PHARMACIA CORP /DE/
Form 11-K
July 01, 2002

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

FORM 11-K

[X] ANNUAL REPORT PURSUANT TO SECTION 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the period from January 1, 2001 to December 31, 2001

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ___________to ______________

Commission file number 001-2516

A. Full title of the plan and the address of the plan, if different from that of issuer named below:

PHARMACIA & UPJOHN EMPLOYEE SAVINGS PLAN

B. Name of issuer of the securities held pursuant to the plan and the address of its principal executive office:

PHARMACIA CORPORATION
100 Route 206 North
Peapack, New Jersey 07977

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the trustees (or other persons who administer the employee benefit plan) have duly caused this annual report to be signed on its behalf by the undersigned hereunto duly authorized.

PHARMACIA & UPJOHN EMPLOYEE SAVINGS PLAN

By: /s/ Peter J. McCauley

Peter J. McCauley
Director, Global Pension & Savings Plans
Secretary, Administrative Committee - U.S. Plans
Pharmacia Corporation

June 28, 2002

CONSENT OF INDEPENDENT AUDITORS

PHARMACIA CORPORATION:

We consent to the incorporation by reference in Pharmacia Corporation's Registration Statement on Form S-8 (No. 333-91684) of our report dated June 28, 2001, appearing in this annual report on Form 11-K of the Pharmacia & Upjohn Employee Savings Plan as of December 31, 2001 and for the period from January 1, 2001 to December 31, 2001.

/s/ PricewaterhouseCoopers

PricewaterhouseCoopers

Florham Park, New Jersey
June 28, 2002

THE PHARMACIA & UPJOHN
EMPLOYEE SAVINGS PLAN

Financial Statements

December 31, 2001 and 2000

THE PHARMACIA & UPJOHN EMPLOYEE SAVINGS PLAN
Index to Financial Statements

December 31, 2001 and 2000

Note: Supplemental schedules required by the Employee Retirement Income Security Act of 1974 that have not been included herein are not applicable to the Pharmacia & Upjohn Employee Savings Plan.

[Letterhead of PricewaterhouseCoopers]

Report of Independent Accountants

To the Participants and Administrator of
The Pharmacia & Upjohn Employee Savings Plan

In our opinion, the accompanying statements of net assets available for plan benefits and the related statement of changes in net assets available for plan benefits present fairly, in all material respects, the net assets available for benefits of The Pharmacia & Upjohn Employee Savings Plan (the "Plan") at December 31, 2001 and 2000, and the changes in net assets available for benefits for the year ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Plan's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes 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. We believe that our audits provide a reasonable basis for our opinion.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplemental schedules of Assets Held for Investment Purposes at End of Year as of December 31, 2001 and Reportable Transactions for the year ended December 31, 2001 are presented for the purpose of additional analysis and are not a required part of the basic financial statements but are supplementary information required by the Department of Labor's Rules and Regulations for Reporting and Disclosure under the Employee Retirement Income Security Act of 1974. These supplemental schedules are the responsibility of the Plan's management. The supplemental schedules have been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

/s/ PricewaterhouseCoopers

PricewaterhouseCoopers

June 21, 2002

THE PHARMACIA & UPJOHN EMPLOYEE SAVINGS PLAN

Statements of Net Assets Available for Plan Benefits

	December 31, 2001	December 31, 2000
Assets:		
Investments, at fair value	$1,326,957,418	$1,683,304,487
Investments, at contract value	251,222,778	214,166,263
Total investments	1,578,180,196	1,897,470,750
Receivables:		
Company contributions, net of forfeitures	41,395,385	33,568,691
Participant contributions	1,435,819	3,296,318
Dividends and interest receivable	4,181,192	4,564,239
Other receivables	439,455	1,043,145
Total receivables	47,451,851	42,472,393
Total assets	1,625,632,047	1,939,943,143
Liabilities:		
Notes payable	201,900,000	234,700,000
Interest payable	47,403,058	45,975,096
Other	510,769	622,757
Total liabilities	249,813,827	281,297,853
Net assets available for plan benefits	$1,375,818,220	$1,658,645,290

See accompanying notes to the financial statements.

THE PHARMACIA & UPJOHN EMPLOYEE SAVINGS PLAN
Statement of Changes in Net Assets Available for Plan Benefits

	For the Year Ended December 31, 2001
Additions:	
Additions to net assets attributed to:	
Investment income (loss):	
Net depreciation in fair value of investments	$ (361,449,203)
Interest	14,768,514
Dividends	25,189,646
Interest on participants' loans	3,067,565

Total investment loss	(318,423,478)
Contributions:	
Participant	78,985,477
Rollovers	5,953,129
Company	41,896,121
Total additions (reductions)	(191,588,751)
Deductions:	
Deductions from net assets attributed to:	
Benefits paid to participants	70,686,328
Plan expenses	552,399
Interest on notes payable	19,999,592
Total deductions	91,238,319
Net decrease	(282,827,070)
Net assets available for plan benefits:	
Beginning of year	1,658,645,290
End of year	$ 1,375,818,220

See accompanying notes to the financial statements.

THE PHARMACIA & UPJOHN EMPLOYEE SAVINGS PLAN

Notes to Financial Statements

December 31, 2001 and 2000

1. Description of Plan

The following brief description of the Pharmacia & Upjohn Employee Savings Plan (the "Plan") is provided only for general information. Participants should refer to the Plan Document for a more complete description of the Plan's provisions.

General

Pharmacia & Upjohn Company (the "Company") is the sponsor of the Plan. The Plan is a defined contribution plan with two component parts: a section 401(k) plan and an Employee Stock Ownership Plan (the "ESOP"). The Plan covers substantially all domestic employees of the Company not otherwise covered by another defined contribution plan of the Company.

Administration

The Global Employee Benefits Oversight Committee and the Administrative

Committee - U.S. Plans are responsible for administering plan operations in accordance with the Employee Retirement Income Security Act of 1974 ("ERISA") plan documents. The Global Benefits Investment Committee is responsible for monitoring plan investments.

Contributions

Participants can elect to contribute on a before-tax or after-tax basis from 1% to 18%, in 1% increments, of their Total Pay, as defined in the Plan document. The Internal Revenue Code ("IRC") contains certain limits on participant contributions to a qualified plan, such as a $10,500 limit on a participant's before-tax contributions during the 2001 calendar year. Other limits also apply to highly compensated employees participating in the Plan.

Participants may also elect to make rollover contributions to the Plan from other qualified defined contribution plans.

