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

**FORM 10-Q**

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

For the quarter ended June 30, 2006

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

For the Transition Period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 001-08205

**Rand Capital Corporation**

*(Exact Name of Registrant as specified in its Charter)*

**New York**  
(State or Other Jurisdiction of Incorporation  
or organization)

**16-0961359**  
(IRS Employer  
Identification No.)

**2200 Rand Building, Buffalo, NY**  
(Address of Principal executive offices)

**14203**  
(Zip Code)

**(716) 853-0802**

*(Registrant's Telephone No. Including Area Code)*

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

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

Large accelerated filer  Accelerated filer  Non-accelerated filer

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

As of August 4, 2006 there were 5,718,934 shares of the registrant's common stock outstanding.

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**PART I.**  
**FINANCIAL INFORMATION**

**Item 1. Financial Statements and Supplementary Data**

**Rand Capital Corporation and Subsidiaries**  
**Consolidated Statements of Financial Position**  
**As of June 30, 2006 and December 31, 2005**  
**(Unaudited)**

	June 30, 2006	December 31, 2005
<b>ASSETS</b>		
Investments at fair value (identified cost: 6/30/06 - \$13,747,408; 12/31/05 - \$13,712,890)	\$14,234,428	\$13,370,862
Cash and cash equivalents	1,492,122	1,209,839
Interest receivable (net of allowance: 6/30/06 - \$122,000; 12/31/05 - \$236,870)	386,225	297,619
Deferred tax asset	517,000	846,000
Income tax receivable	—	15,582
Other assets	295,843	323,703
Total assets	<u>\$16,925,618</u>	<u>\$16,063,605</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY (NET ASSETS)</b>		
Liabilities:		
Debentures guaranteed by the SBA	\$ 7,600,000	\$ 7,200,000
Accounts payable and accrued expenses	206,033	167,788
Deferred revenue	67,295	79,883
Income taxes payable	4,251	—
Total liabilities	7,877,579	7,447,671
Stockholders' equity (net assets):		
Common stock, \$.10 par — shares authorized 10,000,000; shares issued 5,763,034	576,304	576,304
Capital in excess of par value	6,973,454	6,973,454
Accumulated net investment (loss)	(5,280,544)	(4,988,326)
Undistributed net realized gain on investments	6,533,819	6,306,925
Net unrealized appreciation (depreciation) on investments	292,212	(205,217)
Treasury stock, at cost, 44,100 shares	(47,206)	(47,206)
Net assets (per share 6/30/2006-\$1.58, 12/31/2005-\$1.51)	<u>9,048,039</u>	<u>8,615,934</u>
Total liabilities and stockholders' equity (net assets)	<u>\$16,925,618</u>	<u>\$16,063,605</u>

See accompanying notes

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**Rand Capital Corporation and Subsidiaries**  
**Condensed Consolidated Statements of Operations**  
**For the Three Months and Six Months Ended June 30, 2006 and 2005**  
**(Unaudited)**

	Three months ended June 30, 2006	Three months ended June 30, 2005	Six months ended June 30, 2006	Six months ended June 30, 2005
<b>Investment income:</b>				
Interest from portfolio companies	\$ 180,438	\$ 137,003	\$ 352,458	\$ 282,923
Interest from other investments	6,196	645	11,339	1,484
Dividend and other investment income	15,103	29,704	28,238	29,704
Other income	11,434	10,707	22,381	21,601
	<u>213,171</u>	<u>178,059</u>	<u>414,416</u>	<u>335,712</u>
<b>Operating expenses:</b>				
Salaries	95,624	88,432	191,908	223,104
Employee benefits	21,227	23,209	53,153	54,729
Directors' fees	23,250	28,250	36,750	36,450
Professional fees	48,467	29,777	75,003	44,840
Stockholders and office operating	41,640	33,980	67,868	58,373
Insurance	10,920	11,550	21,840	23,100
Corporate development	15,770	9,564	28,675	20,777
Other operating	1,936	3,036	4,558	5,212
	<u>258,834</u>	<u>227,798</u>	<u>479,755</u>	<u>466,585</u>
Interest on SBA obligations	112,574	63,761	219,498	114,734
Total expenses	<u>371,408</u>	<u>291,559</u>	<u>699,253</u>	<u>581,319</u>
<b>Investment loss before income taxes</b>	(158,237)	(113,500)	(284,837)	(245,607)
Current income tax expense	5,000	5,000	10,000	4,927
Deferred income tax benefit	(13,708)	(48,157)	(2,619)	(84,157)
<b>Net investment loss</b>	<u>(149,529)</u>	<u>(70,343)</u>	<u>(292,218)</u>	<u>(166,377)</u>
<b>Realized and unrealized gain (loss) on investments:</b>				
Net gain on sales and dispositions	38,941	—	226,894	—
<b>Unrealized appreciation (depreciation) on investments:</b>				
Beginning of period	(94,751)	(248,867)	(342,028)	(586,048)
End of period	487,020	(420,974)	487,020	(420,974)
Change in unrealized appreciation (depreciation) before income taxes	581,771	(172,107)	829,048	165,074
Deferred income tax expense (benefit)	232,708	(68,843)	331,619	66,157
<b>Net change in unrealized appreciation (depreciation)</b>	<u>349,063</u>	<u>(103,264)</u>	<u>497,429</u>	<u>98,917</u>
<b>Net realized and unrealized gain (loss) on investments</b>	<u>388,004</u>	<u>(103,264)</u>	<u>724,323</u>	<u>98,917</u>
<b>Net increase (decrease) in net assets from operations</b>	<u>\$ 238,475</u>	<u>\$ (173,607)</u>	<u>\$ 432,105</u>	<u>\$ (67,460)</u>
<b>Weighted average shares outstanding</b>	5,718,934	5,718,934	5,718,934	5,718,934
<b>Basic and diluted net increase (decrease) in net assets from operations per share</b>	\$ 0.04	\$ (0.03)	\$ 0.08	\$ (0.01)

See accompanying notes

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**Rand Capital Corporation and Subsidiaries**  
**Condensed Consolidated Statements of Cash Flows**  
**For the Six Months Ended June 30, 2006 and 2005**  
**(Unaudited)**

