American Homes 4 Rent
Form S-11/A
December 11, 2013
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As filed with the Securities and Exchange Commission on December 11, 2013

Registration No. 333-192592

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

Amendment No. 1

to

FORM S-11

FOR REGISTRATION UNDER

THE SECURITIES ACT OF 1933 OF SECURITIES

OF CERTAIN REAL ESTATE COMPANIES

AMERICAN HOMES 4 RENT

(Exact name of registrant as specified in governing instruments)

30601 Agoura Road, Suite 200

Agoura Hills, California 91301

(805) 413-5300

(Address, including zip code, and telephone number, including area code, of registrant s principal executive offices)

Sara H. Vogt-Lowell

Senior Vice President and Chief Legal Officer

American Homes 4 Rent

30601 Agoura Road, Suite 200

Agoura Hills, California 91301

(805) 413-5300

(Name, address, including zip code, and telephone number, including area code, of agent for service)

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Approximate date of commencement of proposed sale to the public: As soon as practicable after the effective date of this Registration Statement.

If any of the Securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act, check the following box: ¨

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If delivery of the prospectus is expected to be made pursuant to Rule 434, check the following box. ¨

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

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

The registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment which specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, as amended, or until this registration statement shall become effective on such date as the Commission, acting pursuant to Section 8(a), may determine.

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The information in this preliminary prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This preliminary prospectus is not an offer to sell these securities and it is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

Subject to Completion, dated December 11, 2013

PROSPECTUS

4,000,000 SHARES

5.000% SERIES B PARTICIPATING PREFERRED SHARES

American Homes 4 Rent is an internally managed Maryland real estate investment trust, or REIT, focused on acquiring, renovating, leasing and operating single-family homes as rental properties. We are selling 4,000,000 shares of our 5.000% Series B participating preferred shares of beneficial interest, $0.01 par value per share, or our Series B Participating Preferred Shares, in this offering. This is the original issuance of our Series B Participating Preferred Shares. The following is a summary of key terms of our Series B Participating Preferred Shares:

Liquidation Preference and Home Price Appreciation Amount. The Series B Participating Preferred Shares have an initial liquidation preference of $25.00 per share, or the initial liquidation preference, that may be increased by an additional Home Price Appreciation Amount, or the HPA Amount, that takes into account the cumulative change in value from September 30, 2013 of an index tracking the purchase prices of single-family homes located in our top 20 markets, by estimated total investment, as of September 30, 2013 and a constant investor participation percentage of 50%. The HPA Amount will be subject to a cap as described below and will become fixed and cease to accrue on and after December 31, 2020.

Dividends. We will pay quarterly cumulative dividends, in arrears, on our Series B Participating Preferred Shares from and including the date of original issuance on the last day of each March, June, September and December. The first dividend is scheduled to be paid on March 31, 2014 to record holders as of March 15, 2014. The dividend rate of 5.000% per annum will be applied to the initial liquidation preference from the issue date to but excluding December 31, 2020. Thereafter, a dividend rate of 10.000% per annum will be applied to the initial liquidation preference plus the HPA Amount.

Redemption at Our Option. After December 31, 2017, we may redeem for cash all but not less than all of the Series B Participating Preferred Shares by paying the liquidation preference (including any HPA Amount), plus any accrued and unpaid dividends, to, but excluding, the redemption date.

Conversion at Our Option. After December 31, 2017, we may convert all but not less than all of the Series B Participating Preferred Shares into our Class A common shares of beneficial interest, $0.01 par value per share, or our Class A common shares, using a conversion ratio per Series B Participating Preferred Share equal to (i) the sum of the initial liquidation preference and the HPA Amount, plus any accrued and unpaid dividends to, but excluding, the conversion date (to occur on the fourth business day following the notice of conversion), divided by (ii) the one-day volume-weighted average trading price, or the VWAP, of our Class A common shares on the New York Stock Exchange, or NYSE, as reported by Bloomberg, if available, on the date the notice of conversion is issued.

Cap. Until December 31, 2020, the amount payable upon any redemption, conversion or liquidation event will be subject to a cap such that the total internal rate of return when considering the initial liquidation preference, the HPA Amount and all dividends (whether paid or accrued) on the Series B Participating Preferred Shares will not exceed 9.0%.

Change of Control. If there is a Change of Control (as defined), holders of Series B Participating Preferred Shares will have certain conversion rights, subject to our right to redeem the Series B Participating Preferred Shares.

No current market exists for our Series B Participating Preferred Shares. We intend to apply to list the Series B Participating Preferred Shares on the NYSE under the symbol AMHPRB. If the listing application is approved, we expect trading of the Series B Participating Preferred Shares to commence within 30 days after initial delivery of the shares.

We are an emerging growth company under the U.S. federal securities laws and are subject to reduced public company reporting requirements. Investing in our Series B Participating Preferred Shares involves risks. See Risk Factors beginning on page 31 for factors you should consider before investing in our Series B Participating Preferred Shares.

	Per Share	Total
Public offering price	$ 25.00	$ 100,000,000
Underwriting discounts and commissions(1)	$	$
Proceeds, before expenses, to us	$	$

(1) We refer to you to Underwriting beginning on page 221 of this prospectus for additional information regarding underwriter compensation.
We have granted the underwriters an option to purchase up to an additional 600,000 Series B Participating Preferred Shares from us at the public offering price, less the underwriting discount, within 30 days after the date of this prospectus.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The underwriters expect to deliver the Series B Participating Preferred Shares through The Depository Trust Company on or about , 2013, which is the business day following the pricing of this offering.

Raymond James **Jefferies** **Citigroup**

Keefe, Bruyette & Woods
A Stifel Company

Credit Suisse

Prospectus dated , 2013

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You should rely only on the information contained in this prospectus, any free writing prospectus prepared by us or other information to which we have referred you. We have not, and the underwriters have not, authorized anyone to provide you with different or additional information. If anyone provides you with different or inconsistent information, you should not rely on it. We are not, and the underwriters are not, making an offer to sell these securities in any jurisdiction where the offer or sale is not permitted. The information in this prospectus and any free writing prospectus is current only as of their respective dates or on the date or dates that such information is presented. Our business, financial condition, results of operations, and prospects may have changed since those dates.

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Market, Industry and Other Data

We have obtained certain market and industry data from publicly available industry publications. These sources generally state that the information they provide has been derived from sources believed to be reliable, but that the accuracy and completeness of the information are not guaranteed. We believe that this data is generally reliable, but we have not independently verified this information.

Certain Terms Used in This Prospectus

Unless the context otherwise requires or indicates, we define certain terms in this prospectus as follows:

We, our company, the Company, the REIT, our and us refer to American Homes 4 Rent, a Maryland real estate investment trust, and its subsidiaries taken as a whole (including our operating partnership and its subsidiaries).

Our operating partnership refers to American Homes 4 Rent, L.P., a Delaware limited partnership, and its subsidiaries taken as a whole.

AH LLC refers to American Homes 4 Rent, LLC, a Delaware limited liability company formed by B. Wayne Hughes, our founder and chairman of our board of trustees.

Alaska Joint Venture refers to an investment vehicle between AH LLC and the Alaska Permanent Fund Corporation, acting for and on behalf of the funds that the Alaska Permanent Fund Corporation is designated by Alaska Statutes 37.13 to manage and invest, or APFC.

Alaska Joint Venture Acquisition refers to our operating partnership s acquisition of the Alaska Joint Venture on June 11, 2013. Unless the context otherwise requires or indicates, all references to our business, our portfolio and our acquisition and management activities reflect the completion of the Alaska Joint Venture Acquisition. See Certain Relationships and Related Party Transactions for more information on the Alaska Joint Venture Acquisition.

Our former manager refers to our former external manager and advisor, American Homes 4 Rent Advisor, LLC, a Delaware limited liability company previously wholly owned by AH LLC, that became wholly owned by us following the Management Internalization.

Our former property manager refers to American Homes 4 Rent Management Holdings, LLC, a Delaware limited liability company previously wholly owned by AH LLC, that became wholly owned by us following the Management Internalization.

AH LLC Portfolio refers to the 2,770 single-family homes that we purchased from AH LLC on February 28, 2013.

Acquisition cost means:

- with respect to single-family homes in the AH LLC Portfolio, AH LLC s actual purchase price of the property (including closing and other title or escrow costs), without giving effect to the $491.7 million maximum agreed upon valuation of the AH LLC Portfolio under the terms of the contribution agreement pursuant to which we acquired the portfolio.

- with respect to all other single-family homes, the actual purchase price of the property (including broker commissions and closing costs) plus a 5% acquisition fee.

Concurrent private placements refer to AH LLC s purchase of 3,125,000 of our Class A common shares and APFC s purchase of 1,562,500 of our Class A common shares in private placements. The concurrent private placements closed on the same day as our initial public offering.

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Estimated renovation costs refer to the costs incurred or expected to be incurred in preparing the property for rent plus a 5% renovation fee payable to AH LLC. Estimated renovation costs represent the total costs to renovate a property to prepare it for rental. These costs typically include paint, flooring, appliances, blinds and landscaping.

Estimated total investment means the sum of the property s acquisition cost plus its estimated renovation costs payable to AH LLC.

Management Internalization refers to our operating partnership s acquisition of our former manager and our former property manager from AH LLC on June 10, 2013, at which time all administrative, financial, property management and marketing and leasing personnel, including executive management became our fully dedicated personnel. Acquisition and renovation personnel remain personnel of AH LLC but are exclusively dedicated to us until December 10, 2014. Unless the context otherwise requires or indicates, all references to our business, our portfolio and our acquisition and management activities reflect the completion of the Management Internalization and include the acquisition and management activities of AH LLC, our former manager and our former property manager. See Certain Relationships and Related Party Transactions for more information on the Management Internalization.

RJ joint ventures refers to two investment vehicles with accredited investors identified by Raymond James & Associates, Inc. in which we own an approximately one-third interest.

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PROSPECTUS SUMMARY

This summary highlights information contained elsewhere in this prospectus, but it does not contain all of the information that you may consider important in making your investment decision. Therefore, you should read the entire prospectus carefully, including, in particular, the Risk Factors section beginning on page 31 of this prospectus, as well as the financial statements and related notes included elsewhere in this prospectus.

Overview

We are an internally managed Maryland real estate investment trust, or REIT, focused on acquiring, renovating, leasing and operating single-family homes as rental properties. We commenced operations in November 2012 to continue the investment activities of AH LLC, which was founded by our chairman, B. Wayne Hughes, in 2011 to take advantage of the dislocation in the single-family home market. Mr. Hughes has over 40 years of experience in the real estate business and a successful track record as co-founder and former chairman and chief executive officer of Public Storage, a REIT listed on the New York Stock Exchange, or the NYSE. We have an integrated operating platform that consists of approximately 401 personnel dedicated to property management, marketing, leasing, financial and administrative functions. Our acquisition and renovation functions are performed by AH LLC, to whom we will continue to pay an acquisition and renovation fee through December 2014.

As of September 30, 2013, we owned 21,267 single-family properties for an estimated total investment of approximately $3.6 billion and had an additional 416 properties in escrow that we expected to acquire, subject to customary closing conditions, for an estimated total investment of approximately $67.1 million. As of September 30, 2013, we owned properties in selected sub-markets of metropolitan statistical areas, or MSAs, in 22 states, and we continually evaluate potential new target markets that fit our underwriting criteria and are located where we believe we can achieve sufficient scale for internalized property management.

We intend to become a leader in the single-family home rental industry by aggregating a geographically diversified portfolio of high quality single-family homes and developing American Homes 4 Rent into a nationally recognized brand that is well-known for quality, value and tenant satisfaction and is well respected in our communities. Our objective is to generate attractive, risk-adjusted returns for our shareholders through dividends and capital appreciation.

We intend to use the net proceeds of this offering to continue to acquire and renovate single-family properties, including certain escrow properties, and to repay indebtedness we have incurred or expect to incur under our credit facility. In addition to single-family properties, we also may seek to invest in condominium units, townhouses and real estate-related debt investments. Our investments may be made directly or through investment vehicles with third-party investors. In addition to individual property purchases, we may pursue bulk acquisitions from financial institutions, government agencies and competitors.

We have been organized and operated in conformity with the requirements for qualification and taxation as a REIT under U.S. federal income tax laws, commencing with our taxable year ended December 31, 2012, and we expect to satisfy the requirements for qualification and taxation as a REIT under the U.S. federal income tax laws for our taxable year ending December 31, 2013, and subsequent taxable years.

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Our Properties

The table below summarizes certain information with respect to our properties as of September 30, 2013.

Our Properties[1]

									Averages per Property	
	Properties Owned		Estimated Total Investment (2) (3)			Total Book Value (4)				
Market	Units	% of Total	$ millions	% of Total	Avg. per Property	$ millions	% of Total	Avg. per Property	Square Footage	Property Age (years)
Dallas-Fort Worth, TX	1,861	8.8%	$ 297.1	8.2%	$ 159,569	$ 287.5	8.1%	$ 154,462	2,200	10.2
Indianapolis, IN	1,845	8.7%	269.3	7.5%	145,956	$ 267.4	7.6%	144,937	1,879	11.6
Greater Chicago area, IL and IN	1,443	6.8%	230.4	6.4%	159,650	$ 211.4	6.0%	146,525	1,855	12.3
Atlanta, GA	1,341	6.3%	231.8	6.4%	172,742	$ 216.7	6.1%	161,604	2,163	13.0
Houston, TX	1,094	5.1%	189.3	5.2%	173,050	$ 189.4	5.4%	173,135	2,303	9.6
Cincinnati, OH	1,075	5.1%	184.7	5.1%	171,768	$ 183.4	5.2%	170,564	1,845	11.9
Phoenix, AZ	962	4.5%	150.0	4.2%	155,881	$ 143.5	4.1%	149,210	1,811	11.3
Charlotte, NC	961	4.5%	164.7	4.6%	171,386	$ 162.8	4.6%	169,379	1,947	10.7
Nashville, TN	905	4.3%	188.4	5.2%	208,137	$ 181.1	5.1%	200,107	2,190	9.5
Jacksonville, FL	893	4.2%	134.6	3.7%	150,505	$ 129.4	3.7%	144,870	1,926	9.6
All Other (5)	8,887	41.7%	1,573.0	43.5%	177,058	$ 1,557.5	44.1%	175,312	1,904	10.9
Total / Average	**21,267**	**100.0%**	**$ 3,613.1**	**100.0%**	**$ 169,893**	**$ 3,530.1**	**100.0%**	**$ 165,985**	**1,969**	**11.0**

(1) Includes 377 properties owned by the RJ joint ventures in which we hold an approximate one-third interest.

(2) For properties that we acquired directly, Estimated Total Investment represents our actual purchase price (including closing costs) and estimated renovation costs plus a 5% acquisition and renovation fee, if applicable. Estimated renovation costs represent the total costs we have incurred or expect to incur to renovate a property to prepare it for rental. These costs typically include paint, flooring, appliances, blinds and landscaping. Estimated Total Investment differs from Total Book Value only with respect to the properties contributed by AH LLC. For properties contributed by AH LLC, Total Book Value represents the net book value of AH LLC as of the date of contribution. See note 3 below. GAAP means U.S. generally accepted accounting principles.

(3) Estimated Total Investment includes estimated renovation costs in the aggregate of approximately $224 million, approximately $198 million of which represents actual renovation costs incurred through September 30, 2013 and approximately $26 million of which represents estimated remaining costs we expect to incur as of that date to prepare these properties for rental. Estimated renovation costs typically include paint, flooring, appliances, blinds and landscaping.

(4) Total Book Value represents the book value on a GAAP basis of all properties. In the case of AH LLC s contribution of properties to us, for GAAP purposes these transactions are considered to be transactions between entities under common control under the provisions of the Accounting Standards Codification, or ASC, 805, *Business Combinations*. As a result, these properties have been reflected at the net carrying cost of AH LLC. For the properties acquired from the Alaska Joint Venture, the $904.5 million purchase price has been allocated among the properties in accordance with GAAP.

(5) Represents 32 markets in 19 states.

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The table below summarizes certain information with respect to properties in escrow as of September 30, 2013.

Properties in Escrow[(1)]

Market	Properties in Escrow Units	% of Total	Avg. Sq.Ft.	Avg. Age (years)	Estimated Total Investment[(2)] $ millions	Avg. per Property
Columbus, OH	77	18.5%	1,936	12.3	$ 10.8	$ 140,140
Cincinnati, OH	77	18.5%	1,989	11.9	$ 12.1	157,524
Charlotte, NC	38	9.1%	2,146	9.3	$ 6.1	160,487
Raleigh, NC	29	7.0%	1,869	9.0	$ 4.9	169,074
Indianapolis, IN	28	6.7%	1,952	11.7	$ 4.1	147,287
Nashville, TN	24	5.8%	2,401	6.3	$ 5.2	215,999
Winston-Salem, NC	18	4.3%	2,160	11.0	$ 2.8	155,231
Greensboro, NC	14	3.4%	1,869	10.0	$ 2.1	152,981
Jacksonville, FL	13	3.1%	1,852	6.8	$ 1.8	135,481
Dallas-Fort Worth, TX	12	2.9%	2,949	10.8	$ 1.9	161,547
All Other[(3)]	86	20.7%	1,989	10.4	$ 15.3	177,239
Total / Average	416	100.0%	2,033	10.6	$ 67.1	$ 161,318

(1) Includes properties in escrow subject to customary closing conditions. Does not include properties in escrow subject to lender approval. Properties in escrow are typically not occupied at the closing date.

(2) Estimated Total Investment represents our actual purchase price (including closing costs) and estimated renovation costs plus a 5% acquisition and renovation fee. Estimated renovation costs represent the total costs we expect to incur to renovate a property to prepare it for rental. These costs typically include paint, flooring, appliances, blinds and landscaping.

(3) Represents 19 markets in 11 states.

In October 2013, we acquired approximately 583 properties with an estimated total investment of $86.0 million. Additionally, between October 31, 2013 and November 15, 2013 (the latest practicable date before the commencement of this offering), we acquired approximately 397 properties with an estimated total investment of $58.4 million. Approximately 62% of these properties acquired between September 30, 2013 and November 15, 2013 were purchased in foreclosure auctions and the balance through other acquisition channels. At November 15, 2013, we had approximately 573 properties in escrow with an estimated total investment of $96.5 million. The level of purchases for the entire month of November 2013 should not be extrapolated from this partial month information as acquisition activity tends to be higher at the beginning of a month.

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Our Competitive Strengths

We believe that the following strengths enable us to implement our business and growth strategies and compete effectively in the single-family home rental market. For more information, see Our Business and Properties Our Competitive Strengths.

Experienced and tenured management team. We believe the significant experience, expertise and relationships of our executive team drive our business and growth. Our executive team, headed by Mr. Hughes, our Chairman, David Singelyn, our Chief Executive Officer, Jack Corrigan, our Chief Operating Officer, and Peter Nelson, our Chief Financial Officer, each of whom is a former executive of Public Storage, has a successful track record of managing and growing a publicly traded REIT through all stages of the real estate investment cycle. Among other executive positions they have held, Mr. Singelyn was treasurer of Public Storage and was chief executive officer of Public Storage Canadian Properties, or Public Storage Canada, a real estate company previously listed on the Toronto Stock Exchange, and American Commercial Equities, LLC, or ACE; Mr. Corrigan was the chief financial officer of PS Business Parks, a NYSE-listed REIT; and Mr. Nelson was the chief financial officer of Lennar Partners, Inc. and Alexandria Real Estate Equities, Inc., a NYSE-listed REIT.

Large, diversified portfolio of high-quality properties. As of September 30, 2013, we owned 21,267 single-family properties concentrated in select sub-markets of MSAs within 22 states. These homes are located in neighborhoods of cities that we believe remain desirable places to live, despite significantly impacted home prices. In addition, we continually evaluate potential new markets across the country. We are focused on acquiring homes with a number of key property characteristics, including: (i) construction after 1990; (ii) three or more bedrooms; (iii) two or more bathrooms; (iv) a range of $70,000 estimated minimum valuation to $400,000 maximum bid price; and (v) estimated renovation costs not in excess of 25% of estimated value. We target areas with above average median household incomes, well-regarded school districts and access to desirable lifestyle amenities. We believe that homes in these areas will attract tenants with strong credit profiles, produce high occupancy and rental rates and generate long-term property appreciation. Not all of the homes that we may acquire will meet all of these criteria, especially if acquired as part of a bulk purchase.

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Quarterly Acquisition, Renovation and Leasing Rates

(As of September 30, 2013)

Demonstrated property acquisition track record and processes**.** Since its inception in June 2011, AH LLC has developed an effective acquisition process, supported by analytics and dedicated personnel within our target markets, that is capable of efficiently deploying large amounts of capital. The level of our acquisition activity will fluctuate because it depends on the number of suitable investments, as well as on the level of funds available for investment.

Substantial Renovation Capabilities**.** AH LLC has an in-house team of approximately 109 dedicated personnel to oversee the renovation process. This team focuses on renovating our homes to meet our quality standards prior to leasing. We estimate that AH LLC generally completes property renovations within approximately 90 days after a property is available for renovation. From January 1 to September 30, 2013, we completed renovations on 13,754 properties.

Institutional quality management platform and systems**.** Our management platform and systems are fully integrated with AH LLC s acquisition and renovation platform to ensure oversight and coordination of our key functions, including acquisitions, renovations, leasing, property management and accounting. We have developed an extensive property management infrastructure with modern systems and technology, dedicated personnel and local offices in certain of our target markets. Our property management personnel maintain a disciplined focus on controlling costs, driving occupancy and maximizing rental rates through all phases of our properties lifecycles.

As of September 30, 2013, we had approximately 14,384 leased properties, including leases on properties for which we have completed renovations and leases existing at the date of acquisition. The following table summarizes our leasing experience as of September 30, 2013.

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Our Leasing Experience

	Number of Properties[1]				30+ Days Occupancy %[5]	90+ Days Occupancy %[6]	Average Annual Scheduled Rent Per Property
	Not Rent Ready	Leased[2]	Available for Rent 30+ Days[3]	Available for Rent 90+ Days[4]			
Dallas-Fort Worth, TX	496	1,144	1,206	1,178	94.9%	97.1%	$ 17,521
Indianapolis, IN	267	1,238	1,413	1,250	87.6%	99.0%	14,669
Greater Chicago area, IL and IN	604	574	671	602	85.5%	95.3%	19,171
Atlanta, GA	253	973	1,021	1,011	95.3%	96.2%	15,930
Houston, TX	297	613	639	622	95.9%	98.6%	18,193
Cincinnati, OH	227	664	717	676	92.6%	98.2%	16,760
Phoenix, AZ	52	756	832	809	90.9%	93.4%	13,219
Charlotte, NC	110	680	758	691	89.7%	98.4%	15,470
Nashville, TN	56	721	762	738	94.6%	97.7%	17,787
Jacksonville, FL	93	636	649	644	98.0%	98.8%	15,663
All Other[7]	1,692	5,152	6,003	5,445	85.8%	94.6%	16,615
Total / Average	**4,147**	**13,151**	**14,671**	**13,666**	**89.6%**	**96.2%**	**$ 16,417**

(1) Includes single-family properties acquired in the Alaska Joint Venture Acquisition on June 11, 2013.
(2) Includes leases on properties for which we have completed renovations and excludes 1,233 leases with tenants existing at the date of acquisition.
(3) Available for Rent 30+ Days represents the number of properties that have been leased after we have completed renovations or are available for rent (i.e., rent-ready) for a period of greater than 30 days.
(4) Available for Rent 90+ Days represents the number of properties that have been leased after we have completed renovations or are available for rent (i.e., rent-ready) for a period of greater than 90 days.
(5) Occupancy percentage is computed by dividing the number of leased properties by the number of properties available for rent 30+ days.
(6) Occupancy percentage is computed by dividing the number of leased properties by the number of properties available for rent 90+ days.
(7) Represents 32 markets in 19 states.

Substantial alignment of interests of AH LLC and management with our shareholders. Through the Management Internalization, our operating partnership acquired our former manager and former property manager from AH LLC, and we became an internally managed REIT with an integrated operating platform, other than the acquisition and renovation services that AH LLC continues to provide us, on an exclusive basis, until December 10, 2014. In connection with the Management Internalization, AH LLC also received convertible equity securities in our operating partnership that are linked to favorable financial metrics and share appreciation. As of September 30, 2013, AH LLC owned approximately 25% of our Class A common shares assuming that all of its Class B common shares and OP units are converted into, or redeemed for, Class A common shares. As a result, we believe that the economic interests of AH LLC and management are substantially aligned with those of our shareholders.

Successful track record raising capital and strong balance sheet. We have a proven ability to raise significant amounts of debt and equity capital. Since November 2012, we have raised net proceeds of approximately $2.2 billion through two private placements of our Class A common shares, our initial public offering, the concurrent private placements to AH LLC and APFC and our issuance of Series A Participating Preferred Shares. In addition, in March 2013, we entered into a $500 million credit facility with Wells Fargo Bank, National Association, or Wells Fargo. On September 30, 2013, we amended our credit facility to add J.P. Morgan Chase Bank as a lender, expand our borrowing capacity under the credit facility to $800 million and extend the repayment period to September 30, 2018,

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among other things. At October 31, 2013, we had $220 million of borrowings outstanding under our credit facility and cash and cash equivalents on hand of approximately $128 million. At September 30, 2013, we had approximately $3.9 billion in assets.

Our Business and Growth Strategies

Our primary objective is to generate attractive risk-adjusted returns for our shareholders through dividends and capital appreciation. We believe we can achieve this objective by pursuing the following strategies. For more information, see Our Business and Properties Our Business and Growth Strategies.

Secure early-mover advantage and position as a dominant owner/operator of single-family rental properties. Historically, the single-family home rental market has been extremely fragmented, comprised primarily of private and individual property investors in local markets. Until recently, there have been no large-scale, national market owners/operators due primarily to the challenge of efficiently scaling the acquisition and management of many individual homes. With an unprecedented opportunity to acquire a large number of homes at attractive prices, we intend to continue to leverage our expertise and experience in rapidly building an institutional-quality, professionally managed business.

Employ a robust and disciplined property acquisition process. We have exclusive access to AH LLC s established acquisition and renovation platform to acquire high quality single-family homes. AH LLC has approximately 145 full-time personnel dedicated to identifying, evaluating, inspecting and acquiring homes. To date, AH LLC has primarily acquired properties at foreclosure auctions and through broker sales (primarily multiple listing service, or MLS, and short sales). AH LLC may source property acquisition opportunities through portfolio (or bulk) sales from government agencies, financial institutions and competitors.

Assemble a geographically diversified portfolio. We currently are focusing on acquiring single-family homes in selected sub-markets of MSAs within 22 states, with an emphasis on achieving critical mass within each target market. We continually evaluate potential new markets where we may invest and establish operations as opportunities emerge. We select our markets based on steady population growth, strong rental demand and a high level of distressed sales of homes that can be acquired below replacement cost, providing for attractive potential yields and capital appreciation.

Efficiently manage and operate properties. Building on the experience of our executive team at Public Storage and our significant in-house property management capabilities, we strive to create a leading, comprehensive single-family home property management business. As was the case with the self-storage industry, we believe the key to efficiently managing a large number of relatively low-cost properties is to strike the appropriate balance between centralization and decentralization. We utilize local, in-house property management for our properties in all markets where we believe it is economical to do so.

Establish a nationally recognized brand. We are striving to establish American Homes 4 Rent as a nationally recognized brand because we believe that establishing a brand well-known for quality, value and tenant satisfaction will help attract and retain tenants and qualified personnel, as well as support higher rental rates. We believe our brand is gaining recognition within a number of our markets.

Optimize capital structure. We may use leverage to increase potential returns to our shareholders, but we will seek to maintain a conservative and flexible balance sheet. We may also access additional sources of financing. Based in part on our executive team s experience at Public Storage, we believe that preferred shares provide an attractive source of permanent capital.

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Recent Developments

Series A Participating Preferred Shares Offering

In October and November 2013, we issued a total of 5,060,000 5.000% Series A Participating Preferred Shares, or Series A Participating Preferred Shares, at a price of $25.00 per share (including the exercise in full of the underwriters option to purchase additional shares), for gross proceeds of approximately $126.5 million before underwriting discounts and offering costs.

Declaration of Distributions

On November 7, 2013, our board of trustees declared our initial quarterly distribution of $0.05 per Class A common share payable on January 10, 2014 to shareholders of record on December 15, 2013. Additionally, our board of trustees also declared the initial pro-rated quarterly dividend of $0.229167 per share on our Series A Participating Preferred Shares payable on December 31, 2013 to shareholders of record on December 15, 2013.

Securitization Transaction

On November 8, 2013, we announced that we had engaged advisors to assist in structuring and negotiating a securitization transaction secured by a portion of our portfolio of single-family properties. The transaction was approved by our board of trustees. We intend to go to market with the transaction during the first quarter of 2014, subject to, among other matters, conditions in the capital markets, rating agency review and customary closing conditions, and expect that the transaction will be exempt from registration under the Securities Act. There can be no assurances that the contemplated transaction will be completed.

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Our Structure

We were formed as a Maryland REIT on October 19, 2012. The following chart illustrates our current organizational structure:

[1] Our trustees, our executive officers, our dedicated personnel and others have been granted options to purchase an aggregate 1,190,000 of our Class A common shares under the American Homes 4 Rent 2012 Equity Incentive Plan, or the 2012 Incentive Plan.

[2] Consists of 6,860,783 Class A common shares and 635,075 Class B common shares.

[3] Consists of 13,787,292 Class A units, 31,085,974 Series C convertible units, 4,375,000 Series D units and 4,375,000 Series E units.

Securities Outstanding

Class A and Class B Common Shares of the Company

We have two classes of common shares, Class A common shares, and Class B common shares. Each outstanding Class B common share entitles the holder to 50 votes on all matters on which the holders of Class A common shares are entitled to vote, including the election of trustees, and holders of Class A common shares and Class B common shares will vote together as a single class. Each Class B common share has the same economic interest as a Class A common share, and one Class B common share and 49 units of limited partnership in our operating partnership, or OP units, together represent a similar economic value as 50 Class A common shares. Subject to the rights of holders of Series C convertible units of limited partnership in our operating partnership, or Series C units, Series D units and Series E units, holders of OP units and shareholders of our company will have the same rights to distributions. For a description of voting limitations pertaining to certain shareholders, see Description of Equity Shares Common Shares.

Series A Participating Preferred Shares of the Company

For a description of the terms of our Series A Participating Preferred Shares, see Description of Equity Shares Series A Participating Preferred Shares.

Class A Units of our Operating Partnership

In general, beginning 12 months after the date of issuance, Class A units are redeemable by limited partners of our operating partnership (other than us) for cash or, at our election, exchangeable for our Class A common shares on a one-for-one basis. The partnership agreement requires that our operating partnership distribute available cash to its partners on at least a quarterly basis in accordance with their relative percentage interests or specified preferences, if any.

Series A Participating Preferred Units of our Operating Partnership

Our operating partnership issued Series A Participating Preferred Units to us in exchange for the net proceeds from our public offering of Series A Participating Preferred Shares. For a description of the terms of our Series A Participating Preferred Units, see Operating Partnership and the Partnership Agreement Series A Participating Preferred Units.

Series C Convertible Units of our Operating Partnership

On February 28, 2013, we issued to AH LLC 634,408 of our Class B common shares and our operating partnership issued 31,085,974 Series C units in exchange for the AH LLC Portfolio. Holders of the Series C units will be entitled to distributions equal to the actual net cash flow of the properties in the AH LLC Portfolio up to a maximum of 3.9% per unit per year based on a price per unit of $15.50, but will not be entitled to any distributions of income generated by any other properties or operations of our company or any liquidating distributions. Holders of Class A units, including our company and AH LLC, will be entitled to any net cash flow from the AH LLC Portfolio above the maximum yield on the Series C units, as well as distributions of all other cash available for distribution from our operating partnership. At any time, at the option of the holders, the Series C units may be converted into Class A units. If holders of the Series C units have not exercised their right to convert the Series C units into Class A units by the earlier of (i) the third anniversary of the date of original issuance of the Series C units or (ii) the date of commencement of the dissolution, liquidation or winding up of our operating partnership, then the Series C units will automatically convert into Class A units. Holders of Series C units will vote on all operating partnership matters with holders of Class A units.

Series D Convertible Units and Series E Convertible Units of our Operating Partnership

The Series D units are convertible into Class A units, and the Series E units are convertible into Series D units, or if the Series D units have previously converted into Class A units, into Class A units, as described below.

The Series D units do not participate in distributions for 30 months from the date of issuance and do not have liquidating distributions or any voting rights. The Series D units are automatically convertible into Class A units on a one-for-one basis only effective as of the later of (1) 30 months from the date of issuance and (2) the earlier of (i) the date on which adjusted funds from operations, or adjusted FFO, per Class A common share aggregates or exceeds $0.80 over four consecutive quarters following the closing date of the Management

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Internalization or (ii) the date on which the daily closing price of our Class A common shares on the NYSE averages $18.00 or greater for two consecutive quarters following the closing date of the Management Internalization. After 30 months, the Series D units will participate in distributions (other than liquidating distributions) at a rate of 70% of the per unit distributions on the Class A units.

The Series E units do not participate in distributions and do not have any voting rights. The Series E units will automatically convert into Series D units, or if the Series D units have previously converted into Class A units, into Class A units, on February 29, 2016, if certain conditions are satisfied. See Operating Partnership and the Partnership Agreement Series D Convertible Units and Series E Convertible Units.

The tables below set forth the outstanding securities of our company and of our operating partnership, as of November 15, 2013, without giving effect to this offering. For a description of the terms of these securities, see Description of Equity Shares Common Shares and Operating Partnership and the Partnership Agreement.

Securities of Our Company	**Shares**
Class A common shares	184,869,219
Class B common shares	635,075(1)
Series A Participating Preferred Shares	5,060,000(2)

Securities of Our Operating Partnership(3)	**Units**
Class A units	13,787,292(4)
Series C units	31,085,974(5)
Series D units	4,375,000(5)
Series E units	4,375,000(5)

(1) Convertible into Class A common shares on a one-for-one basis.
(2) At our option, the Series A Participating Preferred Shares are redeemable for cash or convertible into Class A common shares, beginning after September 30, 2017. See Description of Equity Shares Series A Participating Preferred Shares.
(3) Excludes securities issued to our company.
(4) Redeemable for cash or, at our option, exchangeable for our Class A common shares on a one-for-one basis, beginning one year after the initial date of issuance.
(5) Convertible into Class A units on a one-for-one basis if certain conditions are satisfied. See Operating Partnership and the Partnership Agreement Series C Convertible Units and Operating Partnership and the Partnership Agreement Series D Convertible Units and Series E Convertible Units.

Our Tax Status

We have elected to be taxed as a REIT, commencing with our first taxable year ended December 31, 2012. Our qualification as a REIT, and maintenance of such qualification, will depend upon our ability to meet, on a continuing basis, various complex requirements under the Internal Revenue Code of 1986, or the Code, relating to, among other things, the sources of our gross income, the composition and values of our assets, our distributions to our shareholders and the concentration of ownership of our equity shares. We believe that, commencing with our initial taxable year ended December 31, 2012, we have been organized in conformity with the requirements for qualification and taxation as a REIT under the Code, and we intend to continue to operate in a manner that will enable us to meet the requirements for qualification and taxation as a REIT. In connection with this offering of our Series B Participating Preferred Shares, we have received an opinion from Hogan Lovells US LLP to the effect that we have been organized and have operated in conformity with the requirements for qualification and taxation as a REIT under the Code, and that our current organization and proposed method of operation will enable us to continue to meet the requirements for qualification and taxation as a REIT.

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As a REIT, we generally will not be subject to U.S. federal income tax on the REIT taxable income that we currently distribute to our shareholders, but taxable income generated by any taxable REIT subsidiary that we may form or acquire will be subject to federal, state and local income tax. Under the Code, REITs are subject to numerous organizational and operational requirements, including a requirement that they distribute annually at least 90% of their REIT taxable income to their shareholders. If we fail to qualify as a REIT in any taxable year and do not qualify for certain statutory relief provisions, our income would be subject to U.S. federal income tax, and we would likely be precluded from qualifying for treatment as a REIT until the fifth calendar year following the year in which we fail to qualify. Even if we qualify as a REIT, we may still be subject to certain U.S. federal, state and local taxes on our income and assets and to U.S. federal income and excise taxes on our undistributed income.

Our Distribution Policy

To qualify as a REIT, we must distribute annually to our shareholders an amount at least equal to 90% of our REIT taxable income, determined without regard to the deduction for dividends paid and excluding any net capital gain. We will be subject to income tax on our taxable income that is not distributed and to an excise tax to the extent that certain percentages of our taxable income are not distributed by specified dates. See Material U.S. Federal Income Tax Considerations. Income as computed for purposes of the foregoing tax rules will not necessarily correspond to our income as determined for financial reporting purposes. We intend to distribute our taxable income to our shareholders and retain the balance of our cash available for distribution for reinvestment in properties. However, our cash available for distribution may be less than the amount required to meet the distribution requirements for REITs under the Code, and we may be required to borrow money, sell assets or make taxable distributions of our equity shares or debt securities to satisfy the distribution requirements. Additionally, we may pay future distributions from the proceeds from this offering or other securities offerings and thus all or a portion of such distributions may constitute a return of capital for federal income tax purposes.

The timing and frequency of distributions authorized by our board of trustees in its sole discretion and declared by us will be based upon a variety of factors deemed relevant by our board of trustees, which may include among others: our actual and projected results of operations; our liquidity, cash flows and financial condition; revenue from our properties; our operating expenses; economic conditions; debt service requirements; limitations under our financing arrangements; applicable law; capital requirements and the REIT requirements of the Code. We cannot guarantee whether or when we will be able to make distributions or that any distributions will be sustained over time. Distributions to our shareholders generally will be taxable to our shareholders as ordinary income, although a portion of such distributions may be designated by us as capital gain dividends or qualified dividend income, or may constitute a return of capital. We will furnish annually to each of our shareholders a statement setting forth distributions paid during the preceding year and their federal income tax treatment. For a discussion of the federal income tax treatment of our distributions, see Material U.S. Federal Income Tax Considerations.

Restrictions on Ownership

Due to limitations on the concentration of ownership of REIT shares imposed by the Code, subject to certain exceptions, our declaration of trust provides that no person may beneficially own more than 8.0% (in value or in number of shares, whichever is more restrictive) of our outstanding common shares or more than 9.9% (in value or in number of shares, whichever is more restrictive) of any class or series of our outstanding preferred shares. Our declaration of trust also prohibits any person from, among other matters, beneficially owning equity shares if such ownership would result in our being closely held within the meaning of Section 856(h) of the Code (without regard to whether the ownership interest is held during the last half of a year) effective upon the completion of our initial public offering; transferring equity shares if such transfer would result in our equity shares being owned by less than 100 persons, effective beginning on the date on which we first have 100 shareholders; and beneficially owning equity shares if such beneficial ownership would otherwise cause us to fail

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to qualify as a REIT under the Code. Our board of trustees may exempt a person from the ownership limits if such person submits to the board of trustees certain information satisfactory to the board of trustees. See Description of Equity Shares Restrictions on Ownership and Transfer.

Emerging Growth Company Status

We currently qualify as an emerging growth company, as defined in the Jumpstart Our Business Startups Act of 2012, or the JOBS Act, and are eligible to take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not emerging growth companies, including, but not limited to, not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act of 2002, or Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements and exemptions from the requirements of holding a non-binding advisory vote on executive compensation and shareholder approval of any golden parachute payments not previously approved. We have not made a decision whether to take advantage of certain of these exemptions. If we do take advantage of any of these exemptions, we do not know if some investors will find our securities less attractive as a result. The result may be a less active trading market for our Class A common shares, our Series A Participating Preferred Shares and/or our Series B Participating Preferred Shares, and those share prices may be more volatile.

In addition, an emerging growth company can take advantage of the extended transition period provided in Section 7(a)(2)(B) of the Securities Act of 1933, as amended, or the Securities Act, for complying with new or revised accounting standards. In other words, an emerging growth company can delay the adoption of certain accounting standards until those standards would otherwise apply to private companies. However, we are choosing to opt out of such extended transition period, and as a result, we will comply with new or revised accounting standards on the relevant dates on which adoption of such standards is required for all public companies which are not emerging growth companies. Our decision to opt out of the extended transition period for complying with new or revised accounting standards is irrevocable.

We could remain an emerging growth company for up to five years, or until the earliest of (i) the last day of the first fiscal year in which our annual gross revenues exceed $1 billion, (ii) the date that we become a large accelerated filer as defined in Rule 12b-2 under the Securities Exchange Act of 1934, as amended, or the Exchange Act, which would occur if the market value of our Class A common shares that are held by non-affiliates exceeds $700 million as of the last business day of our most recently completed second fiscal quarter, or (iii) the date on which we have issued more than $1 billion in non-convertible debt during the preceding three year period.

Summary Risk Factors

An investment in our securities involves risks. You should consider carefully the risks discussed below and described more fully along with other risks under Risk Factors in this prospectus before investing in our securities.

- We are employing a new and untested business model with no proven track record, which may make our business difficult to evaluate.

- We are a recently organized REIT with a limited operating history, and we may not be able to successfully operate our business or generate sufficient operating cash flows to make or sustain distributions on our preferred and common shares.

- We may not be able to effectively manage our growth, and any failure to do so may have an adverse effect on our business and operating results.

- Because we have not yet identified any specific properties (other than properties held in escrow) to acquire with any net proceeds of this offering remaining after repayment of debt, you will be unable to

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evaluate the economic merits of our investments made with such net proceeds before making an investment decision to purchase our Series B Participating Preferred Shares.

We intend to continue to rapidly expand our scale of operations and make acquisitions even if the rental and housing markets are not as favorable as they have been in recent months, which could adversely impact anticipated yields.

Our future growth depends, in part, on the availability of additional debt or equity financing. If we cannot obtain additional financing on terms favorable or acceptable to us, our growth may be limited.

Our credit facility contains financial and operating covenants that could restrict our business and investment activities. Failure to satisfy these covenants could result in a default under our credit facility that could accelerate the maturity of our debt obligations, which would have a material adverse effect on our business, liquidity, results of operations and financial condition and our ability to make distributions on our preferred and common shares.

Our success depends, in part, upon our ability to hire and retain highly skilled managerial, investment, financial and operational personnel, and the past performance of our senior management may not be indicative of future results.

Our investments are and will continue to be concentrated in our target markets and the single-family properties sector of the real estate industry, which exposes us to downturns in our target markets or in the single-family properties sector.

We face significant competition for acquisitions of our target properties, which may limit our strategic opportunities and increase the cost to acquire those properties.

We face significant competition in the leasing market for quality tenants, which may limit our ability to rent our single-family homes on favorable terms or at all.

The large supply of single-family homes becoming available for purchase as a result of the heavy volume of foreclosures, combined with historically low residential mortgage rates, may cause some potential renters to seek to purchase residences rather than lease them and, as a result, cause a decline in the number and quality of potential tenants.

Our evaluation of properties involves a number of assumptions that may prove inaccurate, which could result in us paying too much for properties we acquire or overvaluing our properties or our properties failing to perform as we expect.

Single-family properties that are being sold through short sales or foreclosure sales are subject to risks of theft, mold, infestation, vandalism, deterioration or other damage that could require extensive renovation prior to renting and adversely impact our operating results.

If occupancy levels and rental rates in our target markets do not increase sufficiently to keep pace with rising costs of operations, our income and distributable cash will decline.

We depend on our tenants and their willingness to renew their leases for substantially all of our revenues. Poor tenant selection and defaults and nonrenewals by our tenants may adversely affect our reputation, financial performance and ability to make distributions on our preferred and common shares.

Declining real estate values and impairment charges could adversely affect our earnings and financial condition.

We are self-insured against many potential losses, and uninsured or underinsured losses relating to properties may adversely affect our financial condition, operating results, cash flows and ability to make distributions on our preferred and common shares.

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Mortgage loan modification programs and future legislative action may adversely affect the number of available properties that meet our investment criteria.

Completion of the Management Internalization has exposed us to new and additional responsibilities, costs and risks.

The contribution agreement we entered into in connection with the Management Internalization was negotiated between a special committee of our board of trustees and AH LLC. Therefore, the terms of the agreement may not have been as favorable to us as if it had been negotiated with unaffiliated third parties.

Our board of trustees has approved a very broad investment policy, subject to management oversight, and does not review or approve each acquisition decision made by AH LLC.

We may be adversely affected by lawsuits alleging trademark infringement as such lawsuits could materially harm our brand name, reputation and results of operations.

Our fiduciary duties as the general partner of our operating partnership could create conflicts of interest, which may impede business decisions that could benefit our shareholders.

As long as AH LLC continues to perform acquisition and renovation services for us, we will depend on AH LLC for our external growth.

The Series B Participating Preferred Shares have not been rated.

The Series B Participating Preferred Shares are newly issued securities with no established trading market, which may negatively affect their market value and your ability to transfer or sell your shares. We intend to apply to list the Series B Participating Preferred Shares on the NYSE, but we cannot assure you that the listing will be approved or that a trading market will develop or be sustained.

The Series B Participating Preferred Shares are subordinate to our debt and other liabilities, and your interests could be diluted by the issuance of additional preferred shares and by other transactions.

There is no guarantee that any HPA Amount will accrue or be paid on the Series B Participating Preferred Shares.

Changes in home prices reflected in the POI may have little or no correlation with the actual appreciation or depreciation of homes in our portfolio, and the POI data for our top 20 markets that we will use to calculate the HPA Amount may have little or no correlation with the actual appreciation or depreciation of homes nationwide.

The cumulative change in HPA that occurs during the period measured for purposes of calculating the HPA Amount may differ from the cumulative change in HPA that occurs during the period for which the Series B Participating Preferred Shares are actually outstanding.

The FHFA may no longer publish or may materially change the methodology used in calculating the POI, which could adversely affect the value of our Series B Participating Preferred Shares.

If you hold our Series B Participating Preferred Shares, you will not be entitled to any rights with respect to our common shares, but you will be subject to all changes made with respect to our common shares.

The Change of Control conversion feature of our Series B Participating Preferred Shares may not adequately compensate you and may make it more difficult for a third party to take over our company or discourage a third party from taking over our company.

The market price of Class A common shares received in a conversion of our Series B Participating Preferred Shares may decrease between the date received and the date the Class A common shares are sold.

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Our ability to pay dividends is limited by the requirements of Maryland law.

You should consider the United States federal income tax consequences of owning our Series B Participating Preferred Shares, including the potential for constructive distributions.

Future sales of our common shares or other equity-related securities in the public market could lower the market price of our common shares and adversely impact the value of the Series B Participating Preferred Shares.

Failure to qualify as a REIT, or failure to remain qualified as a REIT, would cause us to be taxed as a regular corporation, which would substantially reduce funds available for distribution to our shareholders.

Organizational Information

Our principal executive offices are located at 30601 Agoura Road, Suite 200, Agoura Hills, California 91301. Our main telephone number is (805) 413-5300. Our Internet website is http://www.americanhomes4rent.com. The contents of our website are not incorporated by reference in or otherwise a part of this prospectus.

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THE OFFERING

The offering terms are summarized below solely for your convenience. For a more complete description of the terms of the Series B Participating Preferred Shares, see Description of Series B Participating Preferred Shares.

Issuer	American Homes 4 Rent, a Maryland REIT
Securities Offered	4,000,000 5.000% Series B participating preferred shares of beneficial interest, $0.01 par value per share, or Series B Participating Preferred Shares (plus up to an additional 600,000 Series B Participating Preferred Shares if the underwriters exercise their option to purchase additional shares in full). We reserve the right to reopen this series and issue additional Series B Participating Preferred Shares at any time either through public or private sales.
Ranking	The Series B Participating Preferred Shares will rank, with respect to dividend rights and rights upon our liquidation, dissolution or winding up: senior to our common shares of beneficial interest, or our common shares, and to any other class or series of our equity shares expressly designated as ranking junior to the Series B Participating Preferred Shares; on parity with any existing or future class of preferred or convertible preferred securities, including our Series A participating preferred shares of beneficial interest, $0.01 par value per share, or Series A Participating Preferred Shares; and junior to any debt securities and any equity shares expressly designated as ranking senior to the Series B Participating Preferred Shares See Description of Series B Participating Preferred Shares Ranking.
Dividends	Holders of the Series B Participating Preferred Shares will be entitled to receive cumulative cash dividends when, as and if authorized by our board of trustees from and including the issue date, payable quarterly in arrears on the last day of March, June, September and December of each year, at the rate of 5.000% per annum of the initial liquidation preference per share (equivalent to the fixed annual rate of $1.25 per share). The first dividend is scheduled to be paid on March 31, 2014 to holders of record as of March 15, 2014 and will be a pro rata dividend from and including the original issue date to but excluding March 31, 2014 in the amount of $ per share. Dividends on the Series B Participating Preferred Shares will accumulate whether or not (i) we have earnings, (ii) there are funds legally available for the payment of such dividends and (iii) such dividends are authorized or declared. Prior to December 31, 2020, no dividends will accrue or be paid on any HPA Amount (as defined below).

On and after December 31, 2020, in lieu of the prior dividend rate, a dividend rate of 10.000% per annum will be paid on the initial

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	liquidation preference per Series B Participating Preferred Share plus the HPA Amount, if any.
Voting Rights	Holders of the Series B Participating Preferred Shares generally will have no voting rights. However, if we are in arrears on dividends, whether or not authorized or declared, on the Series B Participating Preferred Shares for six or more quarterly periods, whether or not consecutive, holders of Series B Participating Preferred Shares (voting separately as a class together with the holders of all other classes or series of preferred shares of beneficial interest, or preferred shares, ranking on parity with the Series B Participating Preferred Shares with respect to the payment of dividends and the distribution of assets upon our liquidation, dissolution or winding up, or parity preferred shares, and upon which like voting rights have been conferred and are exercisable) will be entitled to elect two additional trustees at a special meeting called upon the request of at least 10% of such holders or at our next annual meeting and each subsequent annual meeting of shareholders to serve on our board of trustees until all unpaid dividends with respect to the Series B Participating Preferred Shares and such other classes or series of preferred shares with like voting rights have been paid or declared and set aside for payment. In addition, the affirmative vote or written consent of the holders of at least two-thirds of the outstanding Series B Participating Preferred Shares and each other class or series of parity preferred shares with like voting rights (voting together as a single class) is required for us to authorize, create or increase any class or series of equity shares ranking senior to the Series B Participating Preferred Shares or to amend any provision of our declaration of trust so as to materially and adversely affect the terms of the Series B Participating Preferred Shares. If such amendment to our declaration of trust does not equally affect the terms of the Series B Participating Preferred Shares and the terms of one or more other classes or series of parity preferred shares, the affirmative vote or written consent of the holders of at least two-thirds of the shares outstanding at the time of Series B Participating Preferred Shares, voting separately as a class, is required. Holders of the Series B Participating Preferred Shares also will have the exclusive right to vote on any amendment to our declaration of trust on which holders of the Series B Participating Preferred Shares are otherwise entitled to vote and that would alter only the rights, as expressly set forth in our declaration of trust, of the Series B Participating Preferred Shares. Among other things, we may, without any vote of the holders of our Series B Participating Preferred Shares, issue additional shares of Series B Participating Preferred Shares and may authorize and issue additional classes or series of parity equity securities.
Restrictions on Ownership and Transfer	Due to limitations on the concentration of ownership of REIT shares imposed by the Internal Revenue Code of 1986, as amended, or the Code, subject to certain exceptions, our declaration of trust provides

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	(and the Series B Participating Preferred Shares articles supplementary will provide) that no person may beneficially own more than 8.0% (in value or in number of shares, whichever is more restrictive) of our outstanding common shares or more than 9.9% (in value or in number of shares, whichever is more restrictive) of any class or series of our outstanding preferred shares. In addition, our declaration of trust prohibits (and the Series B Participating Preferred Shares articles supplementary will prohibit) any person from, among other matters, beneficially owning equity shares if such ownership would result in our being closely held within the meaning of Section 856(h) of the Code (without regard to whether the ownership interest is held during the last half of a year); transferring equity shares if such transfer would result in our equity shares being owned by less than 100 persons; and beneficially owning equity shares if such beneficial ownership would otherwise cause us to fail to qualify as a REIT under the Code. Our board of trustees may exempt a person from the ownership limits if such person submits to the board of trustees certain information satisfactory to the board of trustees. See Description of Series B Participating Preferred Shares Restrictions on Ownership and Transfer.
Use of Proceeds	We estimate that the net proceeds to us from the sale of our Series B Participating Preferred Shares in this offering will be approximately $ (or approximately $ if the underwriters exercise their option to purchase additional Series B Participating Preferred Shares in full), after deducting underwriting discounts and estimated offering expenses. We will contribute the net proceeds we receive from this offering to our operating partnership in exchange for Series B participating preferred operating partnership units. Our operating partnership intends to use the net proceeds from this offering (i) to repay the indebtedness we have incurred or expect to incur under our credit facility, (ii) to acquire and renovate single-family properties in accordance with our business strategy described in this prospectus, and (iii) for general business purposes. See Use of Proceeds.
Liquidation Preference	If we liquidate, dissolve or wind up, holders of our Series B Participating Preferred Shares will have the right to receive (i) $25.00 per share, plus (ii) the HPA Amount (if positive), plus (iii) accrued and unpaid dividends (whether or not authorized or declared) to but excluding the date of payment before any distribution or payment is made to holders of our common shares and any other class or series of our equity shares ranking junior to the Series B Participating Preferred Shares as to liquidation, dissolution or winding up. The rights of holders of Series B Participating Preferred Shares to receive this amount will be subject to the proportionate rights of any other class or series of our equity shares ranking on parity with the Series B Participating Preferred Shares as to rights upon liquidation, dissolution or winding up, and junior to the rights of any class or series of our equity shares expressly designated as ranking senior to the Series B Participating Preferred Shares.

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Home Price Appreciation Amount	The initial liquidation preference for the Series B Participating Preferred Shares may be increased by an additional amount, or the HPA Amount. The HPA Amount will equal the product of the $25.00 initial liquidation preference and the Home Price Appreciation Factor, or HPA Factor, described below. However, the HPA Amount at any time after December 31, 2020 will be equal to the HPA Amount calculated with respect to the period ended September 30, 2020, and the HPA Amount will be subject to a cap as described below under the caption HPA Amount Cap.
	The HPA Amount may be realized upon (i) exercise by us of our optional redemption right or conversion right after December 31, 2017, (ii) any conversion or redemption in connection with a Change of Control (as defined below) or (iii) liquidation, dissolution or winding up of the Company. In addition, on and after December 31, 2020, dividends will accrue on the HPA Amount, if any, added to the initial liquidation preference per Series B Participating Preferred Share.
Home Price Appreciation Factor	Home price appreciation, or HPA, represents the cumulative change in value from September 30, 2013 of an index based on the purchase prices of single-family homes located in our top 20 markets, by estimated total investment, as of September 30, 2013, as set forth in the table below. HPA is determined using a House Price Index of the Federal Housing Finance Agency, or FHFA, known as the Quarterly Purchase-Only Index, or POI, specifically the non-seasonally adjusted Purchase-Only Index for the 100 Largest Metropolitan Statistical Areas currently disclosed at the following URL: http://www.fhfa.gov/weblink/hpicbsapo.txt. The contents of the FHFA website are not incorporated by reference in or otherwise part of this prospectus. Other indices referenced in this prospectus will not be used in calculating the HPA Amount.
	The POI is a weighted, repeat-sales index, meaning that it measures average price changes in repeat sales of the same single-family properties. This information is obtained by reviewing repeat transactions involving conforming, conventional mortgages purchased or securitized by Fannie Mae or Freddie Mac since January 1975. Only mortgage transactions involving single-family homes are included. Conforming refers to a mortgage that both meets the underwriting guidelines of Fannie Mae or Freddie Mac and that does not exceed the conforming loan limit that is currently $625,000 for mortgages in the contiguous United States originated after September 30, 2011. Conventional mortgages are those that are neither insured nor guaranteed by the FHA, VA or other federal government entities. Mortgages on properties financed by government-insured loans, such as FHA or VA mortgages, are excluded from the POI, as are properties with mortgages that have a principal amount exceeding the conforming loan limit.
	The POI will be measured from a base date of September 30, 2013. The index values are weighted by our relative estimated total

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investments in each of the 20 markets at September 30, 2013, and such weighting is fixed during the time the HPA Amount accrues.

Cumulative HPA represents the sum of the 20 products of the change in HPA for each market since September 30, 2013 and the relative weighting, expressed as a percentage.

HPA Factor represents the product of the Cumulative HPA, as defined herein, (expressed as a percentage) multiplied by a constant investor participation percentage of 50%. The HPA Amount, at any time it is measured, cannot be negative, so the liquidation preference per Series B Participating Preferred Share will always be at least $25.00.

The FHFA historically has released the POI for a given quarter near the end of the second month after the end of that quarter. We will make available each quarter the quarterly measurement showing the aggregate HPA Amount per Series B Participating Preferred Share across quarters and weighted by markets based on the POI provided by the FHFA. We will also provide updates and maintain such information on the For Investors page of our corporate website.

If at any time prior to December 31, 2020, the FHFA no longer publishes the POI, or if the POI no longer covers one or more of our top 20 markets as of September 30, 2013, we will promptly make a good faith selection of a publicly available alternative index or indices after examining publicly available indices that are reasonably comparable to the POI to cover the market or markets no longer covered by the POI. If we select an alternative source or sources, we will disclose the new source for calculating the HPA Amount on the For Investors page of our corporate website and in a Current Report on Form 8-K filed with the Securities and Exchange Commission, or SEC. If a suitable public alternative source or sources is not available, we will, at our option, either redeem or convert the Series B Participating Preferred Shares within 135 days after the date that the POI was last published, as described in Description of Series B Participating Preferred Shares Redemption Redemption upon an Absence of Suitable Indices Event (in the case of a redemption) or as described in Description of Series B Participating Preferred Shares Conversion Conversion upon an Absence of Suitable Indices Event (in the case of a conversion). We refer to the absence of a suitable alternative source or sources herein as an Absence of Suitable Indices Event.

The following table summarizes our top 20 markets at September 30, 2013 by estimated total investment and assigns market weightings, which shall remain fixed while the Series B Participating Preferred Shares remain outstanding.

The following table also sets forth the historical percentage change in the HPA with respect to each of these markets for the period from September 30, 2012 to September 30, 2013 (which is the most recent four

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quarter period for which POI data is currently available) and the total weighted average percentage change in the HPA during that period. The table sets forth the methodology used to calculate the percentage change for each market and the total weighted average percentage change for all markets using the POI values for each market. In order to measure the percentage change from September 30, 2012, the actual POI value for each market as of September 30, 2012 has been set at a baseline value of 100.0. For the subsequent periods, the table sets forth the change in the POI value relative to the baseline value of 100.0. The information in this table is for illustrative purposes only, is historical, and is not intended to predict future HPA. See Risk Factors The various hypothetical figures and illustrations contained in this prospectus should not be taken as an indication or prediction of future investment results and Risk Factors There is no guarantee that any HPA Amount will accrue or be paid on the Series B Participating Preferred Shares.

		FHFA POI Value (Relative to Sep 30, 2012) as of					
Market	**Relative Weighting Applied in Determining HPA[(1)]**	**Sep 30, 2012[(2)]**	**Dec 31, 2012**	**Mar 31, 2013**	**Jun 30, 2013**	**Sep 30, 2013**	**Percentage Change in HPA from Sep 30, 2012 to Sep 30, 2013**
Dallas-Fort Worth, TX[(3)]	9.860%	100.00	100.46	101.20	106.40	107.81	7.8%
Indianapolis, IN	8.937%	100.00	98.17	102.06	106.03	108.60	8.6%
Atlanta, GA	7.693%	100.00	100.34	104.18	111.73	114.90	14.9%
Greater Chicago Area, IL[(4)]	7.645%	100.00	96.50	97.87	106.33	107.02	7.0%
Houston, TX	6.283%	100.00	101.44	103.75	108.28	110.31	10.3%
Nashville, TN	6.251%	100.00	99.83	101.78	107.19	107.80	7.8%
Cincinnati, OH	6.128%	100.00	96.54	96.67	102.21	104.73	4.7%
Charlotte, NC	5.466%	100.00	97.17	102.30	107.08	109.16	9.2%
Salt Lake City, UT	5.191%	100.00	102.02	106.07	111.13	112.50	12.5%
Tampa, FL	5.168%	100.00	100.27	100.50	108.92	111.21	11.2%
Phoenix, AZ	4.977%	100.00	104.11	106.61	114.90	119.44	19.4%
Jacksonville, FL	4.465%	100.00	97.37	104.98	106.75	110.76	10.8%
Raleigh, NC	4.176%	100.00	97.63	100.60	103.79	105.28	5.3%
Las Vegas, NV	4.156%	100.00	107.52	109.76	120.38	129.22	29.2%
Orlando, FL	3.337%	100.00	103.21	103.06	112.19	114.52	14.5%
Columbus, OH	3.221%	100.00	94.39	96.34	101.98	105.58	5.6%
Greenville, SC	1.882%	100.00	95.70	93.83	101.75	104.02	4.0%
Greensboro, NC	1.827%	100.00	97.66	100.34	102.23	103.29	3.3%
Tucson, AZ	1.760%	100.00	99.47	98.00	102.28	106.11	6.1%
Austin, TX	1.577%	100.00	99.65	100.97	108.35	110.14	10.1%
Total / Total Weighted Average	**100.0%**						**10.3%[(5)]**

(1) Based on estimated total investment in each market as of September 30, 2013. These will be the weighting factors for measurement of HPA and will at no time change as it relates to the Series B Participating Preferred Shares.

(2) For the illustrative purposes of this table, the HPA has been indexed as of September 30, 2012 and, as such, a baseline index value of 100.0 has been assigned to each market as of such date. The FHFA POI values with respect to the other periods presented are relative measures calculated in relation to the baseline index value. The actual HPA will be indexed as of September 30, 2013. See the table on the following page for an illustration of how the HPA will be indexed as of September 30, 2013.

(3) Our Dallas-Fort Worth, TX market is comprised of the Dallas-Plano-Irving and Fort Worth-Arlington Metropolitan Divisions, with each division being given equal weighting for purposes of determining HPA.

(4) The home price index for the Greater Chicago Area, IL market is Chicago-Naperville-Arlington Heights, IL.

(5) Represents the total weighted average percentage change in the HPA for the period from September 30, 2012 to September 30, 2013, based on the market weighting percentages set forth above.

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The following table sets forth, for each of our top 20 markets, the actual POI value as of September 30, 2013, which is the most recent date for which POI data is available and the date from which HPA will be measured for purposes of calculating the HPA Amount. The table also sets forth the calculations performed in order to assign a baseline value of 100.0 for all markets as of September 30, 2013 for purposes of calculating the change in HPA for such markets relative to such date.

Market	Relative Weighting Applied in Determining HPA(1)	Actual POI Value as of Sep 30, 2013(2)	Multiplier Applied to Establish Baseline Value(3)	Assigned Baseline Value(4)
Dallas-Fort Worth, TX(5)	9.860%	190.61	0.525	100.0
Indianapolis, IN	8.937%	169.38	0.590	100.0
Atlanta, GA	7.693%	179.60	0.557	100.0
Greater Chicago Area, IL(6)	7.645%	184.21	0.543	100.0
Houston, TX	6.283%	245.48	0.407	100.0
Nashville, TN	6.251%	233.27	0.429	100.0
Cincinnati, OH	6.128%	170.81	0.585	100.0
Charlotte, NC	5.466%	191.68	0.522	100.0
Salt Lake City, UT	5.191%	327.40	0.305	100.0
Tampa, FL	5.168%	215.50	0.464	100.0
Phoenix, AZ	4.977%	243.04	0.411	100.0
Jacksonville, FL	4.465%	217.47	0.460	100.0
Raleigh, NC	4.176%	200.94	0.498	100.0
Las Vegas, NV	4.156%	143.69	0.696	100.0
Orlando, FL	3.337%	186.00	0.538	100.0
Columbus, OH	3.221%	186.28	0.537	100.0
Greenville, SC	1.882%	202.27	0.494	100.0
Greensboro, NC	1.827%	162.56	0.615	100.0
Tucson, AZ	1.760%	215.05	0.465	100.0
Austin, TX	1.577%	321.54	0.311	100.0

(1) Based on estimated total investment in each market as of September 30, 2013. These will be the weighting factors for measurement of HPA and will at no time change as it relates to the Series B Participating Preferred Shares.