Since 1990, matching contributions have been made through the ESOP. The Company matching contributions are the basis for allocating shares of the Company's Convertible Perpetual Preferred Stock ("Preferred Stock") to participants' accounts. Dividends paid to the participants' ESOP accounts are also allocated in Preferred Stock.

The Company will match 100% of participant contributions, from 1% to 5% of Total Pay, in the form of Preferred Stock within the ESOP. The Plan will allocate shares of Preferred Stock to participants such that, at the time of allocation, the total value of the shares allocated is equivalent to the Company match. The value of a share of Preferred Stock will be the closing price of one share of Pharmacia common stock multiplied by a 1.7255 conversion factor.

Cash dividends on Preferred Stock shares allocated to participants' accounts prior to January 1, 2000 are exchanged for additional shares of Preferred Stock using the $40.30 per-share stated value (the purchase price paid by the ESOP at its inception). Cash dividends on Preferred Stock shares allocated to participants' accounts on or after January 1, 2000 are exchanged for additional shares of Preferred Stock using the Pharmacia common stock price multiplied by the 1.7255 conversion factor.

The Company contributes to the ESOP cash amounts that are necessary to enable the Plan to make its regularly scheduled payments of principal and interest due on the ESOP's outstanding debt and to release Preferred Stock to cover allocations to participant accounts. Employer dividends paid to the ESOP on the unallocated Preferred Stock and certain other funds are also used to repay the debt incurred by the Plan to purchase the Preferred Stock from the Company at the inception of the leveraged ESOP (see Note 4).

Investment Options

Participant contributions received by the Plan are invested at the direction of the participants in accordance with the terms of the Plan document.

Each participant may direct his or her contributions to the following fund options:

(a) Income Fund,
(b) American Balanced Fund,
(c) Indexed Stock Fund,
(d) Neuberger Berman Guardian Fund,
(e) American Century Ultra Fund,
(f) Templeton Foreign Fund,
(g) Pharmacia Common Stock Fund, or
(h) Any combination of the above, provided that a minimum of five percent and a multiple of one percent is directed to each fund selected.

The funds above (not including the Pharmacia Common Stock Fund) are also offered in six pre-mixed portfolios, which are designed to match investments to a level of risk and return that the participant is most comfortable with. Participants may elect to transfer or allocate their participant contribution balances and earnings thereon to any of the above funds.

Company matching contributions and earnings thereon are only posted to the ESOP Fund. Upon completing ten years of employment service and attaining age 55, participants are allowed to transfer a portion of their Pharmacia Common Stock Fund balance (i.e., pertaining to Company contributions and earnings thereon) and their ESOP Fund balance into the other investment fund options. For participants age 55 - 59 and for participants age 60 and older, 25% and 50% can be transferred to other investment funds, respectively. Those age 60 and older that have already diversified their current Common Stock 25%, may only diversify another 25%.

Participant Accounts

Each participant's account is credited with the participant's contributions, Company contributions, and plan earnings. Participants' accounts are valued on a daily basis. The benefit to which a participant is entitled is the benefit that can be provided from the participant's vested account balance.

Vesting

Participants are always 100% vested in their contributions to the Plan and earnings thereon.

As of January 1, 2000, all Company contributions and earnings thereon are 100% vested for all active participants on or after January 1, 2000.

Participants who terminated employment prior to January 1, 2000 with less than five years of employment service and less than three years of participation in the Plan are subject to the vesting schedule below:

Years of Participation	Non-forfeitable Percentage
1 but less than 2	33 1/3%
2 but less than 3	66 2/3%
3 or more	100%

Participants who cease participation in the Plan may be entitled to forfeited amounts if they re-participate in the Plan within five years.

Participant Loans

The Plan has a loan provision which allows participants to borrow from their fund accounts a minimum of $500 up to a maximum equal to the lesser of 50% of their vested account balance or $50,000 (reduced by the highest outstanding loan balance within the previous twelve months). Loan terms range from 1-5 years or up to 10 years for the purchase of a primary residence. Loans for the purchase of a home have a $3,000 minimum loan amount. The loans are secured by the balance in the participant's account and bear a pre-established interest rate. Interest is credited to the account of the participant. Repayments may not necessarily be made to the same fund from which amounts were borrowed. Repayments are credited to the applicable funds based on the participant's investment elections at the time of repayment.

Payment of Benefits

Participants who leave the Company may elect to receive their vested Plan balance. However, their Pharmacia Common Stock Fund and ESOP accounts may be subject to forfeiture based upon years of participation and service (if the participant terminated employment prior to January 1, 2000).

Benefits are paid either in cash or in cash and Pharmacia common stock. Pharmacia common stock is issued only with respect to the participant's accounts in the Pharmacia Common Stock Fund and the ESOP Fund. Upon retirement or death, the full value of the participant's accounts is paid in either a lump sum, in installments or by the purchase of an annuity contract. If a participant elects to receive common stock, each share of the Preferred Stock (based on participant records) will be converted into 1.7255 shares of Pharmacia common stock.

Participants may also elect to make in-service withdrawals subject to certain restrictions.

2. Summary of Accounting Policies

Method of Accounting

The financial statements of the Plan have been prepared on the accrual basis of accounting.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and changes therein, and disclosure of contingent assets and liabilities. Actual results could differ from those estimates.

Investment Valuation and Income Recognition

Shares of mutual funds are valued at quoted market prices which represent the net asset value of shares held by the Plan at year-end. Common/collective trust funds are stated at redemption value as determined by the trustees of such funds based upon the underlying securities stated at fair value. Investments in money market instruments are generally short-term and are valued at cost, which approximates market. Investments in guaranteed investment contracts ("GICs") and synthetic investment contracts ("SICs") are reported at their contract value by the insurance companies and underlying banks, respectively, because these investments have fully benefit-responsive features (see Note 5). Pharmacia Common Stock is valued at quoted market price as of the last business day of the Plan year. The value of outstanding participant loans is determined based on the outstanding principal balance as of the last day of the Plan year, which approximates fair value.

Pharmacia Preferred Stock is valued using the higher of the per-share stated value of $40.30 or the quoted market price of Pharmacia common stock multiplied by 1.7255 on the last business day of the plan year. (Note: Preferred Stock share balances maintained by the plan's trustee and recordkeeper are on a basis equal to one-thousandth of the share balance reflected on the Company's financial statements and the $40,300 stated value.)

Purchases and sales of securities are reflected on a trade-date basis. Dividend income is recorded on the ex-dividend date. Income from other investments is recorded as earned on an accrual basis.

The Plan presents in the statement of changes in net assets available for plan benefits, the net appreciation (depreciation) in the fair value of its investments which consists of the realized gains and losses and the unrealized appreciation (depreciation) on those investments.