	<u>June 30, 2006</u>	<u>June 30, 2005</u>
<b>Cash flows from operating activities:</b>		
Net increase (decrease) in net assets from operations	\$ 432,105	\$ (67,460)
Adjustments to reconcile net increase in net assets to net cash used in operating activities:		
Depreciation and amortization	15,599	10,730
Increase in unrealized appreciation of investments	(829,048)	(165,074)
Deferred tax expense (benefit)	329,000	(18,000)
Net realized gain on portfolio investments	(226,894)	—
Non-cash conversion of debenture interest	(12,877)	(19,097)
Changes in operating assets and liabilities:		
(Increase) in interest receivable	(88,606)	(88,712)
Decrease (increase) in other assets	47,348	(40,110)
Increase (decrease) in accounts payable and accrued liabilities	42,496	(11,617)
(Decrease) increase in deferred revenue	(12,588)	12,040
Total adjustments	(735,570)	(319,840)
<b>Net cash used in operating activities</b>	<b>(303,465)</b>	<b>(387,300)</b>
<b>Cash flows from investing activities:</b>		
Investments originated	(820,000)	(1,451,060)
Proceeds from sale of portfolio investments	950,885	—
Proceeds from loan repayments	74,368	68,725
Capital expenditures	(12,256)	(1,560)
<b>Net cash provided by (used in) investing activities</b>	<b>192,998</b>	<b>(1,383,895)</b>
<b>Cash flows from financing activities:</b>		
Proceeds from SBA debenture	400,000	1,500,000
Origination costs to SBA	(7,250)	(37,500)
<b>Net cash provided by financing activities</b>	<b>392,750</b>	<b>1,462,500</b>
Net increase (decrease) in cash and cash equivalents	<b>282,283</b>	<b>(308,695)</b>
Cash and cash equivalents:		
Beginning of period	<b>1,209,839</b>	626,744
End of period	<b>\$ 1,492,122</b>	<b>\$ 318,049</b>

See accompanying notes

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**Rand Capital Corporation and Subsidiaries**  
**Condensed Consolidated Statements of Changes in Net Assets**  
**For the Three Months and Six Months Ended June 30, 2006 and 2005**  
**(Unaudited)**

	Three months ended June 30, 2006	Three months ended June 30, 2005	Six months ended June 30, 2006	Six months ended June 30, 2005
<b>Net assets at beginning of period</b>	<b>\$ 8,809,564</b>	<b>\$ 9,133,201</b>	<b>\$ 8,615,934</b>	<b>\$ 9,027,054</b>
Net investment loss	(149,529)	(70,343)	(292,218)	(166,377)
Net realized gain on investments	38,941	—	226,894	—
Net change in unrealized appreciation (depreciation) of investments	349,063	(103,264)	497,429	98,917
<b>Net increase (decrease) in net assets from operations</b>	<b>238,475</b>	<b>(173,607)</b>	<b>432,105</b>	<b>(67,460)</b>
<b>Net assets at end of period</b>	<b>\$ 9,048,039</b>	<b>\$ 8,959,594</b>	<b>\$ 9,048,039</b>	<b>\$ 8,959,594</b>

See accompanying notes

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**Rand Capital Corporation and Subsidiaries**  
**Consolidated Schedule of Portfolio Investments**  
**June 30, 2006**  
**(Unaudited)**

Company and Business	Type of Investment	(b) Date Acquired	(c) Equity	Cost	(d) Value	Per Share of Rand
<b>APF Group, Inc. (e)(g)</b> Mount Vernon, NY. Manufacturer of museum quality picture frames and framed mirrors for museums, art galleries, retail frame shops, upscale designers and prominent collectors. www.apfgroup.com	\$500,000 Senior Subordinated note at 12.5% due July 1, 2009. \$94,594 Senior Subordinated note at 14% due July 31, 2007. Warrants to purchase 10.2941 shares of common stock.	7/8/04	6%	\$594,594	\$594,594	.10
<b>Carolina Skiff LLC (e)(g)</b> Waycross, GA. Manufacturer of fresh water, ocean fishing and pleasure boats. www.carolinaskiff.com	\$985,000 Class A preferred membership interest at 11%. Redeemable January 31, 2010. 5% common membership interest.	1/30/04	5%	1,000,000	1,038,000	.18
<b>Concentrix Corporation (e)(g)</b> Pittsford, NY. Marketing service company generating returns through multi-channel demand generation and renewal marketing services. www.concentrix.com	\$600,000 Senior Subordinated note at 14% due November 11, 2007.	6/1/05	0%	600,000	600,000	.10
<b>Contract Staffing</b> Buffalo, NY. PEO providing human resource administration for small businesses. www.contract-staffing.com	Preferred Stock Repurchase Agreement through March 31, 2010 at 5%.	11/8/99	10%	141,400	141,400	.02
<b>EmergingMed.com, Inc. (g)</b> New York, NY. Cancer clinical trial matching and referral service. www.emergingmed.com	\$500,000 Senior subordinated note at 10% due December 19, 2010.	12/19/0	5%	500,000	500,000	.09
<b>Gemcor II, LLC (e)(g)(i)</b> West Seneca, NY. Designs and sells automatic riveting machines used in the assembly of aircraft components. www.gemcor.com	\$250,000 note at 8% due June 28, 2010 with warrant to purchase 6.25 membership units. 25 membership units.	6/28/04	33%	741,097	741,097	.13
<b>G-TEC Natural Gas Systems</b> Buffalo, NY. Manufactures and distributes systems that allow natural gas to be used as an alternative fuel to gases. www.gas-tec.com	41.322% Class A membership interest. 8% cumulative dividend.	8/31/99	41%	400,000	300,000	.05
<b>Innov-X Systems, Inc. (e)(g)</b> Woburn, MA. Manufactures portable x-ray fluorescence (XRF) analyzers used in metals/alloy analysis. www.innovxsys.com	\$350,000 Subordinated Debenture at 8.5% due September 27, 2009. 12,344 warrants to purchase common shares. 3,500 Series A preferred stock. \$250,000 Series B Secured Subordinated term note at 8.5% due March 1, 2010. 12,345 warrants to purchase common shares.	9/27/04	10%	635,000	635,000	.11
<b>Kionix, Inc.</b> Ithaca, NY. Develops innovative MEMS based technology applications. www.kionix.com	30,241 shares Series B preferred stock. (g) 2,862,091 shares Series A preferred stock. 714,285 shares Series B preferred stock.	5/17/02	2%	1,262,340	977,863	.17



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**Rand Capital Corporation and Subsidiaries**  
**Consolidated Schedule of Portfolio Investments**  
**June 30, 2006 (Continued)**  
**(Unaudited)**