(2) Represents the values as published in the POI for each market as of the date of this prospectus. Such values will remain constant for purposes of calculating the HPA Amount, notwithstanding any revisions by the FHFA in subsequent POI releases.

(3) In order to index the POI value for each market as of September 30, 2013, which is the date from which the cumulative change in HPA will be measured for purposes of calculating the HPA Amount, the POI value for each market as of such date is being assigned a baseline index value of 100.0 by multiplying each by the multiplier indicated in the table above. The multipliers set forth above are presented solely for the purpose of indicating the numerical relationship between the actual POI value for each of the markets and the indexed baseline value of 100.0 for such markets. The multipliers will remain constant throughout the term of the Series B Participating Preferred Shares and will not be adjusted to reflect any revisions by the FHFA of the POI values for each market as of September 30, 2013 subsequent to the date of this prospectus.

(4) Equals the product of the actual POI value for each market as of September 30, 2013, multiplied by the baseline multiplier for each market.

(5) Our Dallas-Fort Worth, TX market is comprised of the Dallas-Plano-Irving and Fort Worth-Arlington Metropolitan Divisions, with each division being given equal weighting for purposes of determining HPA.

(6) The home price index for the Greater Chicago Area, IL market is Chicago-Naperville-Arlington Heights, IL.

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The following table illustrates how HPA, as measured by the FHFA s POI, would be applied for purposes of determining the liquidation preference, dividend amounts and annual and total return for the Series B Participating Preferred Shares based on the following hypothetical assumptions:

That the Series B Participating Preferred Shares were issued on December 31, 2013.

Constant annual HPA of 5%.

Dividend rate per annum of 5.000% for the period from the date of issuance to but excluding December 31, 2020.

Dividend rate per annum of 10.000% for the period from and including December 31, 2020 until the Series B Participating Preferred Shares are no longer outstanding.

That during the period presented, there is no liquidation, dissolution or winding up of the Company and that the Company does not exercise its option to redeem or convert the Series B Participating Preferred Shares.

The information in this table is for illustrative purposes only and is not intended to predict future home price appreciation, liquidation preferences, dividend amounts or return on investment. See Risk Factors The various hypothetical figures and illustrations contained in this prospectus should not be taken as an indication or prediction of future investment results and Risk Factors There is no guarantee that any HPA Amount will accrue or be paid on the Series B Participating Preferred Shares.

Illustrative Effect of Hypothetical HPA on Series B Participating Preferred Shares

Year	Date	Cumulative Hypothetical HPA	Investor Participation Percentage	Hypothetical HPA Factor	Hypothetical Cumulative Net HPA Amount	Hypothetical Liquidation Preference (1)	Hypothetical Dividend	Hypothetical Return % Annual	Hypothetical Return % Gross(2)
Offering	December 31, 2013(3)					$ 25.00			
Year 1(4)	December 31, 2014	5.0%	50%	2.5%	$ 0.63	$ 25.63	$ 1.250	7.50	7.50
Year 2(4)	December 31, 2015	10.0%	50%	5.0%	$ 1.25	$ 26.25	$ 1.250	7.50	15.00
Year 3(4)	December 31, 2016	15.0%	50%	7.5%	$ 1.88	$ 26.88	$ 1.250	7.50	22.50
Year 4(4)	December 31, 2017	20.0%	50%	10.0%	$ 2.50	$ 27.50	$ 1.250	7.50	30.00
Year 5(5)	December 31, 2018	25.0%	50%	12.5%	$ 3.13	$ 28.13	$ 1.250	7.50	37.50
Year 6(5)	December 31, 2019	30.0%	50%	15.0%	$ 3.75	$ 28.75	$ 1.250	7.50	45.00
Year 7(5)	December 31, 2020	35.0%	50%	17.5%	$ 4.38	$ 29.38	$ 1.250	7.50	52.50
Year 8(6)	December 31, 2021	40.0%	N/A		$ 4.38	$ 29.38	$ 2.938	11.750	64.25
Year 9(6)	December 31, 2022	45.0%	N/A		$ 4.38	$ 29.38	$ 2.938	11.750	76.00
Year 10(6)	December 31, 2023	50.0%	N/A		$ 4.38	$ 29.38	$ 2.938	11.750	87.75

(1)

Reflects the initial liquidation preference as increased by the hypothetical HPA Amount. The HPA Amount is subject to a cap as described below in this section under -HPA Amount Cap. Such cap would apply (i) in the event of a liquidation, dissolution or winding up of the Company, (ii) if the Company exercises its option to redeem or convert the Series B Participating Preferred Shares prior to

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December 31, 2020 or (iii) on December 31, 2020, which is the date on which the HPA Amount becomes fixed and the date on which dividends begin to accrue on the initial liquidation preference plus the HPA Amount (if any). Assuming a 5% dividend rate, the cap on the HPA Amount would limit the HPA Amount to approximately 4%. To illustrate the application of the cap, assuming a 10% rather than a 5% cumulative hypothetical HPA, and assuming that the company has not redeemed or converted the Series B Participating Preferred Shares or liquidated, on December 31, 2020, the Hypothetical HPA Amount would be fixed at $8.84, reflecting a 9% internal rate of return.

(2) Calculated as (A) cumulative dividends plus (i) hypothetical accrued HPA Amount (for periods prior to December 31, 2020) or (ii) the difference between the initial price of $25.00 and the Adjusted Value (for periods after December 31, 2020) divided by (B) the $25.00 issue price per Series B Participating Preferred Share.

(3) The actual measuring date for the index will be from September 30, 2013. The December 31, 2013 measuring date is for illustrative purposes only.

(4) Prior to January 1, 2018, the Series B Participating Preferred Shares are not convertible or redeemable.

(5) From and after January 1, 2018, the Series B Participating Preferred Shares are redeemable and convertible at our option. See Description of Series B Participating Preferred Shares Redemption Redemption at Our Option and Description of Series B Participating Preferred Shares Conversion Rights Conversion at Our Option.

(6) From and after December 31, 2020, the HPA Amount will equal the HPA Amount calculated with respect to the period ended September 30, 2020, and will thereafter remain fixed at that amount. From and after December 31, 2020, a dividend rate of 10.000% per annum will be applied to the sum of the initial liquidation preference and the HPA Amount calculated with respect to the period ended September 30, 2020.

HPA Amount Cap	Until December 31, 2020, the amount payable upon any conversion, redemption or liquidation event will be subject to a cap, such that the total internal rate of return, when considering the initial liquidation preference, the HPA Amount (if positive), plus dividends (whether paid or accrued) to, but excluding, the date of redemption, conversion or liquidation, will not exceed 9.0%. On December 31, 2020, the HPA Amount will become fixed and cease to accrue and the dividend yield will increase to 10.000% per annum on the liquidation preference plus the HPA Amount.
Redemption at Our Option	We may not redeem the Series B Participating Preferred Shares until after December 31, 2017, except in limited circumstances relating to maintaining our qualification as a REIT, as described in Description of Series B Participating Preferred Shares Redemption at Our Option in this prospectus and pursuant to the special optional redemption provisions upon a change in control that are specified below.
	Any time after December 31, 2017 but before December 31, 2020, we may redeem for cash all but not less than all of the Series B Participating Preferred Shares at a redemption price per Series B Participating Preferred Share equal to the sum of the initial liquidation preference, and any HPA Amount (if positive) plus accrued and unpaid dividends (whether or not authorized or declared) to, but excluding, the redemption date.
	At any time after December 31, 2020, we may redeem for cash all but not less than all of the Series B Participating Preferred Shares at a redemption price per share equal to the initial liquidation preference of $25.00 per share, plus the HPA Amount (if positive) calculated with respect to the period ended September 30, 2020, plus any accrued but unpaid dividends. The initial liquidation preference of $25.00 plus the HPA Amount calculated with respect to the period ended September 30, 2020, is referred to as the Adjusted Value.
Conversion at Our Option	At any time after December 31, 2017, we may convert all but not less than all of the Series B Participating Preferred Shares into our

	Class A common shares. The conversion ratio for such one-time conversion will be determined by a formula and cannot be determined until the conversion date. See Description of Series B Participating Preferred Shares Conversion Rights Conversion at Our Option.
	If such one-time conversion were to occur after December 31, 2017 but before December 31, 2020, the formula for determining the conversion ratio per Series B Participating Preferred Share will be the sum of (i) the initial liquidation preference, (ii) the HPA Amount for the relevant period (if positive) and (iii) any accrued and unpaid dividends to, but excluding, the conversion date (to occur on the fourth business day following the notice of conversion), divided by the one-day volume-weighted average price of our Class A common shares on the NYSE, or VWAP, as reported by Bloomberg, if available, on the day the notice of conversion is issued.
	If such one-time conversion occurs on or after December 31, 2020, the formula for determining the conversion ratio will be (i) the Adjusted Value, plus any accrued and unpaid dividends to, but not including, the conversion date, divided by (ii) the VWAP as reported by Bloomberg on the date the notice of conversion is issued.
	Any Class A common shares issued in connection with a conversion described in this section will be registered under the Securities Act and listed on the NYSE or other national exchange.
Special Redemption Option upon a Change of Control	Upon the occurrence of a Change of Control (as defined below), we may redeem for cash all but not less than all of the Series B Participating Preferred Shares within 120 days after the date on which such Change of Control occurred, at a price equal to the sum of (i) the initial liquidation preference, (ii) the HPA Amount (if positive) and (iii) an amount per Series B Participating Preferred Share equal to all dividends (whether or not authorized or declared) accrued and unpaid thereon to, but excluding, the date of final distribution to such holders, to, but excluding, the redemption date. If, prior to the Change of Control Conversion Date (as defined herein), we exercise our optional redemption rights relating to the Series B Participating Preferred Shares, the holders of Series B Participating Preferred Shares will not be permitted to exercise the conversion right described below.
	A Change of Control means, after the initial issuance of the Series B Participating Preferred Shares, the following have occurred and are continuing:
	the acquisition by any person, including any syndicate or group deemed to be a person under Section 13(d)(3) of the Exchange

	Act, of beneficial ownership, directly or indirectly, through a purchase, merger or other acquisition transaction or series of purchases, mergers or other acquisition transactions of securities of the Company entitling that person to exercise more than 50% of the total voting power of all shares of beneficial interest of the Company entitled to vote generally in the election of our trustees (except that such person will be deemed to have beneficial ownership of all securities that such person has the right to acquire, whether such right is currently exercisable or is exercisable only upon the occurrence of a subsequent condition); and following the closing of any transaction referred to in the bullet point above, neither we nor the acquiring or surviving entity has a class of common securities (or American Depositary Receipts representing such securities) listed on the NYSE, the NYSE MKT or NASDAQ or listed or quoted on an exchange or quotation system that is a successor to the NYSE, the NYSE MKT or NASDAQ.
Conversion Rights of Holders in Connection with a Change of Control	Upon the occurrence of a Change of Control, each holder of Series B Participating Preferred Shares will have the right (unless, prior to the Change of Control Conversion Date, we have provided or provide notice of our election to redeem the Series B Participating Preferred Shares) to convert some or all of the Series B Participating Preferred Shares held by such holder on the Change of Control Conversion Date into a number of our Class A common shares per Series B Participating Preferred Share equal to the lesser of: the quotient obtained by dividing (i) the sum of (x) the initial liquidation preference plus (y) the HPA Amount for the relevant period (if positive) plus (z) any accrued and unpaid dividends (whether or not declared) to, but excluding, the Change of Control Conversion Date (unless the Change of Control Conversion Date is after a record date for a Series B Participating Preferred Shares dividend payment for which full dividends have been declared and prior to the corresponding Series B Participating Preferred Shares dividend payment date, in which case no additional amount for such accrued and unpaid dividend will be included in this sum and such declared dividend will instead be paid, on such dividend payment date, to the holder of record of the Series B Participating Preferred Shares to be converted as of 5:00 p.m. New York City time, on such record date) by (ii) the Class A Share Price; and (i.e., the Share Cap), subject to certain adjustments; subject, in each case, to provisions for the receipt of alternative consideration as described in this prospectus. If, prior to the Change of Control Conversion Date, we have provided or provide a redemption notice, pursuant to our right of redemption in

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	connection with a Change of Control, holders of Series B Participating Preferred Shares will not have any right to convert the Series B Participating Preferred Shares in connection with the Change of Control Conversion Right and any Series B Participating Preferred Shares selected for redemption that have been tendered for conversion will be redeemed on the related date of redemption instead of converted on the Change of Control Conversion Date.
	For definitions of Change of Control Conversion Right, Change of Control Conversion Date and Class A Share Price and for a description of the adjustments and provisions for the receipt of alternative consideration that may be applicable to the Change of Control Conversion Right, see Description of Series B Participating Preferred Shares Conversion Rights.
Listing	We intend to apply to list the Series B Participating Preferred Shares on the NYSE under the symbol AMHPRB. If the listing application is approved, we expect trading of the Series B Participating Preferred Shares to commence within 30 days after initial delivery of the shares.
Settlement	The underwriters expect to deliver the Series B Participating Preferred Shares against payment therefor through The Depository Trust Company on or about , 2013, which is the business day following the pricing of this offering.
Risk Factors	Investing in our Series B Participating Preferred Shares involves various risks. You should read carefully and consider the matters discussed under the caption entitled Risk Factors beginning on page 31 of this prospectus before making a decision to invest our Series B Participating Preferred Shares.

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SUMMARY SELECTED FINANCIAL DATA

The following table presents selected historical consolidated financial information and selected portfolio data as of September 30, 2013 (unaudited) and December 31, 2012 and 2011 and for the nine months ended September 30, 2013 and 2012 (unaudited), for the year ended December 31, 2012 and for the period from June 23, 2011 to December 31, 2011. The selected consolidated financial information presented below under the captions Consolidated Statements of Operations Data and Consolidated Balance Sheets Data have been derived from our consolidated financial statements. Under the provisions of ASC 805, *Business Combinations,* we have reflected transactions between businesses under common control retroactively based on the date AH LLC commenced acquiring properties, June 23, 2011. As such, the statements of operations reflect activity prior to our date of formation, and the properties contributed to us by AH LLC are reflected retroactively on the balance sheets based on AH LLC s net book value. Therefore, our selected consolidated financial data may not be indicative of our past or future results and does not reflect our financial position or results of operations had it been presented as if we had been operating independently during the period presented. Because the information presented below is only a summary and does not provide all of the information contained in our historical consolidated financial statements, including the related notes, you should read it in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements, including the related notes, included elsewhere in this prospectus.

Consolidated Statements of Operations Data

(Amounts in thousands, except share information)

	For the Nine Months Ended September 30, 2013	2012	Year Ended December 31, 2012	Period from June 23, 2011 to December 31, 2011
Revenues:				
Rents from single-family properties	$ 72,887	$ 1,263	$ 4,540	$ 65
Other	1,255			
Total revenues	74,142	1,263	4,540	65
Expenses:				
Property operating expenses				
Leased single-family properties	26,941	493	1,744	27
Vacant single-family properties	13,993	635	1,846	12
General and administrative expense	5,178	3,948	7,199	47
Advisory fees	6,352		937	
Interest expense	370			
Noncash share-based compensation expense	606		70	
Acquisition fees and costs expensed	3,985		869	
Depreciation and amortization	37,827	592	2,111	21
Total expenses	95,252	5,668	14,776	107
Gain on remeasurement of equity method investment	10,945			
Remeasurement of Series E units	(438)			
Income / (loss) from continuing operations	(10,603)	(4,405)	(10,236)	(42)
Discontinued operations				
Gain on disposition of assets	904			
Income from discontinued operations	104			

Total income from discontinued operations	1,008

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	For the Nine Months Ended September 30, 2013	2012	Year Ended December 31, 2012	Period from June 23, 2011 to December 31, 2011
Net income / (loss)	(9,595)	(4,405)	(10,236)	(42)
Noncontrolling interest	9,357			
Conversion of preferred units	10,456			
Net loss attributable to common shareholders	$ (29,408)	$ (4,405)	$ (10,236)	$ (42)
Weighted average shares outstanding basic and diluted	102,729,661	3,301,667	7,225,512	3,301,667
Net loss per share basic and diluted:				
Loss from continuing operations	$ (0.30)	$ (1.33)	$ (1.42)	$ (0.01)
Discontinued operations	0.01			
Net loss attributable to common shareholders per share basic and diluted	$ (0.29)	$ (1.33)	$ (1.42)	$ (0.01)

Consolidated Balance Sheets Data

	As of September 30, 2013 (unaudited) (in thousands)	As of December 31, 2012 (in thousands)	2011 (in thousands)
Single-family properties, net	$ 3,530,122	$ 505,713	$ 3,495
Cash and cash equivalents	158,065	397,198	
Rent and other receivables	6,758	6,586	11
Restricted cash for resident security deposits	21,282		
Escrow deposits, prepaid expenses and other assets	23,861	11,961	17
Deferred costs and other intangibles, net	24,518		
Goodwill	120,655		
Total assets	$ 3,885,261	$ 921,458	$ 3,523
Total liabilities	$ 395,968	$ 16,294	$ 49
Total equity	3,489,293	905,164	3,474
Total liabilities and equity	$ 3,885,261	$ 921,458	$ 3,523

Selected Other Portfolio Data

	As of September 30, 2013 (unaudited) (in thousands)	As of December 31, 2012	2011
Leased single-family properties	14,384	1,164	19

Vacant single-family properties available for lease	2,736	623	2
Single-family properties being renovated	4,147	1,857	12
Total single-family properties owned	21,267	3,644	33

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RISK FACTORS

An investment in our Series B Participating Preferred Shares involves a high degree of risk. Before making an investment decision, you should carefully consider the following risk factors, together with the other information contained in this prospectus. If any of the risks discussed in this prospectus occur, our business, prospects, financial condition, results of operations and our ability to make cash distributions to our shareholders could be materially and adversely affected. In that case, the trading price of our Series B Participating Preferred Shares could decline significantly, and you could lose all or part of your investment. Some statements in this prospectus, including statements in the following risk factors, constitute forward-looking statements. Please refer to the section entitled Forward-Looking Statements.

Risks Related to Our Business

We are employing a new and untested business model with no proven track record, which may make our business difficult to evaluate.

Until very recently, the single-family rental business consisted primarily of private and individual investors in local markets and was managed individually or by small, local property managers. Our investment strategy involves purchasing a large number of residential properties and leasing them to suitable tenants. No peer companies exist with an established track record to enable us to predict whether our investment strategy can be implemented successfully over time. It will be difficult for you to evaluate our potential future performance without the benefit of established track records from companies implementing a similar investment strategy. We may encounter unanticipated problems implementing our investment strategy, which may adversely affect our results of operations and ability to make distributions on our Series B Participating Preferred Shares and cause our share price to decline significantly. We believe the acquisition, operation and management of multi-family residential real estate is the most comparable established model for our business, but in contrast to multi-family operations, the geographic dispersion of single-family properties (even within a local clustering) creates significantly greater operational and maintenance challenges and, potentially, significantly higher per-unit operating costs. In addition, since each home has unique features, appliances and building materials, renovations, maintenance, marketing and operational tasks will be far more varied and demanding than in a typical multi-family setting. We may be unable to operate a large portfolio of single-family rental properties in a cost-effective and profitable manner and our business plan may not succeed. We also can provide no assurance that we will be able to successfully achieve our objective of providing attractive risk-adjusted returns to our shareholders.

We are a recently organized REIT with a limited operating history, and we may not be able to successfully operate our business or generate sufficient cash flows to make or sustain distributions on our preferred and common shares.

We were organized in October 2012, and we commenced operations in November 2012 upon completion of our initial private placement. We have a limited operating history, and, through September 30, 2013, we have not generated any earnings. We may not be able to successfully operate our business or implement our operating policies and investment strategy as described in this prospectus. Furthermore, we may not be able to generate sufficient cash flows to pay our operating expenses, service any debt we may incur in the future and make distributions to our shareholders. Our ability to successfully operate our business and implement our operating policies and investment strategy depends on many factors, including:

- the availability of, and our ability to identify, attractive acquisition opportunities consistent with our investment strategy;
- our ability to contain renovation, maintenance, marketing and other operating costs for our properties;
- our ability to maintain high occupancy rates and target rent levels;
- our ability to compete with other investors entering the single-family sector;

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- costs that are beyond our control, including title litigation, litigation with tenants or tenant organizations, legal compliance, real estate taxes, homeowners association, or HOA, fees and insurance;

- judicial and regulatory developments affecting landlord-tenant relations that may affect or delay our ability to dispossess or evict occupants or increase rents;

- judicial and regulatory developments affecting banks and other mortgage holders ability to foreclose on delinquent borrowers;

- reversal of population, employment or homeownership trends in target markets;

- interest rate levels and volatility, such as the accessibility of short-and long-term financing on desirable terms; and

- economic conditions in our target markets, including changes in employment and household earnings and expenses, as well as the condition of the financial and real estate markets and the economy generally.

In addition, we face significant competition in acquiring attractive properties on advantageous terms, and the value of the properties that we acquire may decline substantially after we purchase them.

We may not be able to effectively manage our growth, and any failure to do so may have an adverse effect on our business and operating results.

We have a limited operating history, and we plan to grow our own property portfolio and operations rapidly. From commencement of our operations in November 2012 through September 30, 2013, we have acquired 21,267 single-family properties in 22 states. Our future operating results may depend on our ability to effectively manage our rapid growth, which is dependent, in part, upon our ability to:

- stabilize and manage a rapidly increasing number of properties and tenant relationships while maintaining a high level of tenant satisfaction and building and enhancing our brand;

- identify and supervise an increasing number of suitable third parties on which we rely to provide certain services to our properties;

- attract, integrate and retain new management and operations personnel as our organization grows in size and complexity;

- continue to improve our operational and financial controls and reporting procedures and systems; and

- scale our technology and other infrastructure platforms to adequately service new properties.

We cannot assure you that we will be able to achieve these results or that we may otherwise be able to manage our growth effectively. Any failure to do so may have an adverse effect on our business and operating results.

Because we have not yet identified any specific properties (other than properties held in escrow) to acquire with any net proceeds of this offering remaining after repayment of debt, you will be unable to evaluate the economic merits of our investments made with such net proceeds before making an investment decision to purchase our Series B Participating Preferred Shares.

Because we have not yet identified any specific properties (other than properties held in escrow) to acquire with the net proceeds of this offering remaining after repayment of debt or committed any portion of the net proceeds of this offering to any specific property investment, you will be unable to evaluate the economic merits of our investments made with such proceeds before making an investment decision to purchase our Series B Participating Preferred Shares.

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We will have broad authority to invest the net proceeds of this offering in any real estate investments that we may identify in the future, and we may use those proceeds to make investments with which you may not agree. You will be unable to evaluate the economic merits of our properties before we invest in them and will be relying on our ability to select attractive investment properties. We also will have broad discretion in implementing policies regarding tenant creditworthiness, and you will not have the opportunity to evaluate potential tenants. In addition, our investment policies may be amended or revised from time to time at the discretion of our board of trustees, without a vote of our shareholders. These factors will increase the uncertainty and the risk of investing in our Series B Participating Preferred Shares.

Although we intend to use the net proceeds of this offering to acquire, renovate and rent single-family properties in our target markets (exclusive of the portion used to repay indebtedness we have incurred or expect to incur under our credit facility), including certain escrowed properties, we cannot assure you that we will be able to do so. Our failure to apply the net proceeds of this offering effectively or find suitable properties to acquire in a timely manner or on acceptable terms could result in losses or returns that are substantially below expectations.

We intend to continue to rapidly expand our scale of operations and make acquisitions even if the rental and housing markets are not as favorable as they have been in recent months, which could adversely impact anticipated yields.

Our long-term growth depends on the availability of acquisition opportunities in our target markets at attractive pricing levels. We believe various factors and market conditions have made homes available for purchase at prices that are below replacement costs. We expect that in the future housing prices will stabilize and return to more normalized levels, and therefore future acquisitions may be more costly. There are many factors that may cause a recovery in the housing market that would result in future acquisitions becoming more expensive and possibly less attractive than recent past and present opportunities, including:

- improvements in the overall economy and job market;
- a resumption of consumer lending activity and greater availability of consumer credit;
- improvements in the pricing and terms of mortgage-backed securities;
- the emergence of increased competition for single-family assets from private investors and entities with similar investment objectives to ours; and
- tax or other government incentives that encourage homeownership.

We have not adopted and do not expect to adopt a policy of making future acquisitions only if they are accretive to existing yields and distributable cash. We plan to continue acquiring properties as long as we believe such properties offer an attractive total return opportunity. Accordingly, future acquisitions may have lower yield characteristics than recent past and present opportunities and if such future acquisitions are funded through equity issuances, the yield and distributable cash per share will be reduced, and the value of our Series B Participating Preferred Shares may decline.

Our future growth depends, in part, on the availability of additional debt or equity financing. If we cannot obtain additional financing on terms favorable or acceptable to us, our growth may be limited.

Part of our business strategy may involve the use of debt and equity financing to increase potential returns to our shareholders in the future. Although we do not believe we need to use leverage to execute our business strategy, our inability in the future to obtain additional financing on attractive terms, or at all, could adversely impact our ability to execute our business strategy, which could adversely affect our growth prospects and future shareholder returns. Our access to capital depends, in part, on:

- general business conditions;

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- financial market conditions;
- the market s perception of our business prospects and growth potential;
- the market price of our Class A common shares;
- our current debt levels; and
- our current and expected earnings, cash flow and distributions.

We cannot assure you that we will be able to obtain debt or equity financing on terms favorable or acceptable to us or at all. If we are unable to do so, we may have to curtail our investment activities, which could limit our growth prospects, and we may be forced to dispose of assets at inopportune times in order to maintain our REIT qualification. Our pace of acquisitions may also depend on the level of funds available for investment. In addition, if we are unable to obtain debt financing, we may have to rely more heavily on additional equity issuances, which may be dilutive to our shareholders, or on less efficient forms of debt financing that require a larger portion of our cash flow from operations, thereby reducing funds available for our operations, future business opportunities, cash distributions to our shareholders and other purposes.

We may also be limited in the amounts we may borrow under our credit facility with Wells Fargo. The amount that may be borrowed under our credit facility is generally based on the lower of 50% of the value of our qualifying leased and un-leased properties and certain other measures based in part on the net income generated by our qualifying leased and un-leased properties, which we refer to as the borrowing base. Because the borrowing base is determined in part by the estimated value of, and the net income generated by, our qualifying leased and un-leased properties and the quantity, value and rentability of properties in our portfolio may fluctuate from time to time, we may be limited in the amounts we are able to borrow under our credit facility.

Our revenue and expenses are not directly correlated, and because a large percentage of our costs and expenses are fixed, we may not be able to adapt our cost structure to offset declines in our revenue.

Most of the expenses associated with our business, such as acquisition costs, renovation and maintenance costs, real estate taxes, HOA fees, personal and ad valorem taxes, insurance, utilities, employee wages and benefits and other general corporate expenses, are relatively inflexible and will not necessarily decrease with a reduction in revenue from our business. Our assets also are prone to depreciation and will require a significant amount of ongoing capital expenditures. Our expenses and ongoing capital expenditures also will be affected by inflationary increases, and certain of our cost increases may exceed the rate of inflation in any given period. By contrast, our rental income is affected by many factors beyond our control such as the availability of alternative rental housing and economic conditions in our target markets. In addition, state and local regulations may require us to maintain properties that we own, even if the cost of maintenance is greater than the value of the property or any potential benefit from renting the property. As a result, we may not be able to fully offset rising costs and capital spending by higher rental rates, which could have a material adverse effect on our results of operations and cash available for distribution.

Our success depends, in part, upon our ability to hire and retain highly skilled managerial, investment, financial and operational personnel, and the past performance of our senior management may not be indicative of future results.

The implementation of our business plan may require that we employ additional qualified personnel. Competition for highly skilled managerial, investment, financial and operational personnel is intense. As additional, large real estate investors have entered the single-family rental business, we have faced increased challenges in hiring and retaining personnel, and we cannot assure our shareholders that we will be successful in attracting and retaining such skilled personnel. If we are unable to hire and retain qualified personnel as required, our growth and operating results could be adversely affected.

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You should not rely upon the past performance of our senior management, as their past performance at Public Storage, which was in the self-storage business, or their other prior professional endeavors may not be indicative of our future results. Other than their experience with our company and AH LLC, which was organized in June 2011, our executive team has no experience in the business of acquiring and renting single-family residences.

We are dependent on our executive officers and dedicated personnel, and the departure of any of our key personnel could materially and adversely affect us.

We rely on a small number of persons to carry out our business and investment strategies. Any of our senior management may cease to provide services to us at any time. The loss of the services of any of our key management personnel, or our inability to recruit and retain qualified personnel in the future, could have an adverse effect on our business and financial results. As we expand, we will continue to need to attract and retain qualified additional senior management but may not be able to do so on acceptable terms or at all.

Our investments are and will continue to be concentrated in our target markets and in the single-family properties sector of the real estate industry, which exposes us to downturns in our target markets or in the single-family properties sector.

Our investments in real estate assets are and will continue to be concentrated in target markets and in the single-family properties sector of the real estate industry. A downturn or slowdown in the rental demand for single-family housing caused by adverse economic, regulatory or environmental conditions, or other events, in our target markets may have a greater impact on the value of our properties or our operating results than if we had more fully diversified our investments. While we have limited experience in this sector, we believe that there may be some seasonal fluctuations in rental demand with demand higher in the spring and summer than in the fall and winter. Such seasonal fluctuations may impact our operating results.

In addition to general, regional, national and international economic conditions, our operating performance will be impacted by the economic conditions in our target markets. We acquire, renovate and rent single-family properties in our target markets, which currently include MSAs within 22 states. As of September 30, 2013, approximately 57% of our properties were concentrated in only five states Texas, Florida, North Carolina, Indiana and Ohio. We base a substantial part of our business plan on our belief that property values and operating fundamentals for single-family properties in these markets will improve significantly over the next several years. However, each of these markets experienced substantial economic downturns in recent years and could experience similar or worse economic downturns in the future. We can provide no assurance as to the extent property values and operating fundamentals in these markets will improve, if at all. If the recent economic downturn in these markets persists or if we fail to accurately predict the timing of economic improvement in these markets, the value of our properties could decline and our ability to execute our business plan may be adversely affected, which could adversely affect our financial condition, operating results and ability to make distributions to our shareholders and cause the value of your investment to decline.

We rely on local, third-party providers for services that may become limited or unavailable and may harm our brand and reputation and operation results.

We rely on local, third-party vendors and service providers, including third-party house improvement professionals, leasing agents and property management companies in situations when it is cost-effective to do so or our internal staff is unable to perform these functions. We do not have exclusive or long-term contractual relationships with any of these third-party providers, and we can provide no assurance that we will have uninterrupted or unlimited access to their services. Furthermore, selecting, managing and supervising these third-party providers require significant management resources and expertise. If we do not select, manage and supervise appropriate third parties for these services, our brand and reputation and operating results may suffer. Moreover, we may not successfully detect and prevent fraud, incompetence or theft by our third-party providers,

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which could subject us to material liability or responsibility for damages, fines and/or penalties associated with such fraud, incompetence or theft.

In addition, any removal or termination of third-party providers would require us to seek new vendors or providers, which would create delays and adversely affect our operations. If we do not select appropriate third-party providers, or if the third-party providers we do select fail to deliver quality services, our brand and reputation, operating results and cash flows from our properties may be adversely affected, including entities in which we and our affiliates have an interest.

AH LLC may not be able to effectively control the timing and costs relating to the renovation of properties, which may adversely affect our operating results and our ability to make distributions on our preferred and common shares.

Nearly all of our properties require some level of renovation immediately upon their acquisition or in the future following expiration of a lease or otherwise. We may acquire properties that we plan to extensively renovate. We also may acquire properties that we expect to be in good condition only to discover unforeseen defects and problems that require extensive renovation and capital expenditures. To the extent properties are leased to existing tenants, renovations may be postponed until the tenant vacates the premises, and we will pay the costs of renovating. In addition, in order to reposition properties in the rental market, we will be required to make ongoing capital improvements and replacements and may need to perform significant renovations and repairs from time to time that tenant deposits and insurance may not cover.

Our properties have infrastructure and appliances of varying ages and conditions. Consequently, AH LLC routinely retains independent contractors and trade professionals to perform physical repair work, and we are exposed to all of the risks inherent in property renovation, including potential cost overruns, increases in labor and materials costs, delays by contractors in completing work, delays in the timing of receiving necessary work permits, certificates of occupancy and poor workmanship. If our assumptions regarding the costs or timing of renovation across our properties prove to be materially inaccurate, our operating results and ability to make distributions to our shareholders may be adversely affected.

We face significant competition for acquisitions of our target properties, which may limit our strategic opportunities and increase the cost to acquire those properties.

We face significant competition for attractive acquisition opportunities in our target markets from other large real estate investors, some of which have greater financial resources and a lower cost of capital than we do. Several REITs and other funds have recently deployed, and others are expected to deploy in the near future, significant amounts of capital to purchase single-family homes and may have investment objectives that overlap and compete with ours, including in our target markets. This activity has adversely impacted our level of purchases in certain of our target markets. If our business model or a similar model proves to be successful, we can expect competition to intensify significantly. As a result, the purchase price of potential acquisition properties may be significantly elevated, or we may be unable to acquire properties on desirable terms or at all.

We face significant competition in the leasing market for quality tenants, which may limit our ability to rent our single-family homes on favorable terms or at all.

We face competition for tenants from other lessors of single-family properties, apartment buildings and condominium units, and the continuing development of apartment buildings and condominium units in many of our target markets increases the supply of housing and exacerbates competition for tenants. Many of these competitors may successfully attract tenants with better incentives and amenities, which could adversely affect our ability to obtain quality tenants and lease our single-family properties on favorable terms or at all. Additionally, some competing housing options may qualify for government subsidies that may make such options more affordable and therefore more attractive than our properties. At September 30, 2013, we owned 21,267 single-family properties, 14,384, or 67.6%, of which were leased. Our operating results and ability to make distributions to our shareholders would be adversely affected if we are not able to lease our properties on favorable terms or at all.

The large supply of single-family homes becoming available for purchase as a result of the heavy volume of foreclosures, combined with historically low residential mortgage rates, may cause some potential renters to seek to purchase residences rather than lease them and, as a result, cause a decline in the number and quality of potential tenants.

The large supply of foreclosed homes, along with low residential mortgage interest rates currently available and government sponsored programs to promote home ownership, has made home ownership more affordable and more accessible for potential renters who have strong credit. These factors may encourage potential renters to purchase residences rather than lease them, thereby causing a decline in the number and quality of potential tenants available to us.

Our evaluation of properties involves a number of assumptions that may prove inaccurate, which could result in us paying too much for properties we acquire or overvaluing our properties or our properties failing to perform as we expect.

In determining whether a particular property meets our investment criteria, we make a number of assumptions, including assumptions related to estimated time of possession and estimated renovation costs and time frames, annual operating costs, market rental rates and potential rent amounts, time from purchase to leasing and tenant default rates. These assumptions may prove inaccurate. As a result, we may pay too much for properties we acquire or overvalue our properties, or our properties may fail to perform as we expect. Adjustments to the assumptions we make in evaluating potential purchases may result in fewer properties qualifying under our investment criteria, including assumptions related to our ability to lease properties we have purchased. Reductions in the supply of properties that meet our investment criteria may adversely affect our ability to implement our investment strategy and operating results.

Furthermore, the properties that we acquire vary materially in terms of time to possession, renovation, quality and type of construction, location and hazards. Our success depends on our ability to acquire properties that can be quickly possessed, renovated, repaired, upgraded and rented with minimal expense and maintained in rentable condition. AH LLC s ability to identify and acquire such properties is fundamental to our success. In addition, the recent market and regulatory environments relating to single-family residential properties have been changing rapidly, making future trends difficult to forecast. For example, an increasing number of homeowners now wait for an eviction notice or eviction proceedings to commence before vacating foreclosed premises, which significantly increases the time period between the acquisition and leasing of a property. Such changes affect the accuracy of our assumptions and, in turn, may adversely affect our operating results.

Purchasing single-family properties through the foreclosure auction process will subject us to significant risks that could adversely affect our operating results, cash flows and ability to make distributions on our preferred and common shares.

Our business plan involves acquiring single-family properties through the foreclosure auction process simultaneously in a number of markets, which involves monthly foreclosure auctions on the same day of the month in certain markets. As a result, we are only able to visually inspect properties from the street and must purchase these properties without a contingency period and in as is condition with the risk that unknown defects in the property may exist. We also may encounter unexpected legal challenges and expenses in the foreclosure process. Upon acquiring a new property, we may have to evict residents who are in unlawful possession before we can secure possession and control of the property. The holdover occupants may be the former owners or tenants of a property, or they may be squatters or others who are illegally in possession. Securing control and possession from these occupants can be both costly and time-consuming.

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Further, when acquiring properties on an as is basis, title commitments are often not available prior to purchase, and title reports or title information may not reflect all senior liens, which may increase the possibility of acquiring houses outside predetermined acquisition and price parameters, purchasing residences with title defects and deed restrictions, HOA restrictions on leasing or underwriting or purchasing the wrong residence. The policies, procedures and practices we implement to assess the state of title and leasing restrictions prior to purchase may not be effective, which could lead to a material if not complete loss on our investment in such properties. For properties we acquire through the foreclosure auction process, we do not obtain title commitments prior to purchase, and we are not able to perform the type of title review that is customary in acquisitions of real property. As a result, our knowledge of potential title issues will be limited, and no title insurance protection will be in place. This lack of title knowledge and insurance protection may result in third parties having claims against our title to such properties that may materially and adversely affect the values of the properties or call into question the validity of our title to such properties. Without title insurance, we are fully exposed to, and would have to defend ourselves against, such claims. Further, if any such claims are superior to our title to the property we acquired, we risk loss of the property purchased. Any of these risks could adversely affect our operating results, cash flows and ability to make distributions to our shareholders.

Claims of deficiencies in the foreclosure process may result in rescission of our purchases at auction or reduce the supply of foreclosed properties available to us.

Allegations of deficiencies in foreclosure practices could result in claims challenging the validity of some foreclosures that have occurred to date, potentially placing our claim of ownership to the properties at risk. Since we do not have title insurance policies for properties we acquire through the foreclosure auction process, such instances or such proceedings may result in a complete loss without compensation.

Each state has its own laws governing the procedures to foreclose on mortgages and deeds of trust, and state laws generally require strict compliance with these laws in both judicial and non-judicial foreclosures. Recently, courts and administrative agencies have been more actively involved in enforcing state laws governing foreclosures, and in some circumstances have imposed new rules and requirements regarding foreclosures. Some courts have delayed or prohibited foreclosures based on alleged failures to comply with proper transfers of title, notice, identification of parties in interest, documentation and other legal requirements. Further, foreclosed owners and their representatives, including some prominent and well-financed legal firms, have brought litigation questioning the validity and finality of foreclosures that have already occurred. These developments may slow or reduce the supply of foreclosed houses available to us for purchase and may call into question the validity of our title to houses acquired at foreclosure, or result in rescission rights or other borrower remedies, which could result in a loss of a property purchased by us, an increase in litigation costs incurred with respect to properties obtained through foreclosure, or delays in stabilizing and leasing such properties promptly after acquisition.

Properties acquired through bulk sales may subject us to the risk of acquiring properties that do not fit our target investment criteria and may be costly or time consuming to divest, which may adversely affect our operating results.

We have acquired and expect to continue to acquire properties purchased as portfolios in bulk from other owners of single-family homes. To the extent the management and leasing of such properties has not been consistent with our property management and leasing standards, we may be subject to a variety of risks, including risks relating to the condition of the properties, the credit quality and employment stability of the tenants and compliance with applicable laws, among others. In addition, financial and other information provided to us regarding such portfolios during our due diligence may be inaccurate, and we may not discover such inaccuracies until it is too late to seek remedies against such sellers. To the extent we timely pursue such remedies, we may not be able to successfully prevail against the seller in an action seeking damages for such inaccuracies. If we conclude that certain properties purchased in bulk portfolios do not fit our target investment

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criteria, we may decide to sell, rather than renovate and rent, these properties, which could take an extended period of time and may not result in a sale at an attractive price.

Single-family properties that are being sold through short sales or foreclosure sales are subject to risks of theft, mold, infestation, vandalism, deterioration or other damage that could require extensive renovation prior to renting and adversely impact operating results.

When a single-family property is put into foreclosure due to a default by the homeowner on its mortgage obligations or the value of the property is substantially below the outstanding principal balance on the mortgage and the homeowner decides to seek a short sale, the homeowner may abandon the property or cease to maintain the property as rigorously as the homeowner normally would. Neglected and vacant properties are subject to increased risks of theft, mold, infestation, vandalism, general deterioration and other maintenance problems that may persist without appropriate attention and remediation. If we begin to purchase a large volume of properties in bulk sales and are not able to inspect them immediately before closing on the purchase, we may purchase properties that may be subject to these problems, which may result in maintenance and renovation costs and time frames that far exceed our estimates. These circumstances could substantially impair our ability to quickly renovate and lease such properties in a cost efficient manner or at all, which would adversely impact our operating results.

If occupancy levels and rental rates in our target markets do not increase sufficiently to keep pace with rising costs of operations, our rental income and distributable cash will decline.

The success of our business model depends, in part, on conditions in the single-family rental market in our target markets. Our asset acquisitions are premised on assumptions about occupancy levels and rental rates, and if those assumptions prove to be inaccurate, our cash flows and profitability will be reduced. Occupancy levels and rental rates have benefited in recent periods from macro trends affecting the U.S. economy and residential real estate markets in particular, including:

- a tightening of credit that has made it more difficult to finance a home purchase, combined with efforts by consumers generally to reduce their exposure to credit;

- weak economic and employment conditions that have increased foreclosure rates and made it more difficult for families to remain in their homes that were purchased prior to the housing market downturn;

- declining real estate values that have challenged the traditional notion that homeownership is a stable investment; and

- the unprecedented level of vacant housing comprising the real estate owned, or REO, inventory held for sale by banks, government-sponsored entities and other mortgage lenders or guarantors.

We do not expect these favorable trends in the residential rental market to continue indefinitely. Eventually, a strengthening of the U.S. economy and job growth, coupled with government programs designed to keep home owners in their homes and/or other factors may contribute to a stabilization or reversal of the current trend that favors renting rather than homeownership. In addition, we expect that as investors like us increasingly seek to capitalize on opportunities to purchase housing assets at below replacement costs and convert them to productive uses, the supply of single-family rental properties will decrease and the competition for tenants may intensify. A softening of the rental market in our target areas would reduce our rental income and profitability.

Eminent domain could lead to material losses on our investments in our properties.

Governmental authorities may exercise eminent domain to acquire land on which our properties are built in order to build roads and other infrastructure. Any such exercise of eminent domain would allow us to recover only the fair value of the affected properties. Our investment strategy is premised on the concept that this fair

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value will be substantially less than the real value of the property for a number of years, and we could effectively have no profit potential from properties acquired by the government through eminent domain. Several cities also are exploring proposals to use eminent domain to acquire mortgages to assist homeowners to remain in their homes, potentially reducing the supply of single-family properties in our target markets.

We depend on our tenants and their willingness to renew their leases for substantially all of our revenues. Poor tenant selection and defaults and nonrenewals by our tenants may adversely affect our reputation, financial performance and ability to make distributions on our preferred and common shares.

We depend on tenants for substantially all of our revenues. As a result, our success depends in large part upon our ability to attract and retain qualified tenants for our properties. Our reputation, financial performance and ability to make distributions to our shareholders would be adversely affected if a significant number of our tenants fail to meet their lease obligations or fail to renew their leases. For example, tenants may default on rent payments, make unreasonable and repeated demands for service or improvements, make unsupported or unjustified complaints to regulatory or political authorities, use our properties for illegal purposes, damage or make unauthorized structural changes to our properties that are not covered by security deposits, refuse to leave the property upon termination of the lease, engage in domestic violence or similar disturbances, disturb nearby residents with noise, trash, odors or eyesores, fail to comply with HOA regulations, sublet to less desirable individuals in violation of our lease or permit unauthorized persons to live with them. Damage to our properties may delay re-leasing after eviction, necessitate expensive repairs or impair the rental income or value of the property resulting in a lower than expected rate of return. Widespread unemployment and other adverse changes in the economic conditions in our target markets could result in substantial tenant defaults. In the event of a tenant default or bankruptcy, we may experience delays in enforcing our rights as landlord at that property and will incur costs in protecting our investment and re-leasing the property.

Short-term leases of residential property may expose us to the effects of declining market rents, which may adversely affect our operating results and our ability to make distributions on our preferred and common shares.

Substantially all of our leases are of a duration of less than two years and will be one year in the majority of cases. As these leases permit tenants to leave at the end of the lease term without penalty, we anticipate our rental revenues may be affected by declines in market rents more quickly than if our leases were for longer terms. Short-term leases may result in high turnover, which involves costs such as restoring the properties, marketing costs and lower occupancy levels. Because we have a limited track record, we cannot accurately predict our turnover rate or the associated costs we will incur. Moreover, we cannot assure you that our leases will be renewed on equal or better terms or at all. If our tenants do not renew their leases or the rental rates for our properties decrease, our operating results and ability to make distributions to our shareholders could be adversely affected.

Declining real estate values and impairment charges could adversely affect our financial condition and operating results.

We intend to review the carrying value of our properties when circumstances, such as adverse market conditions, indicate potential impairment may exist. If our evaluation indicates that we may be unable to recover the carrying value of a material portion of our real estate investments, an impairment charge will be recorded to the extent that the carrying value exceeds the estimated fair value of the properties. These losses would directly impact our financial condition and operating results. The evaluation of anticipated cash flows is highly subjective and is based in part on assumptions regarding future occupancy, rental rates and capital requirements that could differ materially from actual results in future periods. A declining real estate market may cause us to reevaluate the assumptions used in our impairment analysis. Impairment charges would adversely affect our financial condition and operating results.

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Our financial results in the period or periods immediately following completion of this offering may not be reflective of our earning potential and may cause our Series B Participating Preferred Share price to decline.

Our financial results in the fiscal periods immediately following completion of this offering may not be representative of our future potential. Prior to the full deployment of the net proceeds from this offering, we may invest the undeployed net proceeds in interest-bearing, short-term, investment-grade securities or money market accounts that are consistent with our intention to qualify as a REIT. We expect that these initial investments will provide a lower net return than we expect to receive from the investments described in this prospectus. In addition, because we expect to experience additional growth following this offering, we will have a greater percentage of our portfolio invested in assets in the process of stabilization than we would expect to have as a more mature operation. It will take time and significant cash resources to restore, reposition and lease these properties in the process of stabilization. As a result, newly acquired properties that are not leased at the time of acquisition will not begin generating revenue for some period of time following this offering and will reduce our overall financial performance.

Our net income and FFO may decrease in the near term as a result of the Management Internalization.

Our net income and funds from operations, or FFO, may decrease as a result of the Management Internalization. Now that we are self-managed, our expenses include the compensation and benefits of our officers, dedicated personnel and consultants, as well as overhead previously paid by AH LLC and its affiliates. Furthermore, these dedicated personnel provide us services that were provided by AH LLC and its affiliates. We can provide no assurance that we will be able to continue to provide those services at the same level or for the same costs as provided by subsidiaries of AH LLC under the advisory management agreement and the property management agreement, and there may be unforeseen costs, expenses and difficulties associated with continuing to provide those services on a self-managed basis. If the expenses we assumed as a result of the Management Internalization are higher than any corresponding increase in revenues or decrease in other expenses, our net income and FFO may be lower as a result of the Management Internalization than they otherwise would have been.

We are self-insured against many potential losses, and uninsured or underinsured losses relating to properties may adversely affect our financial condition, operating results, cash flows and ability to make distributions on our preferred and common shares.

We will attempt to ensure that all of the properties we acquire are adequately insured to cover casualty losses. However, many of the policies covering casualty losses may be subject to substantial deductibles and carveouts, and we will be self-insured up to the amount of the deductibles and carveouts. Since some claims against us will not exceed the deductibles under our insurance policies, we will be effectively self-insured for some claims. There are also some losses, including losses from floods, fires, earthquakes, acts of war, acts of terrorism or riots, that may not always be insured against or that are not generally fully insured against because it is not deemed economically feasible or prudent to do so. In addition, changes in the cost or availability of insurance could expose us to uninsured casualty losses.

In the event that any of the properties we acquire incur a casualty loss that is not fully covered by insurance, the value of our assets will be reduced by the amount of any such uninsured loss, and we could experience a significant loss of capital invested and potential revenues in these properties and could potentially remain obligated under any recourse debt associated with the property. Inflation, changes in building codes and ordinances, environmental considerations and other factors might also keep us from using insurance proceeds to replace or renovate a property after it has been damaged or destroyed. Under those circumstances, the insurance proceeds we receive might be inadequate to restore our economic position on the damaged or destroyed property. Any such losses could adversely affect our financial condition, operating results, cash flows and ability to make distributions on our preferred and common shares. In addition, we may have no source of funding to repair or reconstruct the damaged property, and we cannot assure you that any such sources of funding will be available to us for such purposes in the future.

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Contingent or unknown liabilities could adversely affect our financial condition, cash flows and operating results.

We may acquire properties that are subject to contingent or unknown liabilities, including liabilities for or with respect to liens attached to properties, unpaid real estate tax, utilities or HOA charges for which a subsequent owner remains liable, clean-up or remediation of environmental conditions or code violations, claims of customers, vendors or other persons dealing with the acquired entities and tax liabilities, among other things. Purchases of single-family properties acquired at auction, in short sales, from lenders or in bulk purchases typically involve few or no representations or warranties with respect to the properties. In each case, our acquisition may be without any, or with only limited, recourse against the sellers with respect to unknown liabilities or conditions. As a result, if any such liability were to arise relating to our properties, or if any adverse condition exists with respect to our properties that is in excess of our insurance coverage, we might have to pay substantial amounts to settle or cure it, which could adversely affect our financial condition, cash flows and operating results.

In addition, the properties we acquire may be subject to covenants, conditions or restrictions that restrict the use or ownership of such properties, including prohibitions on leasing or requirements to obtain the approval of HOAs prior to leasing. We may not discover such restrictions during the acquisition process, and such restrictions may adversely affect our ability to utilize such properties as we intend.

Security breaches and other disruptions could compromise our information and expose us to liability, which would cause our business and reputation to suffer.

In the ordinary course of our business we acquire and store sensitive data, including intellectual property, our proprietary business information and personally identifiable information of our prospective and current tenants, our employees and third-party service providers in our branch offices and on our networks and website. The secure processing and maintenance of this information is critical to our operations and business strategy. Despite our security measures, our information technology and infrastructure may be vulnerable to attacks by hackers or breached due to employee error, malfeasance or other disruptions. Any such breach could compromise our networks and the information stored there could be accessed, publicly disclosed, lost or stolen. Any such access, disclosure or other loss of information could result in legal claims or proceedings, liability under laws that protect the privacy of personal information, regulatory penalties, disruption to our operations and the services we provide to customers or damage our reputation, which could adversely affect our results of operations and competitive position.

A significant number of our properties are part of HOAs, and we and our tenants are subject to the rules and regulations of such HOAs, which may be arbitrary or restrictive, and violations of such rules may subject us to additional fees and penalties and litigation with such HOAs that would be costly.

A significant number of our properties are part of HOAs, which are private entities that regulate the activities of and levy assessments on properties in a residential subdivision. HOAs in which we own properties may have or enact onerous or arbitrary rules that restrict our ability to renovate, market or lease our properties or require us to renovate or maintain such properties at standards or costs that are in excess of our planned operating budgets. Such rules may include requirements for landscaping, limitations on signage promoting a property for lease or sale, or the use of specific construction materials in renovations. Some HOAs also impose limits on the number of property owners who may rent their homes, which if met or exceeded, would cause us to incur additional costs to resell the property and opportunity costs of lost rental income. Furthermore, many HOAs impose restrictions on the conduct of occupants of homes and the use of common areas and we may have tenants who violate HOA rules and for which we may be liable as the property owner. Additionally, the boards of directors of the HOAs in which we own property may not make important disclosures about the properties or may block our access to HOA records, initiate litigation, restrict our ability to sell our properties, impose assessments or arbitrarily change the HOA rules. We may be unaware of or unable to review or comply with

HOA rules before purchasing the property and any such excessively restrictive or arbitrary regulations may cause us to sell such property at a loss, prevent us from renting such property or otherwise reduce our cash flow from such property, which would have an adverse effect on our returns on these properties.

Joint venture investments that we make may limit our ability to invest in certain markets and could be adversely affected by our lack of sole decision-making authority, our reliance on joint venture partners financial condition and disputes between us and our joint venture partners.

We may co-invest in the future with third parties through partnerships, joint ventures or other entities, acquiring non-controlling interests in or sharing responsibility for managing the affairs of a property, partnership, joint venture or other entity. In such event, we may be subject to restrictions that prohibit us from making investments in certain markets until all of the funds in such partnership, joint venture or other entity are invested or committed, and we would not be in a position to exercise sole decision-making authority regarding the property, partnership, joint venture or other entity which could, among other things, impact our ability to satisfy the REIT requirements. Investments in partnerships, joint ventures or other entities may, under certain circumstances, involve risks not present were a third party not involved, including the possibility that joint venture partners might become bankrupt or fail to fund their share of required capital contributions. Joint venture partners may have economic or other business interests or goals that are inconsistent with our business interests or goals, and may be in a position to take actions contrary to our policies or objectives. Such investments also may have the potential risk of impasses on decisions, such as a sale, because neither we nor the partners would have full control over the partnership or joint venture. Disputes between us and our partners may result in litigation or arbitration that would increase our expenses and prevent our officers and/or trustees from focusing their time and effort on our business. Consequently, actions by, or disputes with, partners might result in subjecting properties owned by the partnership or joint venture to additional risk. In addition, we may in certain circumstances be liable for the actions of our third-party partners or co-venturers.

We anticipate involvement in a variety of litigation.

We anticipate involvement in a range of legal actions in the ordinary course of business. These actions may include eviction proceedings and other landlord-tenant disputes, challenges to title and ownership rights (including actions brought by prior owners alleging wrongful foreclosure by their lender or servicer), and issues with local housing officials arising from the condition or maintenance of the property. These actions can be time consuming and expensive. While we intend to vigorously defend any non-meritorious action or challenge, we cannot assure you that we will not be subject to expenses and losses that may adversely affect our operating results.

We may be adversely affected by lawsuits alleging trademark infringement as such lawsuits could materially harm our brand name, reputation and results of operations.

Several other companies in the United States, including companies in the real estate industry, may use words, phrases or logos similar to those we develop as part of our brand. As a result, we may face potential claims that the use of our brand infringes on their existing trademarks. For example, on or about November 1, 2012, we received notice of a claim that our American Homes 4 Rent brand name may infringe on an existing trademark of a participant in the real estate rental services and rental property management industries. While we intend to vigorously defend against this claim, the defense of any trademark infringement claim can be both costly and disruptive of the time and resources of our management, even if the claim against us is without merit. If we are unable to successfully defend against such a claim, we may be required to pay substantial damages or settlement costs to resolve the claim. In addition, we may be required to re-brand or incur substantial marketing costs to revise our brand to avoid future disputes. Any such trademark infringement claims and potential remedial measures could materially harm our brand name, reputation and results of operations.

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Complying with REIT requirements may limit our ability to hedge risk effectively.

The REIT provisions of the Code may limit our ability to hedge the risks inherent to our operations. As mentioned below, from time to time, we may enter into hedging transactions with respect to one or more of our assets or liabilities. Any income or gain derived by us from transactions that hedge certain risks, such as the risk of changes in interest rates, will not be treated as gross income for purposes of either the 75% or the 95% gross income test, as defined below in Material U.S. Federal Income Tax Considerations, unless specific requirements are met. Such requirements include that the hedging transaction be properly identified within prescribed time periods and that the transaction either (i) hedges risks associated with indebtedness issued by us that is incurred to acquire or carry real estate assets or (ii) manages the risks of currency fluctuations with respect to income or gain that qualifies under the 75% or 95% gross income test (or assets that generate such income). To the extent that we do not properly identify such transactions as hedges, hedge other types of indebtedness or enter into hedges with respect to our assets, the income from those transactions is not likely to be treated as qualifying income for purposes of the 75% and 95% gross income tests. As a result of these rules, we may have to limit the use of hedging techniques that might otherwise be advantageous, which could result in greater risks associated with interest rate or other changes than we would otherwise incur.

Our board of trustees has approved a very broad investment policy, subject to management oversight, and does not review or approve each acquisition decision made by AH LLC.

AH LLC is authorized to follow a very broad investment policy established by our board of trustees and subject to oversight by our management. Our board of trustees periodically reviews and updates the investment policy and also reviews our portfolio of residential real estate, but it does not review or approve AH LLC s specific property acquisitions. In addition, in conducting periodic reviews, our board of trustees may rely primarily on information provided to them by AH LLC and our management. Furthermore, acquisitions may be costly, difficult or impossible to unwind by the time they are reviewed by our board of trustees. AH LLC has great latitude within the broad parameters of the investment policy set by our board of trustees in determining our acquisition strategies, which could result in net returns that are substantially below expectations or that result in material losses, which would adversely affect our business and operating results, or may otherwise not be in the best interests of our shareholders.

As a result of becoming a public company, we will be required to complete an analysis of our internal controls over financial reporting. If we are unable to do so in a timely manner, or if our internal controls are determined to be ineffective, investor confidence in our company may be adversely affected and, as a result, the value of our Series B Participating Preferred Shares may decline.

We will be required, pursuant to Section 404 of the Sarbanes-Oxley Act, to furnish a report by management on, among other things, the effectiveness of our internal controls over financial reporting for the first fiscal year beginning after the completion of our initial public offering. This assessment will need to include disclosure of any material weaknesses identified by our management in our internal control over financial reporting, as well as a statement that our independent registered public accounting firm has issued an opinion on our internal control over financial reporting.

We are in the very early stages of the costly and challenging process of compiling the system and processing documentation necessary to perform the evaluation needed to comply with Section 404. We may not be able to complete our evaluation, testing and any required remediation in a timely fashion. During the evaluation and testing process, if we identify one or more material weaknesses in our internal control over financial reporting, we will be unable to assert that our internal controls are effective.

If we are unable to assert that our internal control over financial reporting is effective, or if our independent registered public accounting firm is unable to express an opinion on the effectiveness of our internal controls, investors could lose confidence in the accuracy and completeness of our financial reports, which could cause the

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price of our Series B Participating Preferred Shares to decline, and we may become subject to investigation or sanctions by the Securities and Exchange Commission, or SEC. We will be required to disclose changes made in our internal control and procedures on a quarterly basis. However, our independent registered public accounting firm will not be required to formally attest to the effectiveness of our internal control over financial reporting pursuant to Section 404 until the later of the year following our first annual report required to be filed with the SEC or the date we are no longer an emerging growth company, as defined in the JOBS Act if we take advantage of the exemptions contained in the JOBS Act. We will remain an emerging growth company for up to five years, although we could lose that status if our revenues exceed $1 billion, if we issue more than $1 billion in non-convertible debt in a three-year period or if the market value of our Class A common shares that are held by non-affiliates exceeds $700 million as of any June 30 before that time, we would cease to be an emerging growth company as of the following December 31. At such time, our independent registered public accounting firm may issue a report that is adverse in the event it is not satisfied with the level at which our controls are documented, designed or operating. Our remediation efforts may not enable us to avoid a material weakness in the future. In addition, to comply with the requirements of being a public company, we may need to undertake various actions, such as implementing new internal controls and procedures and hiring accounting or internal audit staff.

Future debt service obligations could adversely affect our operating results, may require us to sell properties and could adversely affect our ability to make distributions on our preferred and common shares.

Our financing strategy contemplates the use of secured or unsecured debt to finance long-term growth. While we intend to limit the sum of the outstanding principal amount of our consolidated indebtedness to up to 50% of our total assets, our governing documents contain no limitations on the amount of debt that we may incur, and our board of trustees may change our financing strategy at any time without shareholder approval. As a result, we may be able to incur substantial additional debt in the future.

Incurring debt could subject us to many risks, including the risks that:

- our cash flows from operations will be insufficient to make required payments of principal and interest;
- our debt may increase our vulnerability to adverse economic and industry conditions;
- we may be required to dedicate a substantial portion of our cash flows from operations to payments on our debt, thereby reducing cash available for distribution to our shareholders, funds available for operations and capital expenditures, future business opportunities or other purposes;
- we violate restrictive covenants in the documents that govern our indebtedness, which would entitle our lenders to accelerate our debt obligations;
- refinancing of the debt may not be available on favorable terms or at all; and
- the use of leverage could adversely affect our ability to make distributions to our shareholders and the market price of our Series B Participating Preferred Shares.

If we incur debt in the future and do not have sufficient funds to repay our debt at maturity, it may be necessary to refinance the debt through additional debt or equity financings. If, at the time of any refinancing, prevailing interest rates or other factors result in higher interest rates on refinancings, increases in interest expense could adversely affect our operating results and cash flows and, consequently, cash available for distribution to our shareholders. If we are unable to refinance our debt on acceptable terms, we may be forced to dispose of substantial numbers of properties on disadvantageous terms, potentially resulting in losses. To the extent we cannot meet any future debt service obligations, we will risk losing some or all of our properties that may be pledged to secure our obligations to foreclosure. Any unsecured debt agreements we enter into may contain specific cross-default provisions with respect to specified other indebtedness, giving the unsecured lenders the right to declare a default if we are in default under other loans in some circumstances. Defaults under our debt agreements could materially and adversely affect our financial condition and results of operations.

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Our credit facility contains financial and operating covenants that could restrict our business and investment activities. Failure to satisfy these covenants could result in a default under our credit facility that could accelerate the maturity of our debt obligations, which would have a material adverse effect on our business, liquidity, results of operations and financial condition and our ability to make distributions on our preferred and common shares.

Our credit facility contains financial and operating covenants, such as debt ratios, minimum liquidity and adjusted tangible net worth tests and other limitations that may restrict our ability to make distributions or other payments to our shareholders and may restrict our investment activities. Among others, our credit facility requires that we maintain financial covenants relating to the following matters: (i) cash, cash equivalents and borrowing capacity under any credit facilities in an aggregate amount of at least $15,000,000, of which at least $7,500,000 must be in cash and cash equivalents; (ii) a maximum leverage ratio of 1.0 to 1.0; and (iii) adjusted tangible net worth of not less than 85% of our adjusted tangible net worth as of September 30, 2013, plus 85% of the net proceeds of any additional equity capital raises completed on or after September 30, 2013. These covenants may restrict our ability to engage in transactions that we believe would otherwise be in the best interests of our shareholders. Further, such restrictions could make it difficult for us to satisfy the requirements necessary to maintain our qualification as a REIT for U.S. federal income tax purposes. Failure to meet our financial covenants could result from, among other things, changes in our results of operations, the incurrence of additional debt, substantial impairments in the value of our properties or changes in general economic conditions. If we violate covenants in our credit facility or future agreements, we could be required to repay all or a portion of our indebtedness before maturity at a time when we might be unable to arrange financing for such repayment on attractive terms, or at all.

Our credit facility permits us to incur significant indebtedness, which could require that we generate significant cash flow to satisfy the payment and other obligations under our credit facility.

We may incur significant indebtedness in connection with draws under our credit facility. This indebtedness may exceed our cash on hand and/or our cash flows from operating activities. Our ability to meet the payment and other obligations under our credit facility depends on our ability to generate sufficient cash flow in the future. Our ability to generate cash flow, to some extent, is subject to general economic, financial, competitive, legislative and regulatory factors, as well as other factors that are beyond our control. It is possible that our business will not generate cash flow from operations, or that future borrowings will be available to us, in amounts sufficient to enable us to meet our payment obligations under our credit facility. If we are not able to generate sufficient cash flow to service our credit facility and other debt obligations, as well as satisfy the REIT distribution requirement, we may need to refinance or restructure our debt, reduce or delay capital investments, or seek to raise additional capital. If we are unable to implement one or more of these alternatives, we may not be able to meet our payment obligations under our credit facility, which could materially and adversely affect our liquidity.

