporation s portfolio may differ significantly from the values that would be placed on the portfolio if a ready market for the investments existed. Any changes in valuation are recorded in the Corporation s consolidated statement of operations as Net unrealized appreciation on investments.

At times a portion of the Corporation s portfolio may include marketable securities traded in the over-the-counter market. In addition, there may be a portion of the Corporation s portfolio for which no regular trading market exists. In order to realize the full value of a security, the market must trade in an orderly fashion or a willing purchaser must be available when a sale is to be made. Should an economic or other event occur that would not allow markets to trade in an orderly fashion, the Corporation may not be able to realize the fair value of its marketable investments or other investments in a timely manner.

As of December 31, 2008, the Corporation did not have any off-balance sheet investments or hedging investments.

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Item 8. *Financial Statements and Supplementary Data*

The following consolidated financial statements and consolidated supplemental schedule of the Corporation and report of independent auditors thereon are set forth below:

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RAND CAPITAL CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
December 31,

	2008	2007
Assets		
Investments at fair value (identified cost: 2008 $14,386,451, 2007 $13,390,644)	**$ 28,126,282**	$ 26,528,490
Cash and cash equivalents	**2,757,653**	4,396,595
Interest receivable (net of allowance 2008 $122,817, 2007 $122,000)	**1,013,888**	647,001
Other assets	**330,974**	1,150,065
Total assets	**$ 32,228,797**	$ 32,722,151
Liabilities and Stockholders Equity (net assets)		
Liabilities:		
Debentures guaranteed by the SBA	**$ 8,100,000**	$ 8,100,000
Deferred tax liability	**3,490,000**	3,955,000
Income taxes payable	**98,723**	474,465
Accounts payable and accrued expenses	**292,731**	321,210
Deferred revenue	**20,377**	53,653
Total liabilities	**12,001,831**	12,904,328
Stockholders equity (net assets):		
Common stock, $.10 par; shares authorized 10,000,000; shares issued 5,763,034	**576,304**	576,304
Capital in excess of par value	**6,973,454**	6,973,454
Accumulated net investment (loss)	**(3,743,908)**	(3,940,409)
Undistributed net realized gain on investments	**7,735,477**	7,796,289
Net unrealized appreciation on investments	**8,732,845**	8,459,391
Treasury stock, at cost, 44,100 shares	**(47,206)**	(47,206)
Net assets (per share 2008 $3.54 , 2007 $3.47)	**20,226,966**	19,817,823
Total liabilities and stockholders equity (net assets)	**$ 32,228,797**	$ 32,722,151

See accompanying notes

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RAND CAPITAL CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
For The Years Ended December 31, 2008, 2007 and 2006

	2008	2007	2006
Investment income:			
Interest from portfolio companies	**$ 608,180**	$ 618,430	$ 757,824
Interest from other investments	**90,660**	173,664	53,104
Dividend and other investment income	**1,027,377**	1,469,864	432,296
Other income	**30,786**	40,912	83,738
	1,757,003	2,302,870	1,326,962
Operating expenses:			
Salaries	**440,337**	460,917	482,067
Employee benefits	**121,659**	112,147	101,785
Directors fees	**77,250**	77,750	59,500
Professional fees	**248,667**	212,822	116,068
Stockholders and office operating	**120,260**	122,332	108,687
Insurance	**41,489**	43,674	43,674
Corporate development	**65,042**	66,854	54,233
Other operating	**83,972**	51,389	10,769
	1,198,676	1,147,885	976,783
Interest on SBA obligations	**522,062**	503,062	472,526
Bad debt expense	**817**		69,875
Total expenses	**1,721,555**	1,650,947	1,519,184
Investment gain (loss) before income taxes	**35,448**	651,923	(192,222)
Current income tax expense	**672,290**	901,511	401,801
Deferred income tax (benefit) expense	**(772,531)**	(674,994)	670,779
Net investment gain (loss)	**135,689**	425,406	(1,264,802)
Realized and unrealized gain (loss) on investments:			
Net realized (loss) gain on sales and dispositions		(68,748)	3,456,441
Unrealized appreciation (depreciation) on investments:			
Beginning of year	**13,137,846**	9,616,025	(342,028)
End of year	**13,739,831**	13,137,846	9,616,025
Change in unrealized appreciation (depreciation) before income taxes	**601,985**	3,521,821	9,958,053
Deferred income tax expense	**328,531**	1,159,314	3,983,221
Net increase in unrealized appreciation	**273,454**	2,362,507	5,974,832

Net realized and unrealized gain on investments		**273,454**		2,293,759		9,431,273
Net increase in net assets from operations	**$**	**409,143**	$	2,719,165	$	8,166,471
Weighted average shares outstanding		5,718,934		5,718,934		5,718,934
Basic and diluted net increase in net assets from operations per share	$	0.07	$	0.48	$	1.43

See accompanying notes

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RAND CAPITAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS
For The Years Ended December 31, 2008, 2007 and 2006

	2008	2007	2006
Net assets at beginning of period	**$ 19,817,823**	$ 16,782,405	$ 8,615,934
Net investment gain(loss)	**135,689**	425,406	(1,264,802)
Cumulative effect adjustment for uncertain tax positions FIN 48		316,253	
Net realized (loss) gain on sales and dispositions of investments		(68,748)	3,456,441
Net increase in unrealized appreciation	**273,454**	2,362,507	5,974,832
Net increase in net assets from operations	**409,143**	3,035,418	8,166,471
Net assets at end of period	**$ 20,226,966**	$ 19,817,823	$ 16,782,405

See accompanying notes.