Company and Business	Type of Investment	(b) Date Acquired	(c) Equity	Cost	(d) Value	Per Share of Rand
<b>Minrad International, Inc.</b> (AMEX: BUF) (h)(j) Buffalo, NY. Developer of acute care devices and anesthetics. www.minrad.com	343,440 common shares.	8/4/97	1%	465,431	1,363,457	.24
<b>New Monarch Machine Tool, Inc. (e)(g)(i)</b> Cortland, NY. Manufactures and services vertical/horizontal machining centers. www.monarchmt.com	\$527,876.85 note at 12% due January 13, 2009. \$300,000 note at 12% due January 13, 2009. Warrants for 22.84 shares of common stock.	9/24/03	15%	765,328	765,328	.13
<b>Niagara Dispensing Technologies, Inc. (g)</b> Tonawanda, NY. Beverage dispense technology development and products manufacturer, specializing in beer dispensing systems. www.exactpour.com	\$500,000 Senior Subordinated note at 8% due March 7, 2011. Adjustable warrant for 4% of common stock.	3/8/06	4%	500,000	500,000	.09
<b>Photonic Products Group, Inc (OTC:PHPG.OB)(a) (j)</b> (Formerly INRAD, Inc.) Northvale, NJ. Develops and manufactures products for laser photonics industry. www.inrad.com	100 shares convertible Series B preferred stock, 10% dividend. 22,000 shares common stock.	10/31/00	<1%	155,000	128,820	.02
<b>RAMSCO (e)(g)</b> Albany, NY. Distributor of water, sanitary, storm sewer and specialty construction materials to the contractor, highway and municipal markets. www.ramsco.com	\$916,947.23 notes at 13% due November 18, 2007. Warrants to purchase 12.5% of common shares.	11/19/02	13%	916,947	916,947	.16
<b>Rocket Broadband Networks, Inc. (g)</b> Rochester, NY. Communications service provider of satellite TV, broadband internet and VoIP digital phone targeting multiple dwelling units. www.rocketbroadband.com	285,829 Preferred shares.	12/20/05	6%	204,082	204,082	.04
<b>Somerset Gas Transmission Company, LLC</b> Buffalo, NY. Natural gas transportation company. www.somersetgas.com	26.5337 Units.	7/10/02	2%	719,097	786,748	.14
<b>Synacor, Inc. (e)(g)</b> Buffalo, NY. Develops provisioning platforms for aggregation and delivery of content for broadband access providers. <a href="http://www.synacor.com">www.synacor.com</a>	\$350,000 convertible note at 10% due November 18, 2007. 200,000 shares of Series B preferred stock. 59,828 Series A preferred shares. Warrants for 299,146 common shares.	11/18/02	5%	820,000	828,674	.14
<b>Topps Meat Company LLC (e)(g)</b> Elizabeth, NJ. Producer and supplier of premium branded frozen hamburgers and portion controlled meat products. www.toppsmeat.com	Preferred A and Class A common membership interest.	4/3/03	3%	595,000	927,000	.16
<b>Ultra — Scan Corporation</b> Amherst, NY. Biometrics application developer of ultrasonic fingerprint	536,596 common shares, 107,104 Series A-1 preferred shares. (g) 95,284 Series A-1 preferred	12/11/92	3%	938,164	1,203,000	.21

technology-scan.com  
www.ustecnet.com

shares.

<b>UStec, Inc.</b> Victor, NY. Markets digital wiring systems for new home construction. www.ustecnet.com	\$100,000 note at 5% due February 1, 2007 (e). 50,000 common shares. Warrants for 139,395 common shares. <b>(g)</b> \$350,000 Senior Subordinated Convertible Debentures at 6% due February 2, 2008.	6/26/98	<1%	450,500	475,000	.08
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**Rand Capital Corporation and Subsidiaries**  
**Consolidated Schedule of Portfolio Investments**  
**June 30, 2006 (Continued)**  
**(Unaudited)**

Company and Business	Type of Investment	(b) Date Acquired	(c) Equity	Cost	(d) Value	Per Share of Rand
<b>WineIsIt.com, Corp. (e)</b> Amherst, NY. Marketing company specializing in customer loyalty programs supporting the wine and spirit industry. www.wineisit.com	\$20,000 note at 12% due April 26, 2007. (g) \$500,000 Senior Subordinated note at 10% due December 17, 2009. \$250,000 note at 10% due April 16, 2005. Warrants to purchase 100,000 shares Class B common stock.	12/18/02	2%	821,918	571,918	.10
Other Investments	Other	Various		<u>521,510</u>	<u>35,500</u>	<u>.02</u>
	Total portfolio investments			<u>\$13,747,408</u>	<u>\$14,234,428</u>	<u>\$2.48</u>

See accompanying notes

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**Rand Capital Corporation and Subsidiaries**  
**Consolidated Schedule of Portfolio Investments**  
**June 30, 2006 (Continued)**  
**(Unaudited)**

**Notes to Consolidated Schedule of Portfolio Investments**

- (a) Unrestricted securities are freely marketable securities having readily available market quotations. All other securities are restricted securities, which are subject to one or more restrictions on resale and are not freely marketable. At June 30, 2006 restricted securities represented approximately 99% of the value of the investment portfolio. Freed Maxick & Battaglia, CPA's, PC has not examined the business descriptions of the portfolio companies.
  - (b) The Date Acquired column indicates the year in which the Corporation acquired its first investment in the company or a predecessor company.
  - (c) The equity percentages estimate the Corporation's ownership interest in the portfolio investment. The estimated ownership is calculated based on the percent of outstanding voting securities held by the Corporation or the potential percentage of voting securities held by the Corporation or the potential percentage of voting securities held by the Corporation upon exercise of its warrants or conversion of debentures, or other available data. Freed Maxick & Battaglia, CPA's, PC has not audited the equity percentages of the portfolio companies. The symbol "<1%" indicates that the Company holds equity interest of less than one percent.
  - (d) The Corporation has adopted the SBA's valuation guidelines for SBIC's which describes the policies and procedures used in valuing investments. Under the valuation policy of the Corporation, unrestricted securities are valued at the closing price for publicly held securities for the last three days of the month. Restricted securities, including securities of publicly-held companies, which are subject to restrictions on resale, are valued at fair value as determined by the Board of Directors. Fair value is considered to be the amount which the Corporation may reasonably expect to receive for portfolio securities when sold on the valuation date. Valuations as of any particular date, however, are not necessarily indicative of amounts which may ultimately be realized as a result of future sales or other dispositions of securities and these favorable or unfavorable differences could be material. Among the factors considered by the Board of Directors in determining the fair value of restricted securities are the financial condition and operating results, projected operations, and other analytical data relating to the investment. Also considered are the market prices for unrestricted securities of the same class (if applicable) and other matters which may have an impact on the value of the portfolio company.
  - (e) These investments are income producing. All other investments are non-income producing. Income producing investments have generated cash payments of interest or dividends within the last twelve months.
  - (f) Income Tax Information — As of June 30, 2006, the aggregate cost of investment securities approximated \$13.7 million. Net unrealized appreciation aggregated approximately \$487,000 of which \$1,634,000 related to appreciated investment securities and \$1,147,000 related to depreciated investment securities.
  - (g) Rand Capital SBIC, L.P. investment
  - (h) This is a publicly owned company. The Corporation's shares are restricted securities but may be sold in the open market under Rule 144.
  - (i) Reduction in cost and value reflects current principal repayment.
  - (j) Publicly owned company
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**Rand Capital Corporation and Subsidiaries**  
**Notes to the Consolidated Financial Statements**  
**For the Six Months Ended June 30, 2006 and 2005**  
**(Unaudited)**

**Note 1. ORGANIZATION**

Rand Capital Corporation (“Rand” or “Corporation”) was incorporated under the laws of the state of New York on February 24, 1969. Commencing in 1971, Rand operated as a publicly traded, closed-end, diversified management company that was registered under Section 8(b) of the Investment Company Act of 1940 (the “1940 Act”). On August 16, 2001, Rand filed an election to be treated as a business development company (“BDC”) under the 1940 Act, which became effective on the date of filing. A BDC is a specialized type of investment company that is primarily engaged in the business of furnishing capital and managerial expertise to companies that do not have ready access to capital through conventional finance channels. There was no impact on the corporate structure as a result of the change to a BDC. Rand continues to operate as a publicly held venture capital company, listed on the NASDAQ Small Cap Market under the symbol “RAND.”