Disruptions in the financial markets may materially and adversely affect our ability to secure additional financing.

The credit markets continue to experience significant price volatility, dislocations and liquidity disruptions, the concern of which has led many lenders and institutional investors to reduce, and in some cases cease, to provide credit to businesses and has caused spreads on prospective debt financings to widen considerably. Continued uncertainty in these markets may affect our ability to obtain additional debt financing at all or on terms favorable or acceptable to us. These events also may make it more difficult or costly for us to raise capital through the issuance of our equity securities. Our inability to secure additional financing may impede our ability acquire new properties. Disruptions in the financial markets could have a material adverse effect on us, including our business, results of operations and our financial condition.

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Interest expense on our debt may limit our cash available to fund our growth strategies and shareholder distributions.

Higher interest rates could increase debt service requirements on floating rate debt, to the extent we have any, and could reduce funds available for operations, distributions to our shareholders, future business opportunities or other purposes. If we need to repay existing debt during periods of rising interest rates, we could be required to liquidate one or more of our investments in properties at times which may not permit realization of the maximum return on such investments and could result in significant losses.

Failure to hedge effectively against interest rate changes may adversely affect our results of operations and our ability to make shareholder distributions.

Subject to complying with the requirements for REIT qualification, we may obtain in the future one or more forms of interest rate protection in the form of swap agreements, interest rate cap contracts or similar agreements to hedge against the possible negative effects of interest rate fluctuations. However, we cannot assure you that any hedging will adequately relieve the adverse effects of interest rate increases or that counterparties under these agreements will honor their obligations thereunder. In addition, we may be subject to risks of default by hedging counterparties. Adverse economic conditions could also cause the terms on which we borrow to be unfavorable. We could be required to liquidate one or more of our investments at times which may not permit us to receive an attractive return on our investments in order to meet our debt service obligations.

Risks Related to the Real Estate Industry

Our performance and the value of our properties are subject to general economic conditions and risks associated with our real estate assets.

If the properties we acquire do not generate income sufficient to meet operating expenses, including debt service and capital expenditures, our ability to make distributions to our shareholders could be adversely affected. There are significant expenditures associated with an investment in real estate (such as debt service, real estate taxes, insurance and maintenance costs) that generally do not decline when circumstances reduce the income from the property. Income from and the value of the properties we acquire may be adversely affected by the following factors:

- downturns in international, national, regional and local economic conditions (particularly increases in unemployment);
- the attractiveness of the properties we acquire to potential tenants and competition from other properties;
- increases in the supply of or decreases in the demand for similar or competing properties in our target markets;
- bankruptcies, financial difficulties or lease defaults by our tenants;
- changes in interest rates, availability and terms of debt financing;
- changes in operating costs and expenses and our ability to control rents;
- changes in, or increased costs of compliance with, governmental laws, rules, regulations and fiscal policies, including changes in tax, real estate, environmental and zoning laws, and our potential liability thereunder;
- our ability to provide adequate maintenance;

changes in the cost or availability of insurance, including coverage for mold or asbestos;

environmental conditions or retained liabilities for such conditions;

tenant turnover;

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- the illiquidity of real estate investments generally;
- residents perceptions of the safety, convenience and attractiveness of our properties and the neighborhoods where they are acquired;
- the ongoing need for capital improvements, particularly in older properties;
- the ability or unwillingness of residents to pay rent increases;
- civil unrest, acts of God, including earthquakes, floods and other natural disasters, which may result in uninsured losses, and acts of war or terrorism;
- rent control or rent stabilization or other housing laws, which could prevent us from raising rents; and
- increases in property-level maintenance and operating expenses.

For these and other reasons, we cannot assure you that we will be profitable or that we will realize growth in the value of our real estate properties.

Environmentally hazardous conditions may adversely affect our financial condition, cash flows and operating results.

Under various federal, state and local environmental laws, a current or previous owner or operator of real property may be liable for the cost of removing or remediating hazardous or toxic substances on such property. Such laws often impose liability whether or not the owner or operator knew of, or was responsible for, the presence of such hazardous or toxic substances. Even if more than one person may have been responsible for the contamination, each person covered by applicable environmental laws may be held responsible for all of the clean-up costs incurred. In addition, third parties may sue the owner or operator of a site for damages based on personal injury, natural resources or property damage or other costs, including investigation and clean-up costs, resulting from the environmental contamination. The presence of hazardous or toxic substances on one of our properties, or the failure to properly remediate a contaminated property, could give rise to a lien in favor of the government for costs it may incur to address the contamination, or otherwise adversely affect our ability to sell or lease the property or borrow using the property as collateral. Environmental laws also may impose restrictions on the manner in which property may be used or businesses may be operated. A property owner who violates environmental laws may be subject to sanctions which may be enforced by governmental agencies or, in certain circumstances, private parties. In connection with the acquisition and ownership of our properties, we may be exposed to such costs. The cost of defending against environmental claims, of compliance with environmental regulatory requirements or of remediating any contaminated property could materially adversely affect our business, financial condition, results of operations and, consequently, amounts available for distribution to our shareholders.

Compliance with new or more stringent environmental laws or regulations or stricter interpretation of existing laws may require material expenditures by us. We may be subject to environmental laws or regulations relating to our properties, such as those concerning lead-based paint, mold, asbestos, proximity to power lines or other issues. We cannot assure you that future laws, ordinances or regulations will not impose any material environmental liability, or that the current environmental condition of our properties will not be affected by the operations of residents, existing conditions of the land, operations in the vicinity of the properties or the activities of unrelated third parties. In addition, we may be required to comply with various local, state and federal fire, health, life-safety and similar regulations. Failure to comply with applicable laws and regulations could result in fines and/or damages, suspension of personnel, civil liability and/or other sanctions.

Tenant relief laws and rent control laws may negatively impact our rental income and profitability.

As landlord of numerous properties, we will be involved regularly in evicting tenants who are not paying their rent or are otherwise in material violation of the terms of their lease. Eviction activities will impose legal and managerial expenses that will raise our costs. The eviction process is typically subject to legal barriers,

mandatory cure policies and other sources of expense and delay, each of which may delay our ability to gain possession and stabilize the property. Additionally, state and local landlord tenant laws may impose legal duties to assist tenants in relocating to new housing, or restrict the landlord s ability to recover certain costs or charge tenants for damage tenants cause to the landlord s premises. Because such laws vary by state and locality, we and any regional and local property managers we hire will need to be familiar with and take all appropriate steps to comply with all applicable landlord tenant laws, and we will need to incur supervisory and legal expenses to ensure such compliance. To the extent that we do not comply with state or local laws, we may be subjected to civil litigation filed by individuals, in class actions or by state or local law enforcement. We may be required to pay our adversaries litigation fees and expenses if judgment is entered against us in such litigation, or if we settle such litigation.

Furthermore, rent control laws may affect our rental income. Especially in times of recession and economic slowdown, rent control initiatives can acquire significant political support. If rent controls unexpectedly became applicable to certain of our properties, our revenue from and the value of such properties could be adversely affected.

Class action, tenant rights and consumer demands and litigation could directly limit and constrain our operations and may impose on us significant litigation expenses.

Numerous tenants rights and consumers rights organizations exist throughout the country and operate in our target markets, and as we grow in scale, we may attract attention from some of these organizations and become a target of legal demands or litigation. Many such consumer organizations have become more active and better funded in connection with mortgage foreclosure-related issues, and with the large settlements identified below and the increased market for single-family rentals arising from displaced homeownership, some of these organizations may shift their litigation, lobbying, fundraising and grass roots organizing activities to focus on landlord tenant issues. While we intend to conduct our business lawfully and in compliance with applicable landlord-tenant and consumer laws, such organizations might work in conjunction with trial and pro bono lawyers in one state or multiple states to attempt to bring claims against us on a class action basis for damages or injunctive relief. We cannot anticipate what form such legal actions might take, or what remedies they may seek. Additionally, these organizations may lobby local county and municipal attorneys or state attorneys general to pursue enforcement or litigation against us, or may lobby state and local legislatures to pass new laws and regulations to constrain our business operations. If they are successful in any such endeavors, they could directly limit and constrain our operations and may impose on us significant litigation expenses, including settlements to avoid continued litigation or judgments for damages or injunctions.

Acquiring properties during periods when the single-family home sector is experiencing substantial inflows of capital and intense competition may result in inflated purchase prices and increase the likelihood that our properties will not appreciate in value and may, instead, decrease in value.

The allocation of substantial amounts of capital for investment in the single-family home sector and significant competition for income producing real estate may inflate the purchase prices for such assets. To the extent we purchased, or in the future purchase, real estate in such an environment, it is possible that the value of our properties may not appreciate and may, instead, decrease in value, perhaps significantly, below the amount we paid for such properties. In addition to macroeconomic and local economic factors, technical factors, such as a decrease in the amount of capital allocated to the single-family home sector and the number of investors participating in the sector, could cause the value of our properties to decline.

Mortgage loan modification programs and future legislative action may adversely affect the number of available properties that meet our investment criteria.

The U.S. government, through the Federal Reserve, the Federal Housing Administration and the Federal Deposit Insurance Corporation, or FDIC, has implemented a number of programs designed to provide homeowners with assistance in avoiding residential mortgage loan foreclosures, including the Home Affordable

Modification Program, which seeks to provide relief to homeowners whose mortgages are in or may be subject to foreclosure, and the Home Affordable Refinance Program, which allows certain borrowers who are underwater on their mortgage but current on their mortgage payments to refinance their loans. Several states, including states in which our current target markets are located, have adopted or are considering similar legislation. These programs and other loss mitigation programs may involve, among other things, modifying or refinancing mortgage loans or providing homeowners with additional relief from loan foreclosures. Such loan modifications and other measures are intended and designed to lead to fewer foreclosures, which will decrease the supply of properties that meet our investment criteria.

The pace of residential foreclosures is subject to numerous factors. Recently, there has been a backlog of foreclosures due to a combination of volume constraints and legal actions, including those brought by the U.S. Department of Justice, or DOJ, the Department of Housing and Urban Development, or HUD, and State Attorneys General against mortgage servicers alleging wrongful foreclosure practices. Financial institutions also have been subjected to regulatory restrictions and limitations on foreclosure activity by the FDIC. Legal claims brought or threatened by DOJ, HUD and 49 State Attorneys General against the five largest residential mortgage servicers in the country were settled in 2012. As part of this approximately $25 billion settlement, a portion of the settlement funds will be directed to homeowners seeking to avoid foreclosure through mortgage modifications, and servicers are required to adopt specified measures to reduce mortgage obligations in certain situations. It is expected that the settlement will help many homeowners to avoid foreclosures that would otherwise have occurred in the near term, and with lower monthly payments and mortgage debts, for years to come. It is also foreseeable that other residential mortgage servicing companies that were not among the five included in the initial $25 billion settlement will agree to similar settlements that will further reduce the supply of houses in the process of foreclosure.

In addition, numerous federal and state legislatures have considered, proposed or adopted legislation to constrain foreclosures, or may do so in the future. The Dodd-Frank Wall Street Reform and Consumer Protection Act, or Dodd-Frank Act, also created the Consumer Financial Protection Bureau, which supervises and enforces federal consumer protection laws as they apply to banks, credit unions, and other financial companies, including mortgage servicers. It remains uncertain as to whether any of these measures will have a significant impact on foreclosure volumes or what the timing of that impact would be. If foreclosure volumes were to decline significantly, we would expect real estate owned inventory levels to decline or to grow at a slower pace, which would make it more difficult to find target assets at attractive prices and might constrain our growth or reduce our long-term profitability. Also, the number of families seeking rental housing might be reduced by such legislation, reducing rental housing demand in our target markets.

In addition, allegations of deficiencies in foreclosure practices could result in claims challenging the validity of some foreclosures that have occurred to date, potentially placing our claim of ownership to the properties at risk. We cannot be assured that such proceedings would not result in a complete dispossession of property from us without compensation.

Each state has its own laws governing the procedures to foreclose on mortgages and deeds of trust, and state laws generally require strict compliance with these laws in both judicial and non-judicial foreclosures. Recently, courts and administrative agencies have been more actively involved in enforcing state laws governing foreclosures, and in some circumstances have imposed new rules and requirements regarding foreclosures. Some courts have delayed or prohibited foreclosures based on alleged failures to comply with proper transfers of title, notice, identification of parties in interest, documentation and other legal requirements. The increase in the number of foreclosures since 2007 has led legislatures in many states to consider modifications to foreclosure laws to restrict and reduce foreclosures. For example, in 2012, California enacted a law imposing new limitations on foreclosures while a request for a loan modification is pending. Further, foreclosed owners and their legal representatives, including some prominent and well-financed law firms, have brought litigation questioning the validity and finality of foreclosures that have already occurred. These developments may slow or reduce the supply of foreclosed houses available to us for purchase and may call into question the validity of our title to houses acquired at foreclosure, or

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result in rescission rights or other borrower remedies, which could result in a loss of a property purchased by us, an increase in litigation and property maintenance costs incurred with respect to properties obtained through foreclosure, or delays in stabilizing and leasing such properties promptly after acquisition.

We may have difficulty selling our real estate investments, and our ability to distribute all or a portion of the net proceeds from such sale to our shareholders may be limited.

Real estate investments are relatively illiquid and, as a result, we may have a limited ability to sell our properties. When we sell any of our properties, we may recognize a loss on such sale. We may elect not to distribute any proceeds from the sale of properties to our shareholders. Instead, we may use such proceeds for other purposes, including:

- purchasing additional properties;
- repaying debt, if any;
- buying out interests of any co-venturers or other partners in any joint venture in which we are a party;
- creating working capital reserves; or
- making repairs, maintenance or other capital improvements or expenditures to our remaining properties.

Our ability to sell our properties may also be limited by our need to avoid the 100% prohibited transactions tax that is imposed on gain recognized by a REIT from the sale of property characterized as dealer property. In order to ensure that we avoid such characterization, we may be required to hold our properties for a minimum period of time and comply with certain other requirements in the Code or dispose of our properties through a taxable REIT subsidiary or TRS. For more information on taxable REIT subsidiaries see Material U.S. Federal Income Tax Considerations Requirements for Qualification as a REIT Effect of Subsidiary Entities Ownership of Interests in Taxable REIT Subsidiaries.

Risks Related to our Relationship with AH LLC and Conflicts of Interest

As long as AH LLC continues to perform acquisition and renovations services for us, we will depend on AH LLC for our external growth.

Until December 10, 2014, AH LLC will continue to provide us acquisition and renovation services for a fee equal to 5% of the sum of the purchase price and initial renovation costs of each property that we acquire in consideration for its services in identifying, evaluating, acquiring and overseeing the renovation of its residences. Accordingly, through at least that date, we will depend on AH LLC for our external growth and we could be adversely affected if, for any reason, AH LLC is unable to perform its obligations under its agreement with us.

AH LLC may engage in other activities diverting their attention from our business, which could adversely affect the execution of our business and our results of operations.

We are subject to conflicts of interest arising out of our relationship with AH LLC. AH LLC and its affiliates, officers, directors, employees or personnel may engage in any business (other than acquiring, renovating, leasing and operating single-family homes as rental properties without the approval of the board of trustees). As a result, their time and effort may be diverted from our business.

Completion of the Management Internalization has exposed us to new and additional responsibilities, costs and risks.

Completion of the Management Internalization has exposed us to new and additional responsibilities, costs and risks. For example, while we no longer bear the external costs of the advisory management fee paid to our former manager, our direct overhead will increase, as we are now responsible for compensation and benefits of our officers and other personnel that were previously paid by our former manager. If our properties do not perform as

anticipated or if we fail to raise additional financing, we may not be able to cover such additional overhead. We also now are subject to those potential liabilities that are commonly faced by employers, such as workers disability and compensation claims, potential labor disputes and other employee-related liabilities and grievances. Accordingly, the Management Internalization could adversely affect our financial condition and operating results.

Our fiduciary duties as the general partner of our operating partnership could create conflicts of interest, which may impede business decisions that could benefit our shareholders.

As the sole general partner of our operating partnership, we have a fiduciary duty to the other limited partners in the operating partnership, the discharge of which may conflict with the interests of our shareholders. AH LLC is the limited partner of our operating partnership. AH LLC, as the limited partner of our operating partnership, has agreed that, in the event of a conflict in the fiduciary duties owed by us to our shareholders and in our capacity as the general partner of our operating partnership, to such limited partner, we are under no obligation to give priority to the interests of such limited partner.

In addition, AH LLC, as well as any other limited partners, has the right to vote on certain amendments to the operating partnership agreement and to approve certain amendments that would adversely affect their rights. These voting rights may be exercised in a manner that conflicts with the interests of our shareholders.

The contribution agreement and other agreements we entered into in connection with the Management Internalization were negotiated between a special committee of our board of trustees and AH LLC. Therefore, the terms of such agreements may not have been as favorable to us as if they had been negotiated with unaffiliated third parties.

AH LLC is owned, directly or indirectly, by family members or trusts for family members or heirs of B. Wayne Hughes, our non-executive Chairman, David P. Singelyn, our Chief Executive Officer and a trustee, Jack Corrigan, our Chief Operating Officer and a trustee, David Goldberg, our Executive Vice President, and other parties. HF Investments 2010, LLC, which is comprised of trusts established by Mr. Hughes for certain of his heirs, owns an approximately 88.66% membership interest in AH LLC. Additionally, membership interests of AH LLC are owned by family members or trusts for family members of Mr. Singelyn (4.93% membership interest), Mr. Corrigan (4.93% membership interest) and Mr. Goldberg (1% membership interest). Accordingly, such trustees and executive officers received substantial economic benefits as a result of the Management Internalization. As a result of the foregoing, the interests of certain of our trustees and executive officers may differ from, and be in conflict with, the interests of our shareholders. The contribution agreement and other agreements we entered into in connection with the Management Internalization were negotiated between a special committee comprised of all of our independent trustees and AH LLC, and their terms, including the consideration payable to AH LLC, may not be as favorable to us as if they had been negotiated with unaffiliated third parties. In addition, we did not obtain a third-party appraisal of our former manager or our former property manager.

If we determine that AH LLC breached any of the representations, warranties or covenants made by it in the contribution agreement related to the Management Internalization, we may choose not to enforce, or to enforce less vigorously, our rights because of our desire to maintain our ongoing relationship with AH LLC. Moreover, the representations, warranties, covenants and indemnities in the contribution agreement are subject to limits and qualifiers, which may also limit our ability to enforce any remedy under the agreement.

Messrs. Hughes, Singelyn, Corrigan and Goldberg are subject to certain conflicts of interest with regard to enforcing the indemnification provisions contained in the contribution agreement for the Management Internalization and enforcing some of the ancillary agreements to be entered into by us in connection with the Management Internalization.

Messrs. Hughes, Singelyn, Corrigan and Goldberg received beneficial economic interests in our operating partnership s Series D units and Series E units through their direct or indirect interests in AH LLC, which received 4,375,000 Series D units and 4,375,000 Series E units as a result of the Management Internalization.

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Certain provisions of the contribution agreement and the ancillary agreements executed in connection with the Management Internalization may have significant financial impacts on AH LLC. In particular, Messrs. Hughes, Singelyn, Corrigan and Goldberg are subject to conflicts of interest in connection with the enforcement against AH LLC of indemnification obligations under the contribution agreement and other transaction documents that could directly impact their or their family s economic interests.

Because the acquisition and renovation functions will not be internalized earlier than December 10, 2014, we expect to continue to pay AH LLC significant fees, and certain of our executive officers and trustees will have a conflict of interest in connection with decisions regarding internalization of those functions.

We will continue to pay AH LLC a fee equal to 5% of the sum of the purchase price and initial renovation costs of each property that we acquire in consideration for its services in identifying, evaluating, acquiring and overseeing the renovation of its residences. If, for example, we invest $1.5 billion in acquisitions after the closing of the Management Internalization and before December 10, 2014, we will pay AH LLC acquisition and renovation fees of $75 million. AH LLC would continue to bear all of the costs of investigating properties that we do not acquire. After September 10, 2014, we will have the right to offer employment that would commence on December 10, 2014 to all of AH LLC s acquisition and renovation personnel necessary for our operations, and AH LLC will be required to cooperate to transition any employees who choose to accept our offer. If we elect not to transition employees from AH LLC, we could engage AH LLC or a third party on mutually acceptable terms to continue to provide acquisition and renovation services. Because we may still be paying significant fees to AH LLC, Messrs. Hughes, Singelyn, Corrigan and Goldberg, as a result of their personal or family financial interests in AH LLC, will be subject to conflicts of interest in connection with decisions regarding whether to pursue internalization of the acquisition and renovation functions after December 10, 2014 or to enter into a new agreement with AH LLC for these services.

Risks Related to Our Organization and Structure

Provisions of our declaration of trust may limit the ability of a third party to acquire control of us by authorizing our board of trustees to issue additional securities.

Our board of trustees may, without shareholder approval, amend our declaration of trust to increase or decrease the aggregate number of our shares or the number of shares of any class or series that we have the authority to issue and to classify or reclassify any unissued common or preferred shares, and set the preferences, rights and other terms of the classified or reclassified shares. As a result, our board of trustees may authorize the issuance of additional shares or establish a series of common or preferred shares that may delay or prevent a change in control of our company, including transactions at a premium over the market price of our shares, even if shareholders believe that a change in control is in their interest. These provisions, along with the restrictions on ownership and transfer contained in our declaration of trust and certain provisions of Maryland law described below, could discourage unsolicited acquisition proposals or make it more difficult for a third party to gain control of us, which could adversely affect the market price of our securities. See Material Provisions of Maryland Law and of Our Declaration of Trust and Bylaws.

Provisions of Maryland law may limit the ability of a third party to acquire control of us by requiring our board of trustees or shareholders to approve proposals to acquire our company or effect a change in control.

Certain provisions of the Maryland General Corporation Law, or the MGCL, applicable to Maryland real estate investment trusts may have the effect of inhibiting a third party from making a proposal to acquire us or of impeding a change in control under circumstances that otherwise could provide our shareholders with the opportunity to realize a premium over the then-prevailing market price of their shares, including:

- business combination provisions that, subject to limitations, prohibit certain business combinations between us and an interested shareholder (defined generally as any person who beneficially owns 10% or more of the voting power of our outstanding voting shares or an affiliate or associate of ours who, at any time within the two-year period immediately prior to the date in question, was the beneficial owner of 10% or more of the voting power of our then outstanding shares) or an affiliate of any interested shareholder for five years after the most recent date on which the shareholder becomes an interested shareholder, and thereafter imposes two super-majority shareholder voting requirements on these combinations, unless, among other conditions, our common shareholders receive a minimum price, as defined in the MGCL, for their shares and the consideration is received in cash or in the same form as previously paid by the interested shareholder for its shares; and

control share provisions that provide that our control shares (defined as voting shares which, when aggregated with all other shares controlled by the shareholder, entitle the shareholder to exercise one of three increasing ranges of voting power in electing trustees) acquired in a control share acquisition (defined as the direct or indirect acquisition of ownership or control of issued and outstanding control shares) have no voting rights except to the extent approved by our shareholders by the affirmative vote of at least two-thirds of all the votes entitled to be cast on the matter, excluding shares owned by the acquirer, by our officers or by our employees who are also trustees of our company.

By resolution of our board of trustees, we have opted out of the business combination provisions of the MGCL and provided that any business combination between us and any other person is exempt from the business combination provisions of the MGCL, provided that the business combination is first approved by our board of trustees (including a majority of trustees who are not affiliates or associates of such persons). In addition, pursuant to a provision in our bylaws, we have opted out of the control share provisions of the MGCL. However, our board of trustees may by resolution elect to opt in to the business combination provisions of the MGCL and we may, by amending our bylaws, opt in to the control share provisions of the MGCL in the future.

In addition, the unsolicited takeover provisions of Title 3, Subtitle 8 of the MGCL permits our board of trustees, without shareholder approval and regardless of what is currently provided in our declaration of trust or bylaws, to implement certain takeover defenses, including adopting a classified board or increasing the vote required to remove a trustee. Such takeover defenses may have the effect of inhibiting a third party from making an acquisition proposal for us or of delaying, deferring or preventing a change in control of us under the circumstances that otherwise could provide our common shareholders with the opportunity to realize a premium over the then-current market price. In July 2013, our board of trustees and our shareholders approved an amendment to our declaration of trust under which we will elect not to be subject to these provisions.

Our rights and the rights of our shareholders to take action against our trustees and officers are limited, which could limit your recourse in the event of actions not in your best interests.

Under Maryland law, generally, a trustee will not be liable if he or she performs his or her duties in good faith, in a manner he or she reasonably believes to be in our best interests and with the care that an ordinarily prudent person in a like position would use under similar circumstances. In addition, our declaration of trust limits the liability of our trustees and officers to us and our shareholders for money damages, except for liability resulting from:

actual receipt of an improper benefit or profit in money, property or services; or

active and deliberate dishonesty by the trustee or officer that was established by a final judgment as being material to the cause of action adjudicated.

Our declaration of trust authorizes us to indemnify our trustees and officers for actions taken by them in those capacities to the maximum extent permitted by Maryland law. Our bylaws require us to indemnify each trustee and officer, to the maximum extent permitted by Maryland law, in the defense of any proceeding to which he or she is made, or threatened to be made, a party by reason of his or her service to us. In addition, we may be obligated to advance the defense costs incurred by our trustees and officers. As a result, we and our shareholders may have more limited rights against our trustees and officers than might otherwise exist absent the current provisions in our declaration of trust and bylaws or that might exist with other companies. See Material Provisions of Maryland Law and of Our Declaration of Trust and Bylaws Limitation of Trustees and Officers Liability and Indemnification.

Our board of trustees may change our strategy or investment policies, financing strategy or leverage policies without shareholder consent.

Our board of trustees may change any of our strategies, policies or procedures with respect to property acquisitions and divestitures, asset allocation, growth, operations, indebtedness, financing and distributions at any time without the consent of shareholders, which could result in the acquisition of properties that are different from, and possibly riskier than, the types of single-family residential real estate investments described in this prospectus. These changes could adversely affect our financial condition, risk profile, results of operations, the market price of our Series B Participating Preferred Shares and our ability to make distributions to shareholders.

The ability of our board of trustees to revoke our REIT election without shareholder approval may cause adverse consequences to our shareholders.

Our declaration of trust provides that our board of trustees may revoke or otherwise terminate our REIT election, without the approval of our shareholders, if it determines that it is no longer in our best interest to continue to qualify as a REIT. If we cease to be a REIT, we would become subject to federal income tax on our taxable income and would no longer be required to distribute most of our taxable income to our shareholders, which may have adverse consequences on the total return to our shareholders.

Risks Related to This Offering and Ownership of Our Series B Participating Preferred Shares

The Series B Participating Preferred Shares have not been rated.

We have not sought to obtain a rating for the Series B Participating Preferred Shares. However, no assurance can be given that one or more rating agencies might not independently determine to issue such a rating or that such a rating, if issued, would not adversely affect the market price of the Series B Participating Preferred Shares. In addition, we may elect in the future to obtain a rating of the Series B Participating Preferred Shares, which could adversely impact the market price of the Series B Participating Preferred Shares. Ratings only reflect the views of the rating agency or agencies issuing the ratings, and such ratings could be revised downward or withdrawn entirely at the discretion of the issuing rating agency if in its judgment circumstances so warrant. Any such downward revision or withdrawal of a rating could have an adverse effect on the market price of the Series B Participating Preferred Shares.

The Series B Participating Preferred Shares are newly issued securities with no established trading market, which may negatively affect their market value and your ability to transfer or sell your shares. We intend to apply to list the Series B Participating Preferred Shares on the NYSE, but we cannot assure you that the listing will be approved or that a trading market will develop or be sustained.

The Series B Participating Preferred Shares are newly issued securities with no established trading market. We intend to apply to list the Series B Participating Preferred Shares on the NYSE, but we cannot assure you that the Series B Participating Preferred Shares will be approved for listing. An active trading market on the NYSE for the Series B Participating Preferred Shares may not develop or, even if it develops, may not be sustained, in which case the trading price of the Series B Participating Preferred Shares could be adversely affected. In addition, the Series B Participating Preferred Shares offered hereby are a different security than our Series A Participating Preferred Shares and, as such, the past, current or future trading price of our Series A Participating Preferred Shares may not be indicative of the potential value or trading price of our Series B Participating Preferred Shares.

The price of our Series B Participating Preferred Shares could be subject to wide fluctuations in response to a number of factors, including those listed in this Risk Factors section of this prospectus, our financial performance, government regulatory action or inaction, tax laws, interest rates and general market conditions and others such as:

- actual or anticipated variations in our quarterly operating results, financial condition, liquidity or changes in business strategy or prospects;

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- equity issuances by us or resales by our shareholders, or the perception that such issuances or resales may occur;
- increases in market interest rates that may lead investors to demand a higher dividend yield or seek alternative investments paying higher rates;
- publication of research reports about us or the real estate industry;
- changes in market valuations of similar companies;
- changes in home prices reflected in the POI;
- adverse market reaction to any increased indebtedness we incur in the future;
- additions or departures of key personnel;
- actions by shareholders;
- speculation in the press or investment community;
- general market, economic and political conditions, including an economic slowdown or dislocation in the global credit or capital markets;
- our operating performance and the performance of other similar companies;
- failure to maintain our REIT qualification;
- changes in accounting principles or actual or anticipated accounting problems; and
- passage of legislation or other regulatory developments that adversely affect us or our industry.

The Series B Participating Preferred Shares are subordinate to our debt and other liabilities, and your interests could be diluted by the issuance of additional preferred shares and by other transactions.

As of September 30, 2013, our total indebtedness was approximately $238 million, and our other liabilities (other than indebtedness) were approximately $158 million. We may incur significant additional debt to finance future acquisition activities as well as additional liabilities in operating our business. The Series B Participating Preferred Shares are subordinate to all of our existing and future debt. Our existing debt restricts, and our future debt may include restrictions on, our ability to pay dividends to preferred shareholders in the event of a default under the debt facilities. Our declaration of trust currently authorizes the issuance of up to 100,000,000 preferred shares of beneficial interest in one or more series, of which 5,060,000 preferred shares of beneficial interest are currently outstanding. The issuance of additional preferred shares of beneficial interest on parity with or senior to the Series B Participating Preferred Shares would dilute the interests of the holders of the Series B

Participating Preferred Shares, and any issuance of preferred shares of beneficial interest senior to the Series B Participating Preferred Shares or of additional indebtedness could affect our ability to pay dividends on, redeem or pay the liquidation preference on the Series B Participating Preferred Shares. Other than the conversion right afforded to holders of Series B Participating Preferred Shares upon the occurrence of a Change of Control as described under Description of Series B Participating Preferred Shares Conversion Rights and other than the limited voting rights as described under Description of Series B Participating Preferred Shares Voting Rights, none of the provisions relating to the Series B Participating Preferred Shares relate to or limit our indebtedness or afford the holders of the Series B Participating Preferred Shares protection in the event of a highly leveraged or other transaction, including a merger or the sale, lease or conveyance of all or substantially all of our assets or business, that might adversely affect the holders of the Series B Participating Preferred Shares.

The various hypothetical figures and illustrations contained in this prospectus should not be taken as an indication or prediction of future investment results.

The various hypothetical figures and illustrations contained in this prospectus are intended merely to illustrate the impact that such hypothetical terms could have on the liquidation preference, dividend amounts and

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Innovalight, Inc.	$ 1,993,568
Kereos, Inc.	$ 540,000
Kovio, Inc.	$ 1,000,000
NanoGram Corporation	$ 851,393
Mersana Therapeutics, Inc.	$ 500,000
Nanomix, Inc.	$ 680,240
NanoOpto Corporation	$ 268,654
Nextreme Thermal Solutions, Inc.	$ 750,000
Polatis, Inc.	$ 17,942
Polatis, Inc.	$ 13,454
Polatis, Inc.	$ 58,582
SiOnyx, Inc.	$ 2,445,000
Solazyme, Inc.	$ 500,000
Total	$20,595,161

The following tables summarize the fair values of our portfolios of venture capital investments and U.S. government and agency obligations, as compared with their cost, at December 31, 2007, and December 31, 2006:

	December 31,			
		2007		2006
Venture capital investments, at cost	$	82,677,528	$	62,118,800
Net unrealized depreciation [1]		4,567,144		8,450,969
Venture capital investments, at value	$	78,110,384	$	53,667,831

	December 31,			
		2007		2006
U.S. government and agency obligations, at cost	$	59,552,933	$	59,212,598
Net unrealized appreciation (depreciation) [1]		640,660		(556,451)
U.S. government and agency obligations, at value	$	60,193,593	$	58,656,147

[1]At December 31, 2007, and December 31, 2006, the net accumulated unrealized depreciation on investments was $3,926,484 and $9,007,420, respectively.

The following table summarizes the fair value composition of our venture capital investment portfolio at December 31, 2007, and December 31, 2006.

	December 31,	
Category	**2007**	**2006**
Tiny Technology	99.9%	99.9%
Other Venture Capital Investments	0.1%	0.1%
Total Venture Capital Investments	100.0%	100.0%

December 31, 2006

At December 31, 2006, our total assets and net assets were $118,328,590 and $113,930,303, respectively. Our NAV per share at that date was $5.42, and our shares outstanding increased to 21,015,017 at December 31, 2006.

During the twelve months ended December 31, 2006, significant developments included an increase in the value of our venture capital investments of $20,480,498 and a decrease in the value of our investment in U.S. government and agency securities of $37,594,717. The increase in the value of our venture capital investments, from $33,187,333 at December 31, 2005, to $53,667,831 at December 31, 2006, resulted primarily from six new and 10 follow-on investments, partially offset by a net decrease of $3,927,689 in the net value of our previous venture capital investments. The decrease in the value of our U.S. government and agency securities, from $96,250,864 at December 31, 2005, to $58,656,147 at December 31, 2006, was primarily owing to the use of funds for investments totaling $24,408,187, tax payments of $9,425,922, profit-sharing payments of $1,897,072, an increase in unrealized losses of $486,910 and payment of net operating expenses.

During December 2006, the Company also issued stock and received proceeds upon the exercise of employee stock options. Through December 31, 2006, the Company issued 258,672 shares and received proceeds of $2,615,190 as a result of option exercises.

The Company's liabilities decreased from $14,950,378 at December 31, 2005, to $4,398,287 at December 31, 2006, primarily owing to the payment of the tax payable on behalf of shareholders of $8,122,367 in January 2006, the payment of $1,897,072 in profit sharing in March 2006 and the reversal of the accrual for federal and state taxes payable of $1,514,967 recorded at December 31, 2005.

The following table is a summary of additions to our portfolio of venture capital investments made during the twelve months ended December 31, 2006:

New Investments	Cost
D-Wave Systems, Inc.	$ 1,750,547
Evolved Nanomaterial Sciences, Inc.	2,800,000
Innovalight, Inc.	2,500,000
Metabolon, Inc.	2,500,000
SiOnyx, Inc.	750,000
Xradia, Inc.	4,000,000
Follow-on Investments	
Chlorogen, Inc.	$ 221,438
Crystal IS, Inc.	1,098,240
CSwitch Corporation	2,850,000
NanoGram Corporation	1,262,764
NanoOpto Corporation	433,138
NeoPhotonics Corporation	2,750,000
Nextreme	500,000
Polatis, Inc.	89,310
Questech Corporation	12,750
SiOnyx, Inc.	890,000
Total	

$ 24,408,187

Cash Flow

Year Ended December 31, 2007

Net cash used in operating activities for the year ended December 31, 2007, was $4,142,572, primarily owing to the payment of operating expenses.

Cash used in investing activities for the year ended December 31, 2007, was $20,697,886, primarily reflecting a net increase in our investment in U.S. government and agency securities of $235,754 and investments in private placements of $20,595,161, less proceeds from the sale of venture capital investments of $174,669.

Cash provided by financing activities for the year ended December 31, 2007, was $23,098,679, reflecting the issuance of shares in connection with the Stock Plan and the net proceeds from the issuance of 1,300,000 new shares of our common stock on June 25, 2007, in a registered direct follow-on offering.

Year Ended December 31, 2006

Net cash used in operating activities for the year ended December 31, 2006, was $14,955,302, primarily owing both to the payment of various federal, state and local taxes, including the tax paid on behalf of shareholders for the deemed dividend, and to the payment of operating expenses.

Cash provided by investing activities for the year ended December 31, 2006, was $13,198,611, primarily reflecting net proceeds from the sale of U.S. government and agency securities of $37,593,589, less investments in private placements of $24,408,187.

Cash provided by financing activities for the year ended December 31, 2006, was $2,615,190, reflecting the issuance of shares in connection with the Stock Plan.

Year Ended December 31, 2005

Net cash used in operating activities for the year ended December 31, 2005, was $2,914,285, primarily owing to an increase in our operating expenses.

Cash used in investing activities for the year ended December 31, 2005, was $33,049,325, primarily reflecting a net increase in our investment in U.S. government and agency securities of $52,144,482 and investments in private placements of $16,251,339, less proceeds from the sale of venture capital investments of $35,392,200.

Cash provided by financing activities for the year ended December 31, 2005, was $36,526,567, reflecting net proceeds from the issuance of 3,507,500 new shares of our common stock on September 14, 2005, in an underwritten follow-on offering.

Liquidity and Capital Resources

March 31, 2008

Our primary sources of liquidity are cash, receivables and freely marketable securities, net of short-term indebtedness. Our secondary sources of liquidity are restricted securities of companies that are publicly traded.

At March 31, 2008, and December 31, 2007, our total net primary liquidity was $54,309,215 and $61,183,136, respectively, and our secondary liquidity was $0 and $0, respectively.

The decrease in our primary liquidity from December 31, 2007, to March 31, 2008, is primarily owing to the use of funds for investments and payment of net operating expenses.

On June 25, 2007, we completed the sale of 1,300,000 shares of our common stock from our shelf registration statement for gross proceeds of $14,027,000; net proceeds of this offering, after placement agent fees and offering costs of $1,033,832, were $12,993,168. We used the net proceeds of this offering to make new investments in tiny technology, as well as for follow-on investments in our existing venture capital investments and for working capital. Through March 31, 2008, we have used all of the net proceeds from this offering for these purposes.

On April 4, 2008, we filed a Post-Effective Amendment to our registration statement with the SEC on Form N-2 to update our existing shelf registration statement and register an additional 1,300,000 shares of our common stock. After the effective date, the common stock may be sold at prices and on terms to be set forth in one or more supplements to the prospectus from time to time.

December 31, 2007

At December 31, 2007, and December 31, 2006, our total net primary liquidity was $61,183,136 and $61,323,306, respectively, and our secondary liquidity was $0 and $0, respectively.

Our net primary sources of liquidity are more than adequate to cover our gross cash operating expenses over the next 12 months. Our gross cash operating expenses for 2007 and 2006 totaled $6,263,510 and $5,285,448, respectively.

The increase in our primary liquidity from December 31, 2006, to December 31, 2007, is primarily owing to the proceeds received through a registered direct stock offering from a shelf registration statement and proceeds received from stock option exercises, offset by the use of funds for investments and payment of net operating expenses. In the future, we may sell additional shares registered pursuant to our shelf registration statement.

On April 17, 2003, we signed a seven-year sublease for office space at 111 West 57th Street in New York City. On December 17, 2004, we signed a sublease for additional office space at our current location. The subleases expire on April 29, 2010. Total rent expense for our office space in New York City was $178,167 in 2007, $174,625 in 2006 and $171,171 in 2005. Future minimum sublease payments in each of the following years are: 2008 -- $193,083; 2009 -- $197,700; and thereafter, for the remaining term -- $65,969.

December 31, 2006

At December 31, 2006, and December 31, 2005, our total net primary liquidity was $61,323,306 and $97,797,219, respectively, and our secondary liquidity was $0 and $0, respectively.

Our net primary sources of liquidity were more than adequate to cover our gross cash operating expenses over the next 12 months. Our gross cash operating expenses for 2006 and 2005 totaled $5,285,448 and $5,021,066, respectively.

The decrease in our primary liquidity from December 31, 2005, to December 31, 2006, was primarily owing to the use of funds for investments, profit-sharing and tax payments, as well as net operating expenses.

On November 29, 2006, we filed a shelf registration statement with the SEC on Form N-2 to register 4,000,000 shares of our common stock. On December 11, 2006, and on April 23, 2007, we filed amended registration statements with the SEC. On May 11, 2007, the SEC declared the registration statement effective. The common stock may be sold at prices and on terms to be set forth in one or more supplements to the prospectus from time to time.

AVAILABLE INFORMATION

We file annual, quarterly and current reports, proxy statements and other information with the SEC under the Securities Exchange Act of 1934. You can inspect any materials we file with the SEC, without charge, at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at 202-942-8090 for further information on the Public Reference Room. The SEC maintains a web site that contains reports, proxy statements and other information regarding registrants, including us, that file such information electronically with the SEC. The address of the SEC's web site is www.sec.gov. Information contained on the SEC's web site about us is not incorporated into this Prospectus and you should not consider information contained on the SEC's web site to be part of this Prospectus.

You may obtain our annual reports, request other information about us and make shareholder inquiries by calling toll free 1-877-TINY TECH. We also make available our annual reports, free of charge, on our website at www.TinyTechVC.com. Information on our website is not part of this Prospectus and should not be considered as such when making your investment decision.

RISK FACTORS

Investing in our Common Stock involves significant risks relating to our business and investment objective. You should carefully consider the risks and uncertainties described below before you purchase any of our Common Stock. These risks and uncertainties are not the only ones we face. Unknown additional risks and uncertainties, or ones that we currently consider immaterial, may also impair our business. If any of these risks or uncertainties materialize, our business, financial condition or results of operations could be materially adversely affected. In this event, the trading price of our Common Stock could decline, and you could lose all or part of your investment.

Risks related to the companies in our portfolio.

A continuing lack of initial public offering opportunities may cause companies to stay in our portfolio longer, leading to lower returns, write-downs and write-offs.

Beginning in about 2001, many fewer venture capital-backed companies per annum have been able to complete initial public offerings (IPOs) than in the years of the previous decade. Moreover, in 2007, according to VentureSource, the venture capital-backed companies that completed IPOs had a median age of about 8.3 years, which was older than the median age of venture capital-backed IPOs in any period since 2001-2002. Now that some of our companies are becoming more mature, a continuing lack of IPO opportunities for venture capital-backed companies could lead to companies staying longer in our portfolio as private entities still requiring funding. In the best case, such stagnation would dampen returns, and in the worst case, could lead to write-downs and write-offs as some companies run short of cash and have to accept lower valuations in private fundings or are not able to access additional capital at all. A continuing lack of IPO opportunities for venture capital-backed companies is also causing some venture capital firms to change their strategies, which is causing some of them to reduce funding of their portfolio companies, making it more difficult for such companies to access capital and to fulfill their potential, leading in some cases to write-downs and write-offs of such companies by other venture capital firms, such as ourselves, who are co-investors in such companies.

Investing in small, private companies involves a high degree of risk and is highly speculative.

We have invested a substantial portion of our assets in privately held development stage or start-up companies, the securities of which are inherently illiquid. These businesses tend to lack management depth, to have limited or no history of operations and to have not attained profitability. Tiny technology companies are especially risky, involving scientific, technological and commercialization risks. Because of the speculative nature of these investments, these securities have a significantly greater risk of loss than traditional investment securities. Some of our venture capital investments are likely to be complete losses or unprofitable, and some will never realize their potential. We have been and will continue to be risk seeking rather than risk averse in our approach to venture capital and other investments. Neither our investments nor an investment in our Common Stock is intended to constitute a balanced investment program.

We may invest in companies working with technologies or intellectual property that currently have few or no proven commercial applications.

Nanotechnology, in particular, is a developing area of technology, of which much of the future commercial value is unknown, difficult to estimate and subject to widely varying interpretations. There are as of yet relatively few nanotechnology-enabled products commercially available. The timing of additional future commercially available nanotechnology products is highly uncertain.

Our portfolio companies may not successfully develop, manufacture or market their products.

The technology of our portfolio companies is new and in many cases unproven. Their potential products require significant and lengthy product development, manufacturing and marketing efforts. To date, many of our portfolio companies have not developed any commercially available products. In addition, our portfolio companies may not be able to manufacture successfully or to market their products in order to achieve commercial success. Further, the products may never gain commercial acceptance. If our portfolio companies are not able to develop, manufacture or market successful tiny technology-enabled products, they will be unable to generate product revenue or build sustainable or profitable businesses. Adverse conditions in the target markets of our portfolio companies may limit or prevent commercial success regardless of the contribution of tiny technology to these products.

Our portfolio companies working with tiny technology may be particularly susceptible to intellectual property litigation.

Research and commercialization efforts in tiny technology are being undertaken by a wide variety of government, academic and private corporate entities. As additional commercially viable applications of tiny technology emerge, ownership of intellectual property on which these products are based may be contested. From time to time, our portfolio companies are or have been involved in intellectual property disputes and litigation. Any litigation over the ownership of, or rights to, any of our portfolio companies' technologies or products could have a material adverse effect on those companies' values.

Unfavorable general economic conditions, as well as unfavorable conditions specific to the venture capital industry or a segment of portfolio companies, could result in the inability of our portfolio companies to access additional capital, leading to financial losses in our portfolio.

Most of the companies in which we have made or will make investments are susceptible to economic slowdowns or recessions. An economic slowdown or adverse capital or credit market conditions may affect the ability of a company in our portfolio to raise additional capital from venture capital or other sources or to engage in a liquidity event such as an initial public offering or merger. Certain types of portfolio companies, such as those engaged in solar, solid-state lighting and other alternative energy (cleantech) applications, which are currently in favor with the media and investors generally, may have a harder time accessing capital in the future if their industries subsequently fall out of fashion. Adverse economic, capital or credit market conditions may lead to financial losses in our portfolio.

Unstable credit markets could adversely affect our portfolio companies.

Although our portfolio companies rely primarily on equity financing, some of them borrow funds as well. For all but the most established companies, credit markets are currently unstable. During such periods of unstable credit availability, there can be no assurance that our portfolio companies will be able to borrow money on a timely basis or on reasonable terms, which could have a negative impact on their operating performance, raise their cost of capital, or even jeopardize their existence. Furthermore, certain of our portfolio companies manage their cash positions by investing in money-market funds, auction-rate securities, or other short-term securities that are vulnerable to current credit conditions. Lack of liquidity in such investments, or even defaults by issuers of such securities, could restrict the amount of cash available to such portfolio companies. These events could lead to financial losses in our portfolio.

The value of our portfolio could be adversely affected if the technologies utilized by our portfolio companies are found, or even rumored or feared, to cause health or environmental risks, or if legislation is passed that limits the commercialization of any of these technologies.

Nanotechnology has received both positive and negative publicity and is the subject increasingly of public discussion and debate. For example, debate regarding the production of materials that could cause harm to the environment or the health of individuals could raise concerns in the public's perception of nanotechnology, not all of which might be rational or scientifically based. Tiny technology in general and nanotechnology in particular are currently the subject of health and environmental impact research. If health or environmental concerns about tiny technology or nanotechnology were to arise, whether or not they had any basis in fact, our portfolio companies might incur additional research, legal and regulatory expenses, and might have difficulty raising capital or marketing their products. Government authorities could, for social or other purposes, prohibit or regulate the use of nanotechnology. Legislation could be passed that could circumscribe the commercialization of any of these technologies.

Our portfolio companies may generate revenues from the sale of non-tiny technology-enabled products.

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We consider a company to be a tiny technology company if a product or products, or intellectual property covering a product or products, that we consider to be at the microscale or smaller is material to its business plan. The core business of some of these companies may not be tiny technology-enabled products, and therefore their success or failure may not be dependent upon the tiny technology aspects of their business. In addition to developing products that we consider tiny technology, some of these companies may also develop products that we do not consider enabled by tiny technology. Some of these companies will generate revenues from the sale of non-tiny technology-enabled products. Additionally, it is possible that a portfolio company may decide to change its business focus after our initial investment and decide to develop and commercialize non-tiny technology-enabled products.

Risks related to the illiquidity of our investments.

We invest in illiquid securities and may not be able to dispose of them when it is advantageous to do so, or ever.

Most of our investments are or will be equity or equity-linked securities acquired directly from small companies. These equity securities are generally subject to restrictions on resale or otherwise have no established trading market. The illiquidity of most of our portfolio of equity securities may adversely affect our ability to dispose of these securities at times when it may be advantageous for us to liquidate these investments. We may never be able to dispose of these securities.

Unfavorable economic conditions and regulatory changes could impair our ability to engage in liquidity events.

Our business of making private equity investments and positioning our portfolio companies for liquidity events might be adversely affected by current and future capital markets and economic conditions. The public equity markets currently provide less opportunity for liquidity events than at times in the past when there was more robust demand for initial public offerings, even for more mature technology companies than those in which we typically invest. The potential for public market liquidity could further decrease and could lead to an inability to realize potential gains or could lead to financial losses in our portfolio and a decrease in our revenues, net income and assets. Recent government reforms affecting publicly traded companies, stock markets, investment banks and securities research practices have made it more difficult for privately held companies to complete successful initial public offerings of their equity securities, and such reforms have increased the expense and legal exposure of being a public company. Slowdowns in initial public offerings may also be having an adverse effect on the frequency and prices of acquisitions of privately held companies. A lack of merger and/or acquisition opportunities for privately held companies also may be having an adverse effect on the ability of these companies to raise capital from private sources. Public equity market response to companies offering nanotechnology-enabled products is uncertain. An inability to engage in liquidity events could negatively affect our liquidity, our reinvestment rate in new and follow-on investments and the value of our portfolio.

Even if some of our portfolio companies complete initial public offerings, the returns on our investments in those companies would be uncertain.

When companies in which we have invested as private entities complete initial public offerings of their securities, these newly issued securities are by definition unseasoned issues. Unseasoned issues tend to be highly volatile and have uncertain liquidity, which may negatively affect their price. In addition, we are typically subject to lock-up provisions that prohibit us from selling our investments into the public market for specified periods of time after initial public offerings. The market price of securities that we hold may decline substantially before we are able to sell these securities. Most initial public offerings of technology companies in the United States are listed on the Nasdaq Global Market. Government reforms of the Nasdaq Global Market have made market-making by broker-dealers less profitable, which has caused broker-dealers to reduce their market-making activities, thereby making the market for unseasoned stocks less liquid than they might be otherwise.

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Risks related to our Company.

Because there is generally no established market in which to value our investments, our Valuation Committee's value determinations may differ materially from the values that a ready market or third party would attribute to these investments.

There is generally no public market for the equity securities in which we invest. Pursuant to the requirements of the 1940 Act, we value all of the private equity securities in our portfolio at fair value as determined in good faith by a committee of independent members of our Board of Directors, which we call the Valuation Committee, pursuant to Valuation Procedures established by the Board of Directors. As a result, determining fair value requires that judgment be applied to the specific facts and circumstances of each portfolio investment pursuant to specified valuation principles and processes. We are required by the 1940 Act to value specifically each individual investment on a quarterly basis and record unrealized depreciation for an investment that we believe has become impaired. Conversely, we must record unrealized appreciation if we believe that our securities have appreciated in value. Our valuations, although stated as a precise number, are necessarily within a range of values that vary depending on the significance attributed to the various factors being considered.

We use the Black-Scholes-Merton option pricing model to determine the fair value of warrants held in our portfolio. Option pricing models, including the Black-Scholes-Merton model, require the use of subjective input assumptions, including expected volatility, expected life, expected dividend rate, and expected risk-free rate of return. In the Black-Scholes-Merton model, variations in the expected volatility or expected term assumptions have a significant impact on fair value. Because the securities underlying the warrants in our portfolio are not publicly traded, many of the required input assumptions are more difficult to estimate than they would be if a public market for the underlying securities existed.

Without a readily ascertainable market value and because of the inherent uncertainty of valuation, the fair value that we assign to our investments may differ from the values that would have been used had an efficient market existed for the investments, and the difference could be material. Any changes in fair value are recorded in our consolidated statements of operations as a change in the "Net (decrease) increase in unrealized appreciation on investments." See "Determination of Net Asset Value."

In the venture capital industry, even when a portfolio of early-stage, high-technology venture capital investments proves to be profitable over the portfolio's lifetime, it is common for the portfolio's value to undergo a so-called "J-curve" valuation pattern. This means that when reflected on a graph, the portfolio's valuation would appear in the shape of the letter "J," declining from the initial valuation prior to increasing in valuation. This J-curve valuation pattern results from write-downs and write-offs of portfolio investments that appear to be unsuccessful, prior to write-ups for portfolio investments that prove to be successful. Because early-stage companies typically have negative cash flow and are by their nature inherently fragile, a valuation process can more readily substantiate a loss of value than an increase in value. Even if our venture capital investments prove to be profitable in the long run, such J-curve valuation patterns could have a significant adverse effect on our net asset value per share and the value of our Common Stock in the interim. Over time, as we continue to make additional tiny technology investments, this J-curve pattern may be less relevant for our portfolio as a whole, because the individual J-curves for each investment, or series of investments, may overlap with previous investments at different stages of their J-curves.

Changes in valuations of our privately held, early stage companies tend to be more volatile than changes in prices of publicly traded securities.

Investments in privately held, early stage companies are inherently more volatile than investments in more mature businesses. Such immature businesses are inherently fragile and easily affected by both internal and external forces. Our investee companies can lose much or all of their value suddenly in response to an internal or external adverse event. Conversely, these immature businesses can gain suddenly in value in response to an internal or external positive development. Moreover, because our ownership interests in such investments are valued only at quarterly intervals by our Valuation Committee, a committee made up of all of our independent members of our Board of Directors, changes in valuations from one valuation point to another tend to be larger than changes in valuations of marketable securities which are revalued in the marketplace much more frequently, in some highly liquid cases, virtually continuously.

We expect to continue to experience material write-downs of securities of portfolio companies.

Write-downs of securities of our privately held companies have always been a by-product and risk of our business. We expect to continue to experience material write-downs of securities of privately held portfolio companies. Write-downs of such companies occur at all stages of their development. Such write-downs may increase in dollar terms, frequency and as a percentage of our net asset value as our dollar investment activity in privately held companies continues to increase, and the number of such holdings in our portfolio continues to grow. Because the average size of each of our investments in tiny technology has increased from year to year and continues to increase, the average size of our write-downs will probably also increase.

Because we do not choose investments based on a strategy of diversification, the value of our business is subject to greater volatility than the value of companies with more broadly diversified investments.

We do not choose investments based on a strategy of diversification. Therefore, we may be more vulnerable to events affecting a single sector or industry and therefore subject to greater volatility than a company that follows a diversification strategy. Accordingly, an investment in our Common Stock may present greater risk to you than an investment in a diversified company.

We are dependent upon key management personnel for future success, and may not be able to retain them.

We are dependent upon the diligence and skill of our senior management and other key advisers for the selection, structuring, closing and monitoring of our investments. We utilize lawyers, and we utilize outside consultants, including one of our directors, Lori D. Pressman, to assist us in conducting due diligence when evaluating potential investments. There is generally no publicly available information about the companies in which we invest, and we rely significantly on the diligence of our employees and advisers to obtain information in connec-tion with our investment decisions. Our future success to a significant extent depends on the continued service and coordination of our senior management team, and particularly on Charles E. Harris, our Chairman, Chief Executive Officer and a Managing Director, who will be subject to mandatory retirement pursuant to the Company's mandatory retirement policy for senior executives on December 31, 2008; on Douglas W. Jamison, our President, Chief Operating Officer and a Managing Director, who has been designated by our Board of Directors as the successor to Mr. Harris in his positions of Chairman and Chief Executive Officer as of January 1, 2009 upon his retirement; on Daniel B. Wolfe, our Chief Financial Officer and a Managing Director; on Alexei A. Andreev and Michael A. Janse, each an Executive Vice President and Managing Director; and on Sandra M. Forman, our General Counsel, Chief Compliance Officer and Director of Human Resources. The departure of any of our executive officers, key employees or advisers could materially adversely affect our ability to implement our business strategy. We do not maintain for our benefit any key-man life insurance on any of our officers or employees.

We will need to hire additional employees as the size of our portfolio increases.

We anticipate that it will be necessary for us to add investment professionals with expertise in venture capital and/or tiny technology and administrative and support staff to accommodate the increasing size of our portfolio. We may need to provide additional scientific, business, accounting, legal or investment training for our hires. There is competition for highly qualified personnel. We may not be successful in our efforts to recruit and retain highly qualified personnel because the expenses that we incur as a heavily regulated, publicly held company preclude our paying as high a percentage of our total expenses in cash compensation for employees as the private partnerships with which we compete. Although we have the advantage of offering equity incentive compensation, unlike those private partnerships, we cannot permit co-investment in our investments by our employees, and we cannot give our employees 20 percent or higher carried interests in our investments as incentive compensation taxable as long-term capital gains.

The market for venture capital investments, including tiny technology investments, is highly competitive.

We face substantial competition in our investing activities from many competitors, including but not limited to: private venture capital funds; investment affiliates of large industrial, technology, service and financial companies; small business investment companies; hedge funds; wealthy individuals; and foreign investors. Our most significant competitors typically have significantly greater financial resources than we do. Greater financial resources are particularly advantageous in securing lead investor roles in venture capital syndicates. Lead investors typically negotiate the terms and conditions of such financings. Many sources of funding compete for a small number of attractive investment opportunities. Hence, we face substantial competition in sourcing good investment opportunities on terms of investment that are commercially attractive.

In addition to the difficulty of finding attractive investment opportunities, our status as a regulated business development company may hinder our ability to participate in investment opportunities or to protect the value of existing investments.

We are required to disclose on a quarterly basis the names and business descriptions of our portfolio companies and the type and value of our portfolio securities. Most of our competitors are not subject to these disclosure requirements. Our obligation to disclose this information could hinder our ability to invest in some portfolio companies. Additionally, other current and future regulations may make us less attractive as a potential investor than a competitor not subject to the same regulations.

Our failure to make follow-on investments in our portfolio companies could impair the value of our portfolio.

Following an initial investment in a portfolio company, we may make additional investments in that portfolio company as "follow-on" investments, in order to: (1) increase or maintain in whole or in part our ownership percentage; (2) exercise warrants, options or convertible securities that were acquired in the original or subsequent financing; or (3) attempt to preserve or enhance the value of our investment.

We may elect not to make follow-on investments or lack sufficient funds to make such investments. We have the discretion to make any follow-on investments, subject to the availability of capital resources. The failure to make a follow-on investment may, in some circumstances, jeopardize the continued viability of a portfolio company and our initial investment, or may result in a missed opportunity for us to increase our participation in a successful operation, or may cause us to lose some or all preferred rights pursuant to "pay-to-play" provisions that have become common in venture capital transactions. These provisions require proportionate investment in subsequent rounds of financing in order to preserve preferred rights such as anti-dilution protection, liquidation preferences and preemptive rights to invest in future rounds of financing. Even if we have sufficient capital to make a desired follow-on investment, we may elect not to make a follow-on investment because we may not want to increase our concentration of risk, because we prefer other opportunities or because we are inhibited by compliance with business development company requirements or the desire to maintain our tax status.

Bank borrowing or the issuance of debt securities or preferred stock by us, to fund investments in portfolio companies or to fund our operating expenses, would make our total return to common shareholders more volatile.

Use of debt or preferred stock as a source of capital entails two primary risks. The first is the risk of leverage, which is the use of debt to increase the pool of capital available for investment purposes. The use of debt leverages our available common equity capital, magnifying the impact on net asset value of changes in the value of our investment portfolio. For example, a business development company that uses 33 percent leverage (that is, $50 of leverage per $100 of common equity) will show a 1.5 percent increase or decline in net asset value for each 1 percent increase or decline in the value of its total assets. The second risk is that the cost of debt or preferred stock financing may exceed the return on the assets the proceeds are used to acquire, thereby diminishing rather than enhancing the return to common shareholders. If we issue preferred shares or debt, the common shareholders would bear the cost of this leverage. To the extent that we utilize debt or preferred stock financing for any purpose, these two risks would likely make our total return to common shareholders more volatile. In addition, we might be required to sell investments, in order to meet dividend, interest or principal payments, when it might be disadvantageous for us to do so.

As provided in the 1940 Act and subject to some exceptions, we can issue debt or preferred stock so long as our total assets immediately after the issuance, less some ordinary course liabilities, exceed 200 percent of the sum of the debt and any preferred stock outstanding. The debt or preferred stock may be convertible in accordance with SEC guidelines, which might permit us to obtain leverage at more attractive rates. The requirement under the 1940 Act to pay, in full, dividends on preferred shares or interest on debt before any dividends may be paid on our Common Stock means that dividends on our Common Stock from earnings may be reduced or eliminated. An inability to pay dividends on our Common Stock could conceivably result in our ceasing to qualify as a regulated investment company, or RIC, under the Code, which would in most circumstances be materially adverse to the holders of our Common Stock. As of the date hereof, we do not have any debt or preferred stock outstanding.

We are authorized to issue preferred stock, which would convey special rights and privileges to its owners senior to those of Common Stock shareholders.

We are currently authorized to issue up to 2,000,000 shares of preferred stock, under terms and conditions determined by our Board of Directors. These shares would have a preference over our Common Stock with respect to dividends and liquidation. The statutory class voting rights of any preferred shares we would issue could make it more difficult for us to take some actions that might, in the future, be proposed by the Board and/or holders of Common Stock, such as a merger, exchange of securities, liquidation or alteration of the rights of a class of our securities, if these actions were perceived by the holders of the preferred shares as not in their best interests. The issuance of preferred shares convertible into shares of Common Stock might also reduce the net income and net asset value per share of our Common Stock upon conversion.

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

We currently intend to qualify as a RIC for 2008 under the Code. As a RIC, we do not have to pay federal income taxes on our income (including realized gains) that is distributed to our shareholders. Accordingly, we are not permitted under accounting rules to establish reserves for taxes on our unrealized capital gains. If we failed to qualify for RIC status in 2008 or beyond, to the extent that we had unrealized gains, we would have to establish reserves for taxes, which would reduce our net asset value, accordingly. In addition, if we, as a RIC, were to decide to make a deemed distribution of net realized capital gains and retain the net realized capital gains, we would have to establish appropriate reserves for taxes that we would have to pay on behalf of shareholders. It is possible that establishing reserves for taxes could have a material adverse effect on the value of our Common Stock. See "Taxation."

We operate in a heavily regulated environment, and changes to, or non-compliance with, regulations and laws could harm our business.

We are subject to substantive SEC regulations as a business development company. Securities and tax laws and regulations governing our activities may change in ways adverse to our and our shareholders' interests, and interpretations of these laws and regulations may change with unpredictable consequences. Any change in the laws or regulations that govern our business could have an adverse impact on us or on our operations. Changing laws, regulations and standards relating to corporate governance, valuation and public disclosure, including the Sarbanes-Oxley Act of 2002, new SEC regulations, new federal accounting standards and Nasdaq Global Market rules, are creating additional expense and uncertainty for publicly held companies in general, and for business development companies in particular. These new or changed laws, regulations and standards are subject to varying interpretations in many cases because of their lack of specificity, and as a result, their application in practice may evolve over time, which may well result in continuing uncertainty regarding compliance matters and higher costs necessitated by ongoing revisions to disclosure and governance practices.

We are committed to maintaining high standards of corporate governance and public disclosure. As a result, our efforts to comply with evolving laws, regulations and standards have and will continue to result in increased general and administrative expenses and a diversion of management time and attention from revenue-generating activities to compliance activities. In particular, our efforts to comply with Section 404 of the Sarbanes-Oxley Act of 2002 and the related regulations regarding our required assessment of our internal controls over financial reporting and our external auditors' audit of that assessment has required the commitment of significant financial and managerial resources.

Moreover, even though business development companies are not mutual funds, they must comply with several of the regulations applicable to mutual funds, such as the requirement for the implementation of a comprehensive compliance program and the appointment of a Chief Compliance Officer. Further, our Board members, Chief Executive Officer and Chief Financial Officer could face an increased risk of personal liability in connection with the performance of their duties. As a result, we may have difficulty attracting and retaining qualified board members and executive officers, which could harm our business, and we have significantly increased both our coverage under, and the related expense for, directors' and officers' liability insurance. If our efforts to comply with new or changed laws, regulations and standards differ from the activities intended by regulatory or governing bodies, our reputation may be harmed. Also, as business and financial practices continue to evolve, they may render the regulations under which we operate less appropriate and more burdensome than they were when originally imposed. This increased regulatory burden is causing us to incur significant additional expenses and is time consuming for our management, which could have a material adverse effect on our financial performance.