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RAND CAPITAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
For The Years Ended December 31, 2008, 2007 and 2006

	2008	2007	2006
Cash flows from operating activities:			
Net increase in net assets from operations	$ 409,143	$ 2,719,165	$ 8,166,471
Adjustments to reconcile net increase in net assets to net cash used in operating activities:			
Depreciation and amortization	52,230	33,598	26,672
Original issue discount accretion		(62,333)	
Change in interest receivable allowance	817		
Increase in unrealized appreciation of investments	(601,985)	(3,521,821)	(9,958,053)
Deferred tax (benefit) expense	(465,000)	484,453	4,654,000
Net realized loss (gain) on portfolio investments		68,748	(3,456,441)
Payment in kind, interest accrued	(15,380)		
Non-cash conversion of debenture interest	(67,235)	(50,000)	(34,356)
Changes in operating assets and liabilities:			
(Increase) in interest receivable	(367,704)	(139,759)	(209,623)
Decrease (increase) in other assets	779,083	(35,229)	42,440
(Decrease) increase in income taxes payable	(375,742)	63,890	
(Decrease) increase in accounts payable and accrued liabilities	(28,479)	(17,350)	560,246
(Decrease) increase in deferred revenue	(33,276)	8,048	(34,278)
Total adjustments	(1,122,671)	(3,167,755)	(8,409,393)
Net cash used in operating activities	(713,528)	(448,590)	(242,922)
Cash flows from investing activities:			
Investments originated	(1,626,657)	(2,165,266)	(3,383,769)
Proceeds from sale of portfolio investments		255,440	4,374,762
Proceeds from loan repayments	713,465	2,456,509	1,473,322
Capital expenditures	(12,222)	(1,350)	(12,255)
Net cash (used in) provided by investing activities	(925,414)	545,333	2,452,060
Cash flows from financing activities:			
Proceeds from SBA debenture			900,000
Origination costs to SBA			(19,125)
Net cash provided by financing activities			880,875
Net (decrease) increase in cash and cash equivalents	(1,638,942)	96,743	3,090,013
Cash and cash equivalents:			
Beginning of year	4,396,595	4,299,852	1,209,839
End of year	$ 2,757,653	$ 4,396,595	$ 4,299,852

See accompanying notes

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RAND CAPITAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED SCHEDULE OF PORTFOLIO INVESTMENTS
December 31, 2008

Geographic Location, Business Description, (Industry) e	Type of Investment	(b) Date Acquired	(c) Equity	Cost	(d) Value
ol/Non-Affiliate Investments: (k)					
ve, Inc. (dba Adam) (g) NY. Luxury sports wear designer for men and women. sign) www.shopadam.com	Warrants to purchase 1,715 Series A convertible preferred shares.	7/14/06	2%	$ 68,000	$ 133,341
ystems, Inc. (e) (g) NY. Provider of database automation software that helps gain control of their heterogeneous database applications ntralized software console. (Software) www.gridapp.com	$660,000 term note at 4% simple interest, 8% deferred interest (PIK) due January 4, 2012. $6,667 convertible note at 4% due November 28, 2018.	11/25/08	3%	666,667	666,667
. Develops innovative micro-electronic mechanical systems sed inertial sensors used in consumer electronics, and healthcare sectors. (Manufacturing) .com	30,241 shares Series B preferred stock. 696,296 shares Series C preferred stock. (g) 2,862,091 shares Series A preferred stock. 714,285 shares Series B preferred stock.	5/17/02	2%	1,506,043	2,000,000
Inc. (g) Developer of micro mirror technology that replaces silicon fibers in MEMS enabling efficient, wide-angle, Pico be embedded in mobile devices. (Electronics Developer) eriz.com	$100,000 convertible note at 9% due January 9, 2010.	1/9/08		100,000	100,000
roducts Group, Inc (OTC:PHPG.OB) (a) (i) Northvale, s and manufactures products for laser photonics industry. ring) www.inrad.com	66,000 shares common stock.	10/31/00	<1%	165,000	112,000
as Transmission Company, LLC (e) OH. Natural gas transportation company. (Oil and Gas) setgas.com	26.5337 units.	7/10/02	2%	719,097	786,748
c. (g) . Develops provisioning platforms for aggregation and content and services across multiple digital devices. or.com	234,558 Series A preferred shares. 600,000 shares of Series B preferred shares. 240,378	11/18/02	4%	1,349,479	4,168,001

	Series C preferred shares. 897,438 common shares.		
on-Control/ te Investments		$ 4,574,286	$ 7,966,757

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RAND CAPITAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED SCHEDULE OF PORTFOLIO INVESTMENTS
December 31, 2008 (Continued)