**Formation of SBIC Subsidiary**

On January 16, 2002, Rand formed a wholly owned subsidiary, Rand Capital SBIC, L.P., (“Rand SBIC”) for the purpose of operating it as a small business investment company. At the same time, Rand organized another wholly owned subsidiary, Rand Capital Management, LLC (“Rand Management”), as a Delaware limited liability company, to act as the general partner of Rand SBIC. Rand transferred \$5 million in cash to Rand SBIC to serve as “regulatory capital” in January 2002, and on August 16, 2002 Rand received notification that its Small Business Investment Company (SBIC) application and license had been approved by the Small Business Administration (SBA). The approval allows Rand SBIC to obtain loans up to two times its initial \$5 million of “regulatory capital” from the SBA for purposes of making new investments in portfolio companies.

The following discussion will include Rand, Rand SBIC and Rand Management (collectively, the “Corporation”).

The Corporation paid \$100,000 to the SBA to reserve \$10,000,000 of its approved debenture leverage. The fees were paid in two installments of \$50,000 each in July 2003 and in August 2004. These fees were 1% of the face amount of the leverage reserved under the commitment. The fee represents a partial prepayment of the SBA’s nonrefundable 3% leverage fee. As of June 30, 2006, Rand SBIC had drawn \$7,600,000 in leverage from the SBA.

SBA debentures are issued with 10-year maturities. Interest only is payable semi-annually until maturity. Ten-year SBA debentures may be prepaid with a penalty during the first 5 years, and then are pre-payable without penalty. Rand initially capitalized Rand SBIC with \$5 million in Regulatory Capital. Rand SBIC was approved to obtain SBA leverage at a 2:1 matching ratio, resulting in a total capital pool eligible for investment of \$15 million. The Corporation expects to use Rand SBIC as its primary investment vehicle.

The Corporation formed Rand SBIC as a subsidiary for the purpose of causing it to be licensed as a SBIC under the Small Business Investment Act of 1958 (the “SBA Act”) by the SBA, in order to have access to various forms of leverage provided by the SBA to SBIC’s.

On May 28, 2002, the Corporation filed an Exemption Application with the Securities and Exchange Commission (“SEC”) seeking an order under Sections 6(c), 12(d)(1)(J), 57(c), and 57(i) of, and

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Rule 17d-1 under, the 1940 Act for exemptions from the application of Sections 2(a)(3), 2(a)(19), 12(d)(1), 18(a), 21(b), 57(a)(1), (2), (3), and (4), and 61(a) of the 1940 Act to certain aspects of its operations. The application was amended on May 18, 2006 in response to preliminary SEC comments. The application also seeks an order under Section 12(h) of the Securities Exchange Act of 1934 Act (the "Exchange Act") for an exemption from separate reporting requirements under Section 13(a) of the Exchange Act. In general, the Corporation applications seek orders that would permit:

- A BDC (Rand) to operate a BDC/small business investment company (Rand SBIC) as its wholly owned subsidiary in limited partnership form;
- Rand, Rand Management and Rand SBIC to engage in certain transactions that the Corporation would otherwise be permitted to engage in as a BDC if its component parts were organized as a single corporation;
- Rand, as a BDC, and Rand SBIC, as its BDC/SBIC subsidiary, to meet asset coverage requirements for senior securities on a consolidated basis and;
- Rand SBIC, as a BDC/SBIC subsidiary of Rand, as a BDC, to file Exchange Act reports on a consolidated basis as part of Rand's reports.

The Corporation has not identified from among the similar exemption applications on file with the SEC an example of a specific grouping of all of the exemptions requested by the Corporation in its application, but the SEC has commonly granted applications to other companies for orders applicable to each of the exemptions requested and for orders applicable to various combinations of those exemptions, and the Corporation's applications do not appear to raise any specific policy issues that have not also been raised by applications for which exemptions have been granted.

Rand operates Rand SBIC through Rand Management for the same investment purposes, and with investments in similar kinds of securities, as Rand. Rand SBIC's operations are consolidated with those of Rand for both financial reporting and tax purposes.

### **Note 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Basis of Presentation** - In Management's opinion, the accompanying consolidated financial statements include all adjustments necessary for a fair presentation of the consolidated financial position, results of operations, and cash flows for the interim periods presented. Certain information and note disclosures normally included in audited annual financial statements prepared in accordance with U.S. generally accepted accounting principles, have been omitted; however, the Corporation believes that the disclosures made are adequate to make the information presented not misleading. The interim results for the period ending June 30, 2006 are not necessarily indicative of the results for the full year.

These statements should be read in conjunction with the financial statements and the notes included in the Corporation's Annual Report on Form 10-K for the year ended December 31, 2005. Information contained in this filing should also be reviewed in conjunction with the Corporation's related filings with the SEC during the period of time prior to the date of this report. Those filings include, but are not limited to the following:

N-30-B2/ARS	Quarterly & Annual Reports to Shareholders
N-54A	Election to Adopt Business Development Company status
DEF-14A	Definitive Proxy Statement submitted to shareholders
Form 10-K	Annual Report on Form 10-K for the year ended December 31, 2005
Form 10-Q	Quarterly Report on Form 10-Q for the quarters ended March 31, 2006, September 30, 2005 and June 30, 2005
Form N-23C-1	Reports by closed-end investment companies of purchases of their own securities

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Our Corporation's website is [www.randcapital.com](http://www.randcapital.com). Available through our website is the Corporation's annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and other reports filed with the SEC.

**Principles of Consolidation** - The consolidated financial statements include the accounts of Rand, Rand SBIC and Rand Management, collectively, the "Corporation." All intercompany accounts and transactions have been eliminated in consolidation.

**Investments** - Investments are stated at fair value as determined in good faith by the Board of Directors, as described in the Notes to Consolidated Schedule of Portfolio Investments. Certain investment valuations have been determined by the Board of Directors in the absence of readily ascertainable fair values. The estimated valuations are not necessarily indicative of amounts which may ultimately be realized as a result of future sales or other dispositions of securities, and these favorable or unfavorable differences could be material.