Market prices of our Common Stock will continue to be volatile.

We expect that the market price of our Common Stock will continue to be volatile. The price of the Common Stock may be higher or lower than the price you pay for your shares, depending on many factors, some of which are beyond our control and may not be directly related to our operating performance. These factors include the following:

- stock market and capital markets conditions;
- internal developments in our Company with respect to our personnel, financial condition and compliance with all applicable regulations;
- announcements regarding any of our portfolio companies;
- announcements regarding developments in the nanotechnology field in general;
- environmental and health concerns regarding nanotechnology, whether real or perceptual;
- announcements regarding government funding and initiatives related to the development of nanotechnology;
- general economic conditions and trends; and/or
- departures of key personnel.

We will not have control over many of these factors, but expect that our stock price may be influenced by them. As a result, our stock price may be volatile, and you may lose all or part of your investment.

Quarterly results fluctuate and are not indicative of future quarterly performance.

Our quarterly operating results fluctuate 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 we and our portfolio companies encounter competition in our markets and general economic and capital markets 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.

To the extent that we do not realize income or choose not to retain after-tax realized capital gains, we will have a greater need for additional capital to fund our investments and operating expenses.

As a RIC, we must annually distribute at least 90 percent of our investment company taxable income as a dividend and may either distribute or retain our realized net capital gains from investments. As a result, these earnings may not be available to fund investments. If we fail to generate net realized capital gains or to obtain funds from outside sources, it would have a material adverse effect on our financial condition and results of operations as well as our ability to make follow-on and new investments. Because of the structure and objectives of our business, we generally expect to experience net operating losses and rely on proceeds from sales of investments, rather than on investment income, to defray a significant portion of our operating expenses. These sales are unpredictable and may not occur. In addition, as a business development company, in order to pay dividends or repurchase shares, we are generally required to maintain a ratio of at least 200 percent of total assets to total borrowings and preferred stock, which may restrict our ability to borrow to fund these requirements. Lack of capital could curtail our investment activities or impair our working capital.

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Investment in foreign securities could result in additional risks.

We may invest in foreign securities, and we currently have one investment in a foreign security. When we invest in securities of foreign issuers, we may be subject to risks not usually associated with owning securities of U.S. issuers. These risks can include fluctuations in foreign currencies, foreign currency exchange controls, social, political and economic instability, differences in securities regulation and trading, expropriation or nationalization of assets and foreign taxation issues. In addition, changes in government administrations or economic or monetary policies in the United States or abroad could result in appreciation or depreciation of our securities and could favorably or unfavorably affect our operations. It may also be more difficult to obtain and enforce a judgment against a foreign issuer. Any foreign investments made by us must be made in compliance with U.S. and foreign currency restrictions and tax laws restricting the amounts and types of foreign investments.

Although most of our investments are denominated in U.S. dollars, our investments that are denominated in a foreign currency are subject to the risk that the value of a particular currency may change in relation to the U.S. dollar, in which currency we maintain financial statements and valuations. Among the factors that may affect currency values are trade balances, the level of short-term interest rates, differences in relative values of similar assets in different currencies, long-term opportunities for investment and capital appreciation and political developments.

Risks related to this offering.

Investing in our stock is highly speculative and an investor could lose some or all of the amount invested.

Our investment objective and strategies result in a high degree of risk in our investments and may result in losses in the value of our investment portfolio. Our investments in portfolio companies are highly speculative and, therefore, an investor in our Common Stock may lose his or her entire investment. The value of our Common Stock may decline and may be affected by numerous market conditions, which could result in the loss of some or all of the amount invested in our Common Stock. The securities markets frequently experience extreme price and volume fluctuations that affect market prices for securities of companies in general, and technology and very small capitalization companies in particular. Because of our focus on the technology and very small capitalization sectors, and because we are a very small capitalization company ourselves, our stock price is especially likely to be affected by these market conditions. General economic conditions, and general conditions in tiny technology in general and nanotechnology in particular and in the semi-conductor and information technology, life sciences, materials science and other high technology industries, may also affect the price of our Common Stock.

We will have discretion over the use of proceeds of this offering.

We will have flexibility in applying the proceeds of this offering. We may pay operating expenses, including due diligence expenses on potential new investments, from the net proceeds. Our ability to achieve our investment objective may be limited to the extent that the net proceeds of the offering, pending full investment, are used to pay operating expenses.

Our shares might trade at discounts from net asset value or at premiums that are unsustainable over the long term.

Shares of business development companies like us may, during some periods, trade at prices higher than their net asset value and during other periods, as frequently occurs with closed-end investment companies, trade at prices lower than their net asset value. The possibility that our shares will trade at discounts from net asset value or at premiums that are unsustainable over the long term are risks separate and distinct from the risk that our net asset value per share will decrease. The risk of purchasing shares of a business development company that might trade at a discount or unsustainable premium is more pronounced for investors who wish to sell their shares in a relatively short period of time because, for those investors, realization of a gain or loss on their investments is likely to be more dependent upon changes in premium or discount levels than upon increases or decreases in net asset value per share. Our Common Stock may not trade at a price higher than or equal to net asset value per share. On March 31, 2008, our stock closed at $7.13 per share, a premium of $1.27 over our net asset value per share of $5.86 as of March 31, 2008.

The Board of Directors intends to grant stock options to our employees pursuant to the Company's Equity Incentive Plan. When exercised, these options may have a dilutive effect on existing shareholders.

The Board of Directors intends to grant stock options to our employees pursuant to the Company's Equity Incentive Plan. Pursuant to the plan, the Company's Board of Directorsmay grant options from time to time for up to 20 percent of the total shares of stock issued and outstanding. As of the date hereof, options have been granted to all 10 of our officers and to two non-officier employees. When options are exercised, net asset value per share will decrease if the net asset value per share at the time of exercise is higher than the exercise price. Alternatively, net asset value per share will increase if the net asset value per share at the time of exercise is lower than the exercise price. Therefore, existing shareholders will be diluted if the net asset value per share at the time of exercise is higher than the exercise price of the options. Even though issuance of shares pursuant to exercises of options increases the Company's capital, and regardless of whether such issuance results in increases or decreases in net asset value per share, such issuance results in existing shareholders owning a smaller percentage of the shares outstanding.

You have no right to require us to repurchase your shares.

You do not have the right to require us to repurchase your shares of Common Stock.

FORWARD-LOOKING INFORMATION

This Prospectus may contain "forward-looking statements" based on our current expectations, assumptions and estimates about us and our industry. These forward-looking statements involve risks and uncertainties. Words such as "believe," "anticipate," "estimate," "expect," "intend," "plan," "will," "may," "might," "could," "continue" and other similar expressions identify forward-looking statements. In addition, any statements that refer to expectations, projections or other characterizations of future events or circumstances are forward-looking statements. Our actual results could differ materially from those anticipated in the forward-looking statements as a result of several factors more fully described in "Risk Factors" and elsewhere in this Prospectus. The forward-looking statements made in this Prospectus relate only to events as of the date on which the statements are made. We undertake no obligation to update publicly any forward-looking statements for any reason, even if new information becomes available or other events occur in the future.

You should understand that under Sections 27A(b)(2)(B) of the Securities Act of 1933 and Section 21E(b)(2)(B) of the Securities Exchange Act of 1934, the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995 may not as a technical matter apply to statements made in connection with this offering.

USE OF PROCEEDS

We estimate the total net proceeds of the offering to be up to $21,296,000 based on the last reported price for our Common Stock on May 28, 2008 of $7.98.

We expect to invest or reserve for potential follow-on investment the net proceeds of any offering within two years from the completion of such offering. The net proceeds of this offering invested after two years will only be used for follow-on investments. Reserves for follow-on investments in any particular initial investment may be no more than the greater of twice the investment to date or five times the initial investment in the case of seed-stage investments, though we may invest more than the amount reserved for this purpose in any particular portfolio holding. Although we intend to make our initial investments exclusively in companies that we believe are involved significantly in tiny technology, we may also make follow-on investments in existing portfolio companies involved in other technologies. Pending investment in portfolio companies, we intend to invest the net proceeds of any offering of our Common Stock in time deposits and/or income-producing securities that are issued or guaranteed by the federal government or an agency of the federal government or a government-owned corporation, which may well yield less than our operating expense ratio. We may also use the proceeds of this offering for operating expenses, including due diligence expenses on potential investments. Our portfolio companies rarely pay us dividends or interest, and we do not generate enough income from fixed income investments to meet all of our operating expenses. If we pay operating expenses from the proceeds, it will reduce the net proceeds of the offering that we will have available for investment.

PRICE RANGE OF COMMON STOCK

Our Common Stock is traded on the Nasdaq Global Market under the symbol "TINY."

The following table sets forth for the quarters indicated, the high and low sale prices on the Nasdaq Global Market per share of our Common Stock and the net asset value and the premium or discount from net asset value per share at which the shares of Common Stock were trading, expressed as a percentage of net asset value, at each of the high and low sale prices provided.

	Market Price		Net Asset Value ("NAV") Per Share	Premium or (Discount) as a % of NAV	
Quarter Ended	**High**	**Low**	**at End of Period**	**High**	**Low**
March 31, 2006	16.10	12.75	5.60	187.5	127.7
June 30, 2006	14.26	9.57	5.54	157.4	72.7
September 30, 2006	12.99	9.38	5.54	134.5	69.3
December 31, 2006	15.16	11.80	5.42	179.7	117.7
March 31, 2007	13.58	11.00	5.27	157.7	108.7
June 30, 2007	14.32	11.01	5.54	158.5	98.7
September 30, 2007	11.79	9.51	5.69	107.2	67.1
December 31, 2007	11.10	8.00	5.93	87.2	34.9
March 31, 2008	8.98	5.76	5.86	53.2	(1.7)

Historically, the shares of our Common Stock have traded at times at a discount and at other times at a premium to net asset value. The last reported price for our Common Stock on May 28, 2008 was $7.98 per share. As of May 27, 2008, we had approximately 136 shareholders of record.

BUSINESS

We are a venture capital company specializing in tiny technology. We were incorporated as a New York corporation in 1981. In 1995, we elected to be regulated as a business development company under the 1940 Act. Our investment objective is to achieve long-term capital appreciation, rather than current income, by making venture capital investments in early-stage companies. Although our portfolio includes one insignificant non-tiny technology investment made prior to 2001, we now make our initial investments exclusively in tiny technology companies. By making these investments, we seek to provide our shareholders with a specific focus on tiny technology through a portfolio of venture capital investments that address a variety of markets and products. We believe that we are the only publicly traded business development company making initial venture capital investments exclusively in tiny technology.

Nanotechnology, microsystems and microelectromechanical systems, (MEMS), are often referred to collectively as "tiny technology," or "small technology," by scientists and others in this field. Nanotechnology in particular is multidisciplinary and widely applicable, and it incorporates technology that is significantly smaller than is currently in widespread commercial use. Microsystems are measured in micrometers, which are units of measurement in millionths of a meter. Nanotechnology is measured in nanometers, which are units of measurement in billionths of a meter. Because it is a new field, tiny technology, and particularly nanotechnology, has significant scientific, engineering, regulatory and commercialization risks.

Except for our holdings of U.S. treasury securities for liquidity, all of our current investments are in privately held, venture-capital-backed companies. All of our active portfolio companies are involved in tiny technology. We define active portfolio companies as those companies that are currently operating and are not in the process of unwinding their businesses. Tiny technology, particularly nanotechnology, is found in many industries, including pharmaceuticals, medical devices, electronics and cleantech, which includes alternative-energy and energy-saving products. A subset of our tiny-technology companies are focused on the commercialization of cleantech products, which we refer to as our “Tiny Tech for Cleantech” portfolio. The use of nanotechnology-enabled advanced materials for clean energy in particular is an area of increasing global interest, and these types of materials are the cornerstones of new generations of photovoltaics, batteries, solid-state lighting, fuel cells, bio-fuels and other energy-related applications that are the focus of a number of recently funded early-stage companies. Although we have not specifically targeted investments in cleantech companies, as of March 31, 2008, eight of our 31 active portfolio companies were in our "Tiny Tech for Cleantech" portfolio. These companies represented 35.5 percent of the value of the active companies in our portfolio as of March 31, 2008.

As a venture capital company, we make it possible, through the ownership of our shares, for our shareholders to participate in this emerging field of tiny technology at an earlier stage than would typically be possible for them. By making investments in companies that control intellectual property relevant to tiny technology, we are building a portfolio that we believe will be difficult to replicate, as we believe it will likely become increasingly difficult to create new foundational intellectual property in nanotechnology.

As is usual in the venture capital industry, our venture capital investments are primarily in convertible preferred stock, which is usually the most senior security in a portfolio company’s equity capital structure until the company has substantial revenues, and which gives us seniority over the holders of Common Stock (usually including the founders) while preserving fully our participation in the upside potential of the portfolio company through the conversion feature and, in many cases, a dividend right payable in kind (which increases our participation in the portfolio company) or potentially in cash.

We have a long history of investing in venture capital and of business development. Our approach is traditional, including a patient examination of available early stage opportunities, thorough due diligence and close involvement with management. Unlike most private equity and venture capital funds, we will not be subject to any requirement to return capital to investors. Such requirements typically stipulate that these funds can only be invested once and, together with any capital gains on such investment, must be returned to investors, net of fees and carried interest in profits, after a pre-agreed time period. These provisions may cause private equity and venture capital funds to seek investments that are likely to be able to be sold relatively quickly or to seek returns on their investments through mergers, public equity offerings or other liquidity events more quickly than they otherwise might. Because we typically invest as part of a syndicate of venture capital firms, their time horizons often determine ours, though we may provide seed capital before forming a syndicate with other investors, or maintain our investment in an investee company after it goes public, even after our co-investors sell or distribute their shares.

In addition, to the investor, we offer:

- a portfolio consisting of investments that are generally available only to a small, highly specialized group of professional venture capital firms as investors;

- a qualified team of professionals, including six full-time members of management, five of whom are designated as Managing Directors: Charles E. Harris, Douglas W. Jamison, Alexei A. Andreev, Michael A. Janse and Daniel B. Wolfe, and a Vice President, Misti Ushio, to evaluate and monitor investments. One of our directors is also a consultant to us, Lori D. Pressman. These seven professionals collectively have expertise in venture capital, intellectual property and tiny technology to evaluate and monitor investments;

- the opportunity to benefit from our experience in a new field expected to permeate a variety of industries; and

- through the ownership of our publicly traded shares, a measure of liquidity not available in typical underlying venture capital portfolio investments.

While we intend to make initial investments exclusively in companies that we believe are involved significantly in tiny technology, we may also make follow-on investments in our one existing non-tiny technology portfolio company. The balance of our funds is primarily invested in short-term U.S. government and agency securities. We are an internally managed investment company because our officers and employees, under the general supervision of our Board of Directors, control our operations. We have no investment adviser.

Subject to our compliance with business development company and tax code requirements, there are no limitations on the types of securities or other assets, foreign or domestic, in which we may invest. Investments may include the following:

- equity, equity-related securities (including warrants) and debt with equity features from either private or public issuers, whether in corporate, partnership or other form, including development stage or start-up entities;

- debt obligations of all types having varying terms with respect to security or credit support, subordination, purchase price, interest payments and maturity; and

- to a limited extent, intellectual property, including patents, research and development in technology or product development that may lead to patents or other marketable technology.

Neither our investments nor an investment in our securities constitutes a balanced investment program. We have been and will continue to be risk seeking rather than risk averse in our investment approach. We reserve the fullest possible freedom of action regarding the types of investments we make and our relationship with our portfolio companies, subject to our certificate of incorporation, applicable law and regulations, and policy statements described herein. Our tiny technology investment policy is not a "fundamental policy" under the 1940 Act and, accordingly, may be changed without shareholder approval, although we will give shareholders at least 60 days prior written notice of any change.

Our business is subject to federal regulation under the 1940 Act, under which we have elected to operate as a business development company. As a business development company, we are subject to regulatory requirements, the most significant of which relate to our investments and borrowings. The 1940 Act provides that we may not make an investment in non-qualifying assets unless at the time at least 70 percent of the value of our total assets (measured as of the date of our most recently filed financial statements) consists of qualifying assets. We must also maintain a coverage ratio of assets to senior securities (such as debt and preferred stock) of at least 200 percent immediately after giving effect to the issuance of any senior securities. We are also required to offer managerial assistance to our portfolio companies, in addition to our investment. For tax purposes, we are a RIC under the Code.

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We believe that increasing the size of our assets should lower our expenses as a proportion of average net assets because some of our costs, such as administration and public company expenses, are fixed and can be spread over a larger asset base and will decline as a percentage of assets as our assets increase. In addition, with more assets, we expect the average size of our investments to increase. Each due diligence investigation entails expenses whether or not we complete the transaction, and the cost of due diligence, negotiation and documentation of our investments does not vary proportionately with the size of the investment or intended investment.

Some expenses are expected to increase as new investments are made. We plan to add personnel to enable us to enlarge the scope of our activities and our expertise in tiny technology, and our hiring of new employees will increase with more assets under management. We also believe that a larger number of outstanding shares and a larger number of beneficial owners of shares could increase the level of our visibility and improve the trading liquidity of our shares on the Nasdaq Global Market. We may not realize any of these benefits.

Historical Investment Track Record

We incorporated under the laws of the State of New York in August 1981. In 1983, we invested in Otisville BioTech, Inc. Since our investment in Otisville in 1983 through March 31, 2008, we have made a total of 81 venture capital investments, including four private placement investments in securities of publicly traded companies (PIPES). We have exited 47 of these 81 investments, realizing total proceeds of $143,895,288 on our invested capital of $56,349,559. As measured from first dollar in to last dollar out, the average and median holding periods for these 47 investments were 3.77 years and 3.20 years, respectively. As measured by the 165 separate rounds of investment within these 47 investments, the average and median holding periods for the 165 separate rounds of investment were 2.93 years and 2.64 years, respectively. Nineteen of the 47 investments sold were profitable. The average and median holding periods, as measured from first dollar in, of these 19 profitable investments were 4.03 years and 3.35 years, respectively. Of these 19 profitable investments, seven were profitable sales after initial public offerings (IPOs), eight were profitable mergers and acquisitions transactions and four were profitable sales of PIPES. As measured from first dollar in, the average holding period for profitable exits after IPOs, mergers and acquisitions transactions and PIPES were 4.26 years, 4.06 years and 1.07 years, respectively.

Twenty-eight of the 47 investments sold were unprofitable. Twenty-seven of these investments were unprofitable non-IPO disposals, and we sold one investment, Princeton Video Image, Inc., that had had an IPO, at a loss. As measured from the first dollar in, the average holding period for the 27 unprofitable non-IPO exits was 3.49 years and the holding period for the unprofitable IPO exit was 7.74 years. Below is a list of holding periods for our eight historical IPOs. As measured from first dollar in to IPO date, the average and median holding periods were 4.56 years and 3.88 years, respectively.

Historical IPOs	**Holding Period to IPO (yrs)**
Alliance Pharmaceutical Corporation	6.39
Ag Services of America, Inc.	1.39
Molten Metal Technology, Inc.	3.25
Nanophase Technologies Corporation	3.07
Princeton Video Image, Inc. (formerly Princeton Electronic Billboard)	6.63
SciQuest, Inc. (formerly BioSupplyNet)	3.09
Genomica Corporation	4.52
NeuroMetrix, Inc.	8.14
Average	**4.56**

Median	**3.88**

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In 1994, we invested in our first nanotechnology company, Nanophase Technologies Corporation. Recognizing the potential of tiny technology, we continued to monitor developments in the field, and since 2001 we have made tiny technology the exclusive focus of our initial investment activity. From August 2001 through March 2008, all 39 of our initial investments have been in companies involved in the development of products and technologies based on tiny technology.

At March 31, 2008, the remaining tiny technology venture capital investments in our portfolio, including one we invested in initially in 1994, were valued at $83,095,644, or 60.9 percent of our net assets, including net unrealized depreciation of $900,748. At March 31, 2008, we had 31 active tiny technology companies in our portfolio, and from first dollar in, the average and median holding periods for these 31 venture capital investments were 3.16 years and 2.87 years, respectively.

Tiny Technology Companies in Our Active Portfolio as of 3-31-08	**Holding Period (yrs)**
Adesto Technologies Corporation	1.11
Ancora Pharmaceuticals Inc.	0.91
BioVex Group, Inc.	0.51
BridgeLux, Inc. (formerly eLite Optoelectronics, Inc.)	2.87
Cambrios, Inc.	3.39
CFX Battery, Inc. (formerly Lifco, Inc.)	0.78
Crystal IS, Inc.	3.53
CSwitch Corporation	3.85
D-Wave Systems, Inc.	1.95
Ensemble Discovery Corporation	0.82
Innovalight, Inc.	1.95
Kereos, Inc.	2.87
Kovio, Inc.	2.39
Mersana Therapeutics, Inc. (formerly Nanopharma Corporation)	6.13
Metabolon, Inc.	2.22
Molecular Imprints, Inc.	4.01
NanoGram Corporation	4.92
Nanomix, Inc.	3.28
Nanosys, Inc.	4.99
Nantero, Inc.	6.65
NeoPhotonics Corporation 2004	4.32
Nextreme Thermal Solutions, Inc.	3.32
Phoenix Molecular, Inc.	0.46
Polatis, Inc. (formerly Continuum Photonics, Inc.)	5.77
PolyRemedy, Inc.	0.14
Questech Corporation (formerly Intaglio, Ltd.)	13.86
Siluria Technologies, Inc.	0.45
SiOnyx, Inc.	1.89
Solazyme, Inc.	3.35
Starfire Systems, Inc.	3.90
Xradia, Inc.	1.25
Average	**3.16**

Median	**2.87**

Tiny Technology

Tiny technology refers to nanotechnology, microsystems and MEMS, a variety of enabling technologies with critical dimensions below 100 micrometers. In our view, tiny technology is neither an industry nor a single technology. Tiny technology manifests itself in tools, materials, systems and devices that address broad markets, including instrumentation, alternative energy, electronics, photonics, computing, medical devices, pharmaceutical manufacturing, drug delivery and drug discovery. The development and commercialization of tiny technology often require the integration of multiple disciplines, including biology, physics, chemistry, materials science, computer science and the engineering sciences.

Examples of tiny technology-enabled products currently on the market are quite diverse. They include sensors, accelerometers used in automobiles to sense impact and deploy airbags, cosmetics with ingredients that block ultraviolet light but are invisible to the human eye, nanoclays used for strength in the running boards of minivans, textiles with liquid-stain repellant surfaces, fast-acting painkillers and pharmaceutical therapeutics.

The following is a summary of the products currently released or under development by our active portfolio companies:

Tiny Technology Companies in Our Portfolio as of 3-31-08	Products Released / Available for Purchase	Products in Development
Adesto Technologies Corporation		Semiconductor products
Ancora Pharmaceuticals Inc.	Custom carbohydrate synthesis projects	Synthetic carbohydrates for Pharmaceutical markets
BioVex Group, Inc.		Novel biologics for treatment of cancer and infectious disease
BridgeLux, Inc. (formerly eLite Optoelectronics, Inc.)	High brightness LEDs	Additional colors and types of HB-LEDs
Cambrios, Inc.		Transparent conductors
Crystal IS, Inc.	Aluminum Nitride Substrates	High-performance UV Devices
CFX Battery, Inc. (formerly Lifco, Inc.)		Primary and rechargeable batteries
CSwitch Corporation		High-bandwidth configurable switches
D-Wave Systems, Inc.		High-speed analog / quantum computing
Ensemble Discovery Corporation		DNA Programmed chemistry for discovery of new therapeutics
Innovalight, Inc.		Thin-film photovaltics modules
Kereos, Inc.		Emulsion-based targeted therapeutics and molecular imaging agents
Kovio, Inc.		Semiconductor products using printed electronics
Mersana Therapeutics, Inc. (formerly Nanopharma Corporation)		Oncology-focused therapeutic products
Metabolon, Inc.	Metabolomics profiling services, Mselect and MProve Clinical	Biomarker discovery and diagnostic tools
Molecular Imprints, Inc.	Tools for nanoimprint lithography	Production scale tools for nanoimprint lithography
NanoGram Corporation	Tools and service business for discovery and production of nanoparticles	Application specific nanoparticles

Nanomix, Inc.	Carbon-nanotube based hydrogen sensors.	Carbon-nanotube based sensors
Nanosys, Inc.	Nanotechnology-enabled products for optical and life science applications	Flexible electronic devices, non-volatile memory, consumables for life sciences and fuel cells
Nantero, Inc.		Carbon-nanotube based non-volatile memory
NeoPhotonics Corporation	Active and passive optical components for optical networking	Additional products for optical networking

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Tiny Technology Companies in Our Portfolio as of 3-31-08	Products Released / Available for Purchase	Products in Development
Nextreme Thermal Solutions, Inc.	Embedded thermoelectric cooler (eTEC) and UPF Optocooler and cooling LEDs and laser diodes	Thermoelectric devices for thermal management of integrated circuits and for power generation
Phoenix Molecular, Inc.		Products for the separation of chiral molecules
Polatis, Inc. (formerly Continuum Photonics, Inc.)	Microelectromechanical-enabled optical switches	Additional optical switching products
PolyRemedy, Inc.		Robotic manufacturing platform for wound treatment patches
Questech Corporation (formerly Intaglio, Ltd.)	Decorative tiles made of stone and microscale-metal materials	
Siluria Technologies, Inc.		Nanomaterial-enabled products for a diverse set of markets
SiOnyx, Inc.		Optical detectors for detection and imaging of visible and infrared light
Solazyme, Inc.	Algae-produced oil for biodiesel	Algae-produced products including nutraceuticals, industrial chemicals and energy
Starfire Systems, Inc.	Ceramic brake rotors and pads and silicon-carbide polymers	Ceramic-based parts for applications in electronics, aerospace and automotive industries
Xradia, Inc.	3-D x-ray transmission and x-ray fluorescence microscopes and optics	Additional x-ray imaging tools

Within tiny technology, nanotechnology refers to devices and processes with critical dimensions below 0.1 micron, equal to 100 nanometers. A nanometer is 0.000000001 meter, or one billionth of a meter. It is at the scale below 100 nanometers, the nanoscale, that quantum effects begin to dominate classical macroscale physics. At the nanoscale, size- and shape-dependent properties of materials allow previously unattainable material and device performance. Microsystems and MEMS both refer to materials, devices and processes that are on a micrometer size scale. A micrometer, which is also referred to as a micron, is 0.000001 meter, or one millionth of a meter. In practice, any device, or device enabled by components, in a size range from 100 microns down to 0.1 micron may be considered "micro."

Nanotechnology

There are various definitions of nanotechnology. Regardless of the definition used, the technology being defined qualifies as tiny technology. A commonly used measure of nanotechnology includes all materials, devices and processes with critical dimensions below 100 nanometers. Nanotechnology is defined by the U.S. Government's National Nanotechnology Initiative as research and technology development at the atomic, molecular or macromolecular levels, in the length scale of approximately 1 - 100 nanometer range, to provide a fundamental understanding of phenomena and materials at the nanoscale and to create and use structures, devices and systems that have novel properties and functions because of their small and/or intermediate size.

The nanoscale is the scale at which quantum effects begin to dominate classical macroscale physics. At the nanoscale, size- and shape-dependent properties of materials allow heretofore unattainable material and device performance. Nanotechnology science and its implications are currently the subject of intense research and development efforts in governmental, academic and corporate sectors, in the United States and in other countries.

Government research funding and patenting activity, prerequisites to successful commercialization of nanotechnology, have been growing rapidly in recent years. Currently, researchers in the field are collaborating with entrepreneurs and venture capitalists to form companies around nanotechnology platforms. The first generation of nanotechnology products consists of instrumentation that permits visualization and manipulation of matter at the nanoscale, as well as passive nanostructures such as coatings, nanoparticles and polymers. Examples of commercial instrumentation include nanoimprint lithography equipment, new variations of the atomic force microscope and highly sensitive gene and protein detecting arrays. Examples of commercial nanostructures include cosmetics with ingredients that block ultraviolet light but that are invisible to the human eye, nanoclays used for strength in the running boards of minivans, textiles with liquid-stain repellant surfaces and fast-acting painkillers.

We believe that the next generation of nanotechnology products will likely consist of active nanostructures, including transistors, targeted drugs and chemicals, actuators and adaptive structures. Examples of products being developed include semiconductor nanowires that act as tiny transistors; functionalized, drug-delivering polymers that allow the release of therapeutics to be controlled by temperature, pH or a magnetic field at specified locations within the body; and engineered membrane structures for filtration.

We project that longer-term product opportunities may include integrated nanosystems involving heterogeneous nanocomponents and various assembling techniques. Patent applications explaining the science of these discoveries have recently been filed, and the first commercial entities formed to develop these technologies are emerging from universities, federal government labs and industrial research centers. Future product opportunities may include exponentially denser and faster electronic devices, with individual molecules acting as transistors; tissues and organs engineered from self-assembling polymers that form biomimetic structures; and new forms of computing developed by exploiting the superposition of quantum particles.

Microsystems

Microsystems are similar to MEMS, but without mechanical parts. Microsystems are microscale machines that sense information from the environment and provide a response to it. A microsystem often integrates mechanical, fluidic, optical and pneumatic components into a single system.

Examples of two established microsystem technologies include microarrays and lab-on-a-chip. Microarrays can identify thousands of genes simultaneously and usually perform one type of analysis multiple times. Lab-on-a-chip is a small chip containing microfluidic channels that quickly separate liquids and gases in order to permit microsensors to analyze the properties of the liquids and gases. The following are additional fields in which microsystems are currently being used:

- Military/Aerospace — telemetry, communications, guidance systems, control circuitry and avionics.
- Geophysical Exploration — seismic data acquisition and geophysical measurement equipment.
- Medical Instrumentation — instrument motor controls and diagnostic devices.
- Satellite Systems — power monitoring and control circuits.
- Industrial Electronic Systems — measurement and diagnostics on rotating machinery.
- Opto-Electronics — sub-miniature temperature controls and laser diode drivers for data transmission.

MEMS

MEMS often refers to three-dimensional devices with features between one and 100 microns that integrate electrical and mechanical structures. MEMS devices often contain a combination of sensors, actuators, mechanical structures and electronics that detect or respond to thermal, biological, chemical or optical information. To date, most commercial MEMS devices are batch fabricated out of silicon, using techniques based on standard semiconductor processes. Examples of devices incorporating MEMS technology include airbag release systems, smart pens for digital signatures, the Sony AIBO™ entertainment robot and Texas Instruments' Digital Light Processing Cinema™ system.

Although the practical application of tiny technology requires great expertise to implement in manufacturing processes, we believe that tiny technology's broad applicability potentially presents significant and diverse market opportunities. Our strategy is to invest in what we believe to be the best of these tiny technology companies in which we have the opportunity to invest, with emphasis on nanotechnology companies, assuming that we regard the terms of the investment to be acceptable.

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GENERAL DESCRIPTION OF OUR PORTFOLIO COMPANIES

The following are brief descriptions of each portfolio company in which we were invested as of March 31, 2008. The portfolio companies are presented in three categories: companies where we directly or indirectly own more than 25 percent of the outstanding voting securities of the portfolio company; companies where we directly or indirectly own five percent to 25 percent of the outstanding voting securities of the portfolio company or where we hold one or more seats on the portfolio company's Board of Directors and, therefore, are deemed to be an affiliated person under the 1940 Act; and companies where we directly or indirectly own less than five percent of the outstanding voting securities of the portfolio company and where we have no other affiliations. The value described below for each portfolio company is its fair value as determined by the Valuation Committee of our Board of Directors. Each portfolio company that we believe is not significantly involved in tiny technology is designated by an asterisk (*).

Controlled Affiliated Companies:

Evolved Nanomaterial Sciences, Inc. (ENS), was located at 675 Massachusetts Avenue, Cambridge, Massachusetts 02139, and was developing a number of nanotechnology-enabled approaches for the resolution of chiral molecules. As of March 31, 2008, we held 5,870,021 shares of Series A Convertible Preferred Stock (representing 52.10 percent of the total shares of Series A Convertible Preferred Stock Outstanding) of ENS. On September 30, 2007, ENS filed for Chapter 7 bankruptcy. As of the date above, our Valuation Committee valued the Series A Convertible Preferred Stock held by us at $0.

Phoenix Molecular, Inc., located at 111 West 57th Street, New York, New York 10019, is developing a number of nanotechnology-enabled approaches for the resolution of chiral molecules. As of March 31, 2008, we held 1,000 shares of Common Stock (representing 100 percent of the total shares of Common Stock outstanding) of Phoenix Molecular and $75,000 in Convertible Bridge Notes (representing 100 percent of the total Convertible Bridge Notes outstanding). As of the date above, our Valuation Committee valued the total amount of securities of Phoenix Molecular held by us at $77,011. Daniel B. Wolfe and Douglas W. Jamison serve as Directors of the company.

SiOnyx, Inc., located at 100 Cummings Center, Beverly, Massachusetts 01915, is developing silicon-based optoelectronic products enabled by its proprietary material, "Black Silicon." As of March 31, 2008, we held 233,499 shares of Series A Convertible Preferred Stock (representing 100 percent of the total shares of Series A Convertible Preferred Stock outstanding), 2,966,667 shares of Series A-1 Convertible Preferred Stock (representing 42.38 percent of the total shares of Series A-1 Convertible Preferred Stock outstanding), and 4,207,537 shares of Series A-2 Convertible Preferred Stock (representing 22.23 percent of the total shares of Series A-2 Convertible Preferred Stock) of SiOnyx. As of the date above, our Valuation Committee valued the total amount of shares of SiOnyx held by us at $4,304,616. The Chief Executive Officer of the company is Stephen D. Saylor. Charles E. Harris serves as a Director of the company, and Daniel B. Wolfe serves as an observer to the Board of Directors of the company.

Non-Controlled Affiliated Companies:

Adesto Technologies Corporation, located at 1225 Innsbruck Drive, Sunnyvale, California 94089, is a "fables" company that develops semiconductor products. As of March 31, 2008, we held 6,547,619 shares of Series A Convertible Preferred Stock (representing 18.72 percent of the total shares of Series A Convertible Preferred Stock outstanding) of Adesto. As of the above date, our Valuation Committee valued the total amount of shares of Adesto held by us at $2,200,000. The Chief Executive Officer of the company is Narbeh Derhacobian. Michael A. Janse serves as a Director of the company.

Ancora Pharmaceuticals Inc., located at 200 Boston Avenue, Medford, Massachusetts 02155, is developing unique carbohydrate-based therapeutics including immunomodulatory drugs such as vaccines. Ancora also works with pharmaceutical and industrial partners to provide customized carbohydrate material. As of March 31, 2008, we held

909,091 shares of Series B Convertible Preferred Stock (representing 71.23 percent of the total shares of Series B Convertible Preferred Stock outstanding) of Ancora, as well as warrants to purchase 754,717 shares of Series B Convertible Preferred Stock of the company at $1.06 per share. As of the above date, our Valuation Committee valued the total amount of securities of Ancora held by us at $647,364. The Chief Executive Officer of the company is John Pena. Douglas W. Jamison serves as a Director of the company. Misti Ushio serves as an observer to the Board of Directors of the company.

BridgeLux, Inc., located at 1170 Sonora Court, Sunnyvale, California 94086, is developing high-power indium gallium nitride light emitting diodes that are used in various solid state lighting, mobile appliance, signage, and automotive applications. BridgeLux aims to use its proprietary designs and processes to manufacture high-power light emitting diodes in order to decrease the cost of production and increase adoption of solid-state lighting solutions in residential and commercial applications. The company's main competition include companies that manufacture and sell light emitting diodes such as Cree, Inc., Philips Lumileds Lighting Company, and Nichia Corporation. The company is highly dependent on its intellectual property position and its ability to protect this position. Revenue generated by the company may be affected positively or negatively by government regulations that favor one form of lighting solution over another. As of March 31, 2008, we held 1,861,504 shares of Series B Convertible Preferred Stock (representing 11.70 percent of the total shares of Series B Convertible Preferred Stock outstanding),2,130,699 shares of Series C Convertible Preferred Stock (representing 6.61 percent of the total shares of Series C Convertible Preferred Stock outstanding) and 666,667 shares of Series D Convertible Preferred Stock (representing 3.33 percent of the total shares of Series D Convertible Preferred Stock outstanding) of BridgeLux , as well as warrants to purchase 163,900 shares of Series C Convertible Preferred Stock of the company at $0.7136 per share. As of the above date, our Valuation Committee valued of the total amount of securities of BridgeLux held by us at $7,218,652. The Chief Executive Officer of the company is Mark Swoboda. Michael A. Janse serves as an observer to the Board of Directors of the company.

Cambrios Technology Corporation, located at 2450 Bayshore Parkway, Mountain View, California 94043, is developing methods of synthesizing nanomaterials and assembling them into useful structures for use in applications in electronics, solar energy and solid-state lighting. As of March 31, 2008, we held 1,294,025 shares of Series B Convertible Preferred Stock (representing 10.78 percent of the total shares of Series B Convertible Preferred Stock outstanding) and 1,300,000 shares of Series C Convertible Preferred Stock (representing 6.66 percent of the total shares of Series C Convertible Preferred Stock outstanding) of Cambrios. As of the above date, our Valuation Committee valued the total amount of shares of Cambrios held by us at $2,594,025. The Chief Executive Officer of the company is Michael R. Knapp. Michael A. Janse serves as an observer to the Board of Directors of the company.

CFX Battery, Inc., located at 3943 Veselich Avenue, Los Angles, California 90039, is developing primary and rechargeable batteries enabled by nanotechnology. As of March 31, 2008, we held 1,208,262 shares of Series A Convertible Preferred Stock (representing 13.17 percent of the total shares of Series A Convertible Preferred Stock outstanding) of CFX Battery. As of the date above, our Valuation Committee valued the Series A Convertible Preferred Stock held by us at $946,528. The Chief Executive Officer of the company is Joe Fisher. On February 28, 2008, Lifco merged with CFX Battery, Inc. The surviving entity is CFX Battery, Inc. Alexei A. Andreev serves as an observer to the Board of Directors of the company.

Crystal IS, Inc., located at 70 Cohoes Avenue, Green Island, New York 12183, is developing methods to produce large, single-crystal substrates of aluminum nitride (AlN) for use in the gallium nitride semiconductor industry. As of March 31, 2008, we held 391,571 shares of Series A Convertible Preferred Stock (representing 5.66 percent of the total shares of Series A Convertible Preferred Stock outstanding) and 1,300,376 shares of Series A-1 Convertible Preferred Stock (representing 9.51 percent of the total shares of Series A-1 Convertible Preferred Stock outstanding) of Crystal IS, as well as warrants to purchase 21,977 shares of Series A-1 Convertible Preferred Stock of the company at $0.78 per share. As of the date above, our Valuation Committee valued the total amount of securities of Crystal IS held by us at $1,333,255. The Chief Executive Officer of the company is Nicholas J. Wood. Michael A. Janse serves as an observer to the Board of Directors of the company.

CSwitch Corporation, located at 3131 Jay Street, Santa Clara, California 95054, is developing the next generation of low-power, efficient, and highly-integrated system-on-a-chip (SOC) solutions for a wide range of communications-based platforms. As of March 31, 2008, we held 6,863,118 shares of Series A-1 Convertible Preferred Stock (representing 9.76 percent of the total shares of Series A-1 Convertible Preferred Stock outstanding) and $529,852 in Convertible Bridge Notes (representing 9.62 percent of the total Convertible Bridge Notes outstanding) of CSwitch. As of the date above, our Valuation Committee valued the total amount of securities of CSwitch held by us at $3,983,708. The Chief Executive Officer of the company is Doug Laird. Alexei A. Andreev serves as a Director of the company.

D-Wave Systems, Inc., located at 100-4401 Still Creek Drive, Burnaby, British Columbia, V5C 6G9, Canada, is developing high-performance quantum computing systems for commercial use in logistics, bioinformatics, life and physical sciences, quantitative finance and electronic design automation. As of March 31, 2008, we held 2,000,000 shares of Series B Convertible Preferred Stock (representing 13.55 percent of the total number of shares of Series B Convertible Preferred Stock outstanding) and 678,264 shares of Series C Convertible Preferred Stock (representing 4.42 percent of the total shares of Series C Convertible Preferred Stock outstanding) of D-Wave. As of the date above, our Valuation Committee valued the total amount of securities of D-Wave Systems held by us at $2,893,308. The Chief Executive Officer of the company is Herb Martin. Alexei A. Andreev serves as a Director of the company. D-Wave Systems, Inc. is not an eligible portfolio company under the 1940 Act, because it operates primarily outside the United States.

Ensemble Discovery Corporation, located at 99 Erie Street, Cambridge, Massachusetts 02139, is developing classes of drugs and bioassays based on its proprietary DNA-Programmed Chemistry™ (DPC™) platform. Using DPC, Ensemble has built a product platform that will support the development of novel classes of therapeutics and bioassays for research and diagnostics. As of March 31, 2008, we held 1,449,275 shares of Series B Convertible Preferred Stock (representing 13.33 percent of the total shares of Series B Convertible Preferred Stock outstanding) of Ensemble. As of the date above, our Valuation Committee valued the Series B Convertible Preferred Stock held by us at $2,000,000. The Chief Executive Officer of the company is Michael D. Taylor. Daniel B. Wolfe serves as an observer to the Board of Directors of the company.

Innovalight, Inc., located at 965 East Arques, Sunnyvale, California 94085, is developing renewable energy products based on silicon nanotechnology. Innovalight is focused on bringing ultra low-cost solar power modules to the marketplace. The company uses a proprietary silicon-ink process to print thin-film solar power modules. Leveraging the advantages of solvent-based processing, Innovalight aims to accelerate the promise of more affordable solar power solutions for residential and commercial applications. The market for solar-energy solutions is estimated to be $15 billion and expected to grow to $36 billion by 2010. Innovalight is a development company and has yet to generate significant revenues from the commercial sale of products. The company’s main competition in this market include companies such as First Solar, Inc., Evergreen Solar, Inc., Sunpower, Inc., and Canadian Solar, Inc., as these companies are also focused on the commercialization of solar power modules. The company is highly dependent on its intellectual property position and its ability to protect this position. Revenue generated by the company may be affected positively or negatively by government regulations that favor one form of energy generation over another. As of March 31, 2008, we held 16,666,666 shares of Series B Convertible Preferred Stock (representing 33.33 percent of the total shares of Series B Convertible Preferred Stock outstanding) and 5,810,577 shares of Series C Convertible Preferred Stock (representing 7.12 percent of the total shares of Series C Convertible Preferred Stock outstanding) of Innovalight. The Chief Executive Officer of the company is Conrad Burke. The Chief Technical Officer and Vice President of Engineering is Homer Antoniadis. The Chairman of the Board of Directors of the company is Alf Bjørseth. As of the date above, our Valuation Committee valued the total amount of shares held by us at $7,711,784. Michael A. Janse serves as a Director of the company.

Kereos, Inc., located at 4041 Forest Park Ave., Saint Louis, Missouri 63108, is developing molecular imaging agents and targeted therapeutics for the detection and treatment of cancer and cardiovascular disease based on proprietary ligand-targeted emulsion technologies. As of March 31, 2008, we held 545,456 shares of Series B Convertible Preferred Stock (representing 8.06 percent of the total shares of Series B Convertible Preferred Stock outstanding) of Kereos. As of the date above, our Valuation Committee valued the Series B Convertible Preferred Stock held by us at $120,850. The Chief Executive Officer of the company is Robert A. Beardsley. Daniel B. Wolfe serves as an observer to the Board of Directors of the company.

Kovio, Inc., located at 1145 Sonora Court, Sunnyvale, California 94086, is developing semiconductor products using thin film technologies, printed electronics and nanoparticle inks. As of March 31, 2008, we held 2,500,000 shares of

Series C Convertible Preferred Stock (representing 20.21 percent of the total shares of Series C Convertible Preferred Stock outstanding) and 800,000 shares of Series D Convertible Preferred Stock (representing 4.40 percent of the total shares of Series D Convertible Preferred Stock outstanding) of Kovio. As of the date above, our Valuation Committee valued the total amount of shares held by us at $4,125,000. The Chief Executive Officer of the company is Amir Mashkoori. Alexei A. Andreev serves as an observer to the Board of Directors of the company.

Mersana Therapeutics, Inc., located at 840 Memorial Drive, Cambridge, Massachusetts 02139, is a pharmaceutical company founded to develop advanced drug delivery systems based on proprietary molecular constructs and "biological stealth" materials. As of March 31, 2008, we held 68,451 shares of Series A Convertible Preferred Stock (representing 87.50 percent of the total shares of Series A Convertible Preferred Stock outstanding) and 866,500 shares of Series B Convertible Preferred Stock (representing 8.22 percent of the total shares of Series B Convertible Preferred Stock outstanding) of Mersana, as well as warrants to purchase 91,625 shares of Series B Convertible Preferred Stock of the company at a price of $2.00 per share. As of the date above, our Valuation Committee valued the total securities of Mersana held by us at $1,982,876. The Chief Executive Officer of the company is Julie A. Olson. Charles E. Harris serves as a Director of the company. Misti Ushio serves as an observer to the Board of Directors of the company.

Metabolon, Inc., located at 800 Capitola Drive, Durham, North Carolina 27713, is using a proprietary technology platform in metabolomics to map changes in metabolic pathways for the identification of biomarkers and the early diagnosis of disease states. As of March 31, 2008, we held 2,173,913 shares of Series B Convertible Preferred Stock (representing 31.25 percent of the total shares of Series B Preferred Stock outstanding) and 869,565 shares of Series B-1 Convertible Preferred Stock (representing 32.74 percent of the total shares of Series B-1 Convertible Preferred Stock outstanding) of Metablolon as well as warrants to purchase 434,783 shares of Series B-1 Convertible Preferred Stock of the company at a price of $1.15 per share. As of the date above, our Valuation Committee valued the total amount of securities of Metabolon held by us at $2,765,535. The Chief Executive Officer of the company is John Ryals. Douglas W. Jamison serves as an observer to the Board of Directors of the company.

NanoGram Corporation, located at 165 Topaz Street, Milpitas, California 95035, is using its proprietary laser-deposition technologies to deposit inorganic nanocrystals for energy-related applications such as photovoltaics, solid-state lighting and batteries. As of March 31, 2008 we held 63,210 shares of Series I Convertible Preferred Stock (representing 1.99 percent of the total shares of Series I Convertible Preferred Stock outstanding), 1,250,904 shares of Series II Convertible Preferred Stock (representing 12.47 percent of the total shares of Series II Convertible Preferred Stock outstanding) and 1,242,144 shares of Series III Convertible Preferred Stock (representing 6.74 percent of the total shares of Series III Convertible Preferred Stock outstanding) and 432,179 shares of Series IV Convertible Preferred Stock (representing 2.66 percent of the total shares of Series IV Convertible Preferred Stock outstanding) of NanoGram. As of the date above, our Valuation Committee valued the total amount of shares of NanoGram held by us at $5,887,222. The Chief Executive Officer of the company is Kieran F. Drain. Alexei A. Andreev serves as an observer to the Board of Directors of the company.

Nanomix, Inc., located at 5980 Horton Street, Emeryville, California 94608, is developing nanoelectronic sensors that integrate carbon nanotube electronics with silicon microstructures. As of March 31, 2008, we held 977,917 shares of Series C Convertible Preferred Stock (representing 18.12 percent of the total shares of Series C Convertible Preferred Stock outstanding) and 6,802,397 shares of Series D Convertible Preferred Stock (representing 6.49 percent of the total shares of Series D Convertible Preferred Stock outstanding) of Nanomix. As of the above date, our Valuation Committee valued the total amount of shares of Nanomix held by us at $1,010,468. The Chief Executive Officer of the company is Garrett Gruener. Michael A. Janse serves as a Director of the Company.

Nextreme Thermal Solutions, Inc., located at 3908 Patriot Drive, Durham, North Carolina, 27703, is developing next-generation thermoelectrics based on its unique, thin-film technology for applications that require high-performance solutions for thermal management solutions. As of March 31, 2008, we held 1,750,000 shares of Series A Convertible Preferred Stock (representing 16.82 percent of the total shares of Series A Convertible Preferred Stock outstanding) and $377,580 in Convertible Bridge Notes (representing 16.82 percent of the total Convertible Bridge Notes outstanding) of Nextreme. As of the above date, our Valuation Committee valued the total amount of securities of Nextreme held by us at $2,127,580. The Chief Executive Officer of the company is Jesko von Windheim. Douglas W. Jamison serves as a Director of the Company. Daniel B. Wolfe serves as an observer to the Board of Directors of the company.

Questech Corporation, located at 92 Park Street, Rutland, Vermont 05701, manufactures and sells tile and trim products, based on its proprietary technology, with revenue generated from stock products. We originally invested in Questech on May 26, 1994. We did not invest in Questech as a tiny technology company, but Questech's proprietary technology is dependent on micro-scale processes. Thus, Questech may be regarded as a tiny technology holding. As of March 31, 2008, we held 655,454 shares of Common Stock (representing 8.07 percent of the total shares of Common Stock outstanding) of Questech, as well as warrants to purchase 10,000 shares of Common Stock of the company at $1.50 per share. As of the date above, our Valuation Committee valued the total amount of securities of Questech held by us at $129,817. The Chief Executive Officer of the company is Barry J. Culkin.

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Siluria Technologies, Inc., located at 2750 Sand Hill Road, Menlo Park, California 94025, is developing next-generation nanomaterials. As of March 31, 2008, we held 482,218 shares of Series S-2 Convertible Preferred Stock (representing 10.72 percent of the total shares of Series S-2 Convertible Preferred Stock outstanding) of Siluria. As of the above date, our Valuation Committee valued the Series S-2 Convertible Preferred Stock of Siluria held by us at $160,723. The General Manager of the company is Alex Tkachenko. Michael A. Janse serves as an observer to the Board of Directors of the company.

Solazyme, Inc., located at 561 Eccles Avenues, South San Francisco, California 94080, is developing agal biodiesel, industrial chemicals and special ingredients based on synthetic biology. As of March 31, 2008, we held 988,204 shares of Series A Convertible Preferred Stock (representing 12.76 percent of the total shares of outstanding of Series A Convertible Preferred Stock), 495,246 shares of Series B Convertible Preferred Stock (representing 5.77 percent of the total shares of outstanding of Series B Convertible Preferred Stock) and $2,000,000 in Convertible Bridge Notes (representing 32.00 percent of the total Convertible Bridge Notes outstanding) of Solazyme. As of the date above, our Valuation Committee valued the total amount of securities of Solazyme held by us at $3,507,225. The Chief Executive Officer of the company is Jonathan S. Wolfson. Douglas W. Jamison serves as an observer to the Board of Directors of the company.

Xradia, Inc., located at 5052 Commercial Circle, Concord, California 94520, is developing and manufacturing a suite of high-resolution x-ray microscopes and fluorescence imaging systems for non-destructive imaging of embedded internal structures. As of March 31, 2008, we held 3,121,099 shares of Series D Convertible Preferred Stock (representing 57.14 percent of the total shares of Series D Convertible Preferred Stock Outstanding) of Xradia. As of the date above, our Valuation Committee fair valued the Series D Convertible Preferred Stock held by us at $4,000,000. The Chief Executive Officer of the company is Rod Browning. Alexei A. Andreev serves as a Director of the company.

Zia Laser, Inc., was located at 801 University Boulevard SE, Albuquerque, New Mexico 87106, and was developing quantum dot-based semiconductor laser technology for application in microprocessors. As of March 31, 2008, we held 1,500,000 shares of Series C Convertible Preferred Shares (representing 17.48 percent of the total shares of Series C Convertible Preferred Shares outstanding) of Zia Laser. On November 30, 2006, the assets of Zia Laser were acquired by Innolume, Inc. As of the above date, our Valuation Committee valued the Series C Convertible Preferred Shares of Zia Laser held by us at $21,330.

Unaffiliated Companies:

BioVex Group, Inc., located at 34 Commerce Way, Woburn, Massachusetts 01801, is developing biological treatments for cancer and the prevention of infectious disease. As of March 31, 2008, we held 2,799,552 shares of Series E Convertible Preferred Stock (representing 9.92 percent of the total shares of Series E Convertible Preferred Stock outstanding) of BioVex. As of the above date, our Valuation Committee valued the Series E Convertible Preferred Stock of BioVex held by us at $2,500,000. The Chief Executive Officer of the company is Philip Astley-Sparke. Misti Ushio serves as an observer to the Board of Directors of the company.

***Exponential Business Development Company**, located at 460 Oakridge Common, South Salem, New York 10590, is a venture capital partnership that invests in early stage manufacturing, software development and communication technology industries in the Albany area. As of March 31, 2008, we held one Limited Partnership Unit (representing 0.87 percent of the total Limited Partnership Units outstanding) of the company. As of the date above, our Valuation Committee valued the Limited Partnership Unit held by us at $2,219. The manager of the portfolio of the company is NewTek Capital, Inc.

Molecular Imprints, Inc., located at 1807 West Braker Lane, Austin, Texas 78758, is developing lithography systems and technology for manufacturing applications in the areas of nanodevices, microstructures, advanced packaging, bio devices, optical components and semiconductor devices. As of March 31, 2008, we held 1,333,333 shares of Series B Convertible Preferred Stock (representing 6.55 percent of the total shares of Series B Preferred Stock outstanding) and 1,250,000 shares of Series C Convertible Preferred Stock (representing 14.75 percent of the total shares of Series C Convertible Preferred Stock outstanding) of Molecular Imprints, as well as warrants to purchase 125,000 shares of Series C Convertible Preferred Stock of the company at a price of $2.00 per share. As of the date above, our Valuation Committee valued the total amount of securities of Molecular Imprints held by us at $4,500,000. The Chief Executive Officer of the company is Mark Melliar-Smith. Alexei A. Andreev serves as an observer to the Board of Directors of the company.

Nanosys, Inc., located at 2625 Hanover Street, Palo Alto, California 94304, is a company with broad-based intellectual property that is initially commercializing applications in macroelectronics, memory, and fuel cells. These applications incorporate zero and one-dimensional, nanometer-scale materials, such as nanowires and nanodots (quantum dots), as their principal active elements. As of March 31, 2008, we held 803,428 shares of Series C Convertible Preferred Stock (representing 4.00 percent of the total shares of Series C Convertible Preferred Stock outstanding) and 1,016,950 shares of Series D Convertible Preferred Stock (representing 6.28 percent of the total shares of Series D Preferred Stock outstanding) of Nanosys. As of the date above, our Valuation Committee valued the total amount of shares of Nanosys held by us at $5,370,116. The Chief Executive Officer of the company is Steven Goldby.

Nantero, Inc., located at 25-E Olympia Avenue, Woburn, Massachusetts 01801, is developing non-volatile random access memory based on carbon nanotubes. As of March 31, 2008, we held 345,070 shares of Series A Convertible Preferred Stock (representing 8.17 percent of the total shares of Series A Preferred Stock outstanding), 207,051 shares of Series B Convertible Preferred Stock (representing 3.08 percent of the total shares of Series B Convertible Preferred Stock outstanding) and 188,315 shares of Series C Convertible Preferred Stock (representing 3.75 percent of the total shares of Series C Convertible Preferred Stock outstanding) of Nantero. As of the date above, our Valuation Committee valued the total amount of shares of Nantero held by us at $2,246,409. The Chief Executive Officer of the company is Greg Schmergel.

NeoPhotonics Corporation, located at 2911 Zanker Road, San Jose, California 95134, is developing functional optical component arrays to offer integrated optical "systems on a chip" to component vendors. As of March 31, 2008, we held 716,195 shares of Common Stock (representing 1.50 percent of the total shares of Common Stock outstanding), 1,831,256 shares of Series 1 Convertible Preferred Stock (representing 4.05 percent of the total Series 1 Convertible Preferred Stock), 741,898 shares of Series 2 Convertible Preferred Stock (representing 3.46 percent of the total shares of Series 2 Convertible Preferred Stock outstanding) and 2,750,000 shares of Series 3 Convertible Preferred Stock (representing 2.76 percent of the total shares of Series 3 Convertible Preferred Stock outstanding) of NeoPhotonics, as well as warrants to purchase 30,427 shares of Common Stock of the company at $0.15 per share. As of the date above, our Valuation Committee valued the total amount of securities of NeoPhotonics held by us at $5,459,216. The Chief Executive Officer of the company is Timothy S. Jenks. Alexei A. Andreev serves as an observer to the Board of Directors of the company.

Polatis, Inc., located at 5 Fortune Drive, Billerica, Massachusetts 01821, is developing a family of MEMS switches for optical network applications, based on Polatis's proprietary piezoelectric ceramic substrates. As of March 31, 2008, we held 16,775 shares of the Series A-1 Convertible Preferred Stock (representing 6.17 percent of the total shares of Series A-1 Convertible Preferred Stock outstanding), 71,611 shares of Series A-2 Convertible Preferred Stock (representing 4.65 percent of the total Series A-2 Convertible Preferred Stock outstanding), 4,774 shares of Series A-4 Convertible Preferred Stock (representing 4.65 percent of the total shares of Series A-4 Convertible Preferred Stock outstanding) and 16,438 shares of Series A-5 Convertible Preferred Stock (representing 1.79 percent of the total shares of Series A-5 Convertible Preferred Stock outstanding) of Polatis. As of the date above, our Valuation Committee valued the total amount of shares of Polatis held by us at $276,526. The Chief Executive Officer of the company is David Lewis. Lori D. Pressman serves as an observer to the Board of Directors of the company.

PolyRemedy, Inc., located at 2637 Marine Way, Suite 100, Mountain View, California 94043, is developing a robotic manufacturing platform for wound treatment patches. As of March 31, 2008, we held 287,647 shares of Series B-1 Convertible Preferred Stock (representing 1.52 percent of the total shares of the Series B-1 Convertible Preferred Stock outstanding) of PolyRemedy. As of the date above, our Valuation Committee valued the total amount of shares of PolyRemedy held by us at $244,500. The Chief Executive Officer of the company is Daniel A. Eckert. Alexei A. Andreev serves as an observer to the Board of Directors of the company.

Starfire Systems, Inc., located at 10 Hermes Road, Malta, New York 12020, offers a family of patented silicon carbide forming polymers for the manufacture of advanced ceramic materials applications. As of March 31, 2008, we held 375,000 shares of Common Stock (representing 4.59 percent of the total shares of Common Stock outstanding) and 600,000 shares of Series A-1 Convertible Preferred Stock (representing 12.87 percent of the total shares of Series A-1 Convertible Preferred Stock outstanding) of Starfire. As of the above date, our Valuation Committee valued the total amount of shares of Starfire held by us at $750,000. The Chief Executive Officer of the company is Richard M. Saburro. Douglas W. Jamison serves as an observer to the Board of Directors of the company.

Although Ancora, BridgeLux, Crystal IS, Metabolon, Molecular Imprints, NanoGram, Nanomix, Nanosys, NeoPhotonics, Nextreme, Polatis, Questech, Solazyme, Starfire Systems and Xradia are all generating revenues ranging from nominal to significant from commercial sales of products and/or services, they are all still relatively early-stage companies with the attendant risks. Additionally, with the exceptions of BridgeLux, Exponential, Molecular Imprints, NeoPhotonics, Questech and Xradia we consider all of the foregoing portfolio companies to be development-stage companies. This term is used to describe a company that devotes substantially all of its efforts to establishing a new business, and either has not yet commenced its planned principal operations, or it has commenced such operations but has not realized significant revenue from them. Any of the private companies may require additional funding that may not be obtainable at all or on the terms of their most recent fundings, which would result in partial or complete write-downs in the value of our investment. In general, private equity is difficult to obtain, especially in the current capital markets environment. Each company is dependent upon a single or small number of customers and/or key operating personnel. All of the foregoing companies rely heavily upon the technology associated with their respective business or, in the case of Exponential, with the companies in which it invests. Therefore, each company places great importance on its relevant patents, trademarks, licenses, algorithms, trade secrets, franchises or concessions. Lastly, each company is particularly vulnerable to general economic, private equity and capital markets conditions and to changes in government regulation, interest rates or technology.

As a participant in the venture capital business, we invest primarily in private companies for which there is generally no publicly available information. Because of the private nature of these businesses, there is a need to maintain the confidentiality of the financial and other information that we have for the private companies in our portfolio. We believe that maintaining this confidence is important, as disclosure of such information could disadvantage our portfolio companies and could put us at a disadvantage in attracting new investments. Therefore, we do not intend to disclose financial or other information about our portfolio companies, unless required, because we believe doing so may put them at an economic or competitive disadvantage, regardless of our level of ownership or control.

DETERMINATION OF NET ASSET VALUE

Our investments can be classified into five broad categories for valuation purposes:

- Equity-related securities;
- Investments in intellectual property, patents, research and development in technology or product development;
- Long-term fixed-income securities;
- Short-term fixed-income securities; and
- All other securities.

The 1940 Act requires periodic valuation of each investment in our portfolio to determine net asset value. Under the 1940 Act, unrestricted securities with readily available market quotations are to be valued at the current market value; all other assets must be valued at “fair value” as determined in good faith by or under the direction of the Board of Directors.

Our Board of Directors is responsible for (1) determining overall valuation guidelines and (2) ensuring the valuation of investments within the prescribed guidelines.

Our Valuation Committee, comprised of all of the independent Board members, is responsible for reviewing and approving the valuation of our assets within the guidelines established by the Board of Directors.

The values assigned to these investments are based on available information and do not necessarily represent amounts that might ultimately be realized, as such amounts depend on future circumstances and cannot reasonably be determined until the individual investments are actually liquidated or become readily marketable.

Approaches to Determining Fair Value

Statement of Financial Accounting Standards No. 157, "Fair Value Measurements," ("SFAS No. 157") defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price).

The main approaches to measuring fair value utilized are the market approach and the income approach.

- Market Approach: The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities. For example, the market approach often uses market multiples derived from a set of comparables. Multiples might lie in ranges with a different multiple for each comparable. The selection of where within the range each appropriate multiple falls requires judgment considering factors specific to the measurement (qualitative and quantitative).

- Income Approach: The income approach uses valuation techniques to convert future amounts (for example, cash flows or earnings) to a single present value amount (discounted). The measurement is based on the value indicated by current market expectations about those future amounts. Those valuation techniques include present value techniques; option-pricing models, such as the Black-Scholes-Merton formula (a closed-form model) and a binomial model (a lattice model), which incorporate present value techniques; and the multi-period excess earnings method, which is used to measure the fair value of certain assets.

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

- Level 1: Unadjusted quoted prices in active markets for identical assets or liabilities.

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

- Level 3: Unobservable inputs for the asset or liability.

Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

The Company applies the methods for determining fair value discussed above to the valuation of investments in each of the five broad categories as follows:

Equity-Related Securities

Equity-related securities, including warrants, are fair valued using the market or income approaches. The following factors may be considered when the market approach is used to fair value these types of securities: readily available public market quotations; the cost of the Company’s investment; transactions in a company's securities or unconditional firm offers by responsible parties as a factor in determining valuation; the financial condition and operating results of the company; the long-term potential of the business and technology of the company; the values of similar securities issued by companies in similar businesses; multiples to revenue, net income or EBITDA that similar securities issued by companies in similar businesses receive; the proportion of the company's securities we own and the nature of any rights to require the company to register restricted securities under applicable securities laws; and the rights and preferences of the class of securities we own as compared to other classes of securities the portfolio company has issued. When the income approach is used to value warrants, the Company uses the Black-Scholes-Merton formula.

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Investments in Intellectual Property, Patents, Research and Development in Technology or Product Development

These investments are fair valued using the market approach. The Company may consider factors specific to these types of investments when using the market approach including: the cost of the Company's investment; investments in the same or substantially similar intellectual property or patents or research and development in technology or product development or offers by responsible third parties; the results of research and development; product development progress; commercial prospects; term of patent projected markets; and other subjective factors.

As of March 31, 2008, we did not have any investments in intellectual property, patents, research and development in technology or product development.

Long-Term Fixed-Income Securities

Long-term fixed-income securities for which market quotations are readily available are valued using the most recent bid quotations when available.