Payment of Benefits

Benefit payments are recorded when paid.

Plan Expenses

The Plan pays certain outside service provider expenses (e.g., recordkeeping and trustee fees) incurred in the operation of the Plan. Investment manager fees are paid by the Plan and are netted against investment income. Certain other expenses are paid by the Company.

Forfeitures

Forfeited amounts are used to pay expenses of the Plan, interest on ESOP debt incurred by the Plan and to reduce Company contributions. Forfeitures which have not been utilized amounted to $737 and $21,630 as of December 31, 2001 and 2000, respectively.

Risks and Uncertainties

The Plan provides for various investment options in any combination of stocks, mutual funds, common/collective trusts, and other investment securities. Investment securities are exposed to various risks, such as interest rate, market and credit risk. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is possible that changes in risks in the near term would materially affect participants' account balances and the amounts reported in the statement of net assets available for plan benefits and the statement of changes in net assets available for plan benefits.

3. Investments

The following presents investments that represent 5 percent or more of the plan's net assets.

	December 31, 2001	20
Neuberger Berman Guardian Fund (5,006,943 and 4,836,623 units, respectively)	$ 72,300,261	$ 71,7
American Balanced Fund (4,976,248 and 4,068,225 units, respectively)	78,873,531	62,9
Indexed Stock Fund (6,562,885 and 6,596,621 units, respectively)	213,687,551	243,7
American Century Ultra Fund (5,361,812 and 5,292,897 units, respectively)	148,200,486	171,3
Pharmacia Common Stock (5,370,542 and 5,052,303 shares, respectively)*	229,053,616	308,1
Pharmacia Preferred Stock (6,399,670 and 6,517,533 shares, respectively)*	470,968,194	686,0

*Nonparticipant-directed

During 2001, the plan's investments (including gains and losses on investments bought and sold, as well as held during the year) depreciated in value by $361,449,203 as follows:

	2001

Mutual funds	$ (32,148,634)
Common Stock	(95,027,431)
Preferred Stock	(205,450,896)
Common/collective trust funds	(28,822,242)
	$(361,449,203)

4. Nonparticipant-directed Investments

Pharmacia Common Stock Fund

Effective April 1, 1999, the Pharmacia Common Stock Fund was added as an investment option into which participants can direct their contributions and/or transfer existing balances. However, certain Company contribution balances (and earnings thereon) within the Pharmacia Common Stock Fund can only be transferred out of the fund into other investment options after participants satisfy certain age and service requirements. All assets and activity within this fund have been disclosed as nonparticipant-directed for purposes of this report.

Below are the net assets and significant components of the changes in net assets relating to the Pharmacia Common Stock Fund:

	2001	2000
Investments:		
Short-term investment funds	$ 2,193,935	$ 1,747,268
Pharmacia Common Stock	229,053,616	308,190,483
Total investments	231,247,551	309,937,751
Receivables:		
Dividends and interest receivable	4,776	14,993
Receivable from other investment funds	790,011	--
Participant contributions	118,054	221,197
Investments sold	52,874	1,036,379
Total receivables	965,715	1,272,569
Liabilities:		
Payable to other investment funds	--	278,076
Other liabilities	16,419	1,885
Total liabilities	16,419	279,961
Net assets available for plan benefits	$232,196,847	$310,930,359

THE PHARMACIA & UPJOHN EMPLOYEE SAVINGS PLAN

Notes to Financial Statements

December 31, 2001 and 2000

	Year ended December 31, 2001
Additions:	
Additions to net assets attributed to:	
Investment income (loss):	
Net depreciation	$ (95,027,431)
Interest	127,854
Dividends	2,713,345
Total investment loss	(92,186,232)
Transfers from other investment funds, net	21,996,376
Participant contributions (including rollovers)	6,939,607
Total additions (reductions)	(63,250,249)
Deductions:	
Deductions from net assets attributed to:	
Benefits paid to participants	15,483,128
Plan expenses	135
Total deductions	15,483,263
Net decrease	(78,733,512)
Net assets available for plan benefits:	
Beginning of year	310,930,359
End of year	$ 232,196,847

ESOP and Notes Payable

On March 1, 1990, the ESOP borrowed $275 million from the Bank of New York through the issuance of amortizing notes. These notes, which are guaranteed by the Company, mature in 2004 and pay interest at an annual rate of 9.79%. The proceeds of this debt were paid to the Company to liquidate $275 million of an original $300 million loan from the Company to the ESOP. The remaining principal balance on these notes was $154,900,000 with unpaid interest of $15,164,710 and $189,700,000 with unpaid interest of $18,571,630 as of December 31, 2001 and 2000, respectively.

As of March 1, 1990, the ESOP also issued a new note to the Company in settlement of the remaining balance on the original ESOP loan. This note, in the amount of $25 million, carries an interest rate of 6.25% per annum. Interest accrues and is payable, along with principal, no later than the maturity date of February 1, 2005. The balance of this note, including unpaid interest, was $51,239,923 and $48,225,811 at December 31, 2001 and 2000, respectively.

Effective January 31, 1997, the ESOP and State Street Bank entered into an agreement, whereby the ESOP can borrow amounts that in the aggregate cannot exceed $95,000,000 (collectively the "New Loans"). Any such borrowings bear interest at 7.00% per annum and will be due no later than December 31, 2010. No interest shall be due until the maturity date of any New Loans. The proceeds of each New Loan are to be used to pay principal and interest then due on any existing ESOP loans. In relation to New Loans, the ESOP had drawings of $22,000,000 with unpaid interest of $5,998,425 and $20,000,000 with unpaid interest of $4,177,655 as of December 31, 2001 and 2000, respectively.