Amounts reported as realized gains and losses are measured by the difference between the net proceeds of sale or exchange and the cost basis of the investment without regard to unrealized gains or losses reported in prior periods. The cost of securities that have, in the Board of Directors' judgment, become worthless, are written off and reported as realized losses.

**Cash and Cash Equivalents** - Temporary cash investments having a maturity of three months or less when purchased are considered to be cash equivalents.

**Revenue Recognition - Interest Income** - Interest income generally is recognized on the accrual basis except where the investment is in default or otherwise presumed to be in doubt. In such cases, interest is recognized at the time of receipt. A reserve for possible losses on interest receivable is maintained when appropriate.

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

**Deferred Debenture Costs** - SBA debenture origination and commitment costs, which are included in other assets, will be amortized ratably over the terms of the SBA debentures. Amortization expense was \$12,600 for the six months ended June 30, 2006, compared to \$7,130 for the six months ended June 30, 2005.

**Net Assets per Share** - Net assets per share are based on the number of shares of common stock outstanding. There are no common stock equivalents.

**Supplemental Cash Flow Information** - Income taxes refunded (paid) during the six months ended June 30, 2006 and 2005 amounted to \$9,832 and (\$12,721), respectively. Interest paid during the six months ended June 30, 2006 and 2005 amounted to \$172,965 and \$85,881, respectively. During the six months ended June 30, 2006 and 2005, the Corporation converted \$12,877 and \$19,097, respectively, of interest receivable into equity investments.

**Accounting Estimates** - The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of

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the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Stockholders Equity (Net Assets)** - At June 30, 2006 and December 31, 2005, there were 500,000 shares of \$10.00 par value preferred stock authorized and unissued.

The Board of Directors has authorized the repurchase of up to 5% of the Corporation's outstanding stock on the open market through October 27, 2006. During the six month period ended June 30, 2006 the Corporation did not purchase any shares for the treasury.

**Stock Option Plan** - In July 2001, the shareholders of the Corporation authorized the establishment of an Employee Stock Option Plan (the "Plan"). The Plan provides for an award of options to purchase up to 200,000 common shares to eligible employees. In 2002, the Corporation placed the Plan on inactive status as it developed a new profit sharing plan for two of the Corporation's employees in connection with the establishment of its SBIC subsidiary. The profit sharing plan provided for incentive compensation based on a stated percentage of realized gain, capital gains, net of realized capital losses and unrealized depreciation, and limited to a stated percentage of the Corporation's net income. As of June 30, 2006, no stock options had been awarded under the Plan. Because Section 57(n) of the 1940 Act prohibits maintenance of a profit sharing plan for the officers and employees of a BDC where any option, warrant or right is outstanding under an executive compensation plan, no options will be granted under the Plan while any profit sharing plan is in effect with respect to the Corporation.

**Subsequent Event** - Subsequent to the quarter end of June 30, 2006, the Corporation drew down \$500,000 from the SBA and made one investment for \$550,000.

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

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

#### **FORWARD LOOKING STATEMENTS**

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

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

#### **Overview**

The following discussion includes Rand Capital Corporation (“Rand”), Rand Capital SBIC, L.P., (“Rand SBIC”), and Rand Capital Management, LLC (“Rand Management”), (collectively the “Corporation”), its financial position and results of operations.

Rand is incorporated under the laws of New York and is regulated under the 1940 Act as a business development company (“BDC”). In addition, a wholly-owned subsidiary, Rand SBIC is regulated as a Small Business Investment Company (“SBIC”) by the Small Business Administration (“SBA”). The Corporation anticipates that most, if not all, of its investments in the next year will be originated through the SBIC subsidiary.

#### **Critical Accounting Policies**

The Corporation prepares its financial statements in accordance with U.S. generally accepted accounting principles (GAAP) which requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities. For a summary of certain of our significant accounting policies see Note 2 of the consolidated financial statements in December 31, 2005 Form 10-K. A summary of our critical accounting policies can be found in the December 31, 2005 Form 10-K in Item 7. “Management’s Discussion and Analysis of Financial Condition and Results of Operations”.

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### Financial Condition

Overview:

	<u>6/30/06</u>	<u>12/31/05</u>	<u>Increase</u>	<u>% Increase</u>
Total assets	\$16,925,618	\$16,063,605	\$862,013	5.4%
Total liabilities	7,877,579	7,447,671	429,908	5.8%
Net assets	<u>\$ 9,048,039</u>	<u>\$ 8,615,934</u>	<u>\$432,105</u>	<u>5.0%</u>

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

	<u>6/30/06</u>	<u>12/31/05</u>	<u>Increase</u>	<u>% Increase</u>
Investments, at cost	\$13,747,408	\$13,712,890	\$ 34,518	0.3%
Unrealized appreciation (depreciation), net	487,020	(342,028)	829,048	242.4%
Investments at fair value	<u>\$14,234,428</u>	<u>\$13,370,862</u>	<u>\$863,566</u>	<u>6.5%</u>

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

<u>New Investments</u>	<u>Amount</u>
Niagara Dispensing Technologies, Inc. (Niagara Dispensing)	\$ 500,000
New Monarch Machine Tool, Inc. (Monarch)	300,000
WineIsIt.com, Corp. (Wineisit)	<u>20,000</u>
<b>Total of investments made during the six months ended June 30, 2006</b>	<b><u>\$ 820,000</u></b>
<u>Interest conversions:</u>	
Photonic Products Group, Inc. (Photonics)	10,000
Monarch	<u>2,877</u>
<b>Total of new investments and interest conversions during the six months ended June 30, 2006</b>	<b><u>\$ 832,877</u></b>
<b>Sales/Investment Repayments</b>	
Minrad International, Inc. (Minrad)	(453,991)
Vanguard Modular Building Systems (Vanguard)	(270,000)
Monarch	(62,548)
Gemcor II, LLC (Gemcor)	(8,903)
Takeform	<u>(2,917)</u>
<b>Total of sales or investment repayments during the six months ended June 30, 2006</b>	<b><u>(798,359)</u></b>
<b>Total change in investment balance, at cost during the six months ended June 30, 2006</b>	<b><u>\$ 34,518</u></b>

Net asset value per share (NAV) was \$1.58/share at June 30, 2006 versus \$1.51/share at December 31, 2005.

The Corporation's total investments at fair value, whose fair value have been estimated by the Board of Directors, approximated 157% of net assets at June 30, 2006 and 155% of net assets at December 31, 2005.

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Cash and cash equivalents approximated 16.5% of net assets at June 30, 2006 compared to 14.0% at December 31, 2005.