Long-term fixed-income securities for which market quotations are not readily available are fair valued using the market approach. The factors that may be considered when valuing these types of securities by the market approach include: credit quality; interest rate analysis; quotations from broker-dealers; prices from independent pricing services that the Board believes are reasonably reliable; and reasonable price discovery procedures and data from other sources.

Short-Term Fixed-Income Securities

Short-Term fixed-income securities are valued using the market approach in the same manner as long-term fixed-income securities until the remaining maturity is 60 days or less, after which time such securities may be valued at amortized cost if there is no concern over payment at maturity.

All Other Securities

All other securities are reported at fair value as determined in good faith by the Valuation Committee using the approaches for determining valuation as described above. As of March 31, 2008, we did not have any of these investments.

For all other securities, the reported values shall reflect the Valuation Committee's judgment of fair values as of the valuation date using the outlined basic approaches of valuation discussed above. They do not necessarily represent an amount of money that would be realized if we had to sell such assets in an immediate liquidation. Thus, valuations as of any particular date are not necessarily indicative of amounts that we may ultimately realize as a result of future sales or other dispositions of investments we hold.

Determinations of Net Asset Value in Connection with Offerings

In connection with each offering of our Common Stock, our Board of Directors or a committee thereof is required to make the determination that we are not selling our Common Stock at a price below the then current net asset value of our Common Stock at the time at which the sale is made. Our Board of Directors considers the following factors, among others, in making such determination:

- the net asset value of our Common Stock disclosed in the most recent periodic report we filed with the SEC;

- our Management's assessment of whether any material change in the net asset value of our Common Stock has occurred (including through the realization of gains on the sale of our portfolio securities) from the period beginning on the date of the most recently disclosed net asset value of our Common Stock to the period ending two days prior to the date of the sale of our Common Stock; and
- the magnitude of the difference between the net asset value of our Common Stock disclosed in the most recent periodic report we filed with the SEC and our Management's assessment of any material change in the net asset value of our Common Stock since the date of the most recently disclosed net asset value of our Common Stock, and the offering price of our Common Stock in the proposed offering.

Moreover, to the extent that there is even a remote possibility that we may (i) issue our Common Stock at a price below the then current net asset value of our Common Stock at the time at which the sale is made or (ii) trigger the undertaking (which we provided to the SEC in our registration statements) to suspend the offering of our Common stock if the net asset value of our Common Stock fluctuates by certain amounts in certain circumstances until the prospectus is amended, the Board of Directors will elect, in the case of clause (i) above, either to postpone the offering until such time that there is no longer the possibility of the occurrence of such event or to undertake to determine the net asset value of our Common Stock within two days prior to any such sale to ensure that such sale will not be below our then current net asset value, and, in the case of clause (ii) above, to comply with such undertaking or to undertake to determine the net asset value of our Common Stock to ensure that such undertaking has not been triggered.

INVESTMENT POLICIES

Investments and Strategies

The following is a summary description of the types of assets in which we may invest, the investment strategies we may utilize and the attendant risks associated with our investments and strategies. For a full description of our investments and strategies, please refer to our Annual Report on Form 10-K.

Equity, Equity-Related Securities and Debt with Equity Features

We may invest in equity, equity-related securities and debt with equity features. These securities include common stock, preferred stock, debt instruments convertible into common or preferred stock, limited partnership interests, other beneficial ownership interests and warrants, options or other rights to acquire any of the foregoing.

We may make investments in companies with operating histories that are unprofitable or marginally profitable, that have negative net worth or that are involved in bankruptcy or reorganization proceedings. These investments would involve businesses that management believes have turn around potential through the infusion of additional capital and management assistance. In addition, we may make investments in connection with the acquisition or divestiture of companies or divisions of companies. There is a significantly greater risk of loss with these types of securities than is the case with traditional investment securities.

We may also invest in publicly traded securities of whatever nature, including relatively small, emerging growth companies that management believes have long-term growth possibilities. Pursuant to a rule adopted by the SEC, our investments in U.S. non-financial public companies whose securities are not listed on a securities exchange will generally be treated as qualifying assets for purposes of maintaining our business development company status if we acquire such investments in private placements or secondary market transactions.

Warrants, options and convertible or exchangeable securities generally give the investor the right to acquire specified equity securities of an issuer at a specified price during a specified period or on a specified date. Warrants and options fluctuate in value in relation to the value of the underlying security and the remaining life of the warrant or option, while convertible or exchangeable securities fluctuate in value both in relation to the intrinsic value of the security without the conversion or exchange feature and in relation to the value of the conversion or exchange feature, which is like a warrant or option. When we invest in these securities, we incur the risk that the option feature will expire worthless, thereby either eliminating or diminishing the value of our investment.

Our investments in equity securities usually involve securities of private companies that are restricted as to sale and cannot be sold in the open market without registration under the Securities Act of 1933 or pursuant to a specific exemption from these registrations. Opportunities for sale are more limited than in the case of marketable securities, although these investments may be purchased at more advantageous prices and may offer attractive investment opportunities. Even if one of our portfolio companies completes an initial public offering, we are typically subject to a lock-up agreement, and the stock price may decline substantially before we are free to sell. Even if we have registration rights to make our investments more marketable, a considerable amount of time may elapse between a decision to sell or register the securities for sale and the time when we are able to sell the securities. The prices obtainable upon sale may be adversely affected by market conditions or negative conditions affecting the issuer during the intervening time.

Venture Capital Investments

We expect to invest in development stage or start-up businesses. Substantially all of our long-term investments are in thinly capitalized, unproven, small companies focused on risky technologies. These businesses also tend to lack management depth, to have limited or no history of operations and to have not attained profitability. Because of the speculative nature of these investments, these securities have a significantly greater risk of loss than traditional investment securities. Some of our venture capital investments are likely to be complete losses or unprofitable and some will never realize their potential.

We may own 100 percent of the securities of a start-up investment for a period of time and may control the company for a substantial period. Start-up companies are more vulnerable than better capitalized companies to adverse business or economic developments. Start-up businesses generally have limited product lines, service niches, markets and/or financial resources. Start-up companies are not well-known to the investing public and are subject to potential bankruptcy, general movements in markets and perceptions of potential growth.

In connection with our venture capital investments, we may participate in providing a variety of services to our portfolio companies, including the following:

- recruiting management;
- formulating operating strategies;
- formulating intellectual property strategies;
- assisting in financial planning;
- providing management in the initial start-up stages; and
- establishing corporate goals.

We may assist in raising additional capital for these companies from other potential investors and may subordinate our own investment to that of other investors. We may also find it necessary or appropriate to provide additional capital of our own. We may introduce these companies to potential joint venture partners, suppliers and customers. In addition, we may assist in establishing relationships with investment bankers and other professionals. We may also assist with mergers and acquisitions. We do not derive income from these companies for the performance of any of the above services.

We may control, be represented on or have observer rights on the Board of Directors of a portfolio company by one or more of our officers or directors, who may also serve as officers of the portfolio company. We indemnify our officers and directors for serving on the Boards of Directors or as officers of portfolio companies, which exposes us to additional risks. Particularly during the early stages of an investment, we may in effect be involved in the conduct of the operations of the portfolio company. As a venture company emerges from the developmental stage with greater management depth and experience, we expect that our role in the portfolio company’s operations will diminish. Our goal is to assist each company in establishing its own independent capitalization, management and Board of Directors. We expect to be able to reduce our interest in those start-up companies which become successful.

Debt Obligations

We may hold debt securities for income and as a reserve pending more speculative investments. Debt obligations may include U.S. government and agency securities, commercial paper, bankers’ acceptances, receivables or other asset-based financing, notes, bonds, debentures, or other debt obligations of any nature and repurchase agreements related to these securities. These obligations may have varying terms with respect to security or credit support, subordination, purchase price, interest payments and maturity from private, public or governmental issuers of any type located anywhere in the world. We may invest in debt obligations of companies with operating histories that are unprofitable or marginally profitable, that have negative net worth or are involved in bankruptcy or reorganization proceedings, or that are start-up or development stage entities. In addition, we may participate in the acquisition or divestiture of companies or divisions of companies through issuance or receipt of debt obligations. As of March 31, 2008, the debt obligations held in our portfolio consisted of convertible bridge notes and U.S. Treasury securities.

It is likely that our investments in debt obligations will be of varying quality, including non-rated, unsecured, highly speculative debt investments with limited marketability. Investments in lower-rated and non-rated securities, commonly referred to as "junk bonds," are subject to special risks, including a greater risk of loss of principal and non-payment of interest. Generally, lower-rated securities offer a higher return potential than higher-rated securities but involve greater volatility of price and greater risk of loss of income and principal, including the possibility of default or bankruptcy of the issuers of these securities. Lower-rated securities and comparable non-rated securities will likely have large uncertainties or major risk exposure to adverse conditions and are predominantly speculative with respect to the issuer's capacity to pay interest and repay principal in accordance with the terms of the obligation. The occurrence of adverse conditions and uncertainties to issuers of lower-rated securities would likely reduce the value of lower-rated securities held by us, with a commensurate effect on the value of our shares.

The markets in which lower-rated securities or comparable non-rated securities are traded generally are more limited than those in which higher-rated securities are traded. The existence of limited markets for these securities may restrict our ability to obtain accurate market quotations for the purposes of valuing lower-rated or non-rated securities and calculating net asset value or to sell securities at their fair value. Any economic downturn could adversely affect the ability of issuers' lower-rated securities to repay principal and pay interest thereon. The market values of lower-rated and non-rated securities also tend to be more sensitive to individual corporate developments and changes in economic conditions than higher-rated securities. In addition, lower-rated securities and comparable non-rated securities generally present a higher degree of credit risk. Issuers of lower-rated securities and comparable non-rated securities are often highly leveraged and may not have more traditional methods of financing available to them, so that their ability to service their debt obligations during an economic downturn or during sustained periods of rising interest rates may be impaired. The risk of loss owing to default by these issuers is significantly greater because lower-rated securities and comparable non-rated securities generally are unsecured and frequently are subordinated to the prior payment of senior indebtedness. We may incur additional expenses to the extent that we are required to seek recovery upon a default in the payment of principal or interest on our portfolio holdings.

The market value of investments in debt securities that carry no equity participation usually reflects yields generally available on securities of similar quality and type at the time purchased. When interest rates decline, the market value of a debt portfolio already invested at higher yields can be expected to rise if the securities are protected against early call. Similarly, when interest rates increase, the market value of a debt portfolio already invested at lower yields can be expected to decline. Deterioration in credit quality also generally causes a decline in market value of the security, while an improvement in credit quality generally leads to increased value.

Foreign Securities

We may make investments in securities of issuers whose principal operations are conducted outside the United States, and whose earnings and securities are stated in foreign currency. In order to maintain our status as a business development company, our investments in the stocks of companies organized outside the U.S. would be limited to 30 percent of our assets, because we must invest at least 70 percent of our assets in "qualifying assets" and securities of foreign companies are not "qualifying assets."

Compared to otherwise comparable investments in securities of U.S. issuers, currency exchange risk of securities of foreign issuers is a significant variable. The value of these investments to us will vary with the relation of the currency in which they are denominated to the U.S. dollar, as well as with intrinsic elements of value such as credit risk, interest rates and performance of the issuer. Investments in foreign securities also involve risks relating to economic and political developments, including nationalization, expropriation, currency exchange freezes and local recession. Securities of many foreign issuers are less liquid and more volatile than those of comparable U.S. issuers. Interest and dividend income and capital gains on our foreign securities may be subject to withholding and other taxes that may not be recoverable by us. We may seek to hedge all or part of the currency risk of our investments in foreign securities through the use of futures, options and forward currency purchases or sales.

Intellectual Property

We believe there is a role for organizations that can assist in technology transfer. Scientists and institutions that develop and patent intellectual property perceive the need for and rewards of entrepreneurial commercialization of their inventions.

Our form of investment may be:

- funding research and development in the development of a technology;
- obtaining licensing rights to intellectual property or patents;
- acquiring intellectual property or patents; or
- forming and funding companies or joint ventures to further commercialize intellectual property.

Income from our investments in intellectual property or its development may take the form of participation in licensing or royalty income, fee income, or some other form of remuneration. Investment in developmental intellectual property rights involves a high degree of risk that can result in the loss of our entire investment as well as additional risks including uncertainties as to the valuation of an investment and potential difficulty in liquidating an investment. Further, investments in intellectual property generally require investor patience as investment return may be realized only after or over a long period. At some point during the commercialization of a technology, our investment may be transformed into ownership of securities of a development stage or start-up company as discussed under "Venture Capital Investments" above.

Other Strategies

In pursuit of our investment strategy, we may employ one or more of the following strategies in order to enhance investment results.

Borrowing and Margin Transactions

We may from time to time borrow money or obtain credit by any lawful means from banks, lending institutions, other entities or individuals, in negotiated transactions. We may issue, publicly or privately, bonds, debentures or notes, in series or otherwise, with interest rates and other terms and provisions, including conversion rights, on a secured or unsecured basis, for any purpose, up to the maximum amounts and percentages permitted for closed-end investment companies under the 1940 Act. The 1940 Act currently prohibits us from borrowing any money or issuing any other senior securities (other than preferred stock and other than temporary borrowings of up to five percent of our assets), if in giving effect to the borrowing or issuance, the value of our total assets would be less than 200 percent of our total liabilities (other than liabilities not constituting senior securities). We may pledge assets to secure any borrowings. We currently have no leverage and have no current intention to issue preferred stock.

A primary purpose of our borrowing power is for leverage, to increase our ability to acquire investments both by acquiring larger positions and by acquiring more positions. Borrowings for leverage accentuate any increase or decrease in the market value of our investments and thus our net asset value. Since any decline in the net asset value of our investments will be borne first by holders of Common Stock, the effect of leverage in a declining market would be a greater decrease in net asset value applicable to the Common Stock than if we were not leveraged. Any decrease would likely be reflected in a decline in the market price of the Common Stock. To the extent the income derived from assets acquired with borrowed funds exceeds the interest and other expenses associated with borrowing, our total income will be greater than if borrowings were not used. Conversely, if the income from assets is not sufficient to cover the borrowing costs, our total income will be less than if borrowings were not used. If our current income is not sufficient to meet our borrowing costs (repayment of principal and interest), we might have to liquidate our investments when it may be disadvantageous to do so. Our borrowings for the purpose of buying most liquid equity securities will be subject to the margin rules, which require excess liquid collateral marked to market daily. If we are unable to post sufficient collateral, we would be required to sell securities to remain in compliance with the margin rules. These sales might be at disadvantageous times or prices.

Repurchase of Shares

Our shareholders do not have the right to compel us to redeem our shares. We may, however, purchase outstanding shares of our Common Stock from time to time, subject to approval of our Board of Directors and compliance with applicable corporate and securities laws. The Board of Directors may authorize purchases from time to time when they are deemed to be in the best interests of our shareholders, but could do so only after notification to shareholders. The Board of Directors may or may not decide to undertake any purchases of our Common Stock.

Our repurchases of our common shares would decrease our total assets and would therefore likely have the effect of increasing our expense ratio. Subject to our investment restrictions, we may borrow money to finance the repurchase of our Common Stock in the open market pursuant to any tender offer. Interest on any borrowings to finance share repurchase transactions will reduce our net assets. If, because of market fluctuations or other reasons, the value of our assets falls below the required 1940 Act coverage requirements, we may have to reduce our borrowed debt to the extent necessary to comply with the requirement. To achieve a reduction, it is possible that we may be required to sell portfolio securities at inopportune times when it may be disadvantageous to do so. Since 1998, we have repurchased a total of 1,828,740 shares of our Common Stock at a total cost of $3,405,531, or $1.86 per share. On July 23, 2002, because of our strategic decision to invest in tiny technology, our Board of Directors reaffirmed its commitment not to authorize the repurchase of additional shares of our Common Stock.

Portfolio Company Turnover

Changes with respect to portfolio companies will be made as our management considers necessary in seeking to achieve our investment objective. The rate of portfolio turnover will not be treated as a limiting or relevant factor when circumstances exist which are considered by management to make portfolio changes advisable.

Although we expect that many of our investments will be relatively long term in nature, we may make changes in our particular portfolio holdings whenever it is considered that an investment no longer has substantial growth potential or has reached its anticipated level of performance, or (especially when cash is not otherwise available) that another investment appears to have a relatively greater opportunity for capital appreciation. We may also make general portfolio changes to increase our cash to position us in a defensive posture. We may make portfolio changes without regard to the length of time we have held an investment, or whether a sale results in profit or loss, or whether a purchase results in the reacquisition of an investment which we may have only recently sold. Our investments in privately held companies are illiquid, which limits portfolio turnover.

The portfolio turnover rate may vary greatly from year to year as well as during a year and may also be affected by cash requirements.

MANAGEMENT OF THE COMPANY

BOARD OF DIRECTORS AND EXECUTIVE OFFICERS

Set forth below are the names, ages, positions and principal occupations during the past five years of our directors and executive officers. We have no advisory board. Our business address and that of our officers and directors is 111 West 57th Street, Suite 1100, New York, New York 10019.

Executive Officers

Messrs. Harris, Jamison, Wolfe, Andreev and Janse are Managing Directors and are primarily responsible for the day to day management of our portfolio. They have served in this capacity since 1984, 2002, 2008, 2005 and 2007, respectively.

Charles E. Harris. Mr. Harris, 65, currently serves as our Chairman, Chief Executive Officer and as a Managing Director. He has served as our Chief Executive Officer since July 1984 and as a Managing Director since January 2004. He has been a member of our Board of Directors and served as Chairman of the Board since April 1984. He also served as our Chief Compliance Officer from February 1997 to February 2001. He is Chairman of the Board, Chief Executive Officer and a Director of Harris & Harris Enterprises, a wholly owned subsidiary of the Company. His wife serves as our Corporate Secretary. He is a director of Mersana Therapeutics, Inc., and of SiOnyx, Inc., privately held nanotechnology-enabled companies in which we have investments. He was a member of the Advisory Panel for the Congressional Office of Technology Assessment. Prior to joining us, he was Chairman of Wood, Struthers and Winthrop Management Corporation, the investment advisory subsidiary of Donaldson, Lufkin and Jenrette. He is currently a member of the New York Society of Security Analysts. He was, until 2004, a Trustee and head of the Audit Committee of Cold Spring Harbor Laboratory, a not-for-profit institution that conducts research and education programs in the biological sciences, and he is currently a member of its President's Council. He also serves as a Trustee and head of the Audit Committee of the Nidus Center, a not-for-profit, life sciences, business incubator in St. Louis, Missouri. He is a life-sustaining fellow of MIT and a shareholder of its Entrepreneurship Center. He is an "interested person" as defined in Section 2(a)(19) of the 1940 Act, as a beneficial owner of more than five percent of our Common Stock, as a control person and as one of our officers. He was graduated from Princeton University (A.B.) and from the Columbia University Graduate School of Business (M.B.A.).

Douglas W. Jamison. Mr. Jamison, 38, has served as President and as Chief Operating Officer since January 1, 2005, as Treasurer from March 2005 to May 2008, as a Managing Director since January 2004, as Chief Financial Officer from January 2005 through December 2007 and as Vice President from September 2002 through December 2004. He has been a member of our Board of Directors since May 2007. Since January 2005, he has been President and a Director of Harris & Harris Enterprises, Inc., a wholly owned subsidiary of Harris & Harris Group, Inc. Upon Mr. Harris's retirement, scheduled for December 31, 2008, the Board of Directors has named Mr. Jamison to succeed Mr. Harris in Mr. Harris's positions as Chairman and Chief Executive Officer. Mr. Jamison is a director of Ancora Pharmaceuticals, Inc., of Nextreme Thermal Solutions, Inc., and of Phoenix Molecular Corporation, privately held nanotechnology-enabled companies in which we have investments. He is Co-Editor-in-Chief of "Nanotechnology Law & Business." He is Co-Chair of the Advisory Board, Converging Technology Bar Association, a member of the University of Pennsylvania Nano-Bio Interface Ethics Advisory Board and a member of the Advisory Board, Massachusetts Technology Collaborative Nanotechnology Venture Forum. His professional societies include the Association of University Technology Managers. From 1997 to 2002, he worked as a senior technology manager at the University of Utah Technology Transfer Office, where he managed intellectual property in physics, chemistry and the engineering sciences. He was graduated from Dartmouth College (B.A.) and the University of Utah (M.S.).

Daniel B. Wolfe. Mr. Wolfe, 31, has served as Chief Financial Officer and as a Managing Director since January 2008, as Principal from January 2007 to January 2008, as Senior Associate from January 2006 to January 2007, and as Vice President from July 2004 to January 2008. He is a director of Phoenix Molecular Corporation, a privately held nanotechnology-enabled company in which we have an investment. Prior to joining us, he served as a consultant to Nanosys, Inc. (from 2002 to 2004), to CW Group (from 2001 to 2004) and to Bioscale, Inc. (from January 2004 to June 2004). From February 2000 to January 2002, he was the Co-founder and President of Scientific Venture Assessments, Inc., a provider of scientific analysis of prospective investments for venture capital placements and of scientific expertise to high-technology companies. He was graduated from Rice University (B.A., Chemistry), where his honors included the Zevi and Bertha Salsburg Memorial Award in Chemistry and the Presidential Honor Roll, and from Harvard University (A.M., Ph.D., Chemistry), where he was an NSF Predoctoral Fellow.

At our request, Mr. Wolfe was interim Chief Executive Officer of Evolved Nanomaterial Sciences, Inc. ("ENS"), one of our portfolio companies, from July 1, 2007 to September 28, 2007. ENS filed for Chapter 7 bankruptcy on September 30, 2007.

Alexei A. Andreev. Mr. Andreev, 36, has served as an Executive Vice President and as a Managing Director since March 2005. From 2002 to March 2005, he was an Associate with Draper Fisher Jurvetson, a venture capital firm. In 2001, he was a Summer Associate with TLcom Capital Partners, a London-based venture capital fund backed by Morgan Stanley. From 1997 to 2000, he was an Associate at Renaissance Capital Group/Sputnik Funds, a venture capital fund in Moscow, Russia. Previously, he was a researcher at the Centre of Nanotechnology, Isan, in Troitsk, Russia. He is a director of CSwitch Corporation, of D-Wave Systems, Inc., and of Xradia, Inc., privately-held nanotechnology-enabled companies in which we have investments. He is a director of the American Business Association of Russian Expatriates. He was graduated with a B.S. with honors in Engineering/Material Sciences, with a Ph.D. in Solid State Physics from Moscow Steel and Alloys Institute and with an M.B.A. from the Stanford Graduate School of Business.

Michael A. Janse. Mr. Janse, 39, has served as an Executive Vice President and as a Managing Director since April 2007. From January 2007 to April 2007 he was a Principal with ARCH Venture Partners and was an Associate from June 2002 to January 2007, following earlier roles as an intern and then consultant. He concentrated on investment opportunities in advanced semiconductor products, nanotechnology, and novel materials. From 1995 to 2000, Mr. Janse worked in Motorola's Semiconductor Products Sector (now Freescale Semiconductor, Inc.) as a process engineer, and later marketed semiconductor components to manufacturers of personal computers and networking products. He is a director of Adesto Technologies Corp., of Innovalight, Inc., and of Nanomix, Inc., privately-held nanotechnology-enabled companies in which we have investments. He was graduated from Brigham Young University (B.S., Chemical Engineering) and The University of Chicago (M.B.A.).

Sandra Matrick Forman, Esq. Ms. Forman, 42, has served as General Counsel, as Chief Compliance Officer and as Director of Human Resources since August 2004. From 2001 to 2004, she was an Associate at Skadden, Arps, Slate, Meagher & Flom LLP, in the Investment Management Group. From May to August 2000, she was a summer associate with Latham & Watkins LLP in its London office. From August to December 2000, she served as an intern in the office of the General Counsel, United States Department of Defense, Office of the Secretary of Defense. From June to August 1999, she served as an intern for the Honorable Ronald S. Lew, United States Federal District Court, Central District of California. She was graduated from New York University (B.A.), where her honors included National Journalism Honor Society, and from the University of California Los Angeles (J.D.), where her honors included Order of the Coif and membership on the Law Review. She is currently a member of the working group for the National Venture Capital Association model documents.

Misti Ushio. Ms. Ushio, 36, has served as a Vice President and Associate since May 2007. From June 2006 to May 2007, Ms. Ushio was a Technology Licensing Officer at Columbia University. From May 1996 to May 2006, she was employed by Merck & Co., Inc., most recently as a Senior Research Biochemical Engineer with the Bioprocess R&D group. She was graduated from Johns Hopkins University (B.S., Chemical Engineering), Lehigh University (M.S., Chemical Engineering) and University College London (Ph.D., Biochemical Engineering).

Patricia N. Egan. Ms. Egan, 33, has served as Chief Accounting Officer, as Vice President and as Senior Controller since June 2005. From June 2005 to December 2005 and from August 2006 to May 2008, she served as an Assistant Secretary. She also serves as Chief Accounting Officer, as Treasurer and as Secretary of Harris & Harris Enterprises, Inc., a wholly owned subsidiary of the Company. From 1996 to 2005, she served as a Manager at PricewaterhouseCoopers LLP in its financial services group. She was graduated from Georgetown University (B.S., Accounting), where her honors included the Othmar F. Winkler Award for Excellence in Community Service. She is a Certified Public Accountant.

Mary P. Brady. Ms. Brady, 47, has served as a Vice President and Controller since November 2005, and as an Assistant Secretary from November 2005 to May 2008. From 2003 through 2005, she served as a senior accountant at Clarendon Insurance Company in its program accounting group. She served from 2000 to 2003 as a senior associate at PricewaterhouseCoopers LLP in its financial services group. She was graduated Summa Cum Laude from Lehman College (B.S., Accounting). She is a Certified Public Accountant.

Jennifer M. McGovern. Ms. McGovern, 30, has served as an Assistant Vice President, Counsel and an Assistant Secretary from August 2007. From June 2006 to August 2006, she worked as a law clerk at Luskin, Stern & Eisler LLP. From January 2006 to April 2006, she was an intern in the Office of the General Counsel, New York Stock Exchange. From July 1999 to June 2004, she worked at BlackRock, Inc., first as an Analyst, and then as an Associate, in the Private Client Group. She was graduated from Columbia University (B.A., Art History, Economics), and from Brooklyn Law School (J.D.), cum laude, where she was the Managing Editor of the *Brooklyn Journal of International Law* and a member of the Moot Court Honor Society.

Susan T. Harris. Ms. Harris, 63, has served as our Secretary since July 2001. From July 1999 to July 2003, she was employed by Harris & Harris Enterprises, Inc., our wholly owned subsidiary, working primarily in financial public relations. From July 2001 to July 2003, she served as Secretary and Treasurer of Harris & Harris Enterprises, Inc. Since 1972, she has been an investor relations consultant, operating as a sole proprietor prior to 1999, and again from July 2003 to the present. She was graduated from Wellesley College (B.A., Economics). Ms. Harris's husband serves as the Chairman, Chief Executive Officer and as a Managing Director of the Company.

Board of Directors

Our Board of Directors supervises our management. The responsibilities of each director include, among other things, the oversight of the investment approval process, the quarterly valuation of our assets, and the oversight of our financing arrangements.

Interested Directors:

Charles E. Harris. *See biography under "Executive Officers."*

Douglas W. Jamison. *See biography under “Executive Officers.”*

Lori D. Pressman. Ms. Pressman, 50, has served as a member of our Board of Directors since March 2002. She has served as a consultant to us on tiny technology, intellectual property and in our due diligence work on certain prospective investments. She also acts as an observer for us at Board meetings of certain portfolio companies in the Boston area. She is a business consultant providing advisory services to start-ups and venture capital companies , including certain of our portfolio companies. She consults internationally on technology transfer practices and metrics for non-profit and government organizations. From 1999 to 2001, she was Chair of the Survey Statistics and Metrics Committee of the Association of University Technology Managers. From September 1989 to July 2000, she was employed by MIT in its Technology Licensing Office; she served as a Technology Licensing Officer from 1989 to 1995 and as Assistant Director of the Technology Licensing Office from 1996 to 2000. She was graduated from the Massachusetts Institute of Technology (S.B., Physics) and the Columbia School of Engineering (MSEE). She may be considered to be an "interested person" of the Company because of the consulting work she does for us.

Independent Directors:

W. Dillaway Ayres, Jr. Mr. Ayres, 57, has served as a member of our Board of Directors since November 2006. He has served as the Chief Operating Officer of Cold Spring Harbor Laboratory, a research and educational institution in the biological sciences, since November of 2000. Prior to joining Cold Spring Harbor Laboratory in 1998, Mr. Ayres had a 20-year business career during which he worked as a corporate executive, investment banker and entrepreneur. In 1996, he co-founded Business & Trade Network, Inc., a business-to-business, venture capital-backed Internet company. Prior to that he worked for five years as a Managing Director of Veronis, Suhler & Associates, a boutique investment banking firm in New York specializing in the media/ communications industry. At Veronis, Suhler, he focused on investing the firm’s private equity fund. He was graduated from Princeton University (A.B., English) and from the Columbia University Graduate School of Business (M.B.A., Finance).

Dr. C. Wayne Bardin. Dr. Bardin, 73, has served as a member of our Board of Directors since December 1994. Since 1996, he has served as the President of Bardin LLC, a consulting firm to pharmaceutical companies. From 1998 to 2003, he served as President of Thyreos Corp., a privately held, start-up pharmaceutical company. From 1978 through 1996, he was Vice President of The Population Council. His professional appointments have included: Professor of Medicine, Chief of the Division of Endocrinology, The Milton S. Hershey Medical Center of Pennsylvania State University and Senior Investigator, Endocrinology Branch, National Cancer Institute. He has also served as a consultant to several pharmaceutical companies. He has been appointed to the editorial boards of 15 journals. He has also served on national and international committees and boards for the National Institutes of Health, World Health Organization, The Ford Foundation and numerous scientific societies. He was graduated from Rice University (B.A.), Baylor University (M.S., M.D.) and he received a Doctor Honoris Causa from the University of Caen, the University of Paris and the University of Helsinki.

Dr. Phillip A. Bauman. Dr. Bauman, 52, has served as a member of our Board of Directors since February 1998. Since 1999, he has been Senior Attending of Orthopedic Surgery at St. Luke’s/Roosevelt Hospital Center in Manhattan and since 2000, he has served as an elected member of the Executive Committee of the Medical Board of St. Luke's/Roosevelt Hospital. Since 2005, he has been on the Board of Managers for the Hudson Crossing Surgery Center. Since 1997, he has been Assistant Professor of Orthopedic Surgery at Columbia University. Since 1994, he has been a Vice President of Orthopedic Associates of New York. He is an active member of the American Academy of Orthopaedic Surgeons, the American Orthopaedic Society for Sports Medicine, the New York State Society of Orthopaedic Surgeons and the American Medical Association. He was graduated from Harvard College (A.B.), Harvard University (A.M., Biology) and the College of Physicians and Surgeons at Columbia University (M.D.).

G. Morgan Browne. Mr. Browne, 73, has served as a member of our Board of Directors since June 1992. Since 2004, he has been President and since 2000, a Trustee of Planting Fields Foundation, a supporting institution of Planting Fields Arboretum State Historic Park. He is Chairman of the OSI Pharmaceuticals Foundation which supports cancer and diabetes patient care and science education. From 2001 to 2003, he served as Chief Financial Officer of Cold Spring Harbor Laboratory, a not-for-profit institution that conducts research and education programs in the biological sciences. From 1985 to 2000, he was the Administrative Director of Cold Spring Harbor Laboratory. In prior years, he was active in the management of numerous scientifically based companies as an officer, as an individual consultant and as an associate of Laurent Oppenheim Associates, Industrial Management Consultants. He was a founding director of the New York Biotechnology Association. He was graduated from Yale University (B.A.).

Dugald A. Fletcher. Mr. Fletcher, 78, was appointed Lead Independent Director on November 2, 2006. Since 1996, he has served as a member of our Board of Directors. Since 1984, h e has served as President of Fletcher & Company, Inc., a management consulting firm. Until the end of 1997, he was Chairman of Binnings Building Products Company, Inc. His previous business appointments include: adviser to Gabelli/Rosenthal LP, a leveraged buyout fund; Chairman of Keller Industries, building and consumer products; Senior Vice President of Booz-Allen & Hamilton; President of Booz-Allen Acquisition Services; Executive Vice President of Paine Webber Jackson & Curtis and a Director of Paine Webber, Inc.; and President of Baker Weeks and Co., Inc., a New York Stock Exchange member firm. He is currently a Trustee of the Gabelli Growth Fund and a Director of the Gabelli Convertible and Income Securities Fund, Inc. He was graduated from Harvard College (A.B.) and Harvard Business School (M.B.A.).

Charles E. Ramsey. Mr. Ramsey, 65, has served as a member of our Board of Directors since October 2002. Since 1997, he has been a consultant. He is a retired founder and principal of Ramsey/Beirne Associates, Inc., an executive search firm that specialized in recruiting top officers for high technology companies, many of which were backed by venture capital. He is Chairman Emeritus of Bridges to Community, a non-governmental organization dedicated to construction projects in Nicaragua. As Chairman Emeritus, he serves on the Executive, Personnel and Administration and Fund Development Committees. He was graduated from Wittenberg University (B.A.).

James E. Roberts. Mr. Roberts, 62, has served as a member of our Board of Directors since June 1995. Since January 2006, he has been President of AequiCap Insurance Company and since September 2007, President of AequiCap Program Administrators. Mr. Roberts is also a senior officer of various other AequiCap affiliated entities. From November 2002 to October 2005, he was Executive Vice President and Chief Underwriting Officer of the Reinsurance Division of Alea North America Company and Senior Vice President of Alea North America Insurance Company. From October 1999 to November 2002, he was Chairman and Chief Executive Officer of the Insurance Corporation of New York, Dakota Specialty Insurance Company, and Recor Insurance Company Inc., all members of the Trenwick Group, Ltd. From October 1999 to March 2000, he served as Vice Chairman of Chartwell Reinsurance Company (also a member of Trenwick Group, Ltd.) and from March 2000 to November 2002 he was the company's Chairman and CEO. He was graduated from Cornell University (A.B.).

Richard P. Shanley. Mr. Shanley, 61, joined our Board on March 12, 2007. From February 2001 to December 31, 2006, he was a partner of Deloitte & Touche LLP. From March 1976 to January 2001, he was employed by Eisner LLP and was a partner from 1982 until 2001. During his over 30 years of public accounting experience, he served as lead audit partner on numerous audit engagements for public and private companies and companies making public stock offerings, including those requiring application of Sarbanes-Oxley Section 404. He served as lead audit partner primarily for biotech, pharmaceutical and high-tech companies, including companies enabled by nanotechnology. He has been actively involved on the Biotech Council of New Jersey, the New Jersey Technology Council, the New York Biotechnology Association, the Connecticut Venture Group, the Biotechnology Industry Organization and the NanoBusiness Alliance. He is an active member of the New York State Society of Certified Public Accountants and the American Institute of Certified Public Accountants. He is currently serving his fourth term on the New York State Society of CPA's Professional Ethics Committee. He is a licensed Certified Public Accountant in New Jersey and New York. He was graduated from Fordham University (B.S.) and Long Island University (M.B.A. in Accounting).

Committees of the Board of Directors

Our Board of Directors maintains six standing committees: an Executive Committee, an Audit Committee, a Compensation Committee, a Nominating Committee, a Valuation Committee and an Independent Directors Committee. All of the members of each committee other than Mr. Harris and Mr. Jamison (who sit on the Executive Committee) are non-interested directors (as defined in Section 2(a)(19) of the 1940 Act).

The Executive Committee has and may exercise those rights, powers and authority that the Board of Directors from time to time grants to it, except where action by the full Board is required by statute, an order of the SEC or our charter or bylaws. The Executive Committee did not meet as a separate committee and did not act by unanimous written consent in 2007. The members of the Executive Committee are Messrs. Harris (Chairman), Jamison, Browne, Ramsey and Dr. Bardin.

The Audit Committee operates pursuant to a charter that sets forth the responsibilities of the Audit Committee. The Audit Committee's responsibilities include selecting and retaining our independent registered public accounting firm, reviewing with the independent registered public accounting firm the planning, scope and results of their audit and our financial statements and the fees for services performed, reviewing with the independent registered public accounting firm the adequacy of internal control systems, reviewing our annual financial statements and receiving our audit reports and financial statements. The Audit Committee met four times and did not act by unanimous written consent in 2007. The members of the Audit Committee are Messrs. Shanley (Chairman), Roberts, Browne, Ayres and Fletcher, all of whom are considered independent under the rules promulgated by the Nasdaq Global Market.

The Compensation Committee operates pursuant to a written charter and determines the compensation for our executive officers and the amount of salary and bonus to be included in the compensation package for each of our officers. The Compensation Committee met four times and acted by unanimous written consent once in 2007. The members of the Compensation Committee are Messrs. Roberts (Chairman), Fletcher, Ramsey and Dr. Bauman.

The Nominating Committee acts pursuant to a written charter as an advisory committee to the Board by identifying individuals qualified to serve on the Board as directors and on committees of the Board, and recommending nominees to stand for election as directors at the next annual meeting of shareholders. The Nominating Committee met one time and did not act by unanimous written consent in 2007. The members of the Nominating Committee are Dr. Bardin (Chairman) and Messrs. Ayres, Shanley and Dr. Bauman.

The Nominating Committee will consider director candidates recommended by shareholders. In considering candidates submitted by shareholders, the Nominating Committee will take into consideration the needs of the Board and the qualifications of the candidate. The Nominating Committee may also take into consideration the number of shares held by the recommending shareholder and the length of time that such shares have been held. To have a candidate considered by the Nominating Committee, a shareholder must submit the recommendation in writing and must include:

• The name of the shareholder and evidence of the person's ownership of shares of the Company, including the number of shares owned and the length of time of ownership;

• The name of the candidate, the candidate's resume or a listing of his or her qualifications to be a Director of the Company and the person's consent to be named as a Director if selected by the Nominating Committee and nominated by the Board and consent to serve if elected; and

• If requested by the Nominating Committee, a completed and signed director's questionnaire.

The shareholder recommendation and information described above must be sent to the Company's Corporate Secretary, c/o Harris & Harris Group, Inc., 111 West 57th Street, Suite 1100, New York, New York 10019, and must be received by the Corporate Secretary not less than 90 days nor more than 120 days prior to the anniversary of the date of the Company's immediately preceding annual meeting of shareholders or, if the meeting has moved by more than 30 days, it must be received by the Corporate Secretary not later than the close of business on the 10th day following the day on which notice of the date of the annual meeting was mailed or such public disclosure of the date of the annual meeting was made, whichever first occurs.

The Valuation Committee reviews and approves the valuation of our assets, from time to time, as prescribed by the 1940 Act, pursuant to Valuation Procedures established by our Board of Directors. The Valuation Committee met six times and did not act by unanimous written consent in 2007. The members of the Valuation Committee are Messrs. Browne (Chairman), Ayres, Fletcher, Ramsey, Roberts, Shanley and Drs. Bardin and Bauman.

The Independent Directors Committee has the responsibility of proposing corporate governance and long-term planning matters to the Board of Directors and making the required determinations pursuant to the 1940 Act. The Independent Directors Committee met four times and did not act by unanimous written consent in 2007. The members of the Independent Directors Committee are Messrs. Fletcher (Chairman), Ayres, Browne, Ramsey, Roberts, Shanley and Drs. Bardin and Bauman.

On November 2, 2006, the Board of Directors appointed an Ad Hoc Pricing Committee. The Pricing Committee is responsible for approving the price of any offering of our Common Stock, approving the number of shares being offered in such offering, providing final approval of the underwriting agreement and handling any other details as are necessary to effect any transactions pursuant to this registration statement. The members of the Pricing Committee are Messrs. Harris (Chairman), Browne and Dr. Bardin.

The following table sets forth the dollar range of equity securities beneficially owned by each director as of December 31, 2007.

Name of Director	Dollar Range of Equity Securities Beneficially Owned (1)(2)(3)
Interested Directors	
Charles E. Harris(4)	Over $100,000
Douglas W. Jamison (4)	Over $100,000
Lori D. Pressman (5)	$50,001 - $100,000
Independent Directors	
W. Dillaway Ayres, Jr.	$10,001 - $50,000
Dr. C. Wayne Bardin	Over $100,000
Dr. Phillip A. Bauman	Over $100,000
G. Morgan Browne	Over $100,000
Dugald A. Fletcher	Over $100,000
Charles E. Ramsey	Over $100,000
James E. Roberts	Over $100,000

Richard P. Shanley	$10,001 - $50,000

(1) Beneficial ownership has been determined in accordance with Rule 16a-1(a)(2) under the 1934 Act.

(2) The dollar ranges are: none, $1-$10,000, $10,001-$50,000, $50,001-$100,000 and over $100,000.

(3) The dollar ranges are based on the price of the equity securities as of December 31, 2007.

(4) Denotes an individual who is an "interested person" as defined in the 1940 Act.

(5) Denotes an individual who may be considered an "interested person" because of consulting work performed for us.

Principal Shareholders and Ownership by Directors and Executive Officers

Set forth below is information as of May 28, 2008, with respect to the beneficial ownership of our Common Stock by (i) each of our directors and named executive officers (as defined below) and (ii) all of our directors and executive officers as a group. Except as otherwise indicated, to our knowledge, all shares are beneficially owned and investment and voting power is held by the persons named as owners. At this time, we are unaware of any shareholder owning 5 percent or more of the outstanding shares of Common Stock other than the ones noted below. Unless otherwise provided, the address of each holder is c/o Harris & Harris Group, Inc., 111 West 57th Street, Suite 1100, New York, New York 10019.

Name and Address of Beneficial Owner	Amount and Nature of Beneficial Ownership[(1)]	Percentage of Outstanding Common Shares Owned[(2)]
Independent Directors:		
W. Dillaway Ayres, Jr.	6,331	*
Dr. C. Wayne Bardin	29,324[(3)]	*
Dr. Phillip A. Bauman	31,759[(4)]	*
G. Morgan Browne	36,191	*
Dugald A. Fletcher	24,621	*
Charles E. Ramsey	41,717	*
James E. Roberts	26,047	*
Richard P. Shanley	5,324	*
Interested Directors:		
Charles E. Harris	1,928,890[(5)]	8.0
Douglas W. Jamison	330,548[(6)]	1.4
Lori D. Pressman	9,437	*
Named Executive Officers:		
Alexei A. Andreev	334,921[(7)]	1.4
Sandra M. Forman	161,793[(8)]	*
Michael A. Janse	247,782[(9)]	1.1
All directors and executive officers as a group (19 persons)	3,478,364 [(10)]	13.7

* Less than 1 percent.

(1) Beneficial ownership has been determined in accordance with Rule 13d-3 of the Securities Exchange Act of 1934.

(2) The percentage of ownership is based on 23,314,573 shares of common stock outstanding as of May 28, 2008, together with the exercisable options for such shareholder, as applicable. In computing the percentage ownership of a shareholder, shares that can be acquired upon the exercise of outstanding options are not deemed outstanding for purposes of computing the percentage ownership of any other person.

(3) Includes 5,441 shares owned by Bardin LLC for the Bardin LLC Profit-Sharing Keogh.

(4) Includes 5,637 shares owned by Ms. Milbry C. Polk, Dr. Bauman's wife; 100 shares owned by Adelaide Polk-Bauman, Dr. Bauman's daughter; 100 shares owned by Milbry Polk-Bauman, Dr. Bauman's daughter; and 100 shares owned by Mary Polk-Bauman, Dr. Bauman's daughter. Ms. Milbry C. Polk is the custodian for the accounts of the three children.

(5) Includes 1,039,559 shares owned by Mrs. Susan T. Harris, Mr. Harris's wife and our Corporate Secretary, 35,266 shares owned by Mr. Harris and 854,065 shares that can be acquired upon the exercise of outstanding options by Mr. Harris.

(6) Includes 310,905 shares that can be acquired upon the exercise of outstanding options.

(7) Includes 324,652 shares that can be acquired upon the exercise of outstanding options.

(8) Includes 250 shares owned by Edward Forman, Ms. Forman's husband, 270 shares owned jointly with Edward Forman and 154,091 shares that can be acquired upon the exercise of outstanding options by Ms. Forman.

(9) Includes 247,782 shares that can be acquired upon the exercise of outstanding options.

(10) Includes 2,151,404 shares that can be acquired upon the exercise of outstanding options.

EXECUTIVE COMPENSATION

Compensation Discussion & Analysis

Overview

This Compensation Discussion & Analysis ("CD&A") describes the material elements of compensation awarded to, earned by, or paid to our principal executive officer, principal financial officer and the three most highly paid executive officers (other than the principal executive officer and the principal financial officer) serving as such at the end of 2007 (the "named executive officers"), who are:

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- Charles E. Harris, our Chairman, Chief Executive Officer and a Managing Director;
- Douglas W. Jamison, our President, Chief Operating Officer, Chief Financial Officer (in 2007) and a Managing Director;
- Alexei A. Andreev, an Executive Vice President and a Managing Director;
- Michael A. Janse, an Executive Vice President and a Managing Director; and
- Sandra M. Forman, our General Counsel, Chief Compliance Officer and Director of Human Resources.

This CD&A focuses on the information contained in the following tables and related footnotes and narrative for primarily the last completed fiscal year, and we also describe compensation actions taken before or after the last completed fiscal year to the extent it enhances the understanding of our executive compensation for the last completed fiscal year. Pursuant to our Compensation Committee's written charter, the Committee oversees the design and administration of our executive compensation program. The Committee ensures that the total compensation paid to our executive officers is fair, reasonable and competitive.

Compensation Program Objectives and Philosophy

In General. The objectives of the Company's compensation program are to:

- attract, motivate and retain employees by providing market-competitive compensation while preserving company resources;
- maintain our leadership position as a venture capital firm specializing in tiny technology, especially nanotechnology; and
- align management's interests with shareholders' interests.

To achieve the above objectives, the Committee has designed a comprehensive compensation program in 2007 for our executive officers and all 12 of our permanent, full-time employees that is composed of a base salary and equity awards in the form of stock options. The Committee believes that the equity component of compensation is a crucial component of our compensation package. Shorter-term and longer-term vesting stock options are utilized for shorter-term and longer-term incentive, and to make the Company's compensation program more competitive, particularly with compensation programs of private partnerships that, unlike the Company, are able to award carried interests taxable as long-term gains and to permit co-investments in deals. Such private partnerships also are more easily able to pay cash bonuses because they do not have the expenses associated with being publicly traded. Our executive compensation programs and related data are reviewed throughout the year and on an annual basis by the Committee to determine if the compensation program is providing its intended results.

The Committee believes that retention is especially important for a company of our size (12 permanent employees) and the specialized nature of our business. Our employees have been selected and trained to support our focus on investment in tiny-technology companies and our specialized regulation and administration as a business development company. Our tiny-technology focus requires highly specialized scientific knowledge. There are relatively few individuals who have both such scientific knowledge and venture capital experience. Additionally, our business development company structure requires specialized management, administrative, legal and financial knowledge of our specific regulatory regime. Because there are very few business development companies, it would be difficult to find replacements for certain executive, legal and financial positions.

Competitive Market. For our investment-team members, the competition for retention and recruitment is primarily private venture capital firms, hedge funds and, to a lesser extent, investment banking firms. Such a fund commonly pays at least 20 percent of the profits (including capital gains), or carried interest, of each newly-raised fund to the management firm, which awards interests to its partners and employees. For our legal and accounting professionals, in addition to the foregoing, the competition is other public companies without regard to industry, asset management companies and legal and accounting firms. The Company does not have a readily identifiable peer group, because most business development companies are not early-stage venture-capital companies, and most other early-stage venture-capital companies are not publicly traded. Thus, we do not emphasize the use of peer comparison groups in the design of our compensation program. We do utilize compensation comparables, on an individual basis, to the extent that they seem appropriately analogous, as provided to the Committee by an independent compensation consultant, as one factor in determining compensation.

Compensation Process. On an annual basis, the Committee reviews and approves each element of compensation for each of our executive officers, taking into consideration the recommendation of our Chief Executive Officer (for compensation other than his own, which is subject to his employment agreement as discussed below) in the context of the Committee's compensation philosophy, to ensure that the total compensation program and the weight of each of its elements meets the overall objectives discussed above. For the Chief Compliance Officer, the Committee recommends her compensation to the full Board, for approval by at least a majority of the non-interested directors (as defined in Section 2(a)(19) of the 1940 Act).

In 2007, an independent compensation consultant, Johnson & Associates, supplied the Committee with market data on all officers' positions. The information provided for 2007-2008 was for private-equity firms, venture capital firms and broad investment management firms, and was adjusted in an effort to reflect compensation for a venture capital firm with $100 - $200 million in assets under management. Data was also provided for public companies with comparable market capitalizations. Further data was provided for 1940 Act compliance personnel (collectively, the "Identified Group"). The independent consultant did not identify the names of companies included in the Indentified Group. The Committee considers recommendations from the Chief Executive Officer regarding salaries, along with factors such as individual performance, current and potential impact on Company performance, reputation, skills and experience. When determining compensation, the Committee considers the importance of retaining certain key officers whose replacement would be challenging owing to the Company's status as a 1940 Act company and owing to its tiny-technology specialty. The Committee also considers the highly specialized nature of certain positions in determining overall compensation.

When addressing executive compensation matters, the Committee generally meets outside the presence of all executive officers except our Chief Executive Officer and our General Counsel, each of whom leaves the meeting when his/her compensation is reviewed.

Regulatory Considerations. The 1940 Act permits business development companies to either pay out up to 20 percent of net income after taxes through the implementation of a profit-sharing plan or issue up to 20 percent of shares issued and outstanding through implementation of a stock-option plan. The exercise price of stock options may not be less than the current market value at the date of issuance of the options.

We have applied for exemptive relief from the SEC permitting us to issue restricted stock pursuant to the Harris & Harris Group, Inc. 2006 Equity Incentive Plan (the "Stock Plan") to employees and to permit non-employee directors to participate in the Stock Plan. Until such time as we receive such exemptive relief and such provisions are approved by shareholders, we will not issue any shares of restricted stock and our non-employee directors will not participate in the Stock Plan.

The Company has been informed that the SEC has commenced its review of the exemptive application, and we have received and responded to formal written comments. We cannot, however, evaluate whether or when an order regarding our application for the relief requested may be granted.

We have also designed our Stock Plan with the intention that awards made thereunder generally will qualify as performance-based compensation under Section 162(m) of the Internal Revenue Code of 1986 (the "Code"), but we reserve the right to pay amounts thereunder that do not qualify as such performance-based compensation if we determine such payments to be appropriate in light of our compensation objectives from time to time. Section 162(m) of the Code disallows a tax deduction to publicly held companies for compensation paid to their chief executive officer or any of their three other most highly compensated executive officers and chief financial officer, to the extent that compensation exceeds $1 million per covered officer in any fiscal year. However, if compensation qualifies as performance-based, the limitation does not apply.

Our status as a regulated investment company under Subchapter M of the Code makes the deductibility of our compensation arrangements a much less important factor for the Committee to consider than it would be if we were an operating company. Under Subchapter M, the Company cannot deduct operating expenses from its long-term capital gains, which are its most significant form of income. The Company presently has more operating expenses than it can deduct for tax purposes, even before equity compensation.

Compensation Components

The principal elements of our executive compensation program for 2007 are base salary, equity and other benefits and perquisites. The Committee believes that each element is essential to achieve the Company's objectives as set forth above. The Committee is mindful of keeping cash compensation expenses at as low a level of total operating expenses as is consistent with maintaining the Company's competitiveness versus private venture capital funds while meeting the expenses of complying with the regulatory requirements of a publicly traded company. Therefore, the equity component of compensation is key to keeping overall compensation competitive, while making prudent use of the Company's resources.

Base Salaries. We recognize the need to pay our named executive officers, and other employees, a competitive annual base salary. We review base salaries for our named executive officers annually. In 2007, the Committee compared salary ranges for all executive officers against the Identified Group. Base salaries are generally adjusted annually for inflation and also based on changes in the marketplace and an executive's individual performance, salary position among peers, career growth potential and/or a change in responsibilities. Other than Mr. Harris, whose salary was set pursuant to his employment agreement as described below, all of the named executive officers are paid the same base salary.

Effective January 1, 2007, the base salary of Sandra M. Forman, our General Counsel, Chief Compliance Officer and Director of Human Resources, was increased from $215,000 in 2006 to $267,403 in 2007, to remain market competitive for her services and to put her base salary on parity with our Managing Directors.

All other named executive officers received cost of living adjustments in 2007. There presently are no contemplated increases in base salary for any of the named executive officers in 2008 other than cost-of-living adjustments.

Equity Incentive Awards.

In General

Commencing in 2006, we have provided the opportunity for our named executive officers and other employees to earn longer-term and shorter-term equity incentive awards. Equity incentive awards in the form of options potentially generate cash for the Company that can be used for portfolio company investments and for working capital.

Longer-Term Equity Incentive Awards

The longer-term equity incentive awards provide employees with the incentive to stay with us for longer periods of time, which in turn provides us with greater stability. Longer-term equity incentive awards are meant to substitute for carried interest that our investment professionals would receive were they employed by private-sector venture capital firms, which typically pay at least 20 percent of profits before any taxes, and that carried interest is usually in the form of long-term capital gains, not ordinary income. The Committee believes that strategically timed awards of restricted stock are also important to ensuring the retention, stability and desired succession of executive talent, but the Company is not permitted to grant awards of restricted stock unless the Company receives an exemptive order from the SEC to do so. On July 11, 2006, we filed an application with the SEC to obtain such exemptive relief (as described above) and in June 2007 and February 2008, the Company responded to comments from the staff of the SEC on the application. If we receive the exemptive relief, the Committee will not grant any awards of restricted stock unless the amended Stock Plan is approved by shareholders, and such awards would be longer term.

Shorter-Term Equity Incentive Awards

Shorter-term equity incentive awards help to motivate employees in the short term, as we generally do not pay annual cash bonuses. Without cash bonuses or cash retained through the exercise and sale of shorter-term options, the Committee's independent compensation consultant has advised that certain key positions are not competitive when compared with the Identified Group. Shorter-term equity incentive awards also permit each executive officer to increase his/her ownership in Company stock, pursuant to minimum share ownership guidelines established by our Board. Shorter-term vesting periods also have the potential of generating cash for the company in the short term, through the purchase of stock in the course of the exercise of options, that can be used for making venture-capital investments and for working capital.

If the named executive officers, exclusive of Mr. Harris, as he is scheduled to retire on December 31, 2008, do not receive sufficient cash from the exercise and sale of stock options in a year to provide market-competitive total compensation, as determined by the Committee, based on advice from the independent compensation consultant, the Committee will pay the named executive officers cash bonuses. No such discretion was exercised in 2007. The Committee believes that retention of key employees is crucial because of the specialized nature of our business as described more fully below. Additionally, the Committee has considered that, owing to the scheduled retirement of Mr. Harris, the importance of retaining the other team members has increased.

Awards Under the Stock Plan

In accordance with the Stock Plan, which was approved by shareholders at the 2006 Annual Meeting of Shareholders, the Committee can issue options from time to time for up to 20 percent of the total shares of stock issued and outstanding. Thus, the number of shares of stock able to be reserved for the grant of awards under the Stock Plan will automatically increase (or decrease) with each increase (or decrease) in the number of shares of stock issued and outstanding. The Board intends to increase the number of shares reserved for stock option grants (currently 4,662,915) from time to time as the number of outstanding shares increases. The Committee may grant awards under the Stock Plan to the full extent permitted at the time of each grant in order to compete with private equity firms by retaining the specially qualified and trained personnel that have been carefully recruited and developed for the Company's specialized business. Because our primary competitors are organized as private partnerships, they do not have the overhead of a publicly traded company. As a consequence, unlike the Company, they can afford for cash compensation to be a larger percentage of their total expenses. Unlike us, they are not prohibited from paying out at least 20 percent of their profits to key employees, primarily in the form of long-term capital gains. They also, unlike us, are permitted to grant their employees co-investment rights.

Under the Stock Plan, no more than 25 percent of the shares of stock reserved for the grant of the awards under the Stock Plan may be restricted stock awards at any time during the term of the Stock Plan. If any shares of restricted stock are awarded, such awards will reduce on a percentage basis the total number of shares of stock for which options may be awarded. If we do not receive exemptive relief from the SEC to issue restricted stock, all shares granted under the Stock Plan may be subject to stock options. If we were to receive such exemptive relief and were to issue the full 25 percent of the shares of stock reserved for grant under the Stock Plan as restricted stock, no more than 75 percent of the shares granted under the Stock Plan could be subject to stock options. No more than 1,000,000 shares of our common stock may be made subject to awards under the Stock Plan to any individual in any year.

On June 27, 2007, the Committee and the full Board of Directors approved individual stock-option awards for certain officers and employees of the Company. The terms and conditions of the stock options granted were set forth in award agreements between the Company and each award recipient. A total of 1,700,609 stock options were granted with vesting dates ranging from December 2007 to June 2014, with an exercise price of $11.11, which was the closing volume weighted average price on the date of the grant. Upon exercise, the shares will be issued from our previously authorized but unissued shares.

The Committee has generally granted the same number of stock options to each of the Managing Directors, with the exception of Mr. Harris as discussed below. Additionally, in 2007, the Committee granted an additional 50,000 options to Mr. Jamison in anticipation of his growing role in the Company as the successor to Mr. Harris as Chief Executive Officer in 2009 upon Mr. Harris's retirement. In 2007, Mr. Janse received an additional 429,128 options to give him an equivalent number of options to Mr. Andreev.

The number of options per employee and the vesting and expiration dates were originally proposed by the independent consultant after conversations with the Chairman of the Committee and input from the Chief Executive Officer (with respect to options other than his own). All awards granted to executive officers vest subject to continued employment with the Company through each applicable vesting date, except for certain retirees. All stock-option awards to officers will be subject to stock-retention guidelines (as described in the section "Share Ownership Guidelines" below).

In 2006 and 2007, new grants were planned in advance of, and in anticipation of, the expiration of prior grants. Commencing in 2008, the Committee may give quarterly, rather than annual, grants to executive officers. The Committee believes that giving four smaller grants quarterly, rather than one annual grant, will more closely align employees' interests with those of shareholders. We do not time stock option grants in coordination with the release of material, non-public information, nor do we time the release of material, non-public information for the purpose of affecting the value of executive compensation.

Option grants in 2007 were not subject to performance goals. Other than stock options being tied to stock price, no other items of corporate performance were taken into account at the time of grant, because of the difficulty of determining annual performance metrics. Business development companies like us do not report earnings per share; moreover, write-downs and write-offs of investments are an expected part of our risk-seeking strategy, and it is not uncommon for even our most successful investments to take years to come to fruition. The Committee may create performance goals for the vesting of restricted stock (subject to receipt of an exemptive order). If performance goals are used in the future, the Board will have the authority to make equitable adjustments to the performance goals in recognition of unusual or non-recurring events affecting the Company or the financial statements of the Company, in response to changes in applicable laws or regulations or to account for items of gain, loss or expense determined to be extraordinary or unusual in nature or infrequent in occurrence or related to the disposal of a segment of a business or related to a change in accounting principles.

Generally, the Committee is made aware of the tax and accounting treatment of various compensation alternatives. SFAS 123(R) requires us to record the fair value of equity awards on the date of grant as a component of equity. We account for the Stock Plan in accordance with the provisions of SFAS No. 123(R), "Share-Based Payment," which requires that we determine the fair value of all share-based payments to employees, including the fair value of grants of employee stock options, and record these amounts as an expense in the Statement of Operations over the vesting period with a corresponding increase to our additional paid-in capital. The increase to our operating expenses is offset by the increase to our additional paid-in capital, resulting in no net impact to our net asset value. Thus, the granting of options is expected to have no net impact on our net asset value. If and when the options are exercised, the net asset value per share will be decreased if the net asset value per share at the time of exercise is higher than the exercise price, and increased if the net asset value per share at the time of exercise is lower than the exercise price. As a result, although we consider the accounting treatment of granting options, we do not consider the accounting treatment to be a dominant factor in the form and/or design of awards.

Additionally, we do not record tax benefits associated with expensing of stock options, because we intend to qualify as a RIC under Subchapter M of the Code. As a RIC, we cannot use all of our existing operating expenses for tax purposes.

10b5-1 Plans

We have established a policy of permitting our officers to enter into trading plans to sell shares of our common stock in accordance with Rule 10b5-1 of the Securities Act of 1934. The policy allows our participating officers to adopt a pre-arranged stock trading plan to buy or sell pre-determined amounts of our common stock over a period of time. This policy was established in recognition of the liquidity and diversification objectives of our officers, including enabling our officers to sell certain shares of our common stock (such as some of the shares of our common stock they acquire upon exercise of stock options, to pay for the exercise of options, to provide for taxes triggered by the exercise of options and to generate cash from the exercise of options).

Benefits and Perquisites. We provide the opportunity for our named executive officers and other full-time employees to receive certain perquisites and general health and welfare benefits, discussed more fully below, which consist of life- and health-insurance benefits, reimbursement for certain medical expenses and gym-membership fees. We also offer participation in our defined contribution 401(k) plan. For the year ended December 31, 2007, the Committee approved a 401(k) plan match of 100 percent of employee contributions. Except as provided in our employment agreement with Mr. Harris, our executive officers generally receive the same benefits and perquisites as our full-time administrative employees.

Profit Sharing. Prior to the adoption of the Stock Plan, the Company maintained the Amended and Restated Harris & Harris Group, Inc. Employee Profit-Sharing Plan (the "2002 Plan"). Under the 2002 Plan, approximately 90 percent of the amount determined as "qualifying income" was paid out to participants pursuant to distribution percentages determined by the Committee. The remaining payment was paid out after we finalized our tax returns for each plan year. Effective May 4, 2006, the 2002 Plan was terminated. On January 31, 2007, a final profit sharing award of $261,661 was paid to certain participants related to the 2005 plan year after finalization of our tax returns for 2005. Please see the "Non-Equity Incentive Plan Compensation" column and accompanying footnote in the 2007 Summary Compensation Table for more information about profit sharing awards.

Internal Pay Equity. In 2007, the Committee discussed the internal pay equity of the named executive officers. The Committee noted that Mr. Harris's compensation is appropriate based on the unique qualifications and skills required for the Chief Executive Officer position in our Company and his role as Founder. The Committee further noted that our investment professionals work together as a team rather than as a collection of individuals, which was the basis for the Committee's decision to pay all Managing Directors (except for Mr. Harris) identically. The Committee believes that, on a small team, all members must pull their full weight. Accordingly, the Committee believes that the team approach to compensation promotes teamwork among the Managing Directors. The Committee also noted that Ms. Forman's base salary was on parity with the Managing Directors to make her compensation competitive based on her 1940 Act specialty and her management role in the Company as General Counsel, Chief Compliance Officer and Director of Human Resources. The Committee further noted that the Managing Directors should receive more stock options than other employees based on their income-generating role and to keep their total compensation competitive with private venture-capital firms.

Compensation of our Chief Executive Officer

The Committee reviews all elements of the compensation of Charles E. Harris, our Chairman, Chief Executive Officer and a Managing Director, on an annual basis and then makes a determination about his compensation without his presence, subject to his employment agreement.

Pursuant to that agreement, as most recently amended as of August 2, 2007 (the "Employment Agreement"), during the period of employment, Mr. Harris is to receive compensation in the form of base salary, with automatic yearly adjustments to reflect inflation, which amounted to a minimum required base salary of $246,651 for 2006. In addition, the Board may increase such salary, and subsequently decrease it, but not below the level provided for by the automatic adjustments described above. Mr. Harris's base salary for 2006 was increased to $300,000 (thereby also increasing his SERP benefit as described below) in part in recognition of a 74 percent decrease in Mr. Harris's profit-sharing allocation in recent years in order to provide additional profit sharing to other employees. This was the first salary increase for Mr. Harris, other than cost-of-living adjustments, since 1994. Mr. Harris's base salary for 2007 and 2008 was increased to $306,187 and $314,623, respectively, based on cost-of-living adjustments.

In 2007, the Committee granted to Mr. Harris the following stock options:

	Expiration Date of Options	Year of Vesting 2007	2008	Exercise Price
9 Yr NQSO (vest 50% on 12/27/07, 50% vest of 12/27/08)	6/26/2016	120,491	120,490	$11.11

The amount of options granted to Mr. Harris was based on creating long-term incentives for Mr. Harris with respect to strategy and investment, balance sheet, personnel and lease decisions despite his scheduled retirement, in recognition of his role as Founder of the Company, and as an incentive for him to sign upon his retirement a three-year non-compete agreement covering the period after his retirement.