Projected principal loan payments on the ESOP debt (net of future New Loans) are as follows:

Year	Amount
2002	$ 43,700,000
2003	52,600,000
2004	58,600,000
2005	22,216,492
2006 to 2010	24,783,508
Total	$201,900,000

Following are the net assets and significant components of the changes in net assets relating to the ESOP:

THE PHARMACIA & UPJOHN EMPLOYEE SAVINGS PLAN

Notes to Financial Statements

December 31, 2001 and 2000

	December 31, 2001			
	Allocated	Unallocated	Total	Alloca
Investments:				
Short-term investment funds	$ --	$ 12,965,029	$ 12,965,029	$
Pharmacia Preferred Stock, convertible	255,437,529	215,530,665	470,968,194	306,35
Total investments	255,437,529	228,495,694	483,933,223	306,35
Receivables:				
Dividends and interest receivable	--	4,154,909	4,154,909	
Company contributions, net of forfeitures	--	41,395,385	41,395,385	
Other receivables	--	737	737	

Total receivables		45,551,031	45,551,031	
Liabilities:	--			
Notes payable	--	201,900,000	201,900,000	
Interest payable	--	47,403,058	47,403,058	
Total liabilities		249,303,058	249,303,058	
Net assets available for plan benefits	$255,437,529	$ 24,743,667	$280,181,196	$306,35

THE PHARMACIA & UPJOHN EMPLOYEE SAVINGS PLAN

Notes to Financial Statements

December 31, 2001 and 2000

	Year ended December 31, 2001		
	Allocated	Unallocated	Total
Additions:			
Additions to net assets attributed to:			
Investment income (loss):			
Net depreciation	$ (89,298,487)	$(116,152,409)	$(205,450,8
Interest	--	218,179	218,1
Dividends	7,867,240	8,366,383	16,233,6
Total investment loss	(81,431,247)	(107,567,847)	(188,999,0
Company contributions	--	41,896,121	41,896,1
Allocation of 501,149 shares of Preferred Stock for Company matching contributions	39,878,104		39,878,1
Total additions (reductions)	(41,553,143)	(65,671,726)	(107,224,8
Deductions:			
Deductions from net assets attributed to:			
Benefits paid to participants	(9,374,622)	--	(9,374,6
Interest on notes payable	--	(19,999,592)	(19,999,5
Transfers to other investment funds	12,821	--	12,8
Allocation of 501,149 shares of Preferred Stock for Company matching contributions		(39,878,104)	(39,878,1
Total deductions	(9,361,801)	(59,877,696)	(69,239,4
Net decrease	(50,914,944)	(125,549,422)	(176,464,3
Net assets available for plan benefits:			

Beginning of year	306,352,473	150,293,089	456,645,5
End of year	$ 255,437,529	24,743,667	$ 280,181,1

5. Investment Contracts

The Income Fund consists primarily of benefit responsive GICs and SICs. The contract value of the GICs and SICs represents the cost or face-value of the contract plus accrued interest. At December 31, 2001 and 2000, the Plan held GICs with a contract value of $25,303,802 and $30,147,174, respectively. The contract value of the SICs represents fair value of the underlying asset plus the contract-value of the wrapper contract associated with the underlying asset. At December 31, 2001 and 2000, fair values of assets underlying the SIC's were $231,584,946 and $185,229,622, respectively. Participants may ordinarily direct the withdrawal or transfer of all or a portion of their investment at contract value.

There are no reserves against contract value for credit risk of the contract issuers or otherwise. The average portfolio yield and crediting interest rates were approximately 6% for 2001 and 2000. For GICs, the crediting interest rate, specified in the contract, is agreed upon with the issuers and is maintained for the life of the contract. For SICs, the rate is based on a formula which consists of the yield to maturity, duration, and the book and market values. The rate for SICs is periodically reset, usually quarterly, and cannot be reset below 0%.

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THE PHARMACIA & UPJOHN EMPLOYEE SAVINGS PLAN

Notes to Financial Statements

December 31, 2001 and 2000

6. Reconciliation of Financial Statements to Form 5500

The following is a reconciliation of net assets available for plan benefits according to the financial statements to Form 5500.

	December 31, 2001	2000
Net assets available for plan benefits per the financial statements	$ 1,375,818,220	$ 1,658,645,29
Amounts allocated to withdrawing participants	(1,144,000)	(1,075,94
Defaulted loans deemed to be distributions	(95,385)	-
Net assets available for plan benefits per Form 5500	$ 1,374,578,835	$ 1,657,569,34

The following is a reconciliation of benefits paid to participants according to the financial statements to Form 5500:

	Year ended December 31, 2001
Benefits paid to participants per the financial statements	$ 70,686,328
Add: Amounts allocated to withdrawing participants at December 31, 2001	1,144,000
Less: Amounts allocated to withdrawing participants at December 31, 2000	(1,075,946)
Benefits paid to participants per Form 5500	$ 70,754,382

Amounts allocated to withdrawing participants are recorded on Form 5500 for benefit claims that have been processed and approved for payment prior to December 31 but not yet paid as of that date.

The following is a reconciliation of net gain (loss) per the financial statements to the Form 5500:

	Year ended December 31, 2001
Net decrease per financial statements	$(282,827,070)
Add: Amounts allocated to withdrawing participants at December 31, 2000	1,075,946
Less: Amounts allocated to withdrawing participants at December 31, 2001	(1,144,000)
Certain deemed distributions of participant loans at December 31, 2001	(95,385)
Net gain (loss) per the Form 5500	$(282,990,509)

7. Related-Party Transactions

The Plan holds shares of Pharmacia common stock and preferred stock. At

December 31, 2001 and 2000, the Plan owned 5,370,542 and 5,052,303 shares of Pharmacia Corporation common stock at a cost of $117,753,110 and $87,782,347, respectively. At December 31, 2001 and 2000, the Plan owned 6,399,670 and 6,517,533 shares of Pharmacia Corporation preferred stock at a cost of $257,920,598 and $262,656,580, respectively. In addition, Plan funds are invested in a short-term investment fund as well as SICs issued by State Street Bank & Trust Company, a trustee of the Plan. At December 31, 2001 and 2000, the fair value of the State Street Bank & Trust Company short-term investment account was $21,542,503 and $43,355,639, respectively and the contract value of the SICs was $0 for 2001 and $15,232,902 for 2000.

8. Plan Termination

Although it has not expressed any intent to do so, the Company has the right under the Plan to discontinue its contributions at any time and to terminate the Plan subject to the provisions of ERISA. In the event of Plan termination, participants would become 100 percent vested in their entire plan balance (including match and discretionary contributions and earnings thereon).

9. Tax Status of the Plan

The Plan obtained its latest determination letter on April 18, 1996, in which the Internal Revenue Service indicated that the Plan, as then designed, was in compliance with the applicable requirements of the IRC. The Plan has been amended since receiving the determination letter. However, the Company believes that the Plan is currently designed and being operated in compliance with the applicable requirements of the IRC. Therefore, no provision for income taxes has been included in the Plan's financial statements. The Company applied for a new determination letter in February 2002.

10. Subsequent Event

Effective March 1, 2002, the Plan's net assets were transferred to a new trustee, The Northern Trust Company.