### Results of Operations

#### Investment Income

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

#### *Comparison of the six months ended June 30, 2006 to the six months ended June 30, 2005*

	June 30, 2006	June 30, 2005	Increase (Decrease)	%Increase (Decrease)
Interest from portfolio companies	\$352,458	\$282,923	\$ 69,535	24.6%
Interest from other investments	11,339	1,484	9,855	664.1%
Dividend and other investment income	28,238	29,704	(1,466)	(4.9%)
Other income	22,381	21,601	780	3.6%
<b>Total investment income</b>	<b>\$414,416</b>	<b>\$335,712</b>	<b>\$ 78,704</b>	<b>23.4%</b>

Interest from portfolio companies — Portfolio interest income increased \$69,535 or 24.6% during the six months ended June 30, 2006 as compared to the same period in the prior year. This increase is attributable to the fact that 66% of the total of the new investments during 2005 and the first six months of 2006 originated out of Rand and Rand SBIC are debenture instruments that earn interest income at a blended interest rate of approximately 10.5%.

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

Company	Interest Rate	Investment Cost	Year that Interest Accrual Ceased
G-Tec	8%	400,000	2004
WineIsIt.com	10%	821,918	2005

Interest from other investments - The increase in interest income is primarily due to higher yields on idle cash balances.

Dividend and other investment income - Dividend income is comprised of distributions from Limited Liability Companies (LLC's) that the Corporation has invested in. The Corporation's investment agreements with certain LLC companies require the entities to distribute funds to the Corporation for payment of income taxes on its allocable share of the entities' profits. These dividends will fluctuate based upon the profitability of the entities and the timing of the distributions. Dividend income for the six months ended June 30, 2006 consisted of distributions from Topps Meat Company LLC (Topps) for \$17,647, Gemcor II, LLC (Gemcor) for \$7,833, Carolina Skiff LLC (Carolina Skiff) for \$1,584 and Vanguard Modular Building Systems (Vanguard) for \$1,174. Dividend income for the six months ended

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June 30, 2005 consisted of distributions from Topps for \$16,719, Carolina Skiff for \$11,811 and Vanguard for \$1,174.

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

The slight increase in other income for the six months ended June 30, 2006 can be attributed to the fact that the Corporation charged closing fees on only 4 of the 14 investments generated through the Corporation in 2005 and the first six months of 2006. The annualized financing fee income based on the existing portfolio will be approximately \$32,000 annually in 2006 and 2007 and less than \$10,000 annually thereafter. In addition board attendance fees are included in this line item and amounted to \$4,000 for the six months ended June 30, 2006 and \$3,000 for same period ending June 30, 2005.

### **Operating Expenses**

	<u>June 30, 2006</u>	<u>June 30, 2005</u>	<u>Increase</u>	<u>% Increase</u>
Total Expenses	\$ 699,253	\$ 581,319	\$117,934	20%

Operating expenses predominately consist of interest expense on SBA obligations, employee compensation and benefits, directors' fees, shareholder related costs, office expenses, professional fees, and expenses related to identifying and reviewing investment opportunities. The increase in operating expenses during the six months ended June 30, 2006 can be primarily attributed to the 91% or \$104,764 increase in SBA interest expense. The SBA interest expense was \$219,498 for the six months ended June 30, 2006 and \$114,734 for the six months ended June 30, 2005. The Corporation has borrowed \$7,600,000 from the SBA as of June 30, 2006 at an average borrowing rate, including surcharges, of approximately 5.8%. Interest costs will continue to increase in 2006 and beyond as the Corporation continues to draw down SBA leverage up to the maximum approved leverage of \$10 million. This interest is paid on a semi-annual basis.

In addition, salaries decreased 14% or (\$31,196) from \$223,104 for the six months ended June 30, 2005 to \$191,908 for the six months ended June 30, 2006. This decrease is due to the fact that the executive officers were not paid bonuses during the first six months of 2006 as they were during the six months ended June 30, 2005. Professional fees were \$75,003 for the six months ended June 30, 2006 and \$44,840 for the six months ended June 30, 2005. This represents an increase of 67% or \$30,163 and can be attributed to the increasing legal, audit and tax costs due to the increasingly more complex regulatory environment in which the Corporation operates.

### **Net Realized Gains and Losses on Investments**

During the six months ended June 30, 2006, the Corporation recognized a net realized gain of \$307,894 on its sale of 334,541 shares of Minrad. The average sales price of Minrad was \$2.33/share and the basis of the stock was \$1.36/share. The Corporation incurred \$16,727 in broker transaction fees that were netted against the realized gain. In addition, the Corporation sold its interest in Vanguard during the six months ended June 30, 2006 and recognized a (\$81,000) loss on the disposition. There were no realized gains/losses for the six months ended June 30, 2005.

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### **Net Change in Unrealized Appreciation (Depreciation) of Investments**

The Corporation recorded a net increase in unrealized appreciation on investments of \$829,048 during the six months ended June 30, 2006, as compared to an increase of \$165,074 during the six months ended June 30, 2005. The increase in unrealized appreciation (depreciation) on investments of \$829,048 is due to the following valuation changes made by the Corporation:

	<b>June 30, 2006</b>
Minrad valuation to market	\$ 834,310
Vanguard Sale	135,000
Photonics valuation to market	(4,400)
Minrad Stock Sales	(135,862)
<b>Total Change in net Unrealized Appreciation during the six months ended June 30, 2006</b>	<b>\$ 829,048</b>

The Corporation held 343,440 shares of Minrad stock at June 30, 2006. These shares were valued the average closing price for the last three days of the period ending June 30, 2006. The total value of the remaining Minrad shares amounted to \$1,363,457 and included unrealized appreciation of \$898,026. Minrad is a public stock (AMEX symbol: BUF) and the Corporation's Minrad shares are restricted subject to SEC Rule 144.

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

For the six month period ending June 30, 2005, the Corporation recognized appreciation of \$509,000 on its 667,981 shares of Minrad to reflect a change in pricing from a private offering of preferred stock. In addition, the Corporation decreased its value in Kionix by (\$284,477) during the six months ended June 30, 2005 due to the fact that the portfolio company failed to achieve certain performance milestones, therefore changing the liquidation preferences of the Series A and B securities. This caused the Corporation to reprice its shares in Kionix from \$0.35/share to \$0.25/share. Somerset's value was decreased by (\$50,349) during the six months ended June 30, 2005 based on a round of financing that caused the price per membership unit to decrease.

All of these value adjustments are consistent with the Corporation's established valuation policy.

### **Net Increase in Net Assets from Operations**

The Corporation accounts for its operations under U.S. generally accepted accounting principles for investment companies. The principal measure of its financial performance is "net increase (decrease) in net assets from operations" on its consolidated statements of operations. For the six months ended June 30, 2006, the net increase in net assets from operations was \$432,105 as compared to a net decrease in net assets from operations of \$(67,460) for the same six month period in 2005. This increase is attributed to the realized and unrealized appreciation recognized on the Minrad shares offset by the net investment losses for the same period discussed above.