Company and Business	Type of Investment	(b) Date Acquired	(c) Equity		Cost		(d) Value		Per Share of Rand
Affiliate Investments: (l) **APF Group, Inc. (e) (g)** Yonkers, NY. Manufacturer of museum quality picture frames and framed mirrors for museums, art galleries, retail frame shops, upscale designers and prominent collectors. (Manufacturing) www.apfgroup.com	$587,786 consolidated senior subordinated note at 8% due June 30, 2011. $13,514 senior subordinated note at 14% due June 30, 2011. Warrants to purchase 10.2941 shares of common stock.	7/8/04	6%	$	607,335	$	300,000	$	.05
Associates Interactive, LLC (e) (g) Buffalo, NY. Provider of training content and certifications used to train retail sales associates. (Education and Training) www.associatesinteractive.com	$247,813 promissory note at 9% due December 19, 2012. Investor units totaling 21.88% of company.	10/15/07	22%		250,000		250,000		.04
Carolina Skiff LLC (e) (g) Waycross, GA. Manufacturer of fresh water, ocean fishing and pleasure boats. (Manufacturing) www.carolinaskiff.com	$985,000 Class A preferred membership interest at 7.5%. Redeemable January 31, 2010. 5% common membership interest. (j) Interest receivable $638,693.	1/30/04	5%		1,000,000		1,000,000		.18
EmergingMed.com, Inc. (g) New York, NY. Cancer clinical trial matching and referral service. (Software) www.emergingmed.com	$500,000 senior subordinated note at 10% due December 19, 2010. Warrants for 5.5% of common stock. (j) Interest receivable $151,667.	12/19/05	7%		500,000		500,000		.09
		12/10/07	6%		637,414		400,000		.07

Golden Goal LLC (g) Fort Ann, NY. Youth soccer and lacrosse tournament park. (Sports and Entertainment) www.goldengoalpark.com	191,811 Class C units at 4%.					
Innov-X Systems, Inc. (g) Woburn, MA. Manufactures portable x-ray fluorescence (XRF) analyzers used in metals/alloy analysis. (Manufacturing) www.innovxsys.com	2,642 Series A convertible preferred stock. Warrants for 21,596 common shares. 8% cumulative dividend. (j) Interest receivable $162,411.	9/27/04	9%	1,000,000	8,761,700	1.54
Niagara Dispensing Technologies, Inc. (e) Amherst, NY. Beverage dispensing technology development and products manufacturer, specializing in rapid pour beer dispensing systems for high volume stadium and concession operations. (Manufacturing) www.exactpour.com	202,081 Series B preferred stock. (g) 463,691 Series A preferred stock. 518,752 Series B preferred stock.	3/8/06	14%	1,281,783	1,170,783	.20

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RAND CAPITAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED SCHEDULE OF PORTFOLIO INVESTMENTS
December 31, 2008 (Continued)

Company and Business	Type of Investment	(b) Date Acquired	(c) Equity	Cost	(d) Value	Per Share of Rand
RAMSCO (e) (g) Albany, NY. Distributor of water, sanitary, storm sewer and specialty construction materials to the contractor, highway and municipal construction markets. (Distributor) www.ramsco.com	$300,000 promissory notes at 9% due October 20, 2010. Warrants for 5.99% of common stock.	11/19/02	6%	300,000	300,000	.05
SOMS Technologies, LLC (g) Valhalla, NY. Produces and markets the microGreen Extended Performance Oil Filter. (Auto Parts Developer) www.microgreenfilter.com	$250,000 secured convertible note at 10% due December 2, 2010.	12/2/08		250,000	250,000	.04
Ultra Scan Corporation Amherst, NY. Biometrics application developer of ultrasonic fingerprint technology. (Electronics Hardware/Software) www.ultra-scan.com	536,596 common shares. 107,104 Series A-1 preferred shares. (g) 95,284 Series A-1 preferred shares.	12/11/92	4%	938,164	1,203,000	.21
Subtotal Affiliate Investments				$ 6,764,696	$ 14,135,483	$ 2.47
Control Investments(m)						
Gemcor II, LLC (e) (g) (h) West Seneca, NY. Designs and sells automatic riveting machines used in the assembly of aircraft components. (Manufacturing) www.gemcor.com	$250,000 subordinated note at 8% due June 28, 2010 with warrant to purchase 6.25 membership units. 25 membership units.	6/28/04	31%	603,200	5,803,201	1.02

G-TEC Natural Gas Systems Buffalo, NY. Manufactures and distributes systems that allow natural gas to be used as an alternative fuel to gases. (Manufacturing) www.gas-tec.com	28.925% Class A membership interest. 8% cumulative dividend.	8/31/99	29%	400,000	198,000	.03
Subtotal Control Investments				$ 1,003,200	$ 6,001,201	$ 1.05
Other Investments (e)	Various			2,044,269	22,841	.00
	Total portfolio investments (f)			$ 14,386,451	$ 28,126,282	$ 4.92

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RAND CAPITAL CORPORATION AND SUBSIDIARIES

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