On June 28, 2001, the Global Employee Benefits Oversight Committee approved the amendment and restatement of the Plan, to be effective July 1, 2002. The New Plan, to be named the Pharmacia Savings Plan, will include the Retirement Choice Program and New Investment Options. Under the Retirement Choice program, participants will have a choice of two retirement benefit options. Option 1 offers additional Pension Plan benefits and Option 2 offers additional Savings Plan benefits. Participants will receive a pension and savings benefit under either option and can choose between Options 1 and 2 on an annual basis. In addition, the New Plan will offer New Investment Options in the form of eight core investment funds and four pre-mixed investment funds. The eight core investment funds are the Income Fund, the Core Bond Fund, the Value Stock Fund, the Large Company Stock Fund, the Growth Stock Fund, the Mid-Small Company Stock Fund, the International Stock Fund, and Pharmacia Common Stock Fund. The pre-mixed funds are the Conservative Pre-Mixed Fund, the Moderate Pre-Mixed Fund, the Moderately Aggressive Pre-Mixed Fund and the Aggressive Pre-mixed Fund. These funds offer varying degrees of risk and return. They are invested in the Core Bond Fund, the Large Company Stock Fund, the Mid-Small Company Stock Fund, and the International Stock Fund in predetermined percentages to form the funds. Participant account balances in the Pharmacia Savings and Investment Plan ("Pharmacia SIP") are to be transferred into the New Plan on July 1, 2002. All Plan assets are to be invested in the New Investment Options as of July 1, 2002.

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Supplemental Schedules

THE PHARMACIA & UPJOHN EMPLOYEE SAVINGS PLAN

Schedule H, line 4i--Schedule of Assets (Held at End of Year)

December 31, 2001

EIN# 38-1123360
Plan# 002

(a)	(b) Identity of Issue, Borrower, Lessor, or Similar Party	(c) Description of Investment including Maturity Date, Rate of Interest, Collateral, Par, or Maturity	(d) Cost	(e) Current
	Common Stock:			
*	Pharmacia Corporation	Common stock, $2.00 par value; 5,370,542 shares	$ 117,753,110	$229,05
	Total common stock		$ 117,753,110	$229,05
	Preferred stock:			
*	Pharmacia Corporation convertible - unallocated	Preferred stock, $.01 par value; 2,928,701 shares	$ 118,015,360	$215,53
*	Pharmacia Corporation convertible - allocated	Preferred stock, $.01 par value; 3,470,969 shares	139,905,238	255,43
	Total preferred stock		$ 257,920,598	$470,96
	Mutual Funds:			
	American Century Ultra	Mutual fund: 5,361,812 units	$ 171,057,482	$148,20
	American Balanced	Mutual fund: 4,976,248 units	74,755,873	78,87
	Neuberger Berman Guardian	Mutual fund: 5,006,943 units	96,399,183	72,30
	Templeton Foreign	Mutual fund: 6,721,194 units	65,726,893	62,17

	Total mutual funds		$ 407,939,431	$361,54
	Common/Collective Trust Funds:			
	Barclays Global Investors Equity Index Fund	Common/Collective Trust Fund: 6,562,885 units	$ 148,356,498	$213,68
	Total Common/Collective Trust Fund		$ 148,356,498	$213,68
	Short-Term Investment Funds:			
*	State Street Bank & Trust Co. Short-Term Investment Fund	Money market fund	$ 21,542,503	$ 21,54
	Total Short-Term Investment Funds		$ 21,542,503	$21,542

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* Represents a party-in-interest to the Plan.

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THE PHARMACIA & UPJOHN EMPLOYEE SAVINGS PLAN

Schedule H, line 4i--Schedule of Assets (Held at End of Year)

December 31, 2001

EIN# 38-1123360
Plan# 002

(a)	(b) Identity of Issue, Borrower, Lessor, or Similar Party	(c) Description of Investment including Maturity Date, Rate of Interest, Collateral, Par, or Maturity	(d) Cost	(e) Current
	Guaranteed investment contracts - insurance companies:			
	American Int'l Life ICON Contract No. GIC-18305	Interest rate: 5.73% Maturity date: 11/06/2003	$ 8,343,324	$ 8,343
	John Hancock Mutual Life Ins. Co. Contract No. GAC-14500	Interest rate: 5.90% Maturity date: 02/10/2004	8,252,398	8,252
	Principal Mutual Life Ins. Co. Contract No. 4238722	Interest rate: 7.03% Maturity date: 09/29/2003	5,440,890	5,440
	Travelers Insurance Co. Contract No. GR17755	Interest rate: 7.10% Maturity date: 07/31/2003	3,267,190	3,267
	Total Guaranteed Investment Contracts - Contract Value		$25,303,802	$25,303

THE PHARMACIA & UPJOHN EMPLOYEE SAVINGS PLAN

Schedule H, line 4i--Schedule of Assets (Held at End of Year)

December 31, 2001

EIN# 38-1123360
Plan# 002

(a)	(b) Identity of Issue, Borrower, Lessor, or Similar Party	(c) Description of Investment including Maturity Date, Rate of Interest, Collateral, Par, or Maturity	(d) Cost	(e) Current
	Synthetic Investment Contracts**:			
	AIG Financial Products (3 contracts)			
	Contract No. 302427	Wrapper Contract SCAMT 96-3(A)		$
		Total Contract Value	$ 4,613,749	
		Interest rate: 5.59%		
		Maturity date: 07/15/2004		
	Contract No. 180162	Wrapper Contract American Express 97-1 (A)		
		Total Contract Value	5,031,506	
		Interest rate: 5.95%		
		Maturity date: 09/16/2002		
	Contract No. 212753	Wrapper Contract First USA 1997-6 (A) FUSAM		
		Total Contract Value	7,059,402	
		Interest rate: 5.40%		
		Maturity date: 07/17/2002		
	Chase Manhattan Bank (1 contract)	Wrapper Contract FEDHMLN: 6.875% 1/15/05		
	Contract No. 434193	Total Contract Value	5,127,575	
		Interest rate: 7.13%		
		Maturity date: 01/18/2005		
	Monumental Life Ins. Co ABS Insurance Co. (4 contracts)	Wrapper Contract Global Wrap		
	Contract No. MDA00349TR	Total Contract Value	36,862,492	
		Interest rate: 5.59%		
		Maturity date: N/A		

** A synthetic investment contract is comprised of two components, an underlying asset and a wrapper contract. The underlying asset is valued at representative quoted market prices. The wrapper contract is valued as the difference between the fair value of the underlying asset and the contract value. Contract value represents contributions made under the contract, plus earnings, less Plan withdrawals and administrative expenses. The wrapper contract guarantees the Plan contract value.