### **Liquidity and Capital Resources**

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

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As of June 30, 2006, the Corporation's total liquidity, consisting of cash and cash equivalents, was \$1,492,122.

As of June 30, 2006 the Corporation had paid \$100,000 to the SBA to reserve its approved \$10,000,000 leverage. It has drawn down \$7,600,000 of this leverage as of June 30, 2006. The remaining SBA leverage is guaranteed by the SBA to be available through September 30, 2008. These SBA borrowings will have a balloon maturity beginning in 2014.

Management expects that it will be necessary to continue to draw down SBA leverage in the current fiscal year in order to fund operations and new investments.

The Corporation has investments at cost at June 30, 2006 of approximately \$13.7 million, of which approximately 49%, or \$6.7 million, provide for returns of interest at an annual blended rate of 10.6%. \$1.85 million of the \$6.7 million in interest bearing instruments provide for the deferral of interest payments after December 31, 2007. The Corporation's current outstanding debt to the SBA of \$7.6 million carries a blended interest cost of 5.8%, which requires semi-annual payments of interest. The Corporation's focus is to continue to make investments that provide for current returns of cash in the form of interest and dividends to provide funding to repay current SBA interest charges and to also fund its operating costs. Net cash used in operating activities has averaged approximately \$455,000 over the last three years and management anticipates this amount will continue at similar levels. The cash flow may fluctuate based on possible expenses associated with compliance with new regulations. Management believes that the cash and cash equivalents at June 30, 2006, coupled with the anticipated additional SBIC leverage draw downs and interest and dividend payments on its portfolio investments, will provide the Corporation with the liquidity necessary to fund operations and new investments over the next twelve months. The Corporation's cash flows related to its investing activities will continue to fluctuate based on its success in originating investments and its ability to realize gains on liquidation of investments.

### **Risk Factors and Other Considerations**

#### **The Corporation's Portfolio Investments are Illiquid**

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

#### **Investing in Private Companies involves a High Degree of Risk**

The Corporation typically invests a substantial portion of its assets in small and medium sized private companies. These private businesses may be thinly capitalized, unproven companies with risky technologies and may lack management depth and have not attained profitability. Because of the speculative nature and the lack of a public market for these investments, there is significantly greater risk of loss than is the case with traditional investment securities. The Corporation expects that some of its venture capital investments will be a complete loss or will be unprofitable and that some will appear to be likely to become successful but never realize their potential. The Corporation has been risk seeking rather than risk averse in its approach to venture capital and other investments. Neither the Corporation's investments nor an investment in the Corporation is intended to constitute a balanced investment program.

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

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

There is typically no public market for equity securities of the small privately held companies in which the Corporation invests. As a result, the valuations of the equity securities in the Corporation's portfolio are stated at fair value as determined by the good faith estimate of the Corporation's Board of Directors in accordance with the established SBA valuation policy. In the absence of a readily ascertainable market value, the estimated value of the Corporation's portfolio of securities may differ significantly, favorably or unfavorably, from the values that would be placed on the portfolio if a ready market for the equity securities existed. Any changes in estimated net asset value are recorded in the statement of operations as "Net change in unrealized appreciation (depreciation)."

### **Investing in The Corporation's Shares May be Inappropriate for the Investor's Risk Tolerance**

The Corporation's investments, in accordance with its investment objective and principal strategies, result in a far above average amount of risk and volatility and may well result in loss of principal. The Corporation's investments in portfolio companies are highly speculative and aggressive and, therefore, an investment in its shares may not be suitable for investors for whom such risk is inappropriate.

### **The Corporation is Subject to Risks Created by its Regulated Environment**

The Corporation is regulated by the SBA and the SEC. Changes in the laws or regulations that govern SBICs and BDCs could significantly affect the Corporation's business. Regulations and laws may be changed periodically, and the interpretations of the relevant regulations and laws are also subject to change. Any change in the regulations and laws governing the Corporation's business could have a material impact on its financial condition or its results of operations.

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

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

### **The Economic Environment May Change**

The value of the Corporation's common stock may decline and may be affected by numerous market conditions, which could result in the loss of some or the entire amount invested in its shares. The securities markets frequently experience extreme price and volume fluctuations which affect market prices for securities of companies generally, and technology and very small capitalization companies in particular. General economic conditions, and general conditions in the Internet and information technology, life sciences, material sciences and other high technology industries, will also affect the stock price.

### **The Corporation is Dependent Upon Key Management Personnel for Future Success**

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

### **The Corporation Operates in a Competitive Market for Investment Opportunities**

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

### **Fluctuations of Quarterly Results**

The Corporation's quarterly operating results could 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 portfolio companies encounter competition in their markets and general economic conditions. As a result of these factors, results for any one quarter should not be relied upon as being indicative of performance in future quarters.

### **Item 3. Quantitative and Qualitative Disclosures about Market Risk**

The Corporation's investment activities contain elements of risk. The portion of the Corporation's investment portfolio consisting of equity and equity-linked debt securities in private companies is subject to valuation risk. Because there is typically no public market for the equity and equity-linked debt securities in which it invests, the valuation of the equity interests in the portfolio is stated at "fair value" as determined in good faith by the Board of Directors in accordance with the Corporation's investment valuation policy. (The discussion of valuation policy contained in Item 1 "Financial Statements" and Supplementary Data in the "Notes to Consolidated Schedule of Portfolio Investments" and is hereby incorporated herein by reference.) In the absence of a readily ascertainable market value, the estimated value of the Corporation's portfolio may differ significantly from the values that would be placed on the portfolio if a ready market for the investments existed. Any changes in valuation are recorded in the Corporation's consolidated Statement of Operations as "Net change in unrealized appreciation (depreciation)."

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

As of June 30, 2006 the Corporation did not have any off-balance sheet investments or hedging investments.

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### **Item 4. Controls and Procedures**

*Evaluation of Disclosure Controls and Procedures.* Our management, with the participation of our principal executive officer and principal financial officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)), as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on such evaluation, our principal executive officer and principal financial officer have concluded that as of such date, our disclosure controls and procedures were designed to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in applicable SEC rules and forms and were effective.

*Changes in Internal Control Over Financial Reporting.* There have been no significant changes in our internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Rule 13a-15 or Rule 15d-15 that occurred during our last fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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**PART II.  
OTHER INFORMATION**

**Item 1. Legal Proceedings**

None

**Item 1A. Risk Factors**

We have had no material changes to risk factors as previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2005.