Under his employment agreement, Mr. Harris is entitled to participate in all compensation and employee benefit plans or programs, and to receive all benefits, perquisites, and emoluments, for which salaried employees are eligible. Under the Employment Agreement, we furnish Mr. Harris with certain perquisites, which include a company car, health-club membership, personal trainer, membership in certain social or country clubs, a reimbursement for an annual physical examination and up to a $5,000 annual reimbursement, adjusted for inflation, over the period of the agreement, for personal financial or tax advice.

The Employment Agreement also provides Mr. Harris with life insurance for the benefit of his designated beneficiary in the amount of at least $2,000,000; provides reimbursement for uninsured medical expenses, not to exceed $10,000 per annum, adjusted for inflation, over the period of the agreement; provides Mr. Harris and his spouse with long-term care insurance; and provides Mr. Harris with disability insurance providing for continuation of 100 percent of his base salary for a specified period. These benefits are for the term of the Employment Agreement. The Employment Agreement provides that the term of Mr. Harris's employment may not be extended beyond December 31, 2008, unless a committee of the Board consisting of non-interested Directors extends the date by one year pursuant to the Executive Mandatory Retirement Benefit Plan, and Mr. Harris agrees to serve beyond December 31, 2008.

Mr. Harris's Employment Agreement also provides for a supplemental executive retirement plan (the "SERP") and a severance compensation agreement for his benefit. See "2007 Non-Qualified Deferred Compensation" below for more information about the SERP. For more information about Mr. Harris's severance compensation, please see "Potential Payments upon Termination or Change in Control" below.

The Committee determined that the Employment Agreement, the severance compensation agreement and the awards made to Mr. Harris in 2007 pursuant to the Stock Plan are appropriate based on the unique qualifications and skills required for the Chief Executive Officer position in our Company. Our Chief Executive Officer must have expertise in managing a public company, managing a business development company and managing a venture-capital company. He must also have knowledge of tiny technology, particularly nanotechnology, have stature within both the nanotechnology community and the venture-capital community and have relationships with the investment banking community.

Share Ownership Guidelines

Our Board of Directors has established a retained stock-ownership policy for our officers. Pursuant to the policy, each executive officer is expected to own at least 25 percent of the net shares (after sales of stock to cover the purchase price and taxes triggered by the exercise of options) that he or she purchases in a calendar year through the exercise of options covering up to $75,000 of underlying stock based on current market value on the day of each transaction. Each executive officer must then retain at least 50 percent of the net shares (after sales of stock to cover the purchase price and taxes triggered by the exercise of options) above $75,000 until his or her purchases reach the following share ownership levels:

	Ownership Level
Managing Directors (including CEO)	$4,500,000
Other Deal Team Members (including General Counsel)	$2,500,000
Other Officers	1 X Base Salary

After reaching the above ownership levels, each executive officer is expected to retain 25 percent of the net shares (after sales of stock to cover the purchase price and taxes triggered by the exercise of options) that he or she purchases in any calendar year through the exercise of options. The policy aligns the interests of our officers and directors with the interests of shareholders. Our Chief Executive Officer currently exceeds the guidelines. Other executive officers are working toward the ownership levels as stock options are exercised.

Compensation and Share Ownership of Our Managing Directors

Messrs. Harris, Jamison, Andreev, Janse and Wolfe are Managing Directors and are primarily responsible for the day-to-day management of our portfolio. They have served in this capacity since 1984, 2002, 2005, 2007 and 2008 respectively, although the title "Managing Director" was first utilized by our Company in 2004.

See the “Compensation Discussion and Analysis - Compensation of our Chief Executive Officer” above for more information about the compensation of Mr. Harris. Messrs. Jamison, Andreev, Janse and Wolfe each receive a fixed base salary as determined by our Compensation Committee, participate in the Equity Incentive Plan (as described above) and receive all benefits, perquisites, and emoluments for which salaried employees are eligible.

The following table sets forth the dollar range of equity securities beneficially owned by each Managing Director as of December 31, 2007.

Name of Managing Director	**Dollar Range of Equity Securities Beneficially Owned** [(1)(2)]
Charles E. Harris	Over $1,000,000[(3)]
Douglas W. Jamison	Over $1,000,000[(4)]
Alexei A. Andreev	Over $1,000,000[(5)]
Michael A. Janse	Over $1,000,000[(6)]
Daniel B. Wolfe	$500,001 - $1,000,000[(7)]

(1) Beneficial ownership has been determined in accordance with Rule 16a-1(a)(2) of the 1934 Act.

(2) The dollar ranges are: none, $1-$10,000, $10,001-$50,000, $50,001-$100,000, $100,001-$500,000, $500,001-$1,000,000 and over $1,000,000.

(3) Includes 600,841 shares that can be acquired upon the exercise of outstanding options.

(4) Includes 247,681 shares that can be acquired upon the exercise of outstanding options.

(5) Includes 261,428 shares that can be acquired upon the exercise of outstanding options.

(6) Includes 237,891 shares that can be acquired upon the exercise of outstanding options.

(7) Reported as of May 28, 2008. Mr. Wolfe was promoted to Managing Director as of January 1, 2008. Includes 111,999 shares that can be acquired upon the exercise of outstanding options.

Related Party Transactions

In the ordinary course of business, the Company enters into transactions with portfolio companies that may be considered related party transactions. Other than these transactions, for the fiscal year ended December 31, 2007, there were no transactions, or proposed transactions, in which the registrant was or is a participant in which any related person had or will have a direct or indirect material interest.

In order to ensure that the Company does not engage in any prohibited transactions with any persons affiliated with the Company, the Company has implemented procedures, which are set forth in the Company’s Compliance Manual. Our Audit Committee must review in advance any "related party" transaction, or series of similar transactions, to which the Company or any of its subsidiaries was or is to be a party, in which the amount involved exceeds $120,000 and in which such related party had, or will have, a direct or indirect material interest. The Board of Directors reviews these procedures on an annual basis.

In addition, the Company’s Code of Conduct for Directors and Employees ("Code of Conduct"), which is signed by all employees and directors on an annual basis, requires that all employees and directors avoid any conflict, or the appearance of a conflict, between an individual’s personal interests and the interests of the Company. Pursuant to the

Code of Conduct, each employee and director must disclose any conflicts of interest, or actions or relationships that might give rise to a conflict, to the Chief Compliance Officer. The Independent Directors Committee is charged with monitoring and making recommendations to the Board of Directors regarding policies and practices relating to corporate governance. If there were any actions or relationships that might give rise to a conflict of interest, such actions or relationships would be reviewed and approved by the Board of Directors.

Remuneration of Named Executive Officers

2007 Summary Compensation Table

The following table sets forth a summary for the years ended December 31, 2007, and December 31, 2006, of the cash and non-cash compensation paid to our named executive officers. The primary elements of each named executive officer’s total compensation reported in the table are base salary and equity incentives consisting of stock options. The Summary Compensation Table should be read in conjunction with the CD&A and the other tables and narrative descriptions that follow.

Name and Principal Position	Year	Salary ($)	Option Awards[1] ($)	Non-Equity Incentive Plan Compensation [2] ($)	Change in Pension Value and Nonqualified Compensation Earnings[3] ($)	All Other Compensation ($)[4][6][7]	Total ($)
Charles E. Harris Chairman of the Board, Chief Executive Officer, Managing Director[5]	2007	306,187	3,374,224	0	42,063	418,479	4,140,953
	2006	300,000	2,034,482	29,067	54,692	405,628	2,823,869
Douglas W. Jamison President, Chief Operating Officer, Chief Financial Officer (2007), Managing Director, Former Vice President	2007	267,403	953,931	0	0	15,500	1,236,834
	2006	262,000	668,677	3,957	--	15,000	949,634
Alexei A. Andreev Managing Director, Executive Vice President	2007	267,403	897,250	0	--	15,500	1,180,153
	2006	262,000	668,677	0	--	15,000	945,677
Michael A. Janse Managing Director, Executive Vice President[8]	2007	184,211	873,201	0	--	45,500	1,102,912
	2006	--	--	--	--	--	--
Sandra M. Forman, Esq.	2007	267,403	559,229	0	--	15,500	842,132

General Counsel, Chief Compliance Officer, Director of Human Resources	2006	215,000	381,595	1,580	--	15,000	613,175

(1) The figures in this column do not represent amounts actually paid to the named executive officers, but represent the aggregate dollar amount of compensation cost recognized by us in 2007 under FAS 123(R) for options granted in 2007 and prior years. We use the Black-Scholes-Merton model to calculate compensation cost under FAS 123(R). You may find more information about the assumptions we use in the Black-Scholes-Merton model under "Fair Valuation of Option Awards."

(2) These amounts represent the actual amounts earned as a result of realized gains during the year ended December 31, 2005, and paid out in 2006 and 2007, under the Harris & Harris Group Employee Profit-Sharing Plan. These 2006 amounts are in addition to the $1,107,088 for Mr. Harris, $165,308 for Mr. Jamison, and $62,685 for Ms. Forman reported in the 2005 proxy and were determined in 2006 based on the finalization of our 2005 tax returns.

(3) Represents increase in pension obligation. There were no preferential or above market earnings on Mr. Harris's deferred compensation.

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(4) The amounts reported for Mr. Harris for 2007 represent actual amounts of benefits paid or payable including personal use of an automobile totaling $10,252, membership in a private club totaling $11,026, membership in a health club and use of a trainer totaling $19,333, medical care reimbursement, consultation with a financial planner totaling $21,505, long-term disability insurance, group term-life insurance, long-term care insurance for him and his wife and $20,500 in employer contributions to the Harris & Harris Group, Inc. 401(k) Plan. It also includes the employer contribution to his SERP totaling $306,187.

(5) In 2007 and 2006, Mr. Harris's wife received compensation of $25,000 and $21,000, respectively for serving as our Secretary.

(6) The amounts reported for Mr. Janse for 2007 represent qualified moving expenses paid totaling $30,000 and $15,500 in employer contributions to the Harris & Harris Group 401(k) Plan.

(7) Except for Mr. Harris (see footnote 4 above), and Mr. Janse (see footnote 6 above), amounts reported for 2007 represent our contributions on behalf of the named executive to the Harris & Harris Group, Inc. 401(k) Plan. The named executive did not earn any other compensation reportable in this column that met the threshold reporting requirements.

(8) Mr. Janse joined the Company in April 2007.

Fair Valuation of Option Awards

We account for the Stock Plan in accordance with the provisions of SFAS No. 123(R), "Share-Based Payment," which requires that we determine the fair value of all share-based payments to employees, including the fair value of grants of employee stock options, and record these amounts as an expense in the Statement of Operations over the vesting period with a corresponding increase to our additional paid-in capital. The increase to our operating expenses is offset by the increase to our additional paid-in capital, resulting in no net impact to our net asset value. Additionally, we do not record the tax benefits associated with the expensing of stock options, because we currently intend to qualify as a RIC under Subchapter M of the Code.

The fair value of each stock option award is estimated on the date of grant using the Black-Scholes-Merton option pricing model as permitted by SFAS No. 123(R). The stock options were awarded in five different grant types, each with different contractual terms. The assumptions used in the calculation of fair value using the Black-Scholes-Merton model for each contract term for grants in 2007 were as follows:

Type of Award	Contractual Term	Number of Options Granted	Expected Term in Yrs	Expected Volatility Factor	Expected Dividend Yield	Risk-free Interest Rates	Fair Value Per Share
Non-qualified stock options	1.5 Years	380,000	1	42.6%	0%	4.93%	$2.11
Non-qualified stock options	2.5 Years	600,540	2	40.1%	0%	4.91%	$2.92
Non-qualified stock options	3.5 Years	338,403	3	44.7%	0%	4.93%	$3.94
Non-qualified stock options	9 Years	381,666	Ranging from	Ranging from 57.8% to	0%	Ranging from 4.97% to	Ranging from $5.92 to

		4.75-6.28	59.9%	5.01%	$6.85
Total	1,700,609				

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An option's expected term is the estimated period between the grant date and the exercise date of the option. As the expected-term period increases, the fair value of the option and the compensation cost will also increase. The expected-term assumption is generally calculated using historical stock option exercise data. The Company does not have historical exercise data to develop such an assumption. In cases where companies do not have historical data and where the options meet certain criteria, SEC Staff Accounting Bulletin 107 ("SAB 107") provides the use of a simplified expected-term calculation. Accordingly, the Company calculated the expected terms using the SAB 107 simplified method.

Expected volatility is the measure of how the stock's price is expected to fluctuate over a period of time. An increase in the expected volatility assumption yields a higher fair value of the stock option. Expected volatility factors for the stock options were based on the historical fluctuations in the Company’s stock price over a period commensurate with the expected term of the option, adjusted for stock splits and dividends.

The expected-dividend yield assumption is traditionally calculated based on a company's historical dividend yield. An increase to the expected-dividend yield results in a decrease in the fair value of the option and resulting compensation cost. Although the Company has declared deemed dividends in previous years, most recently in 2005, the amounts and timing of any future dividends cannot be reasonably estimated. Therefore, for purposes of calculating fair value, the Company has assumed an expected- dividend yield of 0 percent.

The risk-free interest rate assumptions are based on the annual yield on the measurement date of a zero-coupon U.S. Treasury bond, the maturity of which equals the option’s expected term. Higher assumed interest rates yield higher fair values.

2007 Grants of Plan-Based Awards

The following table presents information regarding the equity incentive awards granted to the named executive officers during the fiscal year ended December 31, 2007.

Name	Grant Date	All Other Stock Awards: Number of Shares of Stock or Units (#)	All Other Option Awards: Number of Securities Underlying Options (#)	Exercise or Base Price of Option Awards* ($/Sh)	Closing Price on Grant Date ($)	Grant Date Fair Value of Stock and Option Awards
Charles E. Harris	June 27, 2007	N/A	240,981	$11.11	$11.15	$1,460,345
Douglas W. Jamison	June 27, 2007	N/A	250,000	$11.11	$11.15	$785,737
Alexei A. Andreev	June 27, 2007	N/A	200,000	$11.11	$11.15	$628,590
Michael A. Janse	June 27, 2007	N/A	629,128	$11.11	$11.15	$2,038,717
Sandra M. Forman	June 27, 2007	N/A	135,000	$11.11	$11.15	$420,312

*Equals the closing volume weighted average price on the date of grant.

2007 Outstanding Equity Awards at Fiscal Year-End

The following table presents information regarding the outstanding equity awards held by each of the named executive officers as of December 31, 2007.

	Option Awards			
Name	Number of Securities Underlying Unexercised Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Option Exercise Price ($)	Option Expiration Date
Charles E. Harris	8,820	9,891[1]	$10.11	June 26, 2016
	451,530	230,000[1]	$10.11	June 26, 2016
	20,000	0	$10.11	June 26, 2008
	0	26,666[2]	$10.11	June 26, 2009
	120,491	120,490[3]	$11.11	June 26, 2016
Douglas W. Jamison	8,647	69,237[4]	$10.11	June 26, 2016
	138,200	0	$10.11	June 26, 2008
	53,334	106,666[2]	$10.11	June 26, 2009
	47,500	0	$11.11	Dec. 27, 2008
	0	110,135[3]	$11.11	Dec. 27, 2009
	0	92,365[5]	$11.11	Dec. 27, 2010
Alexei A. Andreev	12,735	69,237[4]	$10.11	June 26, 2016
	157,359	0	$10.11	June 26, 2008
	53,334	106,666[2]	$10.11	June 26, 2009
	38,000	0	$11.11	Dec. 27, 2008
	0	88,108[3]	$11.11	Dec. 27, 2009
	0	73,892[5]	$11.11	Dec. 27, 2010

Michael A. Janse	9,891 228,000 0 0	69,237(6) 0 248,108(3) 73,892(5)	\$11.11 \$11.11 \$11.11 \$11.11	June 26, 2016 Dec. 27, 2008 Dec. 27, 2009 Dec. 27, 2010
Sandra M. Forman	12,600 55,000 25,000 26,600 0 0	69,237(4) 0 50,000(2) 0 61,676(3) 46,724(5)	\$10.11 \$10.11 \$10.11 \$11.11 \$11.11 \$11.11	June 26, 2016 June 26, 2008 June 26, 2009 Dec. 27, 2008 Dec. 27, 2009 Dec. 27, 2010

(1) Options vest 100 percent on June 26, 2008.
(2) Options vest in two equal installments on June 26, 2008, and December 26, 2008.
(3) Options vest 100 percent on December 27, 2008.
(4) Options vest in seven equal installments on June 26, 2008, June 26, 2009, June 26, 2010, June 26, 2011, June 26, 2012, June 26, 2013, and June 26, 2014.
(5) Options vest 100 percent on December 27, 2009.
(6) Options vest in seven equal installments on June 27, 2008, June 27, 2009, June 27, 2010, June 27, 2011, June 27, 2012, June 27, 2013, and June 27, 2014.

2007 Option Exercises and Stock Vested

The following table presents information regarding the exercises of stock options by named executive officers for the fiscal year ended December 31, 2007.

	Option Awards	
Name	Number of Shares Acquired on Exercise (#)	Value Realized on Exercise ($)
Charles E. Harris	192,466	244,291
Douglas W. Jamison	199,048	359,391
Alexei A. Andreev	185,040	343,632
Michael A. Janse	0	0
Sandra M. Forman	121,834	210,136

2007 Pension Benefits

The following table presents information about the pension benefits attributable to the named executive officers as of December 31, 2007, and any pension benefit payments to them during 2007.

Name	Plan Name	Number of Years Credited Service (#)	Present Value of Accumulated Benefits ($)	Payments During Last Fiscal Year ($)
Charles E. Harris	Executive Mandatory Retirement Plan	24	147,302	0
Douglas W. Jamison	Executive Mandatory Retirement Plan	3	0	0

The present value of accumulated benefits amount reported in the table above was calculated pursuant to FAS 87, "Employers' Accounting for Pensions" and FAS 158, "Employers' Accounting for Pensions and Other Postretirement Plans - an amendment of FASB Statements No. 87, 88, 106, and 132(R)." Several statistical and other factors that attempt to anticipate future events are used in calculating the expense and liability values related to our pension plan. These factors include a discount rate assumption of 5.75 percent and use of the 94GAM mortality table. The calculation also assumes that the benefit is earned uniformly over the employees' careers. Any benefit attributable to service prior to the effective date of the plan is amortized over each person's future working lifetime.

Executive Mandatory Retirement Benefit Plan

On March 20, 2003, in order to begin planning for eventual management succession, the Board of Directors voted to establish the Executive Mandatory Retirement Benefit Plan for individuals who are employed by us in a bona fide executive or high policy-making position. The plan was amended and restated effective January 1, 2005, to comply with certain provisions of the Internal Revenue Code. There are currently four individuals that qualify under the plan: Charles E. Harris, the Chairman and Chief Executive Officer, Douglas W. Jamison, the President and Chief Operating Officer, Daniel B. Wolfe, the Chief Financial Officer, and Mel P. Melsheimer, the former President, Chief Operating Officer and Chief Financial Officer. Under this plan, mandatory retirement takes place effective December 31 of the year in which the eligible individuals attain the age of 65. On an annual basis beginning in the year in which the designated individual attains the age of 65, a committee of the Board consisting of non-interested directors may determine for our benefit to postpone the mandatory retirement date for that individual for one additional year.

Under applicable law prohibiting discrimination in employment on the basis of age, we can impose a mandatory retirement age of 65 for our executives or employees in high policy-making positions only if each employee subject to the mandatory retirement age is entitled to an immediate retirement benefit at retirement age of at least $44,000 per year. The benefits payable at retirement to Mr. Harris and Mr. Melsheimer under our existing 401(k) plan do not equal this threshold. The plan was established to provide the difference between the benefit required under the age discrimination laws and that provided under our existing plans. For individuals retiring after 2007, the benefit under the plan is paid to the qualifying individual in the form of a lump sum, and is paid six months and one day after the individual's separation from service with the Company, pursuant to certain exceptions. Mr. Harris's projected mandatory benefit will be approximately $147,302 and paid as a lump sum six months and one day after his expected retirement on December 31, 2008.

2007 Non-Qualified Deferred Compensation

The following table presents information regarding the Company's Amended and Restated Supplemental Executive Retirement Plan for the fiscal year ended December 31, 2007. Other than for Mr. Harris, we do not maintain any pension or non-qualified pension benefits except as disclosed in "Executive Mandatory Retirement" above.

Name	Executive Contributions in Last FY ($)	Registrant Contribution in Last FY ($)(1)	Aggregate Earnings in Last FY ($)	Aggregate Withdrawals/ Distributions ($)	Aggregate Balance at Last FYE ($)
Charles E. Harris	0	306,187	210,533	0	2,667,020

(1) This amount is included in the Summary Compensation Table under "All Other Compensation."

SERP

The Employment Agreement provides that we adopt a supplemental executive retirement plan (the "SERP") for the benefit of Mr. Harris. Under the SERP, we will cause an amount equal to one-twelfth of Mr. Harris's current annual salary to be credited each month (a "Monthly Credit") to a special account maintained on our books for the benefit of Mr. Harris (the "SERP Account"), provided that Mr. Harris is employed by us on the last business day of such month. The amounts credited to the SERP Account are deemed invested or reinvested in such investments as are requested by Mr. Harris and agreed to by the Company. The SERP Account is credited and debited to reflect the deemed investment returns, losses and expenses attributed to such deemed investments and reinvestments in accordance with the terms of the SERP. Mr. Harris's benefit under the SERP equals the balance in the SERP Account and such benefit will always be 100 percent vested (i.e., not forfeitable).

In 2005, Mr. Harris received a $125,000 distribution from the SERP Account. The balance of the SERP Account will be paid in a lump sum on May 30, 2008, and any subsequent balance attributable to subsequent monthly credits will be paid on July 31, 2009.

If Mr. Harris dies before the entire benefit under the SERP Account has been paid to him, the amount remaining in the SERP Account will be distributed to his beneficiary in a lump-sum payment on the 90th day after the date of his death.

Potential Payments upon Termination or Change in Control

Other than Mr. Harris, our Chairman and Chief Executive Officer, none of our executive officers has a change in control agreement or is entitled to any special payments solely upon a change in control.

In the event of termination without cause or by constructive discharge, Mr. Harris's Employment Agreement provides for the continuation of certain benefits over specified periods, as well as severance pay, payable to Mr. Harris (or to his estate if he dies before all payments are made), equal to two times his base salary distributed over a period of two years.

In addition, Mr. Harris is entitled to receive severance pay pursuant to the severance compensation agreement that he entered into with us, effective August 15, 1990, as amended and restated effective as of January 1, 2005. The severance compensation agreement provides that if, following a change in our control, as defined in the agreement, Mr. Harris's employment is terminated by us without cause or by him within one year of such change in control, he shall be entitled to receive compensation in a lump sum payment equal to 2.99 times his average base salary plus other amounts included in Mr. Harris's income as compensation from the Company (but excluding bonus, incentive, profit-sharing plan and equity compensation) as in effect over the most recent five years preceding the year in which the change in control occurred. Under the severance compensation agreement, Mr. Harris is also entitled to receive a lump-sum payment equal to any amounts forfeited on account of his termination, under any employee pension benefit plan, including benefits under the Company's executive mandatory retirement benefit plan. In addition, he is entitled to receive medical and health insurance coverage under the Company's retiree medical benefit plan and all other benefits he would be eligible to receive in the event of termination without cause or by constructive discharge, although no duplicate benefits will be provided. In the event that Mr. Harris is entitled to receive 2.99 times his base salary under the severance compensation agreement, he shall not also be paid two times his base salary under the employment agreement.

On June 30, 1994, we adopted the Medical Benefit Retirement Plan. On February 10, 1997, we amended this plan to include employees who have seven full years of service and have attained 58 years of age. On November 3, 2005, we amended this plan to reverse the 1997 amendment for future retirees and to remove dependents other than spouses from the plan. The coverage is secondary to any government or subsequent employer-provided health-insurance plans. The annual premium cost to us with respect to the entitled retiree shall not exceed $12,000, subject to an index for inflation. As of December 31, 2007, and 2006, we had liabilities of $913,904 and $791,972, respectively, for the plan; there are no plan assets.

The options of retirees who qualify for the Medical Benefit Retirement Plan will remain exercisable (to the extent exercisable at the time of the optionee's termination) post retirement, subject to certain conditions, if such retiree executes a post-termination non-solicitation agreement, in a form reasonably acceptable to the Company, until the expiration of its term.

The following chart sets forth amounts that would have been payable to Mr. Harris had he realized a qualifying termination of employment under his severance agreement or Employment Agreement, determined as if the triggering event had occurred on December 31, 2007. Other than Mr. Harris, we do not maintain any established severance plan for our employees. Due to the number of factors that affect the calculations in the table, actual amounts paid or distributed may be different.

Termination Scenarios

Charles E. Harris	Termination Following Change of Control ($)	Termination Without Cause or Constructive Discharge ($)	Termination for Cause ($)	Mandatory Retirement ($)	Voluntary Termination ($)	Death ($)	Disability ($)
Lump Sum Salary Payments	885,434	612,374	0	0	0	612,374	0
Medical Insurance Benefits	194,423	194,423	0	194,423	194,423	194,423	194,423
Pension Benefits	147,302	0	0	147,302	0	0	0
All Other Perqs.	146,101	146,101	0	0	0	0	373,256
SERP Payments	2,667,020	2,667,020	2,667,020	2,667,020	2,667,020	2,667,020	2,667,020
Total	4,040,280	3,619,918	2,667,020	3,008,745	2,861,443	3,473,817	3,234,699

In addition, pursuant to his stock option agreements, if Mr. Harris voluntarily terminates his employment and executes a post-termination non-solicitation agreement and a post-termination three-year non-compete agreement in forms reasonably acceptable to the Company, his options (to the extent exercisable at the time of his termination) will remain exercisable until the expiration of their terms. If Mr. Harris's employment terminates under any of the other termination scenarios outlined in the table immediately above, his options will remain exercisable for periods ranging from zero to one year, depending on the type of option and termination scenario. Mr. Harris's exercisable options as of December 31, 2007 are reflected in the table "2007 Outstanding Equity Awards at Fiscal Year-End."

Remuneration of Directors

The following table sets forth the compensation paid by us to our directors for the fiscal year ended December 31, 2007. During 2007, we did not grant any stock option awards or pay or accrue any pension or retirement benefits for our directors.

2007 Director Compensation

Name of Director	Fees Earned or Paid in Cash ($)	All Other Compensation ($)	Total ($)
Independent Directors:			
W. Dillaway Ayres, Jr.	42,000	0	42,000
Dr. C. Wayne Bardin	42,000	0	42,000
Dr. Phillip A. Bauman	45,000	0	45,000
G. Morgan Browne	45,000	0	45,000
Dugald A. Fletcher	57,000	0	57,000
Mark A. Parsells(1)	18,823	0	18,823
Charles E. Ramsey	42,000	0	42,000
James E. Roberts	47,250	0	47,250
Richard P. Shanley	29,710	0	29,710
Interested Directors:			
Charles E. Harris(2)	0	0	0
Douglas W. Jamison(2)	0	0	0
Kelly S. Kirkpatrick(3)	22,500	7,500(4)	30,000
Lori D. Pressman	24,000	35,938(5)	59,938

(1) Mark A. Parsells did not stand for re-election at the Annual Meeting held on May 3, 2007.

(2) Mr. Harris and Mr. Jamison do not receive additional compensation as Directors. Refer to the "2007 Summary Compensation Table" for details of Mr. Harris's and Mr. Jamison’s compensation for 2007.

(3) Ms. Kirkpatrick did not stand for re-election at the Annual Meeting of Shareholders held on May 1, 2008.

(4) Represents $7,500 for consulting services. Ms. Kirkpatrick may be considered an "interested person" because of consulting work performed for us.

(5) Represents $35,938 for consulting services. Ms. Pressman may be considered an "interested person" because of consulting work performed for us.

There are no outstanding option awards to directors.

The directors who are not officers receive $1,500 for each meeting of the Board of Directors and $1,500 for each committee meeting they attend, and a monthly retainer of $750. Each non-employee committee Chairman receives an additional monthly retainer of $250. The Lead Independent Director receives an additional monthly retainer of $500. We also reimburse our directors for travel, lodging and related expenses they incur in attending Board and committee meetings. The total compensation and reimbursement for expenses paid or payable to all directors in 2007 was $468,497.

The Board of Directors has adopted a policy that 50 percent of all director fees must be used to purchase our common stock. In 2007, the directors collectively bought 26,555 shares in the open market.

OTHER INFORMATION

We are not subject to any material pending or, to our knowledge, threatened legal proceedings.

Our custodian is J.P. Morgan Chase Bank, 345 Park Avenue, New York, New York 10154-1002.

Our transfer and dividend-paying agent is American Stock Transfer & Trust Company, 59 Maiden Lane, New York, NY 10038.

Our independent registered public accounting firm is PricewaterhouseCoopers LLP, 300 Madison Avenue, New York, NY 10017. It also provides tax return preparation services for us.

BROKERAGE

In 2005, we paid $48,732 in brokerage commissions for the sale of our shares in NeuroMetrix, Inc. We did not effect any transactions in portfolio securities in 2007 or 2006 except for the purchase and sale of treasury securities, for which we do not pay any brokerage commissions. Brokers are selected on the basis of our best judgment as to which brokers are most likely to be in contact with likely buyers of the thinly traded securities of our portfolio companies. We will also consider the competitiveness of such broker’s commission rates. We might pay a premium for a broker’s knowledge of the potential buyers.

DIVIDENDS AND DISTRIBUTIONS

As a regulated investment company under the Code, we will not be subject to U.S. federal income tax on our investment company taxable income that we distribute to shareholders, provided that at least 90 percent of our investment company taxable income for that taxable year is distributed to our shareholders. We currently intend to retain our net capital gains for investment and pay the associated federal corporate income tax. We may change this policy in the future.

To the extent that we retain any net capital gain, we may pay deemed capital gain dividends to shareholders. If we do pay a deemed capital gain dividend, you will not receive a cash distribution, but instead you will receive a tax credit equal to your proportionate share of the tax paid by us. When we declare a deemed dividend, our dividend-paying agent will send you an IRS Form 2439 which will reflect receipt of the deemed dividend income and the tax credit. This tax credit, which we pay at the applicable corporate rate, is normally at a higher rate than the rate payable by individual shareholders on the deemed dividend income. The excess credit can be used by the shareholder to offset other taxes due in that year or to generate a tax refund to the shareholder. In addition, each shareholder’s tax basis in his shares of Common Stock is increased by the excess of the capital gain on which we paid taxes over the amount of taxes we paid. See "Taxation."

We did not pay a cash dividend or declare a deemed capital gain dividend for 2007.

TAXATION

Taxation of the Company

We have elected and qualified and intend to continue to qualify to be taxed as a regulated investment company under Subchapter M of the Code. Accordingly, we must, among other things, (a) derive in each taxable year at least 90 percent of our gross income (including tax-exempt interest) from dividends, interest, payments with respect to certain securities loans, and gains from the sale or other disposition of stock, securities or foreign currencies, or other income (including but not limited to gain from options, futures and forward contracts) derived with respect to our business of investing in stock, securities or currencies; (b) diversify our holdings so that, at the end of each fiscal quarter (i) at least 50 percent of the market value of our total assets is represented by cash and cash items, U.S. government securities, the securities of other regulated investment companies and other securities, with other securities limited, in respect of any one issuer, to an amount not greater than five percent of the value of our total assets and not more than 10 percent of the outstanding voting securities of any issuer (subject to the exception described below), and (ii) not more than 25 percent of the market value of our total assets is invested in the securities of any issuer (other than U.S. government securities and the securities of other regulated investment companies) or of any two or more issuers that we control and that are determined to be engaged in the same business or similar or related trades or businesses, and (c) annually distribute at least 90 percent of our investment company taxable income as a dividend.

In the case of a regulated investment company which furnishes capital to development corporations, there is an exception to the rule relating to the diversification of investments described above. This exception is available only to registered management investment companies which the SEC determines to be principally engaged in the furnishing of capital to other corporations which are principally engaged in the development or exploitation of inventions, technological improvements, new processes, or products not previously generally available ("SEC Certification"). We have received SEC Certification since 1999, including for 2006, but it is possible that we may not receive SEC Certification in future years. Pursuant to the SEC Certification, we are generally entitled to include, in the computation of the 50 percent value of our assets (described in (b)(i) above), the value of any securities of an issuer, whether or not we own more than 10 percent of the outstanding voting securities of the issuer, if the basis of the securities, when added to our basis of any other securities of the issuer that we own, does not exceed five percent of the value of our total assets.

As a regulated investment company, in any fiscal year with respect to which we distribute at least 90 percent of the sum of our (i) investment company taxable income (which includes, among other items, dividends, interest and the excess of any net short-term capital gains over net long-term capital losses and other taxable income other than any net capital gain reduced by deductible expenses) determined without regard to the deduction for dividends paid and (ii) net tax exempt interest (the excess of its gross tax exempt interest over certain disallowed deductions), we (but not our shareholders) generally will not be subject to U.S. federal income tax on investment company taxable income and net capital gains that we distribute to shareholders. To the extent that we retain our net capital gains for investment, we will be subject to U.S. federal income tax. We currently intend to retain our net capital gains for investment and pay the associated federal corporate income tax. We may change this policy in the future.

Amounts not distributed on a timely basis in accordance with a calendar year distribution requirement are subject to a nondeductible four percent excise tax payable by us. To avoid this tax, we must distribute (or be deemed to have distributed) during each calendar year an amount equal to the sum of:

(1) at least 98 percent of our ordinary income (not taking into account any capital gains or losses) for the calendar year;

(2) at least 98 percent of our capital gains in excess of our capital losses (adjusted for certain ordinary losses) for a one-year period generally ending on October 31 of the calendar year (unless an election is made by a company with a November or December year-end to use the company's fiscal year); and

(3) any undistributed amounts from previous years on which we paid no U.S. federal income tax.

While we intend to distribute any income and capital gains in the manner necessary to minimize imposition of the four percent excise tax, sufficient amounts of our taxable income and capital gains may not be distributed to avoid entirely the imposition of the tax. In that event, we will be liable for the tax only on the amount by which we do not meet the foregoing distribution requirement.

If in any particular taxable year, we do not qualify as a regulated investment company, all of our taxable income (including its net capital gains) will be subject to tax at regular corporate rates without any deduction for distributions to shareholders, and distributions will be taxable to the shareholders as ordinary dividends to the extent of our current and accumulated earnings and profits.

We may decide to be taxed as a corporation even if we would otherwise qualify as a regulated investment company.

Company Investments

We may make certain investments which would subject us to special provisions of the Code that, among other things, may affect the character of the gains or losses realized by us and require us to recognize income or gain without receiving cash with which to make distributions.

In the event we invest in foreign securities, we may be subject to withholding and other foreign taxes with respect to those securities. We do not expect to satisfy the requirement to pass through to the shareholders their share of the foreign taxes paid by us.

Due to our expected investments, in general, distributions will not be eligible for the dividends received deduction allowed to corporate shareholders and will not qualify for the reduced rate of tax for qualified dividend income allowed to individuals.

Taxation of Shareholders

Distributions we pay to you from our ordinary income or from an excess of net short-term capital gains over net long-term capital losses (together referred to hereinafter as "ordinary income dividends") are taxable to you as ordinary income to the extent of our earnings and profits. Distributions made to you from an excess of net long-term capital gains over net short-term capital losses ("capital gain dividends"), including capital gain dividends credited to you but retained by us, are taxable to you as long-term capital gains, regardless of the length of time you have owned our shares. Distributions in excess of our earnings and profits will first reduce the adjusted tax basis of your shares and, after the adjusted tax basis is reduced to zero, will constitute capital gains to you (assuming the shares are held as a capital asset). Generally, you will be provided with a written notice designating the amount of any (i) ordinary income dividends no later than 30 days after the close of the taxable year, and (ii) capital gain dividends or other distributions no later than 60 days after the close of the taxable year.

In the event that we retain any net capital gains, we may designate the retained amounts as undistributed capital gains in a notice to our shareholders. If a designation is made, shareholders would include in income, as long-term capital gains, their proportionate share of the undistributed amounts, but would be allowed a credit or refund, as the case may be, for their proportionate share of the corporate tax paid by us. In addition, the tax basis of shares owned by a shareholder would be increased by an amount equal to the difference between (i) the amount included in the shareholder's income as long-term capital gains and (ii) the shareholder's proportionate share of the corporate tax paid by us. Shareholders should consult their tax advisors for further information about the impact of a deemed dividend on their state or local taxes.

Dividends and other taxable distributions are taxable to you even though they are reinvested in additional shares of our Common Stock. If we pay you a dividend in January which was declared in the previous October, November or December to shareholders of record on a specified date in one of these months, then the dividend will be treated for tax purposes as being paid by us and received by you on December 31 of the year in which the dividend was declared.

A shareholder will realize gain or loss on the sale or exchange of our common shares in an amount equal to the difference between the shareholder's adjusted basis in the shares sold or exchanged and the amount realized on their disposition. Generally, gain recognized by a shareholder on the sale or other disposition of our common shares will result in capital gain or loss to you, and will be a long-term capital gain or loss if the shares have been held for more than one year at the time of sale. Any loss upon the sale or exchange of our shares held for six months or less will be treated as a long-term capital loss to the extent of any capital gain dividends received (including amounts credited as an undistributed capital gain dividend) by you. A loss realized on a sale or exchange of our shares will be disallowed if other substantially identical shares are acquired (whether through the automatic reinvestment of dividends or otherwise) within a 61-day period beginning 30 days before and ending 30 days after the date that the shares are disposed of. In this case, the basis of the shares acquired will be adjusted to reflect the disallowed loss.

In general, federal withholding taxes at a 30 percent rate (or a lower rate pursuant to a tax treaty) will apply to distributions to shareholders (except to those distributions designated by us as capital gain dividends) that are nonresident aliens or foreign partnerships, trusts or corporations (a "non-U.S. investor"). Different tax consequences may result if a non-U.S. investor is engaged in a trade or business in the United States or, in the case of an individual, is present in the United States for 183 or more days during a taxable year and certain other conditions are met.

Backup Withholding

We are required in some circumstances to backup withholding on taxable dividends and other payments paid to non-corporate holders of our shares who do not furnish us with their correct taxpayer identification number and certifications, or who are otherwise subject to backup withholding. Backup withholding is not an additional tax. Any amounts withheld from payments made to you may be refunded or credited against your U.S. federal income tax liability, if any, provided that the required information is furnished to the Internal Revenue Service.

The foregoing is a general discussion of the provisions of the Code and the Treasury regulations in effect as they directly govern our taxation and our shareholders. These provisions are subject to change by legislative or administrative action, and any change may be retroactive. The discussion does not purport to deal with all of the U.S. federal income tax consequences applicable to us, or which may be important to particular shareholders in light of their individual investment circumstances or to some types of shareholders subject to special tax rules, such as financial institutions, broker-dealers, insurance companies, tax-exempt organizations, partnerships or other pass-through entities, persons holding notes in connection with a hedging, straddle, conversion or other integrated transaction, persons engaged in a trade or business in the United States or persons who have ceased to be U.S. citizens or to be taxed as resident aliens. Shareholders are urged to consult their tax advisers regarding specific questions as to U.S. federal, foreign, state and local income or other taxes.

CERTAIN GOVERNMENT REGULATIONS

A business development company is regulated by the 1940 Act. A business development company must be organized in the United States for the purpose of investing primarily in companies that are organized in the United States and engaged primarily in businesses other than certain financial businesses and that either do not have any securities listed on a national securities exchange or are controlled by the business development company. In addition, the business development company must make managerial assistance available to these portfolio companies. A business development company may use capital provided by public shareholders and from other sources to invest in what are usually private investments. A business development company provides shareholders the ability to retain the liquidity of a publicly traded stock, while sharing in the possible benefits, if any, of investing primarily in what are usually privately owned companies.

As a business development company, we may not acquire any assets other than "qualifying assets" unless, at the time we make the acquisition, the value of our qualifying assets represents at least 70 percent of the value of our total assets. The principal categories of qualifying assets relevant to our business are:

- securities purchased in transactions not involving any public offering, the issuer of which is an eligible portfolio company;
- securities received in exchange for or distributed with respect to securities described in the bullet above or pursuant to the exercise of options, warrants or rights relating to the securities; and
- cash, cash items, government securities or high quality debt securities (within the meaning of the 1940 Act), maturing in one year or less from the time of investment.

An eligible portfolio company is generally a domestic company that is not an investment company (other than a small business investment company wholly owned by a business development company) and is not engaged primarily in certain financial businesses and that:

- does not have a class of securities registered on a national securities exchange;

- is actively controlled by the business development company and has an affiliate of a business development company on its Board of Directors; or

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· meets other criteria as may be established by the SEC.

Control under the 1940 Act is presumed to exist where a business development company beneficially owns more than 25 percent of the outstanding voting securities of the portfolio company.

To include securities described above as qualifying assets for the purpose of the 70 percent test, a business development company must make available to the issuer of those securities (whether directly or through cooperating parties) significant managerial assistance such as providing significant guidance and counsel concerning the management, operations or business objectives and policies of a portfolio company. We offer to provide managerial assistance to each of our portfolio companies.

As a business development company, we are entitled to issue senior securities in the form of stock or indebtedness, including bank borrowings and debt securities, as long as our senior securities have an asset coverage of at least 200 percent immediately after each issuance. See "Risk Factors."

We may also be prohibited under the 1940 Act from knowingly participating in certain transactions with our affiliates without the prior approval of members of our Board of Directors who are not interested persons and, in some cases, may have to seek prior approval from the SEC.

As with other companies regulated by the 1940 Act, a business development company must adhere to substantive regulatory requirements. A majority of our directors must be persons who are not interested persons, as that term is defined in the 1940 Act. Additionally, we are required to provide and maintain a bond issued by a reputable fidelity insurance company to protect us against larceny and embezzlement. Furthermore, as a business development company, we are prohibited from protecting any director or officer against any liability to us or our shareholders arising from willful malfeasance, bad faith, gross negligence or reckless disregard of the duties involved in the conduct of that person’s office.

We maintain a code of ethics under Rule 17j-1 of the 1940 Act that establishes procedures for personal investment and restricts some transactions by our personnel. Our code of ethics generally does not permit investment by our employees in private securities that may be purchased or held by us. The code of ethics is filed as an exhibit to our registration statement of which this Prospectus is a part. You may read and copy the code of ethics at the SEC’s Public Reference Room in Washington, D.C. You may obtain information on operations of the Public Reference Room by calling the SEC at (800) SEC-0330. In addition, the code of ethics is available on the EDGAR Database on the SEC Internet site at http://www.sec.gov. You may obtain copies of the code of ethics, after paying a duplicating fee, by electronic request at the following email address: publicinfo@sec.gov, or by writing to the SEC’s Public Reference Section, 100 F Street, N.E., Washington, D.C. 20549.

We may not change the nature of our business so as to cease to be, or withdraw our election as, a business development company unless authorized by vote of a majority of the outstanding voting securities, voting on the matter at a meeting at which a quorum is present.

We vote proxies relating to our portfolio securities in what management believes is in the best interest of our shareholders. We carefully review on a case by case basis each proposal submitted to a shareholder vote to determine its impact on the portfolio securities held by us. Although we generally vote against proposals that may have a negative impact on our portfolio securities, we may vote for such a proposal if there exists a compelling long-term reason to do so.

Our proxy voting decisions are made by the Managing Directors who are responsible for monitoring each of our investments. To ensure that our vote is not the product of a conflict of interest, we required that: (i) anyone involved in the decision-making process disclose to our Chief Compliance Officer any potential conflict that he or she is aware of and any contact that he or she has had with any interested party regarding a proxy vote; and (ii) employees involved in the decision-making process or vote administration are prohibited from revealing how we intend to vote on a proposal in order to reduce any attempted influence from interested parties.

Shareholders may obtain information regarding how we voted proxies with respect to our public portfolio companies by making a written request for proxy voting information or by contacting us by telephone at 1-877-TINY-TECH.

CAPITALIZATION

We are authorized to issue 45,000,000 shares of Common Stock, par value $0.01 per share, and 2,000,000 shares of preferred stock, par value $0.10 per share. Each share within a particular class or series thereof has equal voting, dividend, distribution and liquidation rights. When issued, in accordance with the terms thereof, shares of Common Stock will be fully paid and non-assessable. Shares of Common Stock are not redeemable and have no preemptive, conversion, or cumulative voting rights.

The following table shows the number of shares of (i) capital stock authorized, (ii) the amount held by us or for our own account, and (iii) capital stock outstanding for each class of our authorized securities as of May 28, 2008.

Title of Class	Amount Authorized	Amount Held by Company or for its Own Account	Amount Outstanding
Common Stock	45,000,000	1,828,740	23,314,573
Preferred Stock	2,000,000	0	0

Issuance of Preferred Stock

Our Board of Directors is authorized by our articles of incorporation to issue up to 2,000,000 shares of preferred stock having a par value of $0.10 per share. The Board of Directors is authorized to divide the preferred stock into one or more series and to determine the terms of each series, including, but not limited to, the voting rights, redemption provisions, dividend rate and liquidation preference. Any terms must be consistent with the requirements of the 1940 Act. The 1940 Act currently prohibits us from issuing any preferred stock if after giving effect to the issuance the value of our total assets, less all liabilities and indebtedness other than senior securities, would be less than 200 percent of the aggregate amount of senior securities representing indebtedness plus the aggregate involuntary liquidation value of our preferred stock (other than up to 5 percent borrowings for temporary purposes). Leveraging with preferred stock raises the same general potential for loss or gain and other risks as does leveraging with borrowings described above.

Options and Warrants

We have no warrants outstanding. As of May 28, 2008, we had 4,315,776 options outstanding, which were granted pursuant to our Equity Incentive Plan described herein. Under the 1940 Act, we cannot issue options and/or warrants for more than 25 percent of our outstanding voting securities.

PLAN OF DISTRIBUTION

We may sell our Common Stock through underwriters or dealers, directly to one or more purchasers through agents or through a combination of any such methods of sale. Any underwriter or agent involved in the offer and sale of our Common Stock will be named in the applicable Prospectus Supplement.

The distribution of our Common Stock may be effected from time to time in one or more transactions at a fixed price or prices, which may be changed, at prevailing market prices at the time of sale, at prices related to such prevailing market prices, or at negotiated prices, provided, however, that the offering price per share must equal or exceed the net asset value per share of our Common Stock exclusive of any underwriting commissions or discounts.

In connection with the sale of our Common Stock, underwriters or agents may receive compensation from us in the form of discounts, concessions or commissions. Underwriters may sell our Common Stock to or through dealers, and such dealers may receive compensation in the form of discounts, concessions or commissions from the underwriters and/or commissions from the purchasers for whom they may act as agents. Underwriters, dealers and agents that participate in the distribution of our Common Stock may be deemed to be underwriters under the Securities Act of 1933, and any discounts and commissions they receive from us and any profit realized by them on the resale of our Common Stock may be deemed to be underwriting discounts and commissions under the Securities Act of 1933. Any such underwriter or agent will be identified and any such compensation received from us will be described in the applicable Prospectus Supplement. The maximum commission or discount to be received by any NASD member or independent broker-dealer will not exceed eight percent. We will not pay any compensation to any underwriter or agent in the form of warrants, options, consulting or structuring fees or similar arrangements.

Any Common Stock sold pursuant to a Prospectus Supplement will be listed on the Nasdaq Global Market.

Under agreements into which we may enter, underwriters, dealers and agents who participate in the distribution of our Common Stock may be entitled to indemnification by us against certain liabilities, including liabilities under the Securities Act of 1933. Underwriters, dealers and agents may engage in transactions with us, or perform services for us, in the ordinary course of business.

If so indicated in the applicable Prospectus Supplement, we will authorize underwriters or other persons acting as our agents to solicit offers by certain institutions to purchase our Common Stock from us pursuant to contracts providing for payment and delivery on a future date. Institutions with which such contacts may be made include commercial and savings banks, insurance companies, pension funds, investment companies, educational and charitable institutions and others, but in all cases such institutions must be approved by us. The obligations of any purchaser under any such contract will be subject to the condition that the purchase of the Common Stock shall not at the time of delivery be prohibited under the laws of the jurisdiction to which such purchaser is subject. The underwriters and such other agents will not have any responsibility in respect of the validity or performance of such contracts. Such contracts will be subject only to those conditions set forth in the Prospectus Supplement, and the Prospectus Supplement will set forth the commission payable for solicitation of such contracts.

In order to comply with the securities laws of certain states, if applicable, our Common Stock offered hereby will be sold in such jurisdictions only through registered or licensed brokers or dealers.

LEGAL MATTERS

Certain legal matters will be passed on by Skadden, Arps, Slate, Meagher & Flom LLP, New York, New York, our special counsel in connection with the offering of Common Stock.

EXPERTS

Our audited financial statements as of December 31, 2007 and 2006 and for each of the three years in the period ended December 31, 2007 are included in this Registration Statement in reliance on the report of PricewaterhouseCoopers LLP, independent registered public accounting firm, given on the authority of that firm as experts in accounting and auditing. PricewaterhouseCoopers LLP is located at 300 Madison Avenue, New York, New York 10017.

We will furnish, without charge, a copy of such financial statements upon request by writing to 111 West 57th Street, Suite 1100, New York, New York 10019, Attention: Investor Relations, or calling 1-800-TINY-TECH.

FURTHER INFORMATION

We are subject to the informational requirements of the 1934 Act and in accordance therewith file reports, proxy statements and other information with the SEC. The reports, proxy statements and other information filed by us can be inspected and copied at public reference facilities maintained by the SEC at 100 F Street, N.E., Washington, D.C. 20549, its New York Regional Office, 3 World Financial Center, Suite 400, New York, New York 10281 and its Chicago Regional Office, 175 West Jackson Boulevard, Suite 900, Chicago, Illinois 60604. You can obtain information on the operation of the Public Reference room by calling the SEC at (800) SEC-0330. The SEC also maintains a website that contains reports, proxy statements, and other information. The address of the SEC's website is http://www.sec.gov. Copies of this material may also be obtained from the Public Reference Branch, Office of Consumer Affairs and Information Services of the SEC at 100 F Street, N.E., Washington, D.C. 20549, at prescribed rates.

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PRIVACY POLICY

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

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

We restrict access to non-public personal information about our shareholders to our employees and to employees of our service providers and their affiliates with a legitimate business need for the information. We maintain physical, electronic and procedural safeguards designed to protect the non-public personal information of our shareholders.

CONSOLIDATED FINANCIAL STATEMENTS

HARRIS & HARRIS GROUP, INC.
INDEX TO CONSOLIDATED FINANCIAL STATEMENTS AND SCHEDULES

Documents

Management's Report on Internal Control Over Financial Reporting

Management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934 as a process designed by, or under the supervision of, the Company's principal executive and principal financial officers and effected by the Company's Board of Directors, management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

- pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Company;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the Company; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

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

Management has assessed the effectiveness of our internal control over financial reporting as of December 31, 2007. In making its assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control-Integrated Framework. Based on the results of this assessment, management (including our Chief Executive Officer and Chief Financial Officer) has concluded that, as of December 31, 2007, the Company's internal control over financial reporting was effective.

The effectiveness of the Company's internal control over financial reporting has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report which appears on page F-3 of this Registration Statement.

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of Harris & Harris Group, Inc.:

In our opinion, the accompanying consolidated statements of assets and liabilities including the consolidated schedules of investments, and the related consolidated statements of operations, changes in net assets, cash flows, and the financial highlights present fairly, in all material respects, the financial position of Harris & Harris Group, Inc. and its subsidiaries ("the Company") at December 31, 2007 and December 31, 2006, and the results of their operations, their cash flows, the changes in their net assets, and the financial highlights for each of the three years in the period ended December 31, 2007, in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in Management's Report on Internal Control over Financial Reporting appearing on page 52 of the 2007 Annual Report to Shareholders. Our responsibility is to express opinions on these financial statements and on the Company's internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

As more fully disclosed in Note 2 of the Notes to Consolidated Financial Statements, the financial statements include investments valued at $78,110,384 (56.5% of net assets) at December 31, 2007, the fair values of which have been estimated by the Board of Directors in the absence of readily ascertainable market values. These estimated values may differ significantly from the values that would have been used had a ready market for the investments existed, and the differences could be material.

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

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

/s/ PricewaterhouseCoopers LLP
New York, New York
March 12, 2008

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HARRIS & HARRIS GROUP, INC.
CONSOLIDATED STATEMENTS OF ASSETS AND LIABILITIES

ASSETS

	December 31, 2007		December 31, 2006	
Investments, at value (Cost: $142,230,461 at 12/31/07, $121,331,398 at 12/31/06)	$	138,303,977	$	112,323,978
Cash and cash equivalents		330,009		2,071,788
Restricted funds (Note 7)		2,667,020		2,149,785
Receivable from portfolio company		524		0
Receivable from broker (Note 4)		0		819,905
Interest receivable		647,337		625,372
Prepaid expenses		488,667		10,945
Other assets		455,798		326,817
Total assets	$	142,893,332	$	118,328,590

LIABILITIES & NET ASSETS

Accounts payable and accrued liabilities (Note 7)	$	4,515,463	$	4,115,300
Accrued profit sharing (Note 5)		0		261,661
Deferred rent		14,525		21,326
Total liabilities		4,529,988		4,398,287
Net assets	$	138,363,344	$	113,930,303
Net assets are comprised of: Preferred stock, $0.10 par value, 2,000,000 shares authorized; none issued	$	0	$	0
Common stock, $0.01 par value, 45,000,000 shares authorized at 12/31/07 and 12/31/06; 25,143,313 issued at 12/31/07 and 22,843,757 issued at 12/31/06		251,434		228,438
Additional paid in capital (Note 10)		160,927,691		129,801,201
Accumulated net realized loss		(15,483,766)		(3,686,385)
Accumulated unrealized depreciation of investments		(3,926,484)		(9,007,420)
Treasury stock, at cost (1,828,740 shares at 12/31/07 and 12/31/06)		(3,405,531)		(3,405,531)
Net assets	$	138,363,344	$	113,930,303
Shares outstanding		23,314,573		21,015,017

Net asset value per outstanding share	$	5.93	$	5.42

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

HARRIS & HARRIS GROUP, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS

	Year Ended December 31, 2007	Year Ended December 31, 2006	Year Ended December 31, 2005
Investment income:			
Interest from:			
Fixed-income securities	$ 2,705,597	$ 2,991,261	$ 1,409,273
Portfolio companies	0	0	65,620
Miscellaneous income	39	37,500	65,969
Total investment income	2,705,636	3,028,761	1,540,862
Expenses:			
Salaries, benefits and stock-based compensation (Note 4)	11,435,329	7,933,276	2,459,033
Administration and operations	1,432,653	1,250,080	1,319,354
Profit-sharing provision (Note 5)	0	50,875	1,796,264
Professional fees	902,911	737,828	830,062
Rent	235,998	239,846	211,582
Directors' fees and expenses	435,060	340,750	308,874
Depreciation	63,113	64,916	64,713
Custodian fees	28,115	24,125	16,741
Total expenses	14,533,179	10,641,696	7,006,623
Net operating loss	(11,827,543)	(7,612,935)	(5,465,761)
Net realized gain from investments:			
Realized gain from investments	118,137	31,338	23,862,037
Income tax expense (benefit) (Note 8)	87,975	(227,355)	9,653,248
Net realized gain from investments	30,162	258,693	14,208,789
Net decrease (increase) in unrealized depreciation on investments:			
Change as a result of investment sales	0	0	(23,181,420)
Change on investments held	5,080,936	(4,418,870)	19,790,298
Change in unrealized depreciation on investments	5,080,936	(4,418,870)	(3,391,122)
Income tax (benefit) (Note 8)	0	0	(1,364,470)
Net decrease (increase) in unrealized depreciation on investments	5,080,936	(4,418,870)	(2,026,652)
Net (decrease) increase in net assets resulting from operations:			
Total	$ (6,716,445)	$ (11,773,112)	$ 6,716,376
Per average basic and diluted outstanding share	$ (0.30)	$ (0.57)	$ 0.36
Average outstanding shares	22,393,030	20,759,547	18,471,770

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

HARRIS & HARRIS GROUP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31, 2007	Year Ended December 31, 2006	Year Ended December 31, 2005
Cash flows used in operating activities:			
Net (decrease) increase in net assets resulting from operations	$ (6,716,445)	$ (11,773,112)	$ 6,716,376
Adjustments to reconcile net increase (decrease) in net assets resulting from operations to net cash used in operating activities:			
Net realized and unrealized (gain) loss on investments	(5,199,073)	4,420,619	(20,470,915)
Deferred income taxes	0	0	(1,364,470)
Depreciation and amortization	(60,009)	(426,168)	346,019
Taxes payable on behalf of shareholders on deemed dividend	0	0	8,122,367
Stock-based compensation expense	8,050,807	5,038,956	0
Changes in assets and liabilities:			
Restricted funds	(517,235)	(419,351)	(138,463)
Receivable from portfolio company	(524)	75,000	(65,000)
Interest receivable	(21,965)	(376,808)	(189,603)
Income tax receivable	0	0	(7,023)
Prepaid expenses	(477,722)	(7,951)	539,496
Other receivables	819,905	(819,905)	0
Other assets	(152,012)	(176,325)	11,599
Accounts payable and accrued liabilities	400,163	1,002,643	268,525
Accrued profit sharing	(261,661)	(1,846,197)	1,796,264
Deferred rent	(6,801)	(9,677)	(3,927)
Current income tax liability	0	(9,637,026)	1,524,470
Net cash used in operating activities	(4,142,572)	(14,955,302)	(2,914,285)
Cash flows from investing activities:			
Net (purchase) sale of short-term investments and marketable securities	(235,754)	37,593,589	(52,144,482)
Investment in private placements and loans	(20,595,161)	(24,408,187)	(16,251,339)
Proceeds from sale of investments	174,669	28,295	35,392,200
Purchase of fixed assets	(41,640)	(15,086)	(45,704)
Net cash (used in) provided by investing activities	(20,697,886)	13,198,611	(33,049,325)
Cash flows from financing activities:			
Proceeds from public offering, net (Note 10)	12,993,168	0	36,526,567
Proceeds from stock option exercises (Note 4)	10,105,511	2,615,190	0

Net cash provided by financing activities		23,098,679		2,615,190		36,526,567
Net (decrease) increase in cash and cash equivalents:						
Cash and cash equivalents at beginning of the year		2,071,788		1,213,289		650,332
Cash and cash equivalents at end of the year		330,009		2,071,788		1,213,289
Net (decrease) increase in cash and cash equivalents	$	(1,741,779)	$	858,499	$	562,957
Supplemental disclosures of cash flow information:						
Income taxes paid	$	80,236	$	9,425,922	$	0

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

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HARRIS & HARRIS GROUP, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS

	Year Ended December 31, 2007	Year Ended December 31, 2006	Year Ended December 31, 2005
Changes in net assets from operations:			
Net operating loss	$ (11,827,543)	$ (7,612,935)	$ (5,465,761)
Net realized gain on investments	30,162	258,693	14,208,789
Net (increase) in unrealized depreciation on investments as a result of sales	0	0	(23,181,420)
Net decrease (increase) in unrealized depreciation on investments held	5,080,936	(4,418,870)	19,790,298
Net change in deferred taxes	0	0	1,364,470
Net (decrease) increase in net assets resulting from operations	(6,716,445)	(11,773,112)	6,716,376
Changes in net assets from capital stock transactions:			
Issuance of common stock upon the exercise of stock options	9,996	2,587	0
Issuance of common stock on offering	13,000	0	35,075
Additional paid in capital on common stock issued	23,075,683	2,612,603	36,491,492
Stock-based compensation expense	8,050,807	5,038,956	0
Net increase in net assets resulting from capital stock transactions	31,149,486	7,654,146	36,526,567
Changes in net assets from adoption of SFAS No. 158	0	61,527	0
Net increase (decrease) in net assets	24,433,041	(4,057,439)	43,242,943
Net Assets:			
Beginning of the year	113,930,303	117,987,742	74,744,799
End of the year	$ 138,363,344	$ 113,930,303	$ 117,987,742

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

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HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2007

	Method of Valuation (1)	Shares/ Principal		Value
Investments in Unaffiliated Companies (2)(3) - 15.25% of net assets at value				
Private Placement Portfolio (Illiquid) - 15.25% of net assets at value				
BioVex Group, Inc. (4)(5)(6)(7)(8) - Developing novel biologics for treatment of cancer and infectious disease				
Series E Convertible Preferred Stock	(B)	2,799,552	$	2,500,000
Exponential Business Development Company (4)(5) -- Venture capital partnership focused on early stage companies				
Limited Partnership Interest	(B)	1		2,026
Molecular Imprints, Inc. (4)(5) -- Manufacturing nanoimprint lithography capital equipment				
Series B Convertible Preferred Stock	(B)	1,333,333		2,000,000
Series C Convertible Preferred Stock	(B)	1,250,000		2,389,250
Warrants at $2.00 expiring 12/31/11	(B)	125,000		110,750
				4,500,000
Nanosys, Inc. (4)(5)(7) -- Developing zero and one-dimensional inorganic nanometer-scale materials and devices				
Series C Convertible Preferred Stock	(B)	803,428		2,370,113
Series D Convertible Preferred Stock	(B)	1,016,950		3,000,003
				5,370,116
Nantero, Inc. (4)(5)(7) -- Developing a high-density, nonvolatile, random access memory chip, enabled by carbon nanotubes				
Series A Convertible Preferred Stock	(B)	345,070		1,046,908
Series B Convertible Preferred Stock	(B)	207,051		628,172
Series C Convertible Preferred Stock	(B)	188,315		571,329
				2,246,409
NeoPhotonics Corporation (4)(5) -- Developing and manufacturing optical devices and components				
Common Stock	(B)	716,195		133,141
Series 1 Convertible Preferred Stock	(B)	1,831,256		1,831,256
Series 2 Convertible Preferred Stock	(B)	741,898		741,898
Series 3 Convertible Preferred Stock	(B)	2,750,000		2,750,000
Warrants at $0.15 expiring 01/26/10	(B)	16,364		1,325
Warrants at $0.15 expiring 12/05/10	(B)	14,063		1,139

				5,458,759
Polatis, Inc. (4)(5)(7)(9) -- Developing MEMS-based optical networking components				
Series A-1 Convertible Preferred Stock	(B)	16,775		0
Series A-2 Convertible Preferred Stock	(B)	71,611		132,653
Series A-4 Convertible Preferred Stock	(B)	4,774		8,768
Series A-5 Convertible Preferred Stock	(B)	16,438		135,105
				276,526
Starfire Systems, Inc. (4)(5)(7) -- Producing ceramic-forming polymers Common Stock	(B)	375,000		150,000
Series A-1 Convertible Preferred Stock	(B)	600,000		600,000
				750,000
Total Unaffiliated Private Placement Portfolio (cost: $21,435,392)			**$**	**21,103,836**
Total Investments in Unaffiliated Companies (cost: $21,435,392)			**$**	**21,103,836**

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

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HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2007