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THE PHARMACIA & UPJOHN EMPLOYEE SAVINGS PLAN

Schedule H, line 4i--Schedule of Assets (Held at End of Year)

December 31, 2001

EIN# 38-1123360
Plan# 002

(a)	(b) Identity of Issue, Borrower, Lessor, or Similar Party	(c) Description of Investment including Maturity Date, Rate of Interest, Collateral, Par, or Maturity	(d) Cost	(e) Current
	Contract No. BDA00379TR-14	Wrapper Contract DCAT00-D A3 6.66% 1 05		
		Total Contract Value Interest rate: 6.97% Maturity date: 11/10/2003	4,008,590	
	Contract No. BDA00379TR-13	Wrapper Contract FNR 98-36 PM 6.25%		
		Total Contract Value Interest rate: 7.29% Maturity date: 06/19/2006	4,913,720	
	Contract No. BDA00379TR-11	Wrapper Contract FHLMC 7% 2/15/2003		
		Total Contract Value Interest rate: 6.91% Maturity date: 02/18/2003	10,271,058	
	Morgan Guaranty (2 contracts) Contract No. Upjohn06	Wrapper Contract FNR 98-63 PD 5.5 6/21		
		Total Contract Value Interest rate: 5.58% Maturity date: 12/27/2005	5,002,458	

Contract No. Upjohn05A	Wrapper Contract CSFB 00-C1 A1 7.325%		
	Total Contract Value Interest rate: 7.05% Maturity date: 07/15/2008	4,722,667	
Rabobank Nederland (3 contracts) Contract No. UPJ030101	Wrapper Contract FH R 2082 VA 6.5 1/06		
	Total Contract Value Interest rate: 5.37% Maturity date: 01/17/2006	5,000,967	
Contract No. UPJ110001	Wrapper Contract CARAT 00-2 (A4) 6.46 7/06		
	Total Contract Value Interest rate: 6.60% Maturity date: 12/16/2002	4,010,633	

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THE PHARMACIA & UPJOHN EMPLOYEE SAVINGS PLAN

Schedule H, line 4i--Schedule of Assets (Held at End of Year)

December 31, 2001

EIN# 38-1123360
Plan# 002

(a)	(b) Identity of Issue, Borrower, Lessor, or Similar Party	(c) Description of Investment including Maturity Date, Rate of Interest, Collateral, Par, or Maturity	(d) Cost	(e) Current
	Contract No. UPJ060101	Wrapper Contract Global Wrap		(37,
		Total Contract Value Interest rate: 5.58% Maturity date: N/A	36,862,492	36,
	UBS AG (3 contracts) Contract No. 3080	Wrapper Contract Global Wrap		(37,
		Total Contract Value Interest rate: 5.58% Maturity date: N/A	36,862,238	36,
	Contract No. 2778	Wrapper Contract		(

	FHR 2076 PC 6 3/22		5,
	Total Contract Value Interest rate: 5.84% Maturity date: 08/15/2005	5,690,061	5,
Contract No. 2789	Wrapper Contract COMT 00-2 A 7.2 8/08		4,
	Total Contract Value Interest rate: 5.42% Maturity date: 06/15/2005	4,245,040	4,
West Deutsche Landesbank (3 contracts)	Wrapper Contract Global Wrap		(37,
Contract No. WLB6218	Total Contract Value Interest rate: 5.59% Maturity date: N/A	36,862,491	36,
Contract No. WLB6202	Wrapper Contract FHR 1243 P 7.2 4/07		(4,
	Total Contract Value Interest rate: 7.49% Maturity date: 04/17/2006	4,710,840	4,
Contract No. WLB6210	Wrapper Contract FHR 1610 PM 6.25 4/22		4,
	Total Contract Value Interest rate: 5.84% Maturity date: 09/17/2007	4,060,997	4,

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THE PHARMACIA & UPJOHN EMPLOYEE SAVINGS PLAN

Schedule H, line 4i--Schedule of Assets (Held at End of Year)

December 31, 2001

EIN# 38-1123360
Plan# 002

(a)	(b) Identity of Issue, Borrower, Lessor, or Similar Party	(c) Description of Investment including Maturity Date, Rate of Interest, Collateral, Par, or Maturity	(d) Cost	(e) Current
	Total Synthetic Investment Contracts - Contract Value		$ 225,918,976	$ 225

Total Investment Contracts		$ 251,222,778	$ 251
Participant loans:			
Participant loans	Interest rate: 5.75% - 12%	$ -	$ 30
Total Investments		$1,204,734,918	$ 1,578

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THE PHARMACIA & UPJOHN EMPLOYEE SAVINGS PLAN

Schedule H, line 4j--Schedule of Reportable Transactions

For the Year Ended December 31, 2001

EIN# 38-1123360
Plan# 002

(a) Identify of Party Involved	(b) Description of Asset	Number of Transactions	(c) Purchase Price	(d) Selling Price
State Street Bank & Trust *Company	Short-term Investment Fund	216	93,256,656	--
		314		93,213,228

(e) Lease Rental	(f) Expense Incurred with Transaction	(g) Cost of Asset	(h) Current Value of Asset on Transaction Date	(i) Net Gain or (Loss)
--	--	93,256,656	93,256,656	--
--	--	93,213,228	93,213,228	--

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* Represents a party-in-interest to the Plan.

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Part II

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

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

2006 Quarter ending:	**High**	**Low**
March 31st	$ 1.43	$ 1.30
June 30th	$ 1.48	$ 1.42
September 30th	$ 1.90	$ 1.68
December 31st	$ 3.55	$ 3.40

2005 Quarter ending:	**High**	**Low**
March 31st	$ 1.67	$ 1.36
June 30th	$ 1.47	$ 1.17
September 30th	$ 1.34	$ 1.16
December 31st	$ 1.53	$ 1.09

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

Profit Sharing and Stock Option Plans

In July 2001, the 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 the Corporation s employees in connection with the establishment of its SBIC subsidiary. As of December 31, 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.

In 2002, the Corporation established a non-equity incentive Profit Sharing Plan for its executive officers in accordance with Section 57(n) of the Investment Company Act of 1940 (the 1940 Act). The profit sharing plan provides for incentive compensation to the named executive officers based on a stated percentage of net realized capital gains and unrealized depreciation of Rand SBIC. There have been no accruals for, nor contributions to, the Profit Sharing Plan since the Plan inception in 2002.

On March 16, 2007 the Corporation had a total of 1,116 shareholders, which included 111 record holders of its common stock, and an estimated 1,005 shareholders with shares beneficially owned in nominee name or under clearinghouse positions of brokerage firms or banks.

On October 18, 2001 the Board of Directors authorized the repurchase of up to 5% of the Corporation s outstanding stock through purchases on the open market which was extended through October 26, 2007. During 2003 and 2002 the Corporation purchased 44,100 shares for a total cost of $47,206, which were placed in the treasury. No shares were repurchased during the years ended December 31, 2006, 2005 or 2004.