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

None

**Item 3. Defaults upon Senior Securities**

None

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

At the Annual Meeting of Shareholders of Rand Capital Corporation, Buffalo, New York, on the 27<sup>th</sup> day of April, 2006, the following represents the results of balloting:

The following nominees for election as directors received the number of votes set opposite their respective names:

	<u>VOTES FOR</u>	<u>VOTES WITHHELD</u>
Allen F. Grum	4,791,300	26,216
Erland E. Kailbourne	4,792,300	25,216
Ross B. Kenzie	4,791,175	26,341
Willis S. McLeese	4,628,851	188,665
Reginald B. Newman II	4,792,300	25,216
Jayne K. Rand	4,647,143	170,373
Robert M. Zak	4,791,300	26,216

**Item 5. Other Information**

None

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### **Item 6. Exhibits**

#### **(a) Exhibits**

The following exhibits are filed with this report or are incorporated herein by reference to a prior filing, in accordance with Rule 12b-32 under the Securities Exchange Act of 1934.

- (3)(i) Certificate of Incorporation of the Corporation, incorporated by reference to Exhibit (a)(1) of Form N-2 filed with the Securities Exchange Commission on April 22, 1997.
- (3)(ii) By-laws of the Corporation incorporated by reference to Exhibit (b) of Form N-2 filed with the Securities Exchange Commission on April 22, 1997.
- (4) Specimen certificate of common stock certificate, incorporated by reference to Exhibit (b) of Form N-2 filed with the Securities Exchange Commission on April 22, 1997.
- (10.1) Employee Stock Option Plan — incorporated by reference to Appendix B to the Corporation’s definitive Proxy Statement filed on June 1, 2002.\*
- (10.3) Agreement of Limited Partnership for Rand Capital SBIC, L.P. – incorporated by reference to Exhibit 10.3 to the Corporation’s Form 10-K filed for the year ended December 31, 2001.
- (10.4) Certificate of Limited Partnership of Rand Capital SBIC, L.P. – incorporated by reference to Exhibit 10.4 to the Corporation’s Form 10-K filed for the year ended December 31, 2001.
- (10.5) Limited Liability Corporation Agreement of Rand Capital Management, LLC – incorporated by reference to Exhibit 10.5 to the Corporation’s Form 10-K Report filed for the year ended December 31, 2001.
- (10.6) Certificate of Formation of Rand Capital Management, LLC– incorporated by reference to Exhibit 10.6 to the Corporation’s Form 10-K Report filed for the year ended December 31, 2001.
- (10.7) N/A
- (10.8) Profit Sharing Plan – incorporated by reference to Exhibit 10.8 to the Corporation’s Form 10-K Report filed for the year ended December 31, 2002.\*
- (21) Subsidiaries of the Corporation – incorporated by reference to Exhibit 21 to the Corporation’s Form 10-K Report filed for the year ended December 31, 2001.
- (31.1) Certification of the Chief Executive Officer Pursuant to Rules 13a-14(a)/15d-14(a) under the Securities Exchange Act of 1934, as amended, filed herewith
- (31.2) Certification of Chief Financial Officer Pursuant to Rules 13a-14(a)/15d-14(a) under the Securities Exchange Act of 1934, as amended, filed herewith
- (32.1) Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 – Rand Capital Corporation – filed herewith
- (32.2) Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 – Rand Capital SBIC, L.P. – filed herewith

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\* Management contract or compensatory plan.

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**Signatures**

**Pursuant to the requirements of Section 13 or 15(d) of Securities Exchange Act of 1934, the registrant has duly caused this Report on Form 10-Q to be signed on its behalf by the undersigned thereunto duly authorized.**

Dated: August 8, 2006

RAND CAPITAL CORPORATION

By: /s/ Allen F. Grum

Allen F. Grum, President

By: /s/ Daniel P. Penberthy

Daniel P. Penberthy, Treasurer

RAND CAPITAL SBIC, L.P.

By: RAND CAPITAL MANAGEMENT LLC

General Partner

By: RAND CAPITAL CORPORATION

Member

By: /s/ Allen F. Grum

Allen F. Grum, President

By: /s/ Daniel P. Penberthy

Daniel P. Penberthy, Treasurer

**EXHIBIT 31.1**

**CERTIFICATION**

**Chief Executive Officer Pursuant to Rules 13a-14(a)/15d-14(a) under the Securities Exchange Act of 1934, as amended**

I, Allen F. Grum, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Rand Capital Corporation, Rand Capital SBIC, L.P. and Rand Capital Management, LLC:
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: August 8, 2006

/s/ Allen F. Grum

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Allen F. Grum, President  
(Chief Executive Officer of Rand Capital Corporation and equivalent of Chief Executive Officer of Rand Capital SBIC, L.P.)

**EXHIBIT 31.2**

**CERTIFICATION**

**Chief Financial Officer Pursuant to Rules 13a-14(a)/15d-14(a) under the Securities Exchange Act of 1934, as amended**

I, Daniel P. Penberthy, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Rand Capital Corporation, Rand Capital SBIC, L.P. and Rand Capital Management, LLC:
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: August 8, 2006

/s/ Daniel P. Penberthy

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Daniel P. Penberthy, Treasurer  
(Chief Financial Officer of Rand Capital  
Corporation and equivalent of Chief Financial  
Officer of Rand Capital SBIC, L.P.)

**EXHIBIT 32.1**

**CERTIFICATION**

**Pursuant to 18 U.S.C Section 1350 as Adopted Pursuant to Section 906  
Of the Sarbanes-Oxley Act of 2002**

Pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, each of the undersigned officers of Rand Capital Corporation (the "Company"), does hereby certify, to such officer's knowledge, that:

The Quarterly Report on Form 10-Q for the quarter ended June 30, 2006 (the Form 10-Q) of the Company fully complies with the requirement of section 13(a) or 15(d) of the Securities Exchange Act of 1934 and the information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 8, 2006

s/s/ Allen F. Grum

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Allen F. Grum, President  
(Chief Executive Officer)

Dated: August 8, 2006

/s/ Daniel P. Penberthy

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Daniel P. Penberthy, Treasurer  
(Chief Financial Officer)

**EXHIBIT 32.2**

**CERTIFICATION**

**Pursuant to 18 U.S.C Section 1350 as Adopted Pursuant to Section 906  
Of the Sarbanes-Oxley Act of 2002**

Pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, each of the undersigned officers of Rand Capital SBIC, L.P. (the "Company"), does hereby certify, to such officer's knowledge, that:

The Quarterly Report on Form 10-Q for the quarter ended June 30, 2006 (the Form 10-Q) of the Company fully complies with the requirement of section 13(a) or 15(d) of the Securities Exchange Act of 1934 and the information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 8, 2006

*/s/ Allen F. Grum*

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Allen F. Grum, President of Rand Capital  
Corporation  
(equivalent of chief executive officer of  
Rand Capital SBIC, L.P.)

Dated: August 8, 2006

*/s/ Daniel P. Penberthy*

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Daniel P. Penberthy, Treasurer of Rand  
Capital Corporation  
(equivalent of chief financial officer of  
Rand Capital SBIC, L.P.)