	Method of Valuation (1)		Shares/ Principal		Value
Investments in Non-Controlled Affiliated Companies (2)(10) - 38.06% of net assets at value					
Private Placement Portfolio (Illiquid) - 38.06% of net assets at value					
Adesto Technologies Corporation (4)(5)(6)(7) -- Developing semiconductor-related products enabled at the nanoscale					
Series A Convertible Preferred Stock	(B)		3,416,149	$	1,147,826
Ancora Pharmaceuticals Inc. (4)(5)(6)(7) - Developing synthetic carbohydrates for pharmaceutical markets and for internal drug development programs					
Series B Convertible Preferred Stock	(B)		909,091		639,062
Warrants at $1.06 expiring 05/01/08	(B)		754,717		60,377
					699,439
BridgeLux, Inc. (4)(5)(11) -- Manufacturing high-power light emitting diodes					
Series B Convertible Preferred Stock	(B)		1,861,504		2,792,256
Series C Convertible Preferred Stock	(B)		2,130,699		3,196,050
Warrants at $0.7136 expiring 02/02/2017	(B)		98,340		138,856
Warrants at $0.7136 expiring 04/26/2017	(B)		65,560		92,833
					6,219,995
Cambrios Technologies Corporation (4)(5)(7) -- Developing nanowire-enabled electronic materials for the display industry					
Series B Convertible Preferred Stock	(B)		1,294,025		1,294,025
Series C Convertible Preferred Stock	(B)		1,300,000		1,300,000
					2,594,025
Chlorogen, Inc. (4)(5)(12) -- Developed patented chloroplast technology to produce plant-made proteins					
Series A Convertible Preferred Stock	(B)		4,478,038		0
Series B Convertible Preferred Stock	(B)		2,077,930		0
Secured Convertible Bridge Note (including interest)	(B)	$	176,811		0
					0
Crystal IS, Inc. (4)(5)(7) -- Developing single-crystal aluminum nitride substrates for optoelectronic devices					
Series A Convertible Preferred Stock	(B)		391,571		305,425
Series A-1 Convertible Preferred Stock	(B)		1,300,376		1,014,294
Warrants at $0.78 expiring 05/05/2013	(B)		15,231		9,550
Warrants at $0.78 expiring 05/12/2013	(B)		2,350		1,473

Warrants at $0.78 expiring 08/08/2013	(B)		4,396	2,796
				1,333,538
CSwitch, Inc. (4)(5)(7)(13) -- Developing next-generation, system-on- a-chip solutions for communications-based platforms				
Series A-1 Convertible Preferred Stock	(B)		6,863,118	3,431,559
Secured Convertible Bridge Note (including interest)	(B)	$	529,852	541,581
				3,973,140
D-Wave Systems, Inc. (4)(5)(7)(14) -- Developing high-performance quantum computing systems				
Series B Convertible Preferred Stock	(B)		2,000,000	2,226,488

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

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HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2007

	Method of Valuation (1)	Shares/ Principal		Value
Investments in Non-Controlled Affiliated Companies (2)(10) - 38.06% of net assets at value (cont.)				
Private Placement Portfolio (Illiquid) - 38.06% of net assets at value (cont.)				
Ensemble Discovery Corporation (4)(5)(6)(7) - Developing DNA Programmed Chemistry for the discovery of new classes of therapeutics and bioassays				
Series B Convertible Preferred Stock	(B)	1,449,275	$	2,000,000
Innovalight, Inc. (4)(5)(7) - Developing renewable energy products enabled by silicon-based nanomaterials				
Series B Convertible Preferred Stock	(B)	16,666,666		5,718,216
Series C Convertible Preferred Stock	(B)	5,810,577		1,993,568
				7,711,784
Kereos, Inc. (4)(5)(7) -- Developing emulsion-based imaging agents and targeted therapeutics to image and treat cancer and cardiovascular disease				
Series B Convertible Preferred Stock	(B)	545,456		159,743
Kovio, Inc. (4)(5)(7) -- Developing semiconductor products using printed electronics and thin-film technologies				
Series C Convertible Preferred Stock	(B)	2,500,000		3,125,000
Series D Convertible Preferred Stock	(B)	800,000		1,000,000
				4,125,000
Lifco, Inc. (4)(5)(6)(7)(15) -- Developing energy solutions using nanostructured materials				
Series A Convertible Preferred Stock	(B)	1,208,262		946,528
Mersana Therapeutics, Inc. (4)(5)(7)(16) -- Developing advanced polymers for drug delivery				
Series A Convertible Preferred Stock	(B)	68,451		136,902
Series B Convertible Preferred Stock	(B)	866,500		1,733,000
Warrants at $2.00 expiring 10/21/10	(B)	91,625		118,380
				1,988,282
Metabolon, Inc. (4)(5)(7) - Discovering biomarkers through the use of metabolomics				
Series B Convertible Preferred Stock	(B)	2,173,913		2,500,000
NanoGram Corporation (4)(5)(7) -- Developing a broad				

suite of intellectual property utilizing nanoscale materials			
Series I Convertible Preferred Stock	(B)	63,210	124,524
Series II Convertible Preferred Stock	(B)	1,250,904	2,464,281
Series III Convertible Preferred Stock	(B)	1,242,144	2,447,024
Series IV Convertible Preferred Stock	(B)	432,179	851,393
			5,887,222
Nanomix, Inc. (4)(5)(7) -- Producing nanoelectronic sensors that integrate carbon nanotube electronics with silicon microstructures			
Series C Convertible Preferred Stock	(B)	977,917	330,228
Series D Convertible Preferred Stock	(B)	6,802,397	680,240
			1,010,468

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

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HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2007

	Method of Valuation (1)	Shares/ Principal	Value
Investments in Non-Controlled Affiliated Companies (2)(10) - 38.06% of net assets at value (cont.)			
Private Placement Portfolio (Illiquid) - 38.06% of net assets at value (cont.)			
NanoOpto Corporation (4)(5)(17) -- Manufactured discrete and integrated optical communications sub-components on a chip by utilizing nano manufacturing and nano coating technology			
Series A-1 Convertible Preferred Stock	(B)	267,857	$ 0
Series B Convertible Preferred Stock	(B)	3,819,935	0
Series C Convertible Preferred Stock	(B)	1,932,789	0
Series D Convertible Preferred Stock	(B)	1,397,218	0
Warrants at $0.4359 expiring 03/15/10	(B)	193,279	0
Secured Convertible Bridge Note (including interest)	(B)	$ 268,654	105,714
			105,714
Nextreme Thermal Solutions, Inc. (4)(5)(7) -- Developing thin-film thermoelectric devices for cooling and energy conversion			
Series A Convertible Preferred Stock	(B)	1,750,000	1,750,000
Questech Corporation (4)(5) -- Manufacturing and marketing proprietary metal and stone decorative tiles			
Common Stock	(B)	655,454	589,259
Warrants at $1.50 expiring 11/19/08	(B)	5,000	1,085
Warrants at $1.50 expiring 11/19/09	(B)	5,000	1,910
			592,254
Siluria Technologies, Inc. (4)(5)(6)(7) - Developing new-generation nanomaterials			
Series S-2 Convertible Preferred Stock	(B)	482,218	160,723
Solazyme, Inc. (4)(5)(7) -- Developing energy-harvesting machinery of photosynthetic microbes to produce industrial and pharmaceutical molecules			
Series A Convertible Preferred Stock	(B)	988,204	997,691
Series B Convertible Preferred Stock	(B)	495,246	500,000
			1,497,691
Xradia, Inc. (4)(5) - Designing, manufacturing and selling ultra high resolution 3D x-ray microscopes and fluorescence imaging systems			

Series D Convertible Preferred Stock	(B)	3,121,099		4,000,000
Zia Laser, Inc. (4)(5)(18) -- Developed quantum dot semiconductor lasers				
Series C Convertible Preferred Stock	(B)	1,500,000		21,329
Total Non-Controlled Private Placement Portfolio (cost: $54,306,393)			**$**	**52,651,189**
Total Investments in Non-Controlled Affiliated Companies (cost: $54,306,393)			**$**	**52,651,189**

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

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HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2007

	Method of Valuation (1)		Shares/ Principal		Value
Investments in Controlled Affiliated Companies (2)(19) - 3.15% of net assets at value					
Private Placement Portfolio (Illiquid) - 3.15% of net assets at value					
Evolved Nanomaterial Sciences, Inc. (4)(5)(20) -- Developed nanoscale-enhanced approaches for the resolution of chiral molecules					
Series A Convertible Preferred Stock	(B)		5,870,021	$	0
Phoenix Molecular Corporation (4)(5)(6)(7) - Developing technology to enable the separation of difficult-to-separate materials.					
Common Stock	(B)		1,000		10
Unsecured Convertible Bridge Note (including interest)	(B)	$	50,000		50,733
					50,743
SiOnyx, Inc. (4)(5)(7) -- Developing silicon-based optoelectronic products enabled by its proprietary "Black Silicon"					
Series A Convertible Preferred Stock	(B)		233,499		135,686
Series A-1 Convertible Preferred Stock	(B)		2,966,667		1,723,930
Series A-2 Convertible Preferred Stock	(B)		4,207,537		2,445,000
					4,304,616
Total Controlled Private Placement Portfolio (cost: $6,935,743)				**$**	**4,355,359**
Total Investments in Controlled Affiliated Companies (cost: $6,935,743)				**$**	**4,355,359**
Total Private Placement Portfolio (cost: $82,677,528)				**$**	**78,110,384**
U.S. Government and Agency Securities - 43.50% of net assets at value					
U.S. Treasury Bill -- due date 02/21/08	(J)	$	2,750,000		2,738,725
U.S. Treasury Notes -- due date 02/15/08, coupon 3.375%	(H)		15,005,000		15,006,200
U.S. Treasury Notes -- due date 05/15/08, coupon 3.75%	(H)		9,000,000		9,010,530
U.S. Treasury Notes -- due date 09/15/08, coupon	(H)		5,000,000		4,991,800

3.125%				
U.S. Treasury Notes -- due date 01/15/09, coupon 3.25%	(H)	3,000,000		3,005,160
U.S. Treasury Notes -- due date 02/15/09, coupon 4.50%	(H)	5,100,000		5,176,908
U.S. Treasury Notes -- due date 04/15/09, coupon 3.125%	(H)	3,000,000		3,001,410
U.S. Treasury Notes -- due date 07/15/09, coupon 3.625%	(H)	3,000,000		3,023,910
U.S. Treasury Notes -- due date 10/15/09, coupon 3.375%	(H)	3,000,000		3,018,510
U.S. Treasury Notes -- due date 01/15/10, coupon 3.625%	(H)	3,000,000		3,034,680
U.S. Treasury Notes -- due date 04/15/10, coupon 4.00%	(H)	3,000,000		3,060,930
U.S. Treasury Notes -- due date 07/15/10, coupon 3.875%	(H)	3,000,000		3,060,930
U.S. Treasury Notes -- due date 10/15/10, coupon 4.25%	(H)	2,000,000		2,063,900
Total Investments in U.S. Government and Agency Securities (cost: $59,552,933)			**$**	**60,193,593**
Total Investments (cost: $142,230,461)			**$**	**138,303,977**

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

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HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2007

Notes to Consolidated Schedule of Investments

(1) See Footnote to Consolidated Schedule of Investments on page F-21 for a description of the Valuation Procedures.

(2) Investments in unaffiliated companies consist of investments in which we own less than five percent of the voting shares of the portfolio company. Investments in non-controlled affiliated companies consist of investments in which we own five percent or more, but less than 25 percent, of the voting shares of the portfolio company, or where we hold one or more seats on the portfolio company's Board of Directors but do not control the company. Investments in controlled affiliated companies consist of investments in which we own 25 percent or more of the voting shares of the portfolio company or otherwise control the company.

(3) The aggregate cost for federal income tax purposes of investments in unaffiliated companies is $21,435,392. The gross unrealized appreciation based on the tax cost for these securities is $1,732,194. The gross unrealized depreciation based on the tax cost for these securities is $2,063,750.

(4) Legal restrictions on sale of investment.

(5) Represents a non-income producing security. Equity investments that have not paid dividends within the last 12 months are considered to be non-income producing.

(6) Initial investment was made during 2007.

(7) These investments are development stage companies. A development stage company is defined as a company that is devoting substantially all of its efforts to establishing a new business, and either it has not yet commenced its planned principal operations, or it has commenced such operations but has not realized significant revenue from them.

(8) With our purchase of Series E Convertible Preferred Stock of BioVex, we received a warrant to purchase a number of shares of common stock of BioVex as determined by dividing 624,999.99 by the price per share at which the common stock is offered and sold to the public in connection with the initial public offering. The ability to exercise this warrant is therefore contingent on BioVex completing successfully an initial public offering before the expiration date of the warrant of September 27, 2012. The exercise price of this warrant shall be 110 percent of the initial public offering price.

(9) Continuum Photonics, Inc., merged with Polatis, Ltd., to form Polatis, Inc.

(10) The aggregate cost for federal income tax purposes of investments in non-controlled affiliated companies is $54,306,393. The gross unrealized appreciation based on the tax cost for these securities is $10,915,201. The gross unrealized depreciation based on the tax cost for these securities is $12,570,405.

(11) BridgeLux, Inc., was previously named eLite Optoelectronics, Inc.

(12) On November 30, 2007, Chlorogen filed a Certificate of Dissolution with the state of Delaware.

(13) With our investment in a secured convertible bridge note issued by CSwitch, we received a warrant to purchase a number of shares of the class of stock sold in the next financing of CSwitch equal to $529,322.36, the principal of the note, divided by the lowest price per share of the class of stock sold in the next financing of CSwitch. The ability to exercise this warrant is therefore contingent on CSwitch completing successfully a subsequent round of financing. The warrant will expire five years from the date of the close of the next round of financing. The cost basis of this warrant is $529.32.

(14) D-Wave Systems, Inc., is located and is doing business primarily in Canada. We invested in D-Wave Systems, Inc., through D-Wave USA, a Delaware company. Our investment is denominated in Canadian dollars and is subject to foreign currency translation. See "Note 2. Summary of Significant Accounting Policies."

The accompanying notes are an integral part of this consolidated schedule.

HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2007

(15) On February 28, 2008, Lifco, Inc., merged with CFX Battery, Inc., to form CFX Battery, Inc.

(16) Mersana Therapeutics, Inc., was previously named Nanopharma Corp.

(17) On July 19, 2007, NanoOpto Corporation sold its assets to API Nanotronics, Inc.

(18) On November 30, 2006, the assets of Zia Laser, Inc., were acquired by Innolume, Inc.

(19) The aggregate cost for federal income tax purposes of investments in controlled affiliated companies is $6,935,743. The gross unrealized appreciation based on the tax cost for these securities is $219,616. The gross unrealized depreciation based on the tax cost for these securities is $2,800,000.

(20) On September 30, 2007, Evolved Nanomaterial Sciences, Inc., filed for Chapter 7 bankruptcy.

The accompanying notes are an integral part of this consolidated schedule.

HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2006

	Method of Valuation (3)	Shares/ Principal		Value
Investments in Unaffiliated Companies (6)(7) - 15.61% of net assets				
Private Placement Portfolio (Illiquid) - 15.61% of net assets				
AlphaSimplex Group, LLC (2) -- Investment management company headed by Dr. Andrew W. Lo, holder of the Harris & Harris Group Chair at MIT				
Limited Liability Company Interest	(B)	--	$	10,521
Exponential Business Development Company (1)(2) -- Venture capital partnership focused on early stage companies				
Limited Partnership Interest	(B)	--		0
Molecular Imprints, Inc. (1)(2) -- Manufacturing nanoimprint lithography capital equipment				
Series B Convertible Preferred Stock	(A)	1,333,333		2,000,000
Series C Convertible Preferred Stock	(A)	1,250,000		2,500,000
Warrants at $2.00 expiring12/31/11	(B)	125,000		0
				4,500,000
Nanosys, Inc. (1)(2)(5) -- Developing zero and one-dimensional inorganic nanometer-scale materials for use in nanotechnology-enabled systems				
Series C Convertible Preferred Stock	(C)	803,428		2,370,113
Series D Convertible Preferred Stock	(C)	1,016,950		3,000,003
				5,370,116
Nantero, Inc. (1)(2)(5) -- Developing a high-density, nonvolatile, random access memory chip, enabled by carbon nanotubes				
Series A Convertible Preferred Stock	(C)	345,070		1,046,908
Series B Convertible Preferred Stock	(C)	207,051		628,172
Series C Convertible Preferred Stock	(C)	188,315		571,329
				2,246,409
NeoPhotonics Corporation (1)(2) -- Developing and manufacturing planar optical devices and components				

Common Stock	(C)	716,195		133,141
Series 1 Convertible Preferred Stock	(C)	1,831,256		1,831,256
Series 2 Convertible Preferred Stock	(C)	741,898		741,898
Series 3 Convertible Preferred Stock	(C)	2,750,000		2,750,000
Warrants at $0.15 expiring 01/26/10	(C)	16,364		164
Warrants at $0.15 expiring 12/05/10	(C)	14,063		140
				5,456,599
Polatis, Inc. (1)(2)(5)(10) -- Developing optical networking components by merging materials, MEMS and electronics technologies				
Series A-1 Convertible Preferred Stock	(B)	16,775		0
Series A-2 Convertible Preferred Stock	(B)	71,611		141,520
Series A-4 Convertible Preferred Stock	(B)	4,774		9,435
Series A-5 Convertible Preferred Stock	(B)	5,491		45,127
				196,082
Total Unaffiliated Private Placement Portfolio (cost: $18,107,124)			**$**	**17,779,727**
Total Investments in Unaffiliated Companies (cost: $18,107,124)			**$**	**17,779,727**

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

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HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2006

	Method of Valuation (3)		Shares/ Principal		Value
Investments in Non-Controlled Affiliated Companies (6)(8) -28.20% of net assets					
Private Placement Portfolio (Illiquid) - 28.20% of net assets					
BridgeLux, Inc. (1)(2)(11) -- Manufacturing high-power light emitting diodes					
Series B Convertible Preferred Stock	(A)		1,861,504	$	1,000,000
Cambrios Technologies Corporation (1)(2)(5) -- Developing nanowire-enabled electronic materials for the display industry					
Series B Convertible Preferred Stock	(A)		1,294,025		1,294,025
Chlorogen, Inc. (1)(2)(5) -- Developing patented chloroplast technology to produce plant-made proteins					
Series A Convertible Preferred Stock	(C)		4,478,038		785,000
Series B Convertible Preferred Stock	(C)		2,077,930		364,261
Secured Convertible Bridge Note (including interest)	(A)	$	221,438		225,697
					1,374,958
Crystal IS, Inc. (1)(2)(5) -- Developing single-crystal aluminum nitride substrates for optoelectronic devices					
Series A Convertible Preferred Stock	(C)		391,571		305,425
Series A-1 Convertible Preferred Stock	(C)		1,300,376		1,014,294
Warrants at $0.78 expiring 05/05/2013	(B)		15,231		0
Warrants at $0.78 expiring 05/12/2013	(B)		2,350		0
Warrants at $0.78 expiring 08/08/2013	(B)		4,396		0
					1,319,719
CSwitch, Inc. (1)(2)(5) -- Developing next-generation, system-on-a-chip solutions for communications-based platforms					
Series A-1 Convertible Preferred Stock	(C)		6,700,000		3,350,000
D-Wave Systems, Inc. (1)(2)(4)(5)(13) -- Developing high-performance quantum computing systems					
Series B Convertible Preferred Stock	(A)		2,000,000		1,716,444
Warrants at $0.85 expiring 10/19/07	(B)		1,800,000		0
					1,716,444

Innovalight, Inc. (1)(2)(4)(5) - Developing renewable energy products enabled by silicon-based nanomaterials			
Series B Convertible Preferred Stock	(A)	16,666,666	2,500,000
Kereos, Inc. (1)(2)(5) -- Developing emulsion-based imaging agents and targeted therapeutics to image and treat cancer and cardiovascular disease			
Series B Convertible Preferred Stock	(A)	349,092	960,000
Kovio, Inc. (1)(2)(5) -- Developing semiconductor products using printed electronics and thin-film technologies			
Series C Convertible Preferred Stock	(A)	2,500,000	3,000,000

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

HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2006

	Method of Valuation (3)	Shares/ Principal		Value
Investments in Non-Controlled Affiliated Companies (6)(8) - 28.20% of net assets (cont.)				
Private Placement Portfolio (Illiquid) - 28.20% of net assets (cont.)				
Mersana Therapeutics, Inc. (1)(2)(5)(12) -- Developing advanced polymers for drug delivery				
Series A Convertible Preferred Stock	(C)	68,452	$	136,904
Series B Convertible Preferred Stock	(C)	616,500		1,233,000
Warrants at $2.00 expiring 10/21/10	(B)	91,625		0
				1,369,904
Metabolon, Inc. (1)(2)(4)(5) - Discovering biomarkers through the use of metabolomics				
Series B Convertible Preferred Stock	(A)	2,173,913		2,500,000
NanoGram Corporation (1)(2)(5) -- Developing a broad suite of intellectual property utilizing nanotechnology				
Series I Convertible Preferred Stock	(C)	63,210		64,259
Series II Convertible Preferred Stock	(C)	1,250,904		1,271,670
Series III Convertible Preferred Stock	(C)	1,242,144		1,262,764
				2,598,693
Nanomix, Inc. (1)(2)(5) -- Producing nanoelectronic sensors that integrate carbon nanotube electronics with silicon microstructures				
Series C Convertible Preferred Stock	(B)	9,779,181		790,000
NanoOpto Corporation (1)(2)(5) -- Manufacturing discrete and integrated optical communications sub-components on a chip by utilizing nano manufacturing and nano coating technology				
Series A-1 Convertible Preferred Stock	(B)	267,857		16,400
Series B Convertible Preferred Stock	(B)	3,819,935		560,328
Series C Convertible Preferred Stock	(B)	1,932,789		425,266
Series D Convertible Preferred Stock	(B)	1,397,218		204,951
Warrants at $0.4359 expiring 03/15/10	(B)	193,279		0
				1,206,945

Nextreme Thermal Solutions, Inc. (1)(2)(5) -- Developing thin-film thermoelectric devices			
Series A Convertible Preferred Stock	(A)	1,000,000	1,000,000
Questech Corporation (1)(2) -- Manufacturing and marketing proprietary metal and stone decorative tiles			
Common Stock	(B)	655,454	996,683
Warrants at $1.50 expiring 11/21/07	(B)	3,750	77
Warrants at $1.50 expiring 11/19/08	(B)	5,000	103
Warrants at $1.50 expiring 11/19/09	(B)	5,000	103
			996,966
Solazyme, Inc. (1)(2)(5) -- Developing energy-harvesting machinery of photosynthetic microbes to produce industrial and pharmaceutical molecules			
Series A Convertible Preferred Stock	(C)	988,204	385,400

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

HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2006

	Method of Valuation (3)	Shares/ Principal		Value
Investments in Non-Controlled Affiliated Companies (6)(8) - 28.20% of net assets (cont.)				
Private Placement Portfolio (Illiquid) - 28.20% of net assets (cont.)				
Starfire Systems, Inc. (1)(2)(5) --Producing ceramic-forming polymers				
Common Stock	(A)	375,000	$	150,000
Series A-1 Convertible Preferred Stock	(C)	600,000		600,000
				750,000
Xradia, Inc. (1)(2)(4) - Designing, manufacturing and selling ultra high resolution 3D x-ray microscopes and fluorescence imaging systems.				
Series D Convertible Preferred Stock	(A)	3,121,099		4,000,000
Zia Laser, Inc. (1)(2)(5) -- Developing quantum dot semiconductor lasers				
Series C Convertible Preferred Stock	(C)	1,500,000		15,000
Total Non-Controlled Private Placement Portfolio (cost: $39,571,676)			**$**	**32,128,054**
Total Investments in Non-Controlled Affiliated Companies (cost: $39,571,676)			**$**	**32,128,054**

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

HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2006

	Method of Valuation (3)	Shares/ Principal		Value
Investments in Controlled Affiliated Companies (6)(9) - 3.30% of net assets				
Private Placement Portfolio (Illiquid) - 3.30% of net assets				
Evolved Nanomaterial Sciences, Inc. (1)(2)(4)(5) -- Developing nanotechnology-enhanced approaches for the resolution of chiral molecules				
Series A Convertible Preferred Stock	(A)	5,870,021	$	2,800,000
SiOnyx, Inc. (1)(2)(4)(5) -- Developing silicon-based optoelectronic products enabled by its proprietary, "Black Silicon"				
Series A Convertible Preferred Stock	(C)	233,499		70,050
Series A-1 Convertible Preferred Stock	(C)	2,966,667		890,000
				960,050
Total Controlled Private Placement Portfolio (cost: $4,440,000)			**$**	**3,760,050**
Total Investments in Controlled Affiliated Companies (cost: $4,440,000)			**$**	**3,760,050**
U.S. Government and Agency Securities - 51.48% of net assets				
U.S. Treasury Bill -- due date 1/18/07	(J)	2,217,000		2,212,677
U.S. Treasury Notes -- due date 11/30/07, coupon 4.25%	(H)	6,500,000		6,455,345
U.S. Treasury Notes -- due date 02/15/08, coupon 3.375%	(H)	9,000,000		8,842,860
U.S. Treasury Notes -- due date 05/15/08, coupon 3.75%	(H)	9,000,000		8,862,210
U.S. Treasury Notes -- due date 09/15/08, coupon 3.125%	(H)	5,000,000		4,861,350
U.S. Treasury Notes -- due date 01/15/09, coupon 3.25%	(H)	3,000,000		2,910,930
U.S. Treasury Notes -- due date 02/15/09, coupon 4.50%	(H)	5,100,000		5,069,145
U.S. Treasury Notes -- due date 04/15/09, coupon 3.125%	(H)	3,000,000		2,893,830
U.S. Treasury Notes -- due date 07/15/09, coupon 3.625%	(H)	3,000,000		2,920,890

U.S. Treasury Notes -- due date 10/15/09, coupon 3.375%	(H)	3,000,000		2,894,310
U.S. Treasury Notes -- due date 01/15/10, coupon 3.625%	(H)	3,000,000		2,907,420
U.S. Treasury Notes -- due date 04/15/10, coupon 4.00%	(H)	3,000,000		2,935,560
U.S. Treasury Notes -- due date 07/15/10, coupon 3.875%	(H)	3,000,000		2,920,560
U.S. Treasury Notes -- due date 10/15/10, coupon 4.25%	(H)	2,000,000		1,969,060
Total Investments in U.S. Government and Agency Securities (cost: $59,212,598)			**$**	**58,656,147**
Total Investments (cost: $121,331,398)			**$**	**112,323,978**

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

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HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF DECEMBER 31, 2006

Notes to Consolidated Schedule of Investments

(1) Represents a non-income producing security. Equity investments that have not paid dividends within the last 12 months are considered to be non-income producing.

(2) Legal restrictions on sale of investment.

(3) See Footnote to Schedule of Investments for a description of the Valuation Procedures.

(4) Initial investment was made during 2006.

(5) These investments are development stage companies. A development stage company is defined as a company that is devoting substantially all of its efforts to establishing a new business, and either it has not yet commenced its planned principal operations, or it has commenced such operations but has not realized significant revenue from them.

(6) Investments in unaffiliated companies consist of investments in which we own less than five percent of the voting shares of the portfolio company. Investments in non-controlled affiliated companies consist of investments in which we own five percent or more, but less than 25 percent, of the voting shares of the portfolio company or where we hold one or more seats on the portfolio company's Board of Directors. Investments in controlled affiliated companies consist of investments in which we own 25 percent or more of the voting shares of the portfolio company.

(7) The aggregate cost for federal income tax purposes of investments in unaffiliated companies is $18,107,124. The gross unrealized appreciation based on the tax cost for these securities is $1,732,194. The gross unrealized depreciation based on the tax cost for these securities is $2,059,591.

(8) The aggregate cost for federal income tax purposes of investments in non-controlled affiliated companies is $39,571,676. The gross unrealized appreciation based on the tax cost for these securities is $333,269. The gross unrealized depreciation based on the tax cost for these securities is $7,776,891.

(9) The aggregate cost for federal income tax purposes of investments in controlled affiliated companies is $4,400,000. The gross unrealized appreciation based on the tax cost for these securities is $0. The gross unrealized depreciation based on the tax cost for these securities is $679,950.

(10) Continuum Photonics, Inc., merged with Polatis, Ltd., to form Polatis, Inc.

(11) BridgeLux, Inc., was previously named eLite Optoelectronics, Inc.

(12) Mersana Therapeutics, Inc., was previously named Nanopharma Corp.

(13) D-Wave Systems, Inc., is located and is doing business primarily in Canada. We invested in D-Wave Systems, Inc., through D-Wave USA, a Delaware company. Our investment is denominated in Canadian dollars and is subject to foreign currency translation. Refer to "Note 2. Summary of Significant Accounting Policies."

The accompanying notes are an integral part of this consolidated schedule.

HARRIS & HARRIS GROUP, INC.
FOOTNOTE TO CONSOLIDATED SCHEDULE OF INVESTMENTS

VALUATION PROCEDURES

Our investments can be classified into five broad categories for valuation purposes:

Equity-Related Securities;

Investments in Intellectual Property or Patents or Research and Development in Technology or Product Development;

Long-Term Fixed-Income Securities;

Short-Term Fixed-Income Securities; and

All Other Securities.

The 1940 Act requires periodic valuation of each investment in our portfolio to determine net asset value. Under the 1940 Act, unrestricted securities with readily available market quotations are to be valued at the current market value; all other assets must be valued at "fair value" as determined in good faith by or under the direction of the Board of Directors.

Our Board of Directors is responsible for (1) determining overall valuation guidelines and (2) ensuring the valuation of investments within the prescribed guidelines.

Our Valuation Committee, comprised of all of our independent Board members, is responsible for reviewing and approving the valuation of our assets within the guidelines established by the Board of Directors.

Fair value is generally defined as the amount that an investment could be sold for in an orderly disposition over a reasonable time. Generally, to increase objectivity in valuing our assets, external measures of value, such as public markets or third-party transactions, are utilized whenever possible. Valuation is not based on long-term work-out value, nor immediate liquidation value, nor incremental value for potential changes that may take place in the future.

The values assigned to these investments are based on available information and do not necessarily represent amounts that might ultimately be realized, as these amounts depend on future circumstances and cannot reasonably be determined until the individual investments are actually liquidated or become marketable.

Our valuation policy with respect to the five broad investment categories is as follows:

Equity-Related Securities

Equity-related securities, including warrants, are valued using one or more of the following basic methods of valuation:

A. Cost. This method may be used in the early stages of a company's development until significant positive or negative events occur subsequent to the date of the original investment that dictate a change to another valuation method.

B. Analytical Method. The analytical method is generally used to value an investment position when there is no established public or private market in the company's securities. This valuation method is inherently imprecise and ultimately the result of reconciling the judgments of our Valuation Committee members, based on the data available to them. The resulting valuation, although stated as a precise number, is necessarily within a range of values that vary depending upon the significance attributed to the various factors being considered.

The analytical method considers the following factors:

- The cost of the Company's investment;
- Transactions in a company's securities or unconditional firm offers by responsible parties as a factor in determining valuation;
- The financial condition and operating results of the company;
- The long-term potential of the business and technology of the company;
- The values of similar securities issued by companies in similar businesses;
- Multiples to revenue, net income or EBITDA that similar securities issued by companies in similar businesses receive;
- The proportion of the company's securities we own and the nature of any rights to require the company to register restricted securities under applicable securities laws; and
- The rights and preferences of the class of securities we own as compared to other classes of securities the portfolio company has issued.

When the analytical method is used to value warrants, the Company utilizes the Black-Scholes model.

C. Private Market. The private market method uses actual, executed, historical transactions in a company's securities by responsible third parties as a basis for valuation. The private market method may also use, where applicable, unconditional firm offers by responsible third parties as a basis for valuation.

D. Public Market. The public market method is used when there is an established public market for the class of the company's securities held by us or into which our securities are convertible. We discount market value for securities that are subject to significant legal and contractual restrictions. Other securities, for which market quotations are readily available, are carried at market value as of the time of valuation. Market value for securities traded on securities exchanges or on the Nasdaq Global Market is the last reported sales price on the day of valuation. For other securities traded in the over-the-counter market and listed securities for which no sale was reported on that day, market value is the mean of the closing bid price and asked price on that day. This method is the preferred method of valuation when there is an established public market for a company's securities, as that market provides the most objective basis for valuation. If for any reason, the Valuation Committee determines that market quotations are not reliable, such securities shall be fair valued by the Valuation Committee in accordance with these Valuation Procedures.

Investments in Intellectual Property or Patents or Research and Development in Technology or Product Development

These investments are carried at fair value using the following basic methods of valuation:

E. Cost. This method may be used in the early stages of commercializing or developing intellectual property or patents or research and development in technology or product development until significant positive or adverse events occur subsequent to the date of the original investment that dictate a change to another valuation method.

F. Analytical Method. The analytical method is used to value an investment after analysis of the best available outside information where the factual information available to us dictates that an investment should no longer be valued under either the cost or private market method. This valuation method is inherently imprecise and ultimately the result of reconciling the judgments of our Valuation Committee members. The resulting valuation, although stated as a precise number, is necessarily within a range of values that vary depending upon the significance attributed to the various factors being considered. Some of the factors considered may include the results of research and development, product development progress, commercial prospects, term of patent and projected markets.

The analytical method considers the following factors:

- The cost of the investment;
- Investments in the same or substantially similar intellectual property or patents or research and development in technology or product development or offers by responsible third parties;
- The results of research and development;
- Product development progress;
- Commercial prospects;
- Term of patent;
- Projected markets; and
- Other subjective factors.

G. Private Market. The private market method uses actual third-party investments in intellectual property or patents or research and development in technology or product development as a basis for valuation, using actual executed historical transactions by responsible third parties. The private market method may also use, where applicable, unconditional firm offers by responsible third parties as a basis for valuation.

As of December 31, 2007, and December 31, 2006, we do not have any investments in intellectual property or patents or research and development in technologies or products.

Long-Term Fixed-Income Securities

H. Readily Marketable. Long-term, fixed-income securities for which market quotations are readily available are carried at market value as of the time of valuation using the most recent bid quotations when available.

I. Not Readily Marketable. Long-term, fixed-income securities for which market quotations are not readily available are carried at fair value as determined in good faith by the Valuation Committee on the basis of available data, which may include credit quality and interest rate analysis, as well as quotations from dealers and brokers. Where such quotations are not available, fair value is determined using prices from independent pricing services that the Board believes are reasonably reliable and based on reasonable price discovery procedures and data from other sources.

Short-Term Fixed-Income Securities

J. Short-Term Fixed-Income Securities are valued in the same manner as long-term fixed-income securities until the remaining maturity is 60 days or less, after which time such securities may be valued at amortized cost if there is no concern over payment at maturity.

All Other Securities

K. All Other Securities are reported at fair value as determined in good faith by the Valuation Committee. As of December 31, 2007, and December 31, 2006, we did not have any of these investments.

For all other securities, the reported values shall reflect the Valuation Committee's judgment of fair values as of the valuation date using the outlined basic methods of valuation or any other method of valuation within the prescribed guidelines that the Valuation Committee determines after review and analysis is more appropriate for the particular kind of investment. They do not necessarily represent an amount of money that would be realized if we had to sell such assets in an immediate liquidation. Thus, valuations as of any particular date are not necessarily indicative of amounts that we may ultimately realize as a result of future sales or other dispositions of investments we hold.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. THE COMPANY

Harris & Harris Group, Inc. (the "Company," "us," "our" and "we"), is a venture capital company operating as a business development company ("BDC") under the Investment Company Act of 1940 ("1940 Act"). We operate as an internally managed company whereby our officers and employees, under the general supervision of our Board of Directors, conduct our operations.

We elected to become a BDC on July 26, 1995, after receiving the necessary shareholder approvals. From September 30, 1992, until the election of BDC status, we operated as a closed-end, non-diversified investment company under the 1940 Act. Upon commencement of operations as an investment company, we revalued all of our assets and liabilities in accordance with the 1940 Act. Prior to September 30, 1992, we were registered and filed under the reporting requirements of the Securities Exchange Act of 1934 (the "1934 Act") as an operating company and, while an operating company, operated directly and through subsidiaries.

Harris & Harris Enterprises, Inc.,SM is a 100 percent wholly owned subsidiary of the Company. Harris & Harris Enterprises, Inc., is a partner in Harris Partners I, L.P.,SM and is taxed under Subchapter C of the Code (a “C Corporation”). Harris Partners I, L.P, is a limited partnership and owned our interest in AlphaSimplex Group, LLC. The partners of Harris Partners I, L.P., are Harris & Harris Enterprises, Inc., (sole general partner) and Harris & Harris Group, Inc., (sole limited partner). Harris & Harris Enterprises, Inc., pays taxes on any non-passive investment income generated by Harris Partners I, L.P. The Company consolidates the results of its subsidiaries for financial reporting purposes.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The following is a summary of significant accounting policies followed in the preparation of the consolidated financial statements:

Principles of Consolidation. The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for investment companies and include the accounts of the Company and its wholly owned subsidiaries. All significant inter-company accounts and transactions have been eliminated in consolidation.

Use of Estimates. The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and contingent assets and liabilities as of December 31, 2007, and December 31, 2006, and the reported amounts of revenues and expenses for the twelve months ended December 31, 2007, 2006, and 2005. Actual results could differ from these estimates, and the differences could be material. The most significant estimates relate to the fair valuations of certain of our investments. At December 31, 2007, and 2006, 54.6 percent and 45.4 percent, respectively, of the Company’s total assets represented portfolio investments whose fair values have been determined by the Board of Directors in good faith in the absence of readily available market values.

Cash and Cash Equivalents. Cash and cash equivalents includes demand deposits and money market instruments with maturities of less than three months. Cash and cash equivalents are carried at cost which approximates fair value.

Portfolio Investment Valuations. Investments are stated at "value" as defined in the 1940 Act and in the applicable regulations of the SEC. Value, as defined in Section 2(a)(41) of the 1940 Act, is (i) the market price for those securities for which a market quotation is readily available and (ii) the fair value as determined in good faith by, or under the direction of, the Board of Directors for all other assets. (See "Valuation Procedures" in the "Footnote to Consolidated Schedule of Investments.") At December 31, 2007, and 2006, our financial statements include private venture capital investments valued at $78,110,384 and $53,667,831, respectively, the fair values of which were determined in good faith by, or under the direction, of the Board of Directors. Upon sale of investments, the values that are ultimately realized may be different from what is presently estimated. The difference could be material.

Foreign Currency Translation. The accounting records of the Company are maintained in U.S. dollars. All assets and liabilities denominated in foreign currencies are translated into U.S. dollars based on the rate of exchange of such currencies against U.S. dollars on the date of valuation. For the year ended December 31, 2007, included in the net decrease in unrealized depreciation on investments was a $307,636 gain resulting from foreign currency translation.

Securities Transactions. Securities transactions are accounted for on the date the securities are purchased or sold (trade date).

Interest Income Recognition. Interest income, adjusted for amortization of premium and accretion of discount, is recorded on accrual basis. The Company ceases accruing interest when securities are determined to be non-income producing and writes off any previously accrued interest.

Realized Gain or Loss and Unrealized Appreciation or Depreciation of Portfolio Investments. Realized gain or loss is recognized when an investment is disposed of and is computed as the difference between the Company’s cost basis in the investment at the disposition date and the net proceeds received from such disposition. Realized gains and losses on investment transactions are determined by specific identification. Unrealized appreciation or depreciation is computed as the difference between the fair value of the investment and the cost basis of such investment.

Stock-Based Compensation. The Company has a stock-based employee compensation plan. The Company accounts for the plan in accordance with the provisions of Statement of Financial Accounting Standards ("SFAS") No. 123(R), "Share-Based Payment." See “Note 4. Stock-Based Compensation” for further discussion.

Income Taxes. As we intend to qualify as a RIC under Subchapter M of the Internal Revenue Code, the Company does not provide for income taxes. Our taxes are accounted for in accordance with SFAS No. 109, "Accounting for Income Taxes."

However, we pay federal, state and local income taxes on behalf of our wholly owned subsidiary, Harris & Harris Enterprises, Inc., which is a C corporation. See “Note 8. Income Taxes."

In June 2006, the FASB issued Interpretation 48, "Accounting for Uncertainty in Income Taxes" (“FIN 48”), an interpretation of SFAS No. 109. FIN 48 clarifies the accounting and reporting for income taxes where interpretation of the law is uncertain. FIN 48 prescribes a comprehensive model for the financial statement recognition, measurement, presentation and disclosure of income tax uncertainties with respect to positions taken or expected to be taken in income tax returns. The Company adopted FIN 48 on January 1, 2007, which had no effect on the Company's financial statements. The Company recognizes interest and penalties in income tax expense. See “Note 8. Income Taxes” for further discussion.

Restricted Funds. The Company maintains a rabbi trust for the purposes of accumulating funds to satisfy the obligations incurred by us for the Supplemental Executive Retirement Plan ("SERP") under the employment agreement with Charles E. Harris.

Property and Equipment. Property and equipment are included in "Other Assets" and are carried at cost, less accumulated depreciation of $336,877. Depreciation is provided using the straight-line method over the estimated useful lives of the premises and equipment.

Concentration of Credit Risk. The Company places its cash and cash equivalents with financial institutions and, at times, cash held in checking accounts may exceed the Federal Deposit Insurance Corporation insured limit.

Recent Accounting Pronouncements. In September 2006, FASB issued SFAS No. 157, "Fair Value Measurements." This statement defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. SFAS No. 157 is effective for us on January 1, 2008. The adoption of SFAS No. 157 will not have a material impact on our consolidated financial statements.

In February 2007, the FASB issued Statement No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" ("SFAS No. 159"). SFAS No. 159 would allow the Company an irrevocable election to measure certain financial assets and liabilities at fair value, with unrealized gains and losses on the elected items recognized in earnings at each reporting period. The fair value option may only be elected at the time of initial recognition of a financial asset or financial liability or upon the occurrence of certain specified events. The election is applied on an instrument-by-instrument basis, with a few exceptions, and is applied only to entire instruments and not to portions of instruments. SFAS No. 159 also provides expanded disclosure requirements regarding the effects of electing the fair value option on the financial statements. SFAS No. 159 is effective prospectively for fiscal years beginning after November 15, 2007. The Company is currently evaluating this Statement. However, as investments are carried at fair value, the Company does not anticipate that this Statement will have a significant impact on the consolidated financial statements.

NOTE 3. INVESTMENTS

The private placement portfolio at fair value consisted of the following geographic regions at December 31, 2007, and 2006:

December 31, 2007

Geographic Region		Fair Value	Percentage of Total Private Placement Portfolio	Percentage of Net Assets
West	$	50,124,606	64.2%	36.2%
Northeast	$	16,849,547	21.6%	12.2%
Midwest	$	4,659,743	6.0%	3.4%
Southeast	$	4,250,000	5.4%	3.1%
Outside U.S.	$	2,226,488	2.8%	1.6%
	$	**78,110,384**	**100.0%**	

December 31, 2006

Geographic Region		Fair Value	Percentage of Total Private Placement Portfolio	Percentage of Net Assets
West	$	29,759,833	55.5%	26.1%
Northeast	$	11,856,596	22.1%	10.4%
Midwest	$	6,834,958	12.7%	6.0%
Southeast	$	3,500,000	6.5%	3.1%
Outside U.S.	$	1,716,444	3.2%	1.5%
	$	**53,667,831**	**100.0%**	

NOTE 4. STOCK-BASED COMPENSATION

On March 23, 2006, the Board of Directors of the Company voted to terminate the Employee Profit-Sharing Plan and to establish the Stock Plan, subject to shareholder approval. This proposal was approved at the May 4, 2006, Annual Meeting of Shareholders. The Stock Plan provides for the grant of equity-based awards of stock options to our officers, employees and directors (subject to receipt of an exemptive order described below) and restricted stock (subject to receipt of an exemptive order described below) to our officers and employees who are selected by our Compensation Committee for participation in the plan and subject to compliance with the 1940 Act.

On July 11, 2006, the Company filed an application with the SEC regarding certain provisions of the Stock Plan, and on June 29, 2007, the Company responded to comments from the SEC on the application. In the event that the SEC provides the exemptive relief requested by the application, and we receive any additional stockholder approval required by the SEC, the Compensation Committee may, in the future, authorize awards of stock options under the Stock Plan to non-employee directors of the Company and authorize grants of restricted stock to employees.

A maximum of 20 percent of our total shares of our common stock issued and outstanding are available for awards under the Stock Plan. Under the Stock Plan, no more than 25 percent of the shares of stock reserved for the grant of the awards under the Stock Plan may be restricted stock awards at any time during the term of the Stock Plan. If any shares of restricted stock are awarded, such awards will reduce on a percentage basis the total number of shares of stock for which options may be awarded. If the Company does not receive exemptive relief from the SEC to issue restricted stock, all shares granted under the Stock Plan may be subject to stock options. No more than 1,000,000 shares of our common stock may be made subject to awards under the Stock Plan to any individual in any year.

On June 26, 2006, the Compensation Committee of the Board of Directors of the Company approved individual stock option awards for certain officers and employees of the Company. Both non-qualified stock options ("NQSOs") and incentive stock options ("ISOs"), subject to the limitations of Section 422 of the Internal Revenue Code, were awarded under the Stock Plan. The terms and conditions of the stock options granted were determined by the Compensation Committee and set forth in award agreements between the Company and each award recipient. Options to purchase a total of 3,958,283 shares of stock were granted with vesting periods ranging from December 2006 to June 2014 and with an exercise price of $10.11. Upon exercise, the shares will be issued from our previously authorized shares. The full Board of Directors ratified and approved the grants on August 3, 2006, on which date the Company's common stock price fluctuated between $9.76 and $10.00.

On June 27, 2007, the Compensation Committee of the Board of Directors and the full Board of Directors of the Company approved a new grant of individual NQSO awards for certain officers and employees of the Company. The terms and conditions of the stock options granted were set forth in award agreements between the Company and each award recipient entered into on that date. Options to purchase a total of 1,700,609 shares of stock were granted with vesting periods ranging from December 2007 to June 2014 and with an exercise price of $11.11, which was the closing volume weighted average price of our shares of common stock on June 27, 2007. Upon exercise, the shares would be issued from our previously authorized but unissued shares.

The Company accounts for the Stock Plan in accordance with the provisions of SFAS No. 123(R), “Share-Based Payment,” which requires that we determine the fair value of all share-based payments to employees, including the fair value of grants of employee stock options, and record these amounts as an expense in the Statement of Operations over the vesting period with a corresponding increase to our additional paid-in capital. At December 31, 2007, the increase to our operating expenses was offset by the increase to our additional paid-in capital, resulting in no net impact to our net asset value. Additionally, the Company does not record the tax benefits associated with the expensing of stock options, because the Company currently intends to qualify as a RIC under Subchapter M of the Code.

An option's expected term is the estimated period between the grant date and the exercise date of the option. As the expected term period increases, the fair value of the option and the non-cash compensation cost will also increase. The expected term assumption is generally calculated using historical stock option exercise data. The Company does not have historical exercise data to develop such an assumption. In cases where companies do not have historical data and where the options meet certain criteria, SEC Staff Accounting Bulletin 107 ("SAB 107") provides the use of a simplified expected term calculation. Accordingly, the Company calculated the expected terms using the SAB 107 simplified method.

Expected volatility is the measure of how the stock's price is expected to fluctuate over a period of time. An increase in the expected volatility assumption yields a higher fair value of the stock option. Expected volatility factors for the stock options were based on the historical fluctuations in the Company’s stock price over a period commensurate with the expected term of the option, adjusted for stock splits and dividends.

The expected dividend yield assumption is traditionally calculated based on a company's historical dividend yield. An increase to the expected dividend yield results in a decrease in the fair value of option and resulting compensation cost. Although the Company has declared deemed dividends in previous years, most recently in 2005, the amounts and timing of any future dividends cannot be reasonably estimated. Therefore, for purposes of calculating fair value, the Company has assumed an expected dividend yield of 0 percent.

The risk-free interest rate assumptions are based on the annual yield on the measurement date of a zero-coupon U.S. Treasury bond the maturity of which equals the option's expected term. Higher assumed interest rates yield higher fair values.

The amount of non-cash, stock-based compensation expense recognized in the Consolidated Statements of Operations is based on the fair value of the awards the Company expects to vest, recognized over the vesting period on a straight-line basis for each award, and adjusted for actual forfeitures that occur before vesting. The forfeiture rate is estimated at the time of grant and revised, if necessary, in subsequent periods if the actual forfeiture rate differs from the estimated rate and is accounted for in the current period and prospectively.

The fair value of each stock option award is estimated on the date of grant using the Black-Scholes option pricing model as permitted by SFAS No. 123(R). The stock options granted on June 26, 2006, were awarded in five different grant types, each with different contractual terms. The assumptions used in the calculation of fair value of the stock options granted on June 26, 2006, using the Black-Scholes model for each contract term were as follows:

Type of Award	**Term**	**Number of Options Granted**	**Expected Term in Yrs**	**Expected Volatility Factor**	**Expected Dividend Yield**	**Risk-free Interest Rates**	**Weighted Average Fair Value Per Share**
Non-qualified stock options	1 Year	1,001,017	0.75	37.4%	0%	5.16%	$1.48
Non-qualified stock options	2 Years	815,000	1.625	45.2%	0%	5.12%	$2.63
Non-qualified stock options	3 Years	659,460	2.42	55.7%	0%	5.09%	$3.81
Non-qualified stock options	10 Years	690,000	5.75	75.6%	0%	5.08%	$6.94
Incentive stock options	10 Years	792,806	7.03	75.6%	0%	5.08%	$7.46
Total		3,958,283					$4.25

The stock options granted on June 27, 2007, were awarded in four different grant types, each with different contractual terms. The assumptions used in the calculation of fair value of the stock options granted on June 27, 2007, using the Black-Scholes model for each contract term were as follows:

Type of Award	**Contractual Term**	**Number of Options Granted**	**Expected Term in Yrs**	**Expected Volatility Factor**	**Expected Dividend Yield**	**Risk-free Interest Rates**	**Fair Value Per Share**
Non-qualified stock options	1.5 Years	380,000	1	42.6%	0%	4.93%	$2.11
Non-qualified stock options	2.5 Years	600,540	2	40.1%	0%	4.91%	$2.92
Non-qualified stock options	3.5 Years	338,403	3	44.7%	0%	4.93%	$3.94

Non-qualified stock options	9 Years	381,666	Ranging from 4.75-6.28	Ranging from 57.8% to 59.9%	0%	Ranging from 4.97% to 5.01%	Ranging from $5.92 to $6.85
Total		1,700,609					

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For the years ended December 31, 2007, and December 31, 2006, the Company recognized $8,050,807 and $5,038,956 of compensation expense in the Consolidated Statements of Operations, respectively. As of December 31, 2007, there was approximately $7,810,508 of unrecognized compensation cost related to unvested stock option awards. This cost is expected to be recognized over a weighted-average period of approximately 1.7 years.

For the year ended December 31, 2007, a total of 999,556 options were exercised for total proceeds to the Company of $10,105,511. For the year ended December 31, 2006, a total of 258,672 shares were exercised for total proceeds to the Company of $2,615,190. At December 31, 2006, the Company had a broker receivable totaling $819,905 for proceeds from stock option exercises transacted on December 29, 2006. The Company received these proceeds on January 3, 2007.

The grant date fair value of options vested during the years ended December 31, 2007, and December 31, 2006, was $6,851,874 and $3,781,681, respectively.

For the years ended December 31, 2007, and December 31, 2006, the calculation of the net decrease in net assets resulting from operations per share excludes the stock options because such options were anti-dilutive. The options may be dilutive in future periods in which there is a net increase in net assets resulting from operations, in the event that there is a significant increase in the average stock price in the stock market or significant decreases in the amount of unrecognized compensation cost.

A summary of the changes in outstanding stock options is as follows:

	Shares	Weighted Average Exercise Price	Weighted Average Grant Date Fair Value	Weighted Average Remaining Contractual Term (Yrs)	Aggregate Intrinsic Value
Options Outstanding at December 31, 2006	3,699,611	$ 10.11	$ 4.43		
Granted	1,700,609	$ 11.11	$ 3.68	3.43	
Exercised	(999,556)	$ 10.11	$ 1.97		
Forfeited or Expired	(432,920)		$ 3.99		
Options Outstanding at December 31, 2007	3,967,744	$ 10.54	$ 4.77	4.58	$0
Options Exercisable at December 31, 2007	1,717,125	$ 10.43	$ 4.45	4.18	$0
Options Exercisable and Expected to be Exercisable at December 31, 2007	3,858,226	$ 10.55	$ 4.70	4.47	$0

The aggregate intrinsic value in the table above with respect to options outstanding, exercisable and expected to be exercisable, is calculated as the difference between the Company's closing stock price of $8.79 on the last trading day of 2007 and the exercise price, multiplied by the number of in-the-money options. This calculation represents the total pre-tax intrinsic value that would have been received by the option holders had all options been fully vested and all option holders exercised their awards on December 31, 2007.

For the twelve months ended December 31, 2007, the aggregate intrinsic value of the 999,556 options exercised was $1,700,552. For the twelve months ended December 31, 2006, the aggregate intrinsic value for the 258,672 options exercised was $512,171.

Unless earlier terminated by our Board of Directors, the Stock Plan will expire on May 4, 2016. The expiration of the Stock Plan will not by itself adversely affect the rights of plan participants under awards that are outstanding at the time the Stock Plan expires. Our Board of Directors may terminate, modify or suspend the plan at any time, provided that no modification of the plan will be effective unless and until any required shareholder approval has been obtained. The Compensation Committee may terminate, modify or amend any outstanding award under the Stock Plan at any time, provided that in such event, the award holder may exercise any vested options prior to such termination of the Stock Plan or award.

NOTE 5. EMPLOYEE PROFIT-SHARING PLAN

Prior to the adoption of the Stock Plan, the Company operated the Amended and Restated Harris & Harris Group, Inc. Employee Profit-Sharing Plan (the "2002 Plan"). Effective May 4, 2006, the 2002 Plan was terminated.

The 2002 Plan (and its predecessor) provided for profit sharing by our officers and employees equal to 20 percent of our "qualifying income" for that plan year.

As soon as practicable following the year-end, the Compensation Committee determined whether, and if so how much, qualifying income existed for a plan year. Approximately 90 percent of the amount determined by the Compensation Committee was then paid out to plan participants pursuant to the distribution percentages set forth in the 2002 Plan. The remaining payment was paid out after we finalized our tax returns for that plan year.

At December 31, 2006, we accrued $261,661 for profit sharing related to the 2005 plan year. On March 1, 2006, the Company paid $1,897,072 to plan participants (employees and former employees), which represented approximately 90 percent of the total estimated profit-sharing payment for 2005. The balance of $261,661 related to the 2005 plan year was paid on January 31, 2007, upon finalization of our tax returns.

NOTE 6. DISTRIBUTABLE EARNINGS

As of December 31, 2007, December 31, 2006, and December 31, 2005, there were no distributable earnings. The difference between the book basis and tax basis components of distributable earnings is primarily nondeductible deferred compensation and net operating losses.

On December 20, 2005, the Company declared a designated undistributed capital gain dividend ("deemed dividend") for shareholders of record as of December 31, 2005. The deemed dividend for 2005 was $23,206,763. See “Note 8. Income Taxes.” The Company did not declare dividends for the years ended December 31, 2007, or December 31, 2006.

NOTE 7. EMPLOYEE BENEFITS

Employment Agreement with CEO

Pursuant to his employment agreement, as most recently amended as of August 2, 2007 (the "Employment Agreement"), during the period of employment, Charles E. Harris is to receive compensation in the form of base salary, with automatic yearly adjustments to reflect inflation, which amounted to a minimum required base salary of $246,651 for 2006. In addition, the Board may increase such salary, and subsequently decrease it, but not below the level provided for by the automatic adjustments described above. Mr. Harris's base salary for 2006 was increased to $300,000 (thereby also increasing his SERP benefit as described below) in part in recognition of a 74 percent decrease in Mr. Harris's profit-sharing allocation in recent years in order to provide additional profit sharing to other employees. This was the first salary increase for Mr. Harris, other than cost-of-living adjustments, since 1994. Mr. Harris's base salary for 2007 and 2008 was increased to $306,187 and $314,623, respectively, based on cost-of-living adjustments.

Under his employment agreement, Mr. Harris is entitled to participate in all compensation and employee benefit plans or programs, and to receive all benefits, perquisites, and emoluments for which salaried employees are eligible. Under the Employment Agreement, we furnish Mr. Harris with certain perquisites, which include a company car, health-club membership, membership in certain social or country clubs, a reimbursement for an annual physical examination and up to a $5,000 annual reimbursement, adjusted for inflation, over the period of the agreement, for personal financial or tax advice.

The Employment Agreement also provides Mr. Harris with life insurance for the benefit of his designated beneficiary in the amount of at least $2,000,000; provides reimbursement for uninsured medical expenses, not to exceed $10,000 per annum, adjusted for inflation, over the period of the agreement; provides Mr. Harris and his spouse with long-term care insurance; and provides Mr. Harris with disability insurance providing for continuation of 100 percent of his base salary for a specified period. These benefits are for the term of the Employment Agreement. The Employment Agreement provides that the term of Mr. Harris's employment may not be extended beyond December 31, 2008, unless a committee of the Board consisting of non-interested Directors extends the date by one year pursuant to the Executive Mandatory Retirement Benefit Plan, and Mr. Harris agrees to serve beyond December 31, 2008.

Mr. Harris's Employment Agreement also provides for a supplemental executive retirement plan (the "SERP") and a severance compensation agreement for his benefit as discussed below.

In the event of termination without cause or by constructive discharge, Mr. Harris’s Employment Agreement provides for the continuation of certain benefits over specified periods, as well as severance pay, payable to Mr. Harris (or to his estate if he dies before all payments are made), equal to two times his base salary distributed over a period of two years.

Other than Mr. Harris, our Chairman and Chief Executive Officer, none of our executive officers has a change in control agreement. None of our executive officers is entitled to any special payments solely upon a change in control.

In addition, Mr. Harris is entitled to receive severance pay pursuant to the severance compensation agreement that he entered into with us, effective August 15, 1990, and amended and restated effective as of January 1, 2005. The severance compensation agreement provides that if, following a change in our control, as defined in the agreement, Mr. Harris’s employment is terminated by us without cause or by him within one year of such change in control, he shall be entitled to receive compensation in a lump sum payment equal to 2.99 times his average base salary plus other amounts included in Mr. Harris’s income as compensation from the Company (but excluding bonus, incentive, profit sharing plan and equity compensation) as in effect over the most recent five years preceding the year in which the change in control occurred. Under the severance compensation agreement, Mr. Harris is also entitled to receive a lump sum payment equal to any amounts forfeited on account of his termination, under any employee pension benefit plan, including benefits under the Company’s executive mandatory retirement benefit plan. In addition, he is entitled to receive medical and health insurance coverage under the Company’s retiree medical benefit plan and all other benefits he would be eligible to receive in the event of termination without cause or by constructive discharge, although no duplicate benefits will be provided. In the event that Mr. Harris is entitled to receive 2.99 times his base salary under the severance compensation agreement, he shall not also be paid two times his base salary under the employment agreement.

SERP

The Employment Agreement provides that we adopt a supplemental executive retirement plan (the "SERP") for the benefit of Mr. Harris. Under the SERP, we will cause an amount equal to one-twelfth of Mr. Harris's current annual salary to be credited each month to a special account maintained on our books for the benefit of Mr. Harris, provided that Mr. Harris is employed by us on the last business day of such month. The amounts credited to the SERP Account are deemed invested or reinvested in such investments as are requested by Mr. Harris and agreed to by the Company. The SERP Account is credited and debited to reflect the deemed investment returns, losses and expenses attributed to such deemed investments and reinvestments in accordance with the terms of the SERP. Mr. Harris's benefit under the SERP equals the balance in the SERP Account and such benefit will always be 100 percent vested (i.e., not forfeitable).

In 2005, Mr. Harris received a $125,000 distribution from the SERP Account. The balance of the SERP Account will be paid in a lump sum on May 30, 2008, and any subsequent balance will be paid on July 31, 2009.

If Mr. Harris dies before the entire benefit under the SERP Account has been paid to him, the amount remaining in the SERP Account will be distributed to his beneficiary in a lump-sum payment on the 90th day after the date of his death.

We have established a rabbi trust for the purpose of accumulating funds to satisfy the obligations incurred by us under the SERP, which amounted to $2,667,020 and $2,149,785 at December 31, 2007, and 2006, respectively, and is included in accounts payable and accrued liabilities. The restricted funds for the SERP Account totaled $2,667,020 and $2,149,785 at December 31, 2007, and 2006, respectively. Mr. Harris's rights to benefits pursuant to this SERP will be no greater than those of a general creditor of us.

401(k) Plan

We adopted a 401(k) Plan covering substantially all of our employees. Matching contributions to the plan are at the discretion of the Compensation Committee. For the year ended December 31, 2007, the Compensation Committee approved a 100 percent match which amounted to $176,873. The 401(k) Company match for the years ended December 31, 2006 and 2005 was $155,000 and $119,360, respectively.

Medical Benefit Retirement Plan

On June 30, 1994, we adopted a plan to provide medical and dental insurance for retirees, their spouses and dependents who, at the time of their retirement, have ten years of service with us and have attained 50 years of age or have attained 45 years of age and have 15 years of service with us. On February 10, 1997, we amended this plan to include employees who have seven full years of service and have attained 58 years of age. On November 3, 2005, we amended this plan to reverse the 1997 amendment for future retirees and to remove dependents other than spouses from the plan. The coverage is secondary to any government or subsequent employer provided health insurance plans. The annual premium cost to us with respect to the entitled retiree shall not exceed $12,000, subject to an index for inflation. On December 8, 2003, the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the "Act") was signed into law. The Act introduces a prescription drug benefit under Medicare (Medicare Part D) as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to Medicare Part D. The Act, which went into effect January 1, 2006, provides a 28 percent subsidy for post-65 prescription drug benefits. Our liability assumes our plan is actuarially equivalent under the Act.

The stock options of retirees who qualify for the Medical Benefit Retirement Plan will remain exercisable (to the extent exercisable at the time of the optionee’s termination) post retirement, if such retiree executes a post-termination non-solicitation agreement in a form reasonably acceptable to the Company, until the expiration of its term.

The plan is unfunded and has no assets. The following disclosures about changes in the benefit obligation under our plan to provide medical and dental insurance for retirees are as of the measurement date of December 31:

	2007	**2006**
Accumulated Postretirement Benefit Obligation at Beginning of Year	$ 696,827	$ 675,334
Service Cost	102,676	79,381
Interest Cost	33,935	33,786
Actuarial (Gain)/Loss	(196,248)	(84,879)
Benefits Paid	(8,445)	(6,795)
Accumulated Postretirement Benefit Obligation at End of Year	**$ 628,745**	**$ 696,827**

In accounting for the plan, the assumption made for the discount rate was 6.55 percent and 5.75 percent for the years ended December 31, 2007, and 2006, respectively. The assumed health care cost trend rates in 2007 were 9 percent grading to 6 percent over three years for medical and 5 percent per year for dental. The assumed health care cost trend rates in 2006 were 9 percent grading to 6 percent over three years for medical and 3 percent per year for dental. The effect on disclosure information of a one percentage point change in the assumed health care cost trend rate for each future year is shown below.

	1% Decrease in Rates	Assumed Rates	1% Increase in Rates
Aggregated Service and Interest Cost	$ 105,317	$ 136,611	$ 179,692
Accumulated Postretirement Benefit Obligation	$ 606,717	$ 628,745	$ 883,758

The net periodic postretirement benefit cost for the year is determined as the sum of service cost for the year, interest on the accumulated postretirement benefit obligation and amortization of the transition obligation (asset) less previously accrued expenses over the average remaining service period of employees expected to receive plan benefits. The following is the net periodic postretirement benefit cost for the years ended December 31, 2007, 2006, and 2005:

	2007	2006	2005
Service Cost	$ 102,676	$ 79,381	$ 49,990
Interest Cost on Accumulated Postretirement Benefit Obligation	33,935	33,786	32,573
Amortization of Transition Obligation	0	0	0
Amortization of Net (Gain)/Loss	(6,234)	0	0
Net Periodic Post Retirement Benefit Cost	**$ 130,377**	**$ 113,167**	**$ 82,563**

The Company estimates the following benefits to be paid in each of the following years:

2008	$ 18,489
2009	$ 23,639
2010	$ 25,584
2011	$ 20,213
2012	$ 21,663
2013 through 2017	$135,078

The contribution payable for 2008 is estimated to be $18,489.

On December 31, 2006, the Company adopted the recognition and disclosure provisions of SFAS No. 158. SFAS No. 158 required the Company to recognize the funded status of its retirement benefit plans in the December 31, 2006 statement of assets and liabilities with a corresponding adjustment to net assets. The adjustment to net assets at adoption of $61,527 represents the net unrecognized actuarial gains of $95,145 applicable to the healthcare benefit plan net of $33,618 of unrecognized actuarial losses applicable to the Executive Mandatory Retirement Benefit Plan. Such amounts previously were reflected as a net increase of the plan's funded status in the Company's statement of assets and liabilities pursuant to the provisions of SFAS Nos. 106 and 187. These amounts will be subsequently recognized as net periodic benefit cost pursuant to the Company's historical accounting policy for amortizing such amounts. Further, actuarial gains and losses that arise in subsequent periods and are not recognized as net periodic benefit cost in the same periods will be recognized as a component of net assets. Those amounts will be subsequently recognized as a component of net periodic benefit cost on the same basis as the amounts recognized at adoption of SFAS No. 158.