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Company Performance Graph

The following graph shows a five-year comparison of cumulative total shareholder returns for the Company s common stock, the NASDAQ Market Index, and a Peer Group Index, assuming a base index of $100 at the end of 2001. The cumulative total return for each annual period within the five years presented is measured by dividing (1) the sum of (A) the cumulative amount of dividends for the measurement period, assuming dividend investment, and (B) the difference between share prices at the end and at the beginning of the measurement period by (2) the share price at the beginning of the measurement period.

COMPARE 5-YEAR CUMULATIVE TOTAL RETURN
AMONG RAND CAPITAL, INC.,
NASDAQ MARKET AND PEER GROUP INDEX

ASSUMES $100 INVESTED ON DEC. 31, 2001
ASSUMES DIVIDENDS REINVESTED
FISCAL YEAR ENDING DEC. 31, 2006

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

FISCAL YEAR ENDING

COMPANY/INDEX/MARKET	12/2001	12/2002	12/2003	12/2004	12/2005	12/2006
Rand Capital Corp	100.00	81.10	114.17	122.83	105.51	275.59
Peer Group Index	100.00	74.37	121.46	132.44	131.09	177.41
NASDAQ Market Index	100.00	69.75	104.88	113.70	116.19	128.12

The Peer Group is made up of the following:
Ameritrans Capital Corp (NasdaqCM:AMTC)
Brantley Capital Corp (OTC:BBDC.pk)
Capital Southwest Corp (NasdaqGM:CSWC)
Equus Total Return Inc (NYSE:EQS)
Gladstone Investment CP (NasdaqGS:GAIN)

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Harris & Harris Group (NasdaqGM:TINY)
Macc Private Equities Inc (NasdaqCM:MACC)
MCG Capital Corporation (NasdaqGS:MCGC)
MVC Capital Inc (NYSE:MVC)

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

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

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

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

Balance Sheet Data as of December 31:

	2006	2005	2004	2003	2002
Total assets	$ 29,463,944	$ 16,063,605	$ 12,743,109	$ 9,385,137	$ 9,685,673
Total liabilities	$ 12,681,539	$ 7,447,671	$ 3,716,055	$ 146,649	$ 81,039
Net assets	$ 16,782,405	$ 8,615,934	$ 9,027,054	$ 9,238,488	$ 9,604,634
Net asset value per outstanding share	$ 2.93	$ 1.51	$ 1.58	$ 1.62	$ 1.67
Common stock shares outstanding	5,718,934	5,718,934	5,718,934	5,718,934	5,738,634

Operating Data for the year ended December 31:

	2006	2005	2004	2003	2002
Investment income	$ 1,326,962	$ 736,573	$ 757,704	$ 449,858	$ 261,230
Total expenses	$ 1,519,184	$ 1,265,846	$ 900,812	$ 942,799	$ 858,305
Net investment loss	$ (1,264,802)	$ (175,179)	$ (112,384)	$ (346,043)	$ (738,046)
Net realized gain (loss) on sales and dispositions of investments	$ 3,456,441	$ (382,353)	$ 26,727	$ 87,841	$ 888,399
Net increase (decrease) in unrealized appreciation	$ 5,974,832	$ 146,412	$ (125,777)	$ (86,441)	$ (578,299)
Net increase (decrease) in net assets from operations	$ 8,166,471	$ (411,120)	$ (211,434)	$ (344,643)	$ (427,946)

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

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

Forward Looking Statements

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

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

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.

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

1) a qualified and experienced management team

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

3) a potential for growth in revenue and cash flow

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

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

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

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

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

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

2006 Highlights and Outlook

The Corporation s net asset value increased $1.42 as of December 31, 2006, closing the year at $2.93 per share. The net asset value increased 94%, from $1.51 at December 31, 2005. This was the fourth consecutive quarterly increase in net assets for the Corporation during 2006. At December 31, 2006, the Corporation s total investment portfolio was valued at $23 million, which exceeds its cost basis of $14 million, reflecting $9 million in net unrealized appreciation.

The Corporation s valuation policy provides that valuations may be adjusted for a subsequent equity financing with new investors. In accordance with this policy, during the fourth quarter of 2006, the Corporation recognized unrealized appreciation of $7.76 million on its investment in Innov-X Systems, Inc. (Innov-X) and $2.8 million in unrealized appreciation on its investment in Synacor, Inc. (Synacor). During the year, it also recognized $189,000 in unrealized appreciation in Carolina Skiff LLC (Carolina Skiff) and $452,000 in unrealized depreciation in WineIsIt.com, Corp.

In addition, during 2006 the Corporation recognized a $3.45 gain on the sale of two portfolio securities, liquidating its position in Minrad International, Inc. for a total realized gain of $1.25 million for the year and selling a portion of its

Innov-X shares as part of a new investor financing, recognizing a realized gain of $2.28 million.

The growth in net assets, combined with the realized gains recognized in 2006, resulted in the Corporation s stock surging from trading at a discount to net asset value and a low price of $1.09 in the fourth quarter of 2005 to a high price of $3.55 in the fourth quarter of 2006 which represents a premium to the net asset value.

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During 2006 the Corporation also realized $1,326,962 in total investment income, an increase of $590,000 from the $736,573 of investment income in 2005. The 80% increase is attributable to growth in dividends and interest from portfolio companies, primarily occurring during the third and fourth quarters of 2006

Dividend and other investment income grew primarily because of higher Limited Liability Corporation (LLC) distributions from companies in the portfolio that have improving operational trends, in particular Gemcor II, LLC (Gemcor), Topps Meat Company LLC (Topps), and Carolina Skiff. Gemcor designs and sells automatic riveting machines to manufacturers of airframes, missile bodies, space system accessories, and other aerospace equipment. Topps is a 66 year old manufacturer and supplier of premium frozen meat products. Carolina Skiff is a leading manufacturer of affordable fishing and recreational boats. LLC dividends can fluctuate based on portfolio companies profitability and the timing of distributions.

Also during 2006 certain portfolio companies repaid some or all of their outstanding debenture instruments, including: Innov-X, Synacor, Concentrix Corporation, Ramsco, New Monarch Machine Tool, Inc., Gemcor and APF Group, Inc.. These repayments will impact future earnings by reducing interest income in 2007 and future periods.

The cash balance at December 31, 2006 was $4.3 million which was $3.1 million higher than at the end of 2005. The increase was primarily due to portfolio investment repayments and loan repayments. In addition, the Corporation has $1.9 million of outstanding leverage available from the Small Business Administration (SBA) for future investment. The cash availability will provide sufficient liquidity to fund the Corporation s deal flow in 2007.