For the year ended December 31, 2007, net unrecognized actuarial gains, which resulted from the increase in the discount rate referred to above, increased by $190,014, which represents $196,248 of actuarial gains arising during the year, net of a $6,234 reclassification adjustment which reduced the net periodic benefit cost for the year.

Executive Mandatory Retirement Benefit Plan

On March 20, 2003, in order to begin planning for eventual management succession, the Board of Directors voted to establish the Executive Mandatory Retirement Benefit Plan for individuals who are employed by us in a bona fide executive or high policy-making position. The plan was amended and restated effective January 1, 2005, to comply with certain provisions of the Internal Revenue Code. There are currently four individuals that qualify under the plan: Charles E. Harris, the Chairman and Chief Executive Officer, Douglas W. Jamison, the President and Chief Operating Officer, Daniel B. Wolfe, the Chief Financial Officer, and Mel P. Melsheimer, the former President, Chief Operating Officer and Chief Financial Officer. Under this plan, mandatory retirement takes place effective December 31 of the year in which the eligible individuals attain the age of 65. On an annual basis beginning in the year in which the designated individual attains the age of 65, a committee of the Board consisting of non-interested directors may determine for our benefit to postpone the mandatory retirement date for that individual for one additional year.

Under applicable law prohibiting discrimination in employment on the basis of age, we can impose a mandatory retirement age of 65 for our executives or employees in high policy-making positions only if each employee subject to the mandatory retirement age is entitled to an immediate retirement benefit at retirement age of at least $44,000 per year. The benefits payable at retirement to Mr. Harris and Mr. Melsheimer under our existing 401(k) plan do not equal this threshold. The plan was established to provide the difference between the benefit required under the age discrimination laws and that provided under our existing plans. For individuals retiring after 2007, the benefit under the plan is paid to the qualifying individual in the form of a lump sum, and is paid six months and one day after the individual’s separation from service with the Company, pursuant to certain exceptions.

At December 31, 2007, and 2006, we had accrued $382,932 and $347,075, respectively, for benefits under this plan. At December 31, 2007, $235,630 was accrued for Mr. Melsheimer and $147,302 was accrued for Mr. Harris. Currently, there is no accrual for Mr. Jamison or Mr. Wolfe. This benefit will be unfunded, and the expense as it relates to Mr. Melsheimer and Mr. Harris is being amortized over the fiscal periods through the years ended December 31, 2004, and 2008, respectively. On December 31, 2004, Mr. Melsheimer retired pursuant to the Executive Mandatory Retirement Benefit Plan. His annual benefit under the plan is $22,915. Mr. Harris's projected mandatory benefit will be approximately $147,302 and paid as a lump sum six months and one day after his retirement.

NOTE 8. INCOME TAXES

We filed for the 1999 tax year to elect treatment as a regulated investment company ("RIC") under Subchapter M of the Internal Revenue Code of 1986 (the "Code") and qualified for the same treatment for the years 2000 through 2007. However, there can be no assurance that we will qualify as a RIC for 2008 or subsequent years.

In the case of a RIC, which furnishes capital to development corporations, there is an exception to the rule relating to the diversification of investments required to qualify for RIC treatment. This exception is available only to registered management investment companies which the SEC determines to be principally engaged in the furnishing of capital to other corporations which are principally engaged in the development or exploitation of inventions, technological improvements, new processes, or products not previously generally available ("SEC Certification"). We have received SEC Certification since 1999, including for 2006, but it is possible that we may not receive SEC Certification in future years.

In addition, under certain circumstances, even if we qualified for Subchapter M treatment for a given year, we might take action in a subsequent year to ensure that we would be taxed in that subsequent year as a C Corporation, rather than as a RIC. As a RIC, we must, among other things, distribute at least 90 percent of our investment company taxable income and may either distribute or retain our realized net capital gains on investments.

Provided that a proper election is made, a corporation taxable under Subchapter C of the Code or a C Corporation that elects to qualify as a RIC continues to be taxable as a C Corporation on any gains realized within 10 years of its qualification as a RIC (the "Inclusion Period") from sales of assets that were held by the corporation on the effective date of the RIC election ("C Corporation Assets"), to the extent of any gain built into the assets on such date ("Built-In Gain"). If the corporation fails to make a proper election, it is taxable on its Built-In Gain as of the effective date of its RIC election. We had Built-In Gains at the time of our qualification as a RIC and made the election to be taxed on any Built-In Gain realized during the Inclusion Period.

To the extent that we retain capital gains and declare a deemed dividend to shareholders, the dividend is taxable to the shareholders. We would pay tax on behalf of shareholders, at the corporate rate, on the distribution, and the shareholders would receive a tax credit equal to their proportionate share of the tax paid. We took advantage of this rule for 2005. Included in net realized income from investments for the year ended December 31, 2005, were net realized gains before taxes of $23,862,037, which consisted primarily of a net realized long term capital gain on the sale of our investment in NeuroMetrix, Inc., offset by realized net long term capital losses on the sales of Agile Materials & Technologies, Inc., Experion Systems, Inc., Nanotechnologies, Inc., and Optiva, Inc. We applied $140,751 of our capital loss carryforwards and $501,640 of our pre-1999 loss carryforwards on Built-In Gains to these gains.

In December 2005, we declared a deemed dividend on net taxable realized long-term capital gains of $23,206,763. The Company recorded a tax payable on its Consolidated Statements of Assets and Liabilities of $8,122,367 for taxes payable on behalf of its shareholders. This distribution of $8,122,367 was also recorded as an income tax expense on the Consolidated Statements of Operations for the year ended December 31, 2005. Shareholders of record at December 31, 2005, received a tax credit of $0.39131971 per share. The balance of $15,084,396 was retained by the Company. The Company paid $8,122,367 of taxes on behalf of its shareholders on January 30, 2006. At December 31, 2005, we had $1,514,967 accrued for federal and state income taxes payable upon filing of our 2005 tax returns.

For federal tax purposes, the Company’s 2004 through 2007 tax years remain open for examination by the tax authorities under the normal three year statute of limitations. Generally, for state tax purposes, the Company’s 2004 through 2007 tax years remain open for examination by the tax authorities under a four year statute of limitations.

For the twelve months ended December 31, 2007, we paid $74,454 in interest and penalties related to the federal income tax on Built-In Gains recognized in the Company's 2005 tax year, which is included in income tax expense. During 2007, we paid $10,290 in federal, state and local income taxes. At December 31, 2007, we had $0 accrued for federal, state and local taxes payable by the Company.

We pay federal, state and local taxes on behalf of our wholly owned subsidiary, Harris & Harris Enterprises, Inc., which is taxed as a C Corporation. For the years ended December 31, 2007, 2006, and 2005, our income tax expense (benefit) for Harris & Harris Enterprises, Inc., was $3,231, $9,475 and ($6,411), respectively.

For the years ended December 31, 2007, 2006, and 2005, the Company's income tax (benefit) expense was allocated as follows:

		2007		2006		2005
Investment operations	$	0	$	0	$	0
Realized income on investments		87,975		(227,355)		1,530,881
Taxes paid on behalf of shareholders		0		0		8,122,367
Increase (decrease) in unrealized appreciation on investments		0		(0)		(1,364,470)
Total income tax (benefit) expense	$	87,975	$	(227,355)	$	8,288,778

The above tax expense consists of the following:

	2007	2006	2005
Current	$ 87,975	$ (227,355)	$ 9,653,248
Deferred -- Federal	__0	0	(1,364,470)
Total income tax (benefit) expense	$ 87,975	$ (227,355)	$ 8,288,778

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Continued qualification as a RIC requires us to satisfy certain investment asset diversification requirements in future years. Our ability to satisfy those requirements may not be controllable by us. There can be no assurance that we will qualify as a RIC in subsequent years.

NOTE 9. COMMITMENTS & GUARANTEES

On April 17, 2003, we signed a seven-year sublease for office space at 111 West 57th Street in New York City. On December 17, 2004, we signed a sublease for additional office space at our current location. The subleases expire on April 29, 2010. Total rent expense for our office space in New York City was $178,167 in 2007, $174,625 in 2006 and $171,171 in 2005. Future minimum sublease payments in each of the following years are: 2008 -- $193,083; 2009 -- $197,700; and thereafter, for the remaining term -- $65,969.

In the ordinary course of business, we indemnify our officers and directors, subject to certain regulatory limitations, for loss or liability related to their service on behalf of the Company, including serving on the Boards of Directors or as officers of portfolio companies. At December 31, 2007, and 2006, we believe our estimated exposure is minimal, and accordingly we have no liability recorded.

NOTE 10. CAPITAL TRANSACTIONS

On November 29, 2006, we filed a registration statement with the SEC on Form N-2 to register 4,000,000 shares of our common stock. On December 11, 2006, and on April 23, 2007, we filed amended registration statements with the SEC. On May 11, 2007, the SEC declared the registration statement effective. The common stock may be sold at prices and on terms to be set forth in one or more supplements to the prospectus from time to time.

On June 25, 2007, we completed the sale of 1,300,000 shares of our common stock for gross proceeds of $14,027,000; net proceeds of this offering, after placement agent fees and offering costs of $1,033,832, were $12,993,168.

NOTE 11. CHANGE IN NET ASSETS PER SHARE

The following table sets forth the computation of basic and diluted per share net increases in net assets resulting from operations for the twelve months ended December 31, 2007, 2006, and 2005.

		2007		2006		2005
Numerator for (decrease) increase in net assets per share	$	(6,716,445)	$	(11,773,112)	$	6,716,376
Denominator for basic and diluted weighted average shares		22,393,030		20,759,547		18,471,770
Basic and diluted net (decrease) increase in net assets per share resulting from operations	$	(0.30)	$	(0.57)	$	0.36

NOTE 12. SUBSEQUENT EVENTS

On January 16, 2008, we made a $736,019 follow-on investment that has not yet been announced in a privately held tiny technology portfolio company.

On January 31, 2008, we made a $377,580 follow-on investment that has not yet been announced in a privately held tiny technology portfolio company.

On February 1, 2008, we made a $25,000 follow-on investment that has not yet been announced in a privately held tiny technology portfolio company.

On February 8, 2008, we made a $244,500 new investment in PolyRemedy, Inc.

On February 21, 2008, we made a $1,052,174 follow-on investment that has not yet been announced in a privately held tiny technology portfolio company.

On February 25, 2008, we made a $1,000,001 follow-on investment that has not yet been announced in a privately held tiny technology portfolio company.

On March 7, 2008, we made a $2,000,000 follow-on investment that has not yet been announced in a privately held tiny technology portfolio company.

NOTE 13. SELECTED QUARTERLY DATA (UNAUDITED)

	2007			
	1st Quarter	**2nd Quarter**	**3rd Quarter**	**4th Quarter**
Total investment income	$ 652,498	$ 637,701	$ 743,414	$ 672,023
Net operating loss	$ (2,667,118)	$ (2,891,667)	$ (3,117,595)	$ (3,151,163)
Net increase (decrease) in net assets resulting from operations	$ (6,390,160)	$ (4,093,644)	$ 604,237	$ 3,163,122
Net (decrease) increase in net assets resulting from operations per average outstanding share	$ (0.30)	$ (0.19)	$ 0.03	$ 0.16

	2006			
	1st Quarter	**2nd Quarter**	**3rd Quarter**	**4th Quarter**
Total investment income	$ 804,862	$ 785,265	$ 719,619	$ 719,015
Net operating loss	$ (767,743)	$ (693,887)	$ (2,988,790)	$ (3,162,515)
Net increase (decrease) in net assets resulting from operations	$ (1,653,990)	$ (1,282,997)	$ (2,588,092)	$ (6,248,033)
Net (decrease) increase in net assets resulting from operations per average outstanding share	$ (0.08)	$ (0.06)	$ (0.12)	$ (0.31)

HARRIS & HARRIS GROUP, INC.
FINANCIAL HIGHLIGHTS

	Year Ended December 31, 2007	Year Ended December 31, 2006	Year Ended December 31, 2005
Per Share Operating Performance			
Net asset value per share, beginning of year	$ 5.42	$ 5.68	$ 4.33
Net operating (loss) income*	(0.53)	(0.37)	(0.30)
Net realized income on investments*	0.00	0.01	0.77
Net increase (decrease) in unrealized appreciation (depreciation) as a result of sales*	0.00	0.00	(1.18)
Net increase (decrease) in unrealized appreciation (depreciation) on investments held*	0.23	(0.21)	1.07
Total from investment operations*	(0.30)	(0.57)	0.36
Net increase as a result of stock-based compensation expense*	0.36	0.24	0.00
Net increase as a result of proceeds from exercise of options	0.19	0.07	0.00
Net increase as a result of stock offering	0.26	0.00	0.99
Total increase from capital stock transactions	0.81	0.31	0.99
Net asset value per share, end of year	$ 5.93	$ 5.42	$ 5.68
Stock price per share, end of year	$ 8.79	$ 12.09	$ 13.90
Total return based on stock price	(27.3)%	(13.0)%	(15.1)%
Supplemental Data:			
Net assets, end of year	$ 138,363,344	$ 113,930,303	$ 117,987,742
Ratio of expenses to average net assets	11.6%	9.2%	7.5%
Ratio of net operating loss to average net assets	(9.5)%	(6.6)%	(5.8)%
Cash dividends paid per share	$ 0.00	$ 0.00	$ 0.00
Taxes payable on behalf of shareholders			

on the deemed dividend per share	$ 0.00	$ 0.00	$ 0.39
Number of shares outstanding, end of year	23,314,573	21,015,017	20,756,345

*Based on average shares outstanding.

The accompanying notes are an integral part of this schedule.

HARRIS & HARRIS GROUP, INC.
CONSOLIDATED STATEMENTS OF ASSETS AND LIABILITIES

ASSETS

	March 31, 2008 (Unaudited)	December 31, 2007
Investments, in portfolio securities at value (cost: $84,013,804 and $82,677,528, respectively)	$ 83,097,863	$ 78,110,384
Investments, in U.S. Treasury obligations at value (cost: $52,346,992 and $59,552,933, respectively)	53,589,100	60,193,593
Cash and cash equivalents	210,154	330,009
Restricted funds	2,520,310	2,667,020
Receivable from portfolio company	0	524
Interest receivable	497,488	647,337
Prepaid expenses	412,589	488,667
Other assets	445,135	455,798
Total assets	$ 140,772,639	$ 142,893,332

LIABILITIES & NET ASSETS

	March 31, 2008 (Unaudited)	December 31, 2007
Accounts payable and accrued liabilities	$ 4,218,484	$ 4,515,463
Deferred rent	12,866	14,525
Total liabilities	4,231,350	4,529,988
Net assets	$ 136,541,289	$ 138,363,344
Net assets are comprised of:		
Preferred stock, $0.10 par value, 2,000,000 shares authorized; none issued	$ 0	$ 0
Common stock, $0.01 par value, 45,000,000 shares authorized at 3/31/08 and 12/31/07; 25,143,313 issued at 3/31/08 and 12/31/07	251,434	251,434
Additional paid in capital (Note 5)	162,394,671	160,927,691
Accumulated net realized loss	(23,025,452)	(15,483,766)
Accumulated unrealized appreciation (depreciation) of investments	326,167	(3,926,484)
Treasury stock, at cost (1,828,740 shares at 3/31/08 and 12/31/07)	(3,405,531)	(3,405,531)
Net assets	$ 136,541,289	$ 138,363,344

Shares outstanding		23,314,573		23,314,573
Net asset value per outstanding share	$	5.86	$	5.93

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

HARRIS & HARRIS GROUP, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended March 31, 2008	Three Months Ended March 31, 2007
Investment income:		
Interest from:		
Fixed income securities	$ 576,302	$ 652,498
Total investment income	576,302	652,498
Expenses:		
Salaries, benefits and stock-based compensation (Note 5)	2,433,295	2,534,766
Administration and operations	301,855	380,865
Professional fees	138,232	182,195
Rent	57,854	59,507
Directors' fees and expenses	105,146	141,196
Depreciation	13,985	15,313
Custodian fees	6,553	5,774
Total expenses	3,056,920	3,319,616
Net operating loss	(2,480,618)	(2,667,118)
Net realized loss from investments:		
Realized (loss) from investments	(5,014,870)	(674)
Income tax expense (Note 6)	46,198	84,905
Net realized (loss) from investments	(5,061,068)	(85,579)
Net decrease (increase) in unrealized depreciation on investments:		
Change as a result of investment sales	5,014,653	0
Change on investments held	(762,002)	(3,637,463)
Change in unrealized depreciation on investments	4,252,651	(3,637,463)
Net decrease (increase) in unrealized depreciation on investments	4,252,651	(3,637,463)
Net decrease in net assets resulting from operations:		
Total	$ (3,289,035)	$ (6,390,160)
Per average basic and diluted outstanding share	$ (0.14)	$ (0.30)
Average outstanding shares	23,314,573	21,277,576

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

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HARRIS & HARRIS GROUP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Three Months Ended March 31, 2008	Three Months Ended March 31, 2007
Cash flows used in operating activities:		
Net decrease in net assets resulting from operations	$ (3,289,035)	$ (6,390,160)
Adjustments to reconcile net decrease in net assets resulting from operations to net cash used in operating activities:		
Net realized and unrealized loss on investments	762,219	3,638,137
Depreciation and amortization	(454,332)	(65,730)
Stock-based compensation expense	1,466,980	1,690,181
Changes in assets and liabilities:		
Restricted funds	146,710	(108,880)
Receivable from portfolio company	524	0
Interest receivable	149,849	61,997
Receivable from broker	0	819,905
Prepaid expenses	76,078	(416,635)
Other assets	(2,492)	(10,191)
Accounts payable and accrued liabilities	(296,978)	(209,292)
Accrued profit sharing	0	(261,661)
Deferred rent	(1,659)	(1,700)
Current income tax liability	541	80,795
Net cash used in operating activities	(1,441,595)	(1,173,234)
Cash flows from investing activities:		
Purchase of short-term investments and marketable securities	(21,230,754)	(10,952,109)
Sale of short-term investments and marketable securities	28,883,642	12,165,656
Investment in private placements and loans	(6,435,274)	(4,857,357)
Proceeds from sale of investments	105,714	0
Purchase of fixed assets	(1,588)	(270)
Net cash provided by (used in) investing activities	1,321,740	(3,644,080)
Cash flows from financing activities:		
Proceeds from stock option exercises (Note 5)	0	3,295,978
Net cash provided by financing activities	0	3,295,978
Net decrease in cash and cash equivalents:		
Cash and cash equivalents at beginning of the period	330,009	2,071,788

Cash and cash equivalents at end of the period		210,154		550,452
Net decrease in cash and cash equivalents	$	(119,855)	$	(1,521,336)
Supplemental disclosures of cash flow information:				
Income taxes paid	$	45,657	$	10,252

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

HARRIS & HARRIS GROUP, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS

	Three Months Ended March 31, 2008 (Unaudited)	Year Ended December 31, 2007
Changes in net assets from operations:		
Net operating loss	$ (2,480,618)	$ (11,827,543)
Net realized (loss) gain on investments	(5,061,068)	30,162
Net decrease in unrealized depreciation on investments sold	5,014,653	0
Net (increase) decrease in unrealized depreciation on investments held	(762,002)	5,080,936
Net decrease in net assets resulting from operations	(3,289,035)	(6,716,445)
Changes in net assets from capital stock transactions:		
Issuance of common stock upon the exercise of stock options	0	9,996
Issuance of common stock on offering	0	13,000
Additional paid-in capital on common stock issued	0	23,075,683
Stock-based compensation expense	1,466,980	8,050,807
Net increase in net assets resulting from capital stock transactions	1,466,980	31,149,486
Net (decrease) increase in net assets	(1,822,055)	24,433,041
Net assets:		
Beginning of the period	138,363,344	113,930,303
End of the period	$ 136,541,289	$ 138,363,344

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

HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF MARCH 31, 2008
(Unaudited)

	Method of Valuation (1)	Shares/ Principal		Value
Investments in Unaffiliated Companies (2)(3) - 15.64% of net assets at value				
Private Placement Portfolio (Illiquid) - 15.64% of net assets at value				
BioVex Group, Inc. (4)(5)(6)(7) -- Developing novel biologics for treatment of cancer and infectious disease				
Series E Convertible Preferred Stock	(M)	2,799,552	$	2,500,000
Exponential Business Development Company (4)(5) -- Venture capital partnership focused on early stage companies				
Limited Partnership Interest	(M)	1		2,219
Molecular Imprints, Inc. (4)(5) -- Manufacturing nanoimprint lithography capital equipment				
Series B Convertible Preferred Stock	(M)	1,333,333		2,000,000
Series C Convertible Preferred Stock	(M)	1,250,000		2,399,875
Warrants at $2.00 expiring 12/31/11	(I)	125,000		100,125
				4,500,000
Nanosys, Inc. (4)(5)(6) -- Developing zero and one-dimensional inorganic nanometer-scale materials and devices				
Series C Convertible Preferred Stock	(M)	803,428		2,370,113
Series D Convertible Preferred Stock	(M)	1,016,950		3,000,003
				5,370,116
Nantero, Inc. (4)(5)(6) -- Developing a high-density, nonvolatile, random access memory chip, enabled by carbon nanotubes				
Series A Convertible Preferred Stock	(M)	345,070		1,046,908
Series B Convertible Preferred Stock	(M)	207,051		628,172
Series C Convertible Preferred Stock	(M)	188,315		571,329

2,246,409

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

HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF MARCH 31, 2008
(Unaudited)

	Method of Valuation (1)	Shares/ Principal		Value
Investments in Unaffiliated Companies (2)(3) - 15.64% of net assets at value (cont.)				
Private Placement Portfolio (Illiquid) - 15.64% of net assets at value (cont.)				
NeoPhotonics Corporation (4)(5) -- Developing and manufacturing optical devices and components				
Common Stock	(M)	716,195	$	133,141
Series 1 Convertible Preferred Stock	(M)	1,831,256		1,831,256
Series 2 Convertible Preferred Stock	(M)	741,898		741,898
Series 3 Convertible Preferred Stock	(M)	2,750,000		2,750,000
Warrants at $0.15 expiring 01/26/10	(I)	16,364		1,571
Warrants at $0.15 expiring 12/05/10	(I)	14,063		1,350
				5,459,216
Polatis, Inc. (4)(5)(6)(8) -- Developing MEMS-based optical networking components				
Series A-1 Convertible Preferred Stock	(M)	16,775		0
Series A-2 Convertible Preferred Stock	(M)	71,611		132,653
Series A-4 Convertible Preferred Stock	(M)	4,774		8,768
Series A-5 Convertible Preferred Stock	(M)	16,438		135,105
				276,526
PolyRemedy, Inc. (4)(5)(6)(9) --Developing a robotic manufacturing platform for wound treatment patches				
Series B-1 Convertible Preferred Stock	(M)	287,647		244,500
Starfire Systems, Inc. (4)(5)(6) -- Producing ceramic-forming polymers				
Common Stock	(M)	375,000		150,000
Series A-1 Convertible Preferred Stock	(M)	600,000		600,000
				750,000
Total Unaffiliated Private Placement Portfolio (cost: $21,679,892)			**$**	**21,348,986**

Total Investments in Unaffiliated Companies (cost: $21,679,892)	**$**	**21,348,986**

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

HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF MARCH 31, 2008
(Unaudited)

	Method of Valuation (1)	Shares/ Principal		Value
Investments in Non-Controlled Affiliated Companies (2)(10) - 42.01% of net assets at value				
Private Placement Portfolio (Illiquid) - 42.01% of net assets at value				
Adesto Technologies Corporation (4)(5)(6) -- Developing semiconductor-related products enabled at the nanoscale				
Series A Convertible Preferred Stock	(M)	6,547,619	$	2,200,000
Ancora Pharmaceuticals, Inc. (4)(5)(6) -- Developing synthetic carbohydrates for pharmaceutical applications				
Series B Convertible Preferred Stock	(M)	909,091		639,062
Warrants at $1.06 expiring 05/01/08	(I)	754,717		8,302
				647,364
BridgeLux, Inc. (4)(5)(11) -- Manufacturing high-power light emitting diodes				
Series B Convertible Preferred Stock	(M)	1,861,504		2,792,256
Series C Convertible Preferred Stock	(M)	2,130,699		3,196,050
Series D Convertible Preferred Stock	(M)	666,667		1,000,001
Warrants at $0.7136 expiring 02/02/17	(I)	98,340		137,971
Warrants at $0.7136 expiring 04/26/17	(I)	65,560		92,374
				7,218,652
Cambrios Technologies Corporation (4)(5)(6) -- Developing nanowire-enabled electronic materials for the display industry				
Series B Convertible Preferred Stock	(M)	1,294,025		1,294,025
Series C Convertible Preferred Stock	(M)	1,300,000		1,300,000
				2,594,025
CFX Battery, Inc. (4)(5)(6)(12) -- Developing batteries using nanostructured materials				
Series A Convertible Preferred Stock	(M)	1,208,262		946,528
Crystal IS, Inc. (4)(5)(6) -- Developing single-crystal aluminum nitride substrates for optoelectronic devices				
Series A Convertible Preferred Stock	(M)	391,571		305,425
Series A-1 Convertible Preferred Stock	(M)	1,300,376		1,014,294

Warrants at $0.78 expiring 05/05/13	(I)		15,231	9,352
Warrants at $0.78 expiring 05/12/13	(I)		2,350	1,445
Warrants at $0.78 expiring 08/08/13	(I)		4,396	2,739
				1,333,255
CSwitch Corporation (4)(5)(6)(13) -- Developing next-generation, system-on-a-chip solutions for communications-based platforms				
Series A-1 Convertible Preferred Stock	(M)		6,863,118	3,431,559
Unsecured Convertible Bridge Note (including interest)	(M)	$	529,852	552,149
				3,983,708
D-Wave Systems, Inc. (4)(5)(6)(14) -- Developing high-performance quantum computing systems				
Series B Convertible Preferred Stock	(M)		2,000,000	2,160,584
Series C Convertible Preferred Stock	(M)		678,264	732,724
				2,893,308

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

HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF MARCH 31, 2008
(Unaudited)

	Method of Valuation (1)	Shares/ Principal		Value
Investments in Non-Controlled Affiliated Companies (2)(10) - 42.01% of net assets at value (cont.)				
Private Placement Portfolio (Illiquid) - 42.01% of net assets at value (cont.)				
Ensemble Discovery Corporation (4)(5)(6) -- Developing DNA Programmed Chemistry for the discovery of new classes of therapeutics and bioassays				
Series B Convertible Preferred Stock	(M)	1,449,275	$	2,000,000
Innovalight, Inc. (4)(5)(6) -- Developing solar power products enabled by silicon-based nanomaterials				
Series B Convertible Preferred Stock	(M)	16,666,666		5,718,216
Series C Convertible Preferred Stock	(M)	5,810,577		1,993,568
				7,711,784
Kereos, Inc. (4)(5)(6) -- Developing emulsion-based imaging agents and targeted therapeutics to image and treat cancer and cardiovascular disease				
Series B Convertible Preferred Stock	(M)	545,456		120,850
Kovio, Inc. (4)(5)(6) -- Developing semiconductor products using printed electronics and thin-film technologies				
Series C Convertible Preferred Stock	(M)	2,500,000		3,125,000
Series D Convertible Preferred Stock	(M)	800,000		1,000,000
				4,125,000
Mersana Therapeutics, Inc. (4)(5)(6)(15) -- Developing advanced polymers for drug delivery				
Series A Convertible Preferred Stock	(M)	68,451		136,902
Series B Convertible Preferred Stock	(M)	866,500		1,733,000
Warrants at $2.00 expiring 10/21/10	(I)	91,625		112,974
				1,982,876
Metabolon, Inc. (4)(5)(6) -- Discovering biomarkers through the use of metabolomics				

Series B Convertible Preferred Stock	(M)	2,173,913	1,765,535
Series B-1 Convertible Preferred Stock	(M)	869,565	706,214
Warrants at $1.15 expiring 3/25/15	(I)	434,783	293,786
			2,765,535
NanoGram Corporation (4)(5)(6) -- Developing a broad suite of intellectual property utilizing nanoscale materials			
Series I Convertible Preferred Stock	(M)	63,210	124,524
Series II Convertible Preferred Stock	(M)	1,250,904	2,464,281
Series III Convertible Preferred Stock	(M)	1,242,144	2,447,024
Series IV Convertible Preferred Stock	(M)	432,179	851,393
			5,887,222
Nanomix, Inc. (4)(5)(6) -- Producing nanoelectronic sensors that integrate carbon nanotube electronics with silicon microstructures			
Series C Convertible Preferred Stock	(M)	977,917	330,228
Series D Convertible Preferred Stock	(M)	6,802,397	680,240
			1,010,468

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

HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF MARCH 31, 2008
(Unaudited)

	Method of Valuation (1)		Shares/ Principal		Value
Investments in Non-Controlled Affiliated Companies (2)(10) - 42.01% of net assets at value (cont.)					
Private Placement Portfolio (Illiquid) - 42.01% of net assets at value (cont.)					
Nextreme Thermal Solutions, Inc. (4)(5)(6) -- Developing thin-film thermoelectric devices for cooling and energy conversion					
Series A Convertible Preferred Stock	(M)		1,750,000	$	1,750,000
Unsecured Convertible Bridge Note	(M)	$	377,580		377,580
					2,127,580
Questech Corporation (4)(5) -- Manufacturing and marketing proprietary metal and stone decorative tiles					
Common Stock	(M)		655,454		129,717
Warrants at $1.50 expiring 11/19/08	(I)		5,000		5
Warrants at $1.50 expiring 11/19/09	(I)		5,000		95
					129,817
Siluria Technologies, Inc. (4)(5)(6) -- Developing next-generation nanomaterials					
Series S-2 Convertible Preferred Stock	(M)		482,218		160,723
Solazyme, Inc. (4)(5)(6) -- Developing algal biodiesel, industrial chemicals and special ingredients based on synthetic biology					
Series A Convertible Preferred Stock	(M)		988,204		997,691
Series B Convertible Preferred Stock	(M)		495,246		500,000
Unsecured Convertible Bridge Note (including interest)	(M)	$	2,000,000		2,009,534
					3,507,225
Xradia, Inc. (4)(5) -- Designing, manufacturing and selling ultra-high resolution 3D x-ray microscopes and fluorescence imaging systems					
Series D Convertible Preferred Stock	(M)		3,121,099		4,000,000
Zia Laser, Inc. (4)(5)(16) -- Developed quantum dot					

semiconductor lasers				
Series C Convertible Preferred Stock	(M)	1,500,000		21,330
Total Non-Controlled Private Placement Portfolio (cost: $55,371,901)			**$**	**57,367,250**
Total Investments in Non-Controlled Affiliated Companies (cost: $55,371,901)			**$**	**57,367,250**

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

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HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF MARCH 31, 2008
(Unaudited)

	Method of Valuation (1)		Shares/ Principal		Value
Investments in Controlled Affiliated Companies (2)(17) - 3.21% of net assets at value					
Private Placement Portfolio (Illiquid) - 3.21% of net assets at value					
Evolved Nanomaterial Sciences, Inc. (4)(5)(18) -- Developed nanoscale-enhanced approaches for the resolution of chiral molecules					
Series A Convertible Preferred Stock	(M)		5,870,021	$	0
Phoenix Molecular Corporation (4)(5)(6) -- Developing technology to enable the separation of difficult-to-separate materials.					
Common Stock	(M)		1,000		10
Unsecured Convertible Bridge Note (including interest)	(M)	$	75,000		77,001
					77,011
SiOnyx, Inc. (4)(5)(6) -- Developing silicon-based optoelectronic products enabled by its proprietary "Black Silicon"					
Series A Convertible Preferred Stock	(M)		233,499		135,686
Series A-1 Convertible Preferred Stock	(M)		2,966,667		1,723,930
Series A-2 Convertible Preferred Stock	(M)		4,207,537		2,445,000
					4,304,616
Total Controlled Private Placement Portfolio (cost: $6,962,011)				**$**	**4,381,627**
Total Investments in Controlled Affiliated Companies (cost: $6,962,011)				**$**	**4,381,627**
Total Private Placement Portfolio (cost: $84,013,804)				**$**	**83,097,863**
U.S. Government and Agency Securities - 39.25% of net assets at value					
U.S. Treasury Bill -- due date 04/17/08	(M)	$	3,050,000	$	3,048,384
U.S. Treasury Notes -- due date 05/15/08, coupon 3.75%	(M)		9,000,000		9,026,010

U.S. Treasury Notes -- due date 09/15/08, coupon 3.125%	(M)	5,000,000		5,039,850
U.S. Treasury Notes -- due date 01/15/09, coupon 3.25%	(M)	3,000,000		3,041,490
U.S. Treasury Notes -- due date 02/15/09, coupon 4.50%	(M)	5,100,000		5,228,316
U.S. Treasury Notes -- due date 04/15/09, coupon 3.125%	(M)	3,000,000		3,050,160
U.S. Treasury Notes -- due date 07/15/09, coupon 3.625%	(M)	3,000,000		3,079,440
U.S. Treasury Notes -- due date 10/15/09, coupon 3.375%	(M)	3,000,000		3,081,330
U.S. Treasury Notes -- due date 01/15/10, coupon 3.625%	(M)	3,000,000		3,105,690
U.S. Treasury Notes -- due date 04/15/10, coupon 4.00%	(M)	3,000,000		3,142,020
U.S. Treasury Notes -- due date 07/15/10, coupon 3.875%	(M)	3,000,000		3,155,160
U.S. Treasury Notes -- due date 10/15/10, coupon 4.25%	(M)	2,000,000		2,130,000
U.S. Treasury Notes -- due date 10/31/12, coupon 3.875%	(M)	2,000,000		2,126,100
U.S. Treasury Notes -- due date 02/15/13, coupon 3.875%	(M)	5,000,000		5,335,150
Total Investments in U.S. Government and Agency Securities (cost: $52,346,992)			**$**	**53,589,100**
Total Investments (cost: $136,360,796)			**$**	**136,686,963**

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

HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF MARCH 31, 2008
(Unaudited)

Notes to Consolidated Schedule of Investments

(1) See Footnote to Consolidated Schedule of Investments on page F-51 for a description of the Valuation Procedures.

(2) Investments in unaffiliated companies consist of investments in which we own less than five percent of the voting shares of the portfolio company. Investments in non-controlled affiliated companies consist of investments in which we own five percent or more, but less than 25 percent, of the voting shares of the portfolio company, or where we hold one or more seats on the portfolio company's Board of Directors but do not control the company. Investments in controlled affiliated companies consist of investments in which we own 25 percent or more of the voting shares of the portfolio company or otherwise control the company.

(3) The aggregate cost for federal income tax purposes of investments in unaffiliated companies is $21,679,892. The gross unrealized appreciation based on the tax cost for these securities is $1,732,194. The gross unrealized depreciation based on the tax cost for these securities is $2,063,100.

(4) Legal restrictions on sale of investment.

(5) Represents a non-income producing security. Equity investments that have not paid dividends within the last 12 months are considered to be non-income producing.

(6) These investments are development stage companies. A development stage company is defined as a company that is devoting substantially all of its efforts to establishing a new business, and either it has not yet commenced its planned principal operations, or it has commenced such operations but has not realized significant revenue from them.

(7) With our purchase of Series E Convertible Preferred Stock of BioVex, we received a warrant to purchase a number of shares of common stock of BioVex as determined by dividing 624,999.99 by the price per share at which the common stock is offered and sold to the public in connection with the initial public offering. The ability to exercise this warrant is therefore contingent on BioVex completing successfully an initial public offering before the expiration date of the warrant on September 27, 2012. The exercise price of this warrant shall be 110 percent of the initial public offering price.

(8) Continuum Photonics, Inc., merged with Polatis, Ltd., to form Polatis, Inc.

(9) Initial investment was made during 2008.

(10) The aggregate cost for federal income tax purposes of investments in non-controlled affiliated companies is $55,371,901. The gross unrealized appreciation based on the tax cost for these securities is $10,844,376. The gross unrealized depreciation based on the tax cost for these securities is $8,849,027.

(11) BridgeLux, Inc., was previously named eLite Optoelectronics, Inc.

(12) On February 28, 2008, Lifco, Inc., merged with CFX Battery, Inc. The surviving entity is CFX Battery, Inc.

(13) With our investment in a secured convertible bridge note issued by CSwitch, we received a warrant to purchase a number of shares of the class of stock sold in the next financing of CSwitch equal to $529,322, the principal of the note, divided by the lowest price per share of the class of stock sold in the next financing of CSwitch. The ability to exercise this warrant is therefore contingent on CSwitch completing successfully a subsequent round of financing. The warrant will expire five years from the date of the close of the next round of financing. The cost basis of this warrant is $529.

(14) D-Wave Systems, Inc., is located and is doing business primarily in Canada. We invested in D-Wave Systems, Inc., through D-Wave USA, a Delaware company. Our investment is denominated in Canadian dollars and is subject to foreign currency translation. See "Note 3. Summary of Significant Accounting Policies."

The accompanying notes are an integral part of this consolidated schedule.

HARRIS & HARRIS GROUP, INC.
CONSOLIDATED SCHEDULE OF INVESTMENTS AS OF MARCH 31, 2008
(Unaudited)

(15) Mersana Therapeutics, Inc., was previously named Nanopharma Corp.

(16) On November 30, 2006, the assets of Zia Laser, Inc., were acquired by Innolume Inc.

(17) The aggregate cost for federal income tax purposes of investments in controlled affiliated companies is $6,962,011. The gross unrealized appreciation based on the tax cost for these securities is $219,616. The gross unrealized depreciation based on the tax cost for these securities is $2,800,000.

(18) On September 30, 2007, Evolved Nanomaterial Sciences, Inc., filed for Chapter 7 bankruptcy.

The accompanying notes are an integral part of this consolidated schedule.

HARRIS & HARRIS GROUP, INC.
FOOTNOTE TO CONSOLIDATED SCHEDULE OF INVESTMENTS
(Unaudited)

VALUATION PROCEDURES

I. Determination of Net Asset Value

The 1940 Act requires periodic valuation of each investment in the portfolio of the Company to determine its net asset value. Under the 1940 Act, unrestricted securities with readily available market quotations are to be valued at the current market value; all other assets must be valued at fair value as determined in good faith by or under the direction of the Board of Directors.

The Board of Directors is responsible for (1) determining overall valuation guidelines and (2) ensuring that the investments of the Company are valued within the prescribed guidelines.

The Valuation Committee, comprised of all of the independent Board members, is responsible for reviewing and approving the valuation of the Company’s assets within the guidelines established by the Board of Directors. The Valuation Committee receives information and recommendations from management.

The values assigned to these investments are based on available information and do not necessarily represent amounts that might ultimately be realized, as such amounts depend on future circumstances and cannot reasonably be determined until the individual investments are actually liquidated or become readily marketable.

II. Approaches to Determining Fair Value

Statement of Financial Accounting Standards No. 157, "Fair Value Measurements," ("SFAS No. 157") defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price).

The main approaches to measuring fair value utilized are the market approach and the income approach.

- Market Approach (M): The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities. For example, the market approach often uses market multiples derived from a set of comparables. Multiples might lie in ranges with a different multiple for each comparable. The selection of where within the range each appropriate multiple falls requires judgment considering factors specific to the measurement (qualitative and quantitative).

- Income Approach (I): The income approach uses valuation techniques to convert future amounts (for example, cash flows or earnings) to a single present value amount (discounted). The measurement is based on the value indicated by current market expectations about those future amounts. Those valuation techniques include present value techniques; option-pricing models, such as the Black-Scholes-Merton formula (a closed-form model) and a binomial model (a lattice model), which incorporate present value techniques; and the multi-period excess earnings method, which is used to measure the fair value of certain assets.

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

- Level 1: Unadjusted quoted prices in active markets for identical assets or liabilities.

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

- Level 3: Unobservable inputs for the asset or liability.

Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

III. Investment Categories

The Company's investments can be classified into five broad categories for valuation purposes:

- Equity-related securities;
- Investments in intellectual property, patents, research and development in technology or product development;
- Long-term fixed-income securities;
- Short-term fixed-income securities; and
- All other securities.

The Company applies the methods for determining fair value discussed above to the valuation of investments in each of these five broad categories as follows:

A. EQUITY-RELATED SECURITIES

Equity-related securities, including warrants, are fair valued using the market or income approaches. The following factors may be considered when the market approach is used to fair value these types of securities:

- Readily available public market quotations;
- The cost of the Company's investment;
- Transactions in a company's securities or unconditional firm offers by responsible parties as a factor in determining valuation;
- The financial condition and operating results of the company;
- The long-term potential of the business and technology of the company;
- The values of similar securities issued by companies in similar businesses;
- Multiples to revenue, net income or EBITDA that similar securities issued by companies in similar businesses receive;
- The proportion of the company's securities we own and the nature of any rights to require the company to register restricted securities under applicable securities laws; and
- The rights and preferences of the class of securities we own as compared to other classes of securities the portfolio company has issued.

When the income approach is used to value warrants, the Company uses the Black-Scholes-Merton formula.

B. INVESTMENTS IN INTELLECTUAL PROPERTY, PATENTS, RESEARCH AND DEVELOPMENT IN TECHNOLOGY OR PRODUCT DEVELOPMENT

Such investments are fair valued using the market approach. The Company may consider factors specific to these types of investments when using the market approach including:

- The cost of the Company's investment;
-

Investments in the same or substantially similar intellectual property or patents or research and development in technology or product development or offers by responsible third parties;

- The results of research and development;
- Product development progress;
- Commercial prospects;
- Term of patent;
- Projected markets; and
- Other subjective factors.

C. LONG-TERM FIXED-INCOME SECURITIES

1. Readily Marketable: Long-term fixed-income securities for which market quotations are readily available are valued using the most recent bid quotations when available.

2. Not Readily Marketable: Long-term fixed-income securities for which market quotations are not readily available are fair valued using the market approach. The factors that may be considered when valuing these types of securities by the market approach include:

- Credit quality;
- Interest rate analysis;
- Quotations from broker-dealers;
- Prices from independent pricing services that the Board believes are reasonably reliable; and
- Reasonable price discovery procedures and data from other sources.

D. SHORT-TERM FIXED-INCOME SECURITIES

Short-term fixed-income securities are valued using the market approach in the same manner as long-term fixed-income securities until the remaining maturity is 60 days or less, after which time such securities may be valued at amortized cost if there is no concern over payment at maturity.

E. ALL OTHER SECURITIES

All other securities are reported at fair value as determined in good faith by the Valuation Committee using the approaches for determining valuation as described above.

For all other securities, the reported values shall reflect the Valuation Committee's judgment of fair values as of the valuation date using the outlined basic approaches of valuation discussed in Section II. They do not necessarily represent an amount of money that would be realized if we had to sell such assets in an immediate liquidation. Thus, valuations as of any particular date are not necessarily indicative of amounts that we may ultimately realize as a result of future sales or other dispositions of investments we hold.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE 1. THE COMPANY

Harris & Harris Group, Inc. (the "Company," "us," "our" and "we"), is a venture capital company operating as a business development company ("BDC") under the Investment Company Act of 1940 ("1940 Act"). We operate as an internally managed company whereby our officers and employees, under the general supervision of our Board of Directors, conduct our operations.

We elected to become a BDC on July 26, 1995, after receiving the necessary shareholder approvals. From September 30, 1992, until the election of BDC status, we operated as a closed-end, non-diversified investment company under the 1940 Act. Upon commencement of operations as an investment company, we revalued all of our assets and liabilities in accordance with the 1940 Act. Prior to September 30, 1992, we were registered and filed under the reporting requirements of the Securities Exchange Act of 1934 (the "1934 Act") as an operating company and, while an operating company, operated directly and through subsidiaries.

Harris & Harris Enterprises, Inc.,SM is a 100 percent wholly owned subsidiary of the Company. Harris & Harris Enterprises, Inc., is a partner in Harris Partners I, L.P.,SM and is taxed under Subchapter C of the Code (a “C Corporation”). Harris Partners I, L.P, is a limited partnership and is used to hold certain interests in portfolio companies. The partners of Harris Partners I, L.P., are Harris & Harris Enterprises, Inc., (sole general partner) and Harris & Harris Group, Inc., (sole limited partner). Harris & Harris Enterprises, Inc., pays taxes on any non-passive investment income generated by Harris Partners I, L.P. For the period ended March 31, 2008, there was no non-passive investment income. The Company consolidates the results of its subsidiaries for financial reporting purposes.

NOTE 2. INTERIM FINANCIAL STATEMENTS

Our interim financial statements have been prepared in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X and in conformity with generally accepted accounting principles applicable to interim financial information. Accordingly, they do not include all information and disclosures necessary for a presentation of our financial position, results of operations and cash flows in conformity with generally accepted accounting principles in the United States of America. In the opinion of management, these financial statements reflect all adjustments, consisting only of normal recurring accruals, necessary for a fair presentation of our financial position, results of operations and cash flows for such periods. The results of operations for any interim period are not necessarily indicative of the results for the full year. These financial statements should be read in conjunction with the financial statements and notes thereto contained in our Annual Report on Form 10-K for the fiscal year ended December 31, 2007.

NOTE 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The following is a summary of significant accounting policies followed in the preparation of the consolidated financial statements:

Principles of Consolidation. The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for investment companies and include the accounts of the Company and its wholly owned subsidiaries. All significant inter-company accounts and transactions have been eliminated in consolidation.

Use of Estimates. The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and contingent assets and liabilities as of March 31, 2008, and December 31, 2007, and the reported amounts of revenues and expenses for the three months ended March 31, 2008, and 2007. Actual results could differ from these estimates, and the differences could be material. The most significant estimates relate to the fair valuations of certain of our investments.

Cash and Cash Equivalents. Cash and cash equivalents includes demand deposits and money market instruments with maturities of less than three months. Cash and cash equivalents are carried at cost which approximates value.

Portfolio Investment Valuations. Investments are stated at "value" as defined in the 1940 Act and in the applicable regulations of the SEC. Value, as defined in Section 2(a)(41) of the 1940 Act, is (i) the market price for those securities for which a market quotation is readily available and (ii) the fair value as determined in good faith by, or under the direction of, the Board of Directors for all other assets. (See "Valuation Procedures" in the "Footnote to Consolidated Schedule of Investments.") At March 31, 2008, our financial statements include private venture capital investments valued at $83,097,863, the fair values of which were determined in good faith by, or under the direction, of the Board of Directors. Upon sale of investments, the values that are ultimately realized may be different from what is presently estimated. The difference could be material. Effective January 1, 2008, the Company adopted SFAS No. 157, "Fair Value Measurements," which defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. The adoption of SFAS No. 157 did not have a material impact on the fair value measurements of the Company's investments.

Foreign Currency Translation. The accounting records of the Company are maintained in U.S. dollars. All assets and liabilities denominated in foreign currencies are translated into U.S. dollars based on the rate of exchange of such currencies against U.S. dollars on the date of valuation. For the three months ended March 31, 2008, included in the net decrease in unrealized depreciation on investments was an $80,903 loss resulting from foreign currency translation.

Securities Transactions. Securities transactions are accounted for on the date the securities are purchased or sold (trade date).

Interest Income Recognition. Interest income, adjusted for amortization of premium and accretion of discount, is recorded on accrual basis. The Company ceases accruing interest when securities are determined to be non-income producing and writes off any previously accrued interest.

Realized Gain or Loss and Unrealized Appreciation or Depreciation of Portfolio Investments. Realized gain or loss is recognized when an investment is disposed of and is computed as the difference between the Company’s cost basis in the investment at the disposition date and the net proceeds received from such disposition. Realized gains and losses on investment transactions are determined by specific identification. Unrealized appreciation or depreciation is computed as the difference between the fair value of the investment and the cost basis of such investment.

Stock-Based Compensation. The Company has a stock-based employee compensation plan. The Company accounts for the plan in accordance with the provisions of Statement of Financial Accounting Standards No. 123(R), "Share-Based Payment," ("SFAS No. 123(R)"). See “Note 5. Stock-Based Compensation” for further discussion.

Income Taxes. As we intend to qualify as a RIC under Subchapter M of the Internal Revenue Code, the Company does not provide for income taxes. Our taxes are accounted for in accordance with Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes," and FIN 48, "Accounting for Uncertainty in Income Taxes." The Company recognizes interest and penalties in income tax expense.

We pay federal, state and local income taxes on behalf of our wholly owned subsidiary, Harris & Harris Enterprises, Inc., which is a C corporation. See “Note 6. Income Taxes."

Restricted Funds. The Company maintains a rabbi trust for the purposes of accumulating funds to satisfy the obligations incurred by us for the Supplemental Executive Retirement Plan ("SERP") under the employment agreement with Charles E. Harris.

Property and Equipment. Property and equipment are included in "Other Assets" and are carried at cost, less accumulated depreciation of $350,333. Depreciation is provided using the straight-line method over the estimated useful lives of the premises and equipment.

Concentration of Credit Risk. The Company places its cash and cash equivalents with financial institutions and, at times, cash held in checking accounts may exceed the Federal Deposit Insurance Corporation insured limit.

NOTE 4. FAIR VALUE MEASUREMENTS

At March 31, 2008, our financial assets were categorized as follows in the fair value hierarchy for SFAS No. 157 purposes:

Fair Value Measurement at Reporting Date Using:

Description	March 31, 2008	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
U.S. Government Securities	$ 53,589,100	$ 53,589,100	$ 0	$ 0
Portfolio Companies	$ 83,097,863	$ 0	$ 0	$ 83,097,863
Total	$ 136,686,963	$ 53,589,100	$ 0	$ 83,097,863

The Company recognized no gain or loss at January 1, 2008 as a result of the adoption of SFAS No. 157. The following chart shows the components of change in the financial assets categorized as Level 3, for the three months ended March 31, 2008.

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Portfolio Companies
Beginning Balance, January 1, 2008	$ 78,110,384
Total realized losses included in changes in net assets	(5,014,653)
Total unrealized gains included in changes in net assets	3,651,203
Purchases and interest on bridge notes	6,456,643
Disposals	(105,714)
Ending Balance, March 31, 2008	$ 83,097,863
The amount of total losses for the period included in changes in net assets attributable to the change in unrealized gains or losses relating to assets still held at the reporting date	$ 1,363,452

NOTE 5. STOCK-BASED COMPENSATION

On March 23, 2006, the Board of Directors of the Company voted to terminate the Employee Profit-Sharing Plan and to establish the Stock Plan, subject to shareholder approval. This proposal was approved at the May 4, 2006, Annual Meeting of Shareholders. The Stock Plan provides for the grant of equity-based awards of stock options to our officers, employees and directors (subject to receipt of an exemptive order described below) and restricted stock (subject to receipt of an exemptive order described below) to our officers and employees who are selected by our

Compensation Committee for participation in the plan and subject to compliance with the 1940 Act.

On July 11, 2006, the Company filed an application with the SEC regarding certain provisions of the Stock Plan, and on June 29, 2007, the Company responded to comments from the SEC on the application. In the event that the SEC provides the exemptive relief requested by the application, and we receive any additional stockholder approval required by the SEC, the Compensation Committee may, in the future, authorize awards of stock options under the Stock Plan to non-employee directors of the Company and authorize grants of restricted stock to employees.

A maximum of 20 percent of our total shares of our common stock issued and outstanding are available for awards under the Stock Plan. Under the Stock Plan, no more than 25 percent of the shares of stock reserved for the grant of the awards under the Stock Plan may be restricted stock awards at any time during the term of the Stock Plan. If any shares of restricted stock are awarded, such awards will reduce on a percentage basis the total number of shares of stock for which options may be awarded. If the Company does not receive exemptive relief from the SEC to issue restricted stock, all shares granted under the Stock Plan may be subject to stock options. No more than 1,000,000 shares of our common stock may be made subject to awards under the Stock Plan to any individual in any year.

On March 19, 2008, the Compensation Committee of the Board of Directors and the full Board of Directors of the Company approved a new grant of individual Non-Qualified Stock Option ("NQSO") awards for certain officers and employees of the Company. The terms and conditions of the stock options granted were set forth in award agreements between the Company and each award recipient entered into on that date. Options to purchase a total of 348,032 shares of stock were granted with vesting periods ranging from March 2009 to March 2012 and with an exercise price of $6.18, which was the closing volume weighted average price of our shares of common stock on March 19, 2008. Upon exercise, the shares would be issued from our previously authorized but unissued shares.

The Company accounts for the Stock Plan in accordance with the provisions of SFAS No. 123(R), which requires that we determine the fair value of all share-based payments to employees, including the fair value of grants of employee stock options, and record these amounts as an expense in the Statement of Operations over the vesting period with a corresponding increase to our additional paid-in capital. At March 31, 2008 and December 31, 2007, the increase to our operating expenses was offset by the increase to our additional paid-in capital, resulting in no net impact to our net asset value. Additionally, the Company does not record the tax benefits associated with the expensing of stock options, because the Company currently intends to qualify as a RIC under Subchapter M of the Code.

An option's expected term is the estimated period between the grant date and the exercise date of the option. As the expected term period increases, the fair value of the option and the non-cash compensation cost will also increase. The expected term assumption is generally calculated using historical stock option exercise data. The Company does not have historical exercise data to develop such an assumption. In cases where companies do not have historical data and where the options meet certain criteria, SEC Staff Accounting Bulletin 107 ("SAB 107") provides the use of a simplified expected term calculation. Accordingly, the Company calculated the expected terms using the SAB 107 simplified method.

Expected volatility is the measure of how the stock's price is expected to fluctuate over a period of time. An increase in the expected volatility assumption yields a higher fair value of the stock option. Expected volatility factors for the stock options were based on the historical fluctuations in the Company’s stock price over a period commensurate with the expected term of the option, adjusted for stock splits and dividends.

The expected dividend yield assumption is traditionally calculated based on a company's historical dividend yield. An increase to the expected dividend yield results in a decrease in the fair value of option and resulting compensation cost. Although the Company has declared deemed dividends in previous years, most recently in 2005, the amounts and timing of any future dividends cannot be reasonably estimated. Therefore, for purposes of calculating fair value, the Company has assumed an expected dividend yield of 0 percent.

The risk-free interest rate assumptions are based on the annual yield on the measurement date of a zero-coupon U.S. Treasury bond the maturity of which equals the option’s expected term. Higher assumed interest rates yield higher fair values.

The amount of non-cash, stock-based compensation expense recognized in the Consolidated Statements of Operations is based on the fair value of the awards the Company expects to vest, recognized over the vesting period on a straight-line basis for each award, and adjusted for actual forfeitures that occur before vesting. The forfeiture rate is estimated at the time of grant and revised, if necessary, in subsequent periods if the actual forfeiture rate differs from the estimated rate and is accounted for in the current period and prospectively.

The fair value of each stock option award is estimated on the date of grant using the Black-Scholes-Merton option pricing model as permitted by SFAS No. 123(R). The assumptions used in the calculation of fair value of the stock options granted on March 19, 2008, using the Black-Scholes-Merton model for the contract term was as follows:

Type of Award	Term	Number of Options Granted	Expected Term in Yrs	Expected Volatility Factor	Expected Dividend Yield	Risk-free Interest Rates	Weighted Average Fair Value Per Share
Non-qualified stock options	9.78 Years	348,032	6.14	57.1%	0%	2.62%	$3.45
Total		348,032					$3.45

For the three months ended March 31, 2008, the Company recognized $1,466,980 of compensation expense in the Consolidated Statements of Operations. As of March 31, 2008, there was approximately $7,852,320 of unrecognized compensation cost related to unvested stock option awards. This cost is expected to be recognized over a weighted-average period of approximately 1.9 years.

For the three months ended March 31, 2008, no stock options were exercised.

For the three months ended March 31, 2008, the calculation of the net decrease in net assets resulting from operations per share excludes the stock options because such options were anti-dilutive. The options may be dilutive in future periods in which there is a net increase in net assets resulting from operations, in the event that there is a significant increase in the average stock price in the stock market or in the event of significant decreases in the amount of unrecognized compensation cost.

A summary of the changes in outstanding stock options is as follows:

	Shares	Weighted Average Exercise Price	Weighted Average Grant Date Fair Value	Weighted Average Remaining Contractual Term (Yrs)	Aggregate Intrinsic Value
Options Outstanding at January 1, 2008	3,967,744	$ 10.54	$ 4.77		
Granted	348,032	$ 6.18	$ 3.45	9.75	
Exercised	0	$0	$0		
Forfeited or Expired	- .				
Options Outstanding at March 31, 2008	4,315,776	$ 10.19	$ 4.67	4.77	$330,630
Options Exercisable at March 31, 2008	1,717,125	$ 10.43	$ 4.45	3.93	$0
Options Exercisable and Expected to be	4,233,180	$ 10.19	$ 4.61	4.70	$330,630

Exercisable at March 31, 2008

The aggregate intrinsic value in the table above with respect to options outstanding, exercisable and expected to be exercisable, is calculated as the difference between the Company's closing stock price of $7.13 on the last trading day of the first quarter of 2008 and the exercise price, multiplied by the number of in-the-money options. This represents the total pre-tax intrinsic value that would have been received by the option holders had all options been fully vested and all option holders exercised their awards on March 31, 2008.

Unless earlier terminated by our Board of Directors, the Stock Plan will expire on May 4, 2016. The expiration of the Stock Plan will not by itself adversely affect the rights of plan participants under awards that are outstanding at the time the Stock Plan expires. Our Board of Directors may terminate, modify or suspend the plan at any time, provided that no modification of the plan will be effective unless and until any required shareholder approval has been obtained. The Compensation Committee may terminate, modify or amend any outstanding award under the Stock Plan at any time, provided that in such event, the award holder may exercise any vested options prior to such termination of the Stock Plan or award.

NOTE 6. INCOME TAXES

We filed for the 1999 tax year to elect treatment as a regulated investment company ("RIC") under Subchapter M of the Internal Revenue Code of 1986 (the "Code") and qualified for the same treatment for the years 2000 through 2007. However, there can be no assurance that we will qualify as a RIC for 2008 or subsequent years.

In the case of a RIC which furnishes capital to development corporations, there is an exception to the rule relating to the diversification of investments required to qualify for RIC treatment. This exception is available only to registered management investment companies which the SEC determines to be principally engaged in the furnishing of capital to other corporations which are principally engaged in the development or exploitation of inventions, technological improvements, new processes, or products not previously generally available ("SEC Certification"). We have received SEC Certification since 1999, including for 2006, but it is possible that we may not receive SEC Certification in future years.

In addition, under certain circumstances, even if we qualified for Subchapter M treatment for a given year, we might take action in a subsequent year to ensure that we would be taxed in that subsequent year as a C Corporation, rather than as a RIC. As a RIC, we must, among other things, distribute at least 90 percent of our investment company taxable income and may either distribute or retain our realized net capital gains on investments.

Provided that a proper election is made, a corporation taxable under Subchapter C of the Code or a C Corporation that elects to qualify as a RIC continues to be taxable as a C Corporation on any gains realized within 10 years of its qualification as a RIC (the "Inclusion Period") from sales of assets that were held by the corporation on the effective date of the RIC election ("C Corporation Assets"), to the extent of any gain built into the assets on such date ("Built-In Gain"). If the corporation fails to make a proper election, it is taxable on its Built-In Gain as of the effective date of its RIC election. We had Built-In Gains at the time of our qualification as a RIC and made the election to be taxed on any Built-In Gain realized during the Inclusion Period.

For federal tax purposes, the Company's 2004 through 2007 tax years remain open for examination by the tax authorities under the normal three year statute of limitations. Generally, for state tax purposes, the Company's 2003 through 2007 tax years remain open for examination by the tax authorities under a four year statute of limitations.

During the first quarter of 2008, we paid $15,798 in federal, state and local income taxes. At March 31, 2008, we had $0 accrued for federal, state and local taxes payable by the Company.

We pay federal, state and local taxes on behalf of our wholly owned subsidiary, Harris & Harris Enterprises, Inc., which is taxed as a C Corporation. For the three months ended March 31, 2008, and 2007, our income tax expense (benefit) for Harris & Harris Enterprises, Inc., was $30,400 and $0, respectively.

Continued qualification as a RIC requires us to satisfy certain investment asset diversification requirements in future years. Our ability to satisfy those requirements may not be controllable by us. There can be no assurance that we will qualify as a RIC in subsequent years.

NOTE 7. CAPITAL TRANSACTIONS

On June 25, 2007, we completed the sale of 1,300,000 shares of our common stock for gross proceeds of $14,027,000; net proceeds of this offering, after placement agent fees and offering costs of $1,033,832, were $12,993,168.

On April 4, 2008, we filed a Post-Effective Amendment to our registration statement with the SEC on Form N-2 to update our existing shelf registration statement and register an additional 1,300,000 shares of our common stock. After the effective date, the common stock may be sold at prices and on terms to be set forth in one or more supplements to the prospectus from time to time.

NOTE 8. CHANGE IN NET ASSETS PER SHARE

The following table sets forth the computation of basic and diluted per share net increases in net assets resulting from operations for the three months ended March 31, 2008, and March 31, 2007.

	For the Three Months Ended March 31	
	2008	**2007**
Numerator for decrease in net assets per share	$(3,289,035)	$(6,390,160)
Denominator for basic and diluted weighted average shares	23,314,573	21,277,576
Basic and diluted net decrease in net assets per share resulting from operations	$(0.14)	$(0.30)

NOTE 9. SUBSEQUENT EVENTS

On May 1, 2008, we exercised our warrants to purchase shares of Ancora Pharmaceuticals, Inc., for $800,000.

On May 6, 2008, we made a $2,000,000 new investment in a privately held tiny technology portfolio company.

HARRIS & HARRIS GROUP, INC.
FINANCIAL HIGHLIGHTS
(Unaudited)

	Three Months Ended March 31 2008	2007
Per Share Operating Performance		
Net asset value per share, beginning of period	$ 5.93	$ 5.42
Net operating loss*	(0.11)	(0.13)
Net realized loss on investments*	(0.22)	0
Net decrease in unrealized depreciation as a result of sales*	0.22	0
Net increase in unrealized depreciation on investments held*	(0.03)	(0.17)
Total from investment operations*	(0.14)	(.30)
Net increase as a result of stock-based compensation expense	0.07	0.08
Net increase as a result of proceeds from exercise of options	0.00	0.07
Total increase from capital stock transactions	0.07	0.15
Net asset value per share, end of period	$ 5.86	$ 5.27
Stock price per share, end of period	$ 7.13	$ 12.92
Total return based on stock price [1]	(18.89)%	6.87%
Supplemental Data:		
Net assets, end of period	$ 136,541,289	$ 112,526,302
Ratio of expenses to average net assets [1]	2.2%	2.9%
Ratio of net operating loss to average net assets [1]	(1.8)%	(2.4)%
Cash dividends paid per share	$ 0	$ 0

Tax payable on behalf of shareholders on the deemed dividend per share	$	0	$	0
Number of shares outstanding, end of period		23,314,573		21,341,029

*Based on Average Shares Outstanding.
(1) Not Annualized

The accompanying notes are an integral part of this schedule.

HARRIS & HARRIS GROUP, INC.

2,700,000 Shares

Common Stock

The date of the Prospectus is May 29, 2008

This Prospectus constitutes a part of a registration statement on Form N-2 (together with all the exhibits and the appendix thereto, the "Registration Statement") filed by us with the SEC under the Securities Act. This Prospectus does not contain all of the information set forth in the Registration Statement. Reference is hereby made to the Registration Statement and related exhibits for further information with respect to us and the shares offered hereby. Statements contained herein concerning the provisions of documents are necessarily summaries of the material terms of such documents.

No dealer, salesperson or other person has been authorized to give any information or to make any representations not contained in this Prospectus. If given or made, any information or representation must not be relied upon as having been authorized by us. This Prospectus does not constitute an offer to sell or the solicitation of an offer to buy any security other than the shares of Common Stock offered by this Prospectus, nor does it constitute an offer to sell or the solicitation of an offer to buy shares of Common Stock by anyone in any jurisdiction in which such offer or solicitation would be unlawful.