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

Critical Accounting Policies

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

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

Valuation of Investments

The most significant estimate inherent in the preparation of the Corporation s consolidated financial statements is the valuation of its investments and the related unrealized appreciation or depreciation. The Corporation has adopted the SBA s valuation guidelines for SBICs, which describe the policies and procedures used in valuing investments.

Investments are valued in accordance with the Corporation s established valuation policy and are stated at fair value as determined in good faith by the management of the Corporation and submitted to the Board of Directors for approval. There is no single standard for determining fair value in good faith. As a result, determining fair value requires that judgment be applied to the specific facts and circumstances of each portfolio investment while employing a consistently applied valuation process for investments. The Board of Directors considers fair value to be the amount which the Corporation may reasonably expect to receive for portfolio securities when sold on the valuation date. The Corporation analyzes and values each individual investment on a quarterly basis, and records unrealized depreciation for an investment that it believes has become impaired, including where collection of a loan or realization of an equity security is doubtful. Conversely, the Corporation will record unrealized appreciation if it believes that the underlying portfolio company has appreciated in value and, therefore, its equity security has also

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appreciated in value. These estimated fair values may differ from the values that would have been used had a ready market for the investments existed and these differences could be material if our assumptions and judgments differ from results of actual liquidation events.

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

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

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

Revenue Recognition (Interest Income)

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

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

Recent Accounting Pronouncements

In June 2006 the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* . This Interpretation clarifies that management is expected to evaluate an income tax position taken or expected to be taken for the likelihood of realization before recording any amounts for such position in the financial statements. FIN 48 also requires expanded disclosure with respect to income tax positions taken that are not certain to be realized. This Interpretation is effective for fiscal years beginning after December 15, 2006, and will require management to evaluate every open tax position that exists in every jurisdiction on the date of initial adoption. Certain disclosures are required in Form 10-Q in the period of adoption of FIN 48 which would be the March 31, 2007 Form 10-Q.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements.* SFAS No. 157 defines fair value, establishes a framework for measuring fair value and requires enhanced disclosures about fair value measurements. SFAS No. 157 requires companies to disclose the fair value of their financial instruments according to a fair value hierarchy as defined in the standard. Additionally, companies are required to provide enhanced disclosure regarding financial instruments in one of the categories (level 3), including a reconciliation of the beginning and ending balances separately for each major category of assets and liabilities. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The adoption of SFAS No. 157 will have an impact on the Company s consolidated financial statements from a disclosure standpoint.

In September 2006, the SEC issued Staff Accounting Bulletin No. 108, *Considering the Effects of Prior Year Misstatements When Quantifying Misstatements in Current Year Financial Statements* . Due to diversity in practice

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among registrants, SAB 108 expresses SEC staff views regarding the process by which misstatements in financial statements are evaluated for purposes of determining whether financial statement restatement is necessary. SAB 108 is effective for fiscal years ending after November 15, 2006. The adoption of SAB 108 did not have an impact on the Company s consolidated financial statements.

Financial Condition

Overview:

	12/31/06	12/31/05	Increase	% Increase
Total assets	$ 29,463,944	$ 16,063,605	$ 13,400,339	83.4%
Total liabilities	12,681,539	7,447,671	5,233,868	70.3%
Net assets	$ 16,782,405	$ 8,615,934	$ 8,166,471	94.8%

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

	12/31/06	12/31/05	Increase	% Increase
Investments, at cost	$ 14,033,789	$ 13,712,890	$ 320,899	2.3%
Unrealized appreciation (depreciation), net	9,616,025	(342,028)	9,958,053	2,911.5%
Investments at fair value	$ 23,649,814	$ 13,370,862	$ 10,278,952	76.9%

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

	Amount
<u>**New Investments**</u>	
Innov-X Systems, Inc. (Innov-X)	$ 1,055,148
Adampluseve, LLC (Adam+Eve)	561,000
Synacor Inc. (Synacor)	507,999
Niagara Dispensing Technologies, Inc. (Niagara Dispensing)	500,000
New Monarch Machine Tool, Inc. (Monarch)	300,000
Kionix, Inc (Kionix)	243,704
Rocket Broadband Networks, Inc (Rocket Broadband)	195,918
WineIsIt.com, Corp. (Wineisit)	20,000
Total of investments made during the year ended December 31, 2006	$ 3,383,769

Other Changes:	
Synacor interest conversion	$ 21,479
Photonic Products Group, Inc. (Photonics) interest conversion	10,000
Adam+Eve warrant amortization	5,667
Monarch interest conversion	2,877
Total of other changes	40,023
Total of new investments and other changes during the year ended December 31, 2006	$ 3,423,792

Sales/Investment Repayments	Amount
Minrad International, Inc. (Minrad)	$ (919,422)
Innov-X	(690,148)
Concentrix Corporation (Concentrix)	(600,000)
Synacor	(350,000)
Vanguard Modular Building Systems (Vanguard)	(270,000)
Monarch	(135,214)
RAMSCO	(97,519)
Gemcor II, LLC (Gemcor)	(27,067)
APF Group, Inc. (APF)	(8,106)
Takeform, Inc. (Takeform)	(5,417)
Total of sales or investment repayments during the year ended December 31, 2006	$ (3,102,893)
Total change in investment balance, at cost during the year ended December 31, 2006	$ 320,899

The Corporation borrowed $900,000 in leverage from the SBA during the year ended December 31, 2006 and the total owed to the SBA for Leverage Payable at December 31, 2006 was $8,100,000. These debentures bear a fixed interest rate and an annual fee, averaging 5.9%, payable semi-annually. The debenture principal is repayable in full 10 years from issuance.

Net asset value per share (NAV) was $2.93 per share at December 31, 2006 versus $1.51 per 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 141% of net assets at December 31, 2006 and 155% of net assets at December 31, 2005.

Cash and cash equivalents approximated 26% of net assets at December 31, 2006 compared to 14% at December 31, 2005.

The effect of the realized gains and the change in unrealized appreciation on investments resulted in a net change in the net deferred tax (liability) asset from an $846,000 deferred tax asset at December 31, 2005 to a net deferred tax liability of $(3,808,000) at December 31, 2006.

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 held at high grade financial institutions.

Comparison of the years ended December 31, 2006 and 2005

	December 31, 2006	December 31, 2005	Increase	% Increase
Interest from portfolio companies	$ 757,824	$ 593,125	$ 164,699	27.8%
Interest from other investments	53,104	3,601	49,503	1374.7%
Dividend and other investment income	432,296	94,930	337,366	355.4%
Other income	83,738	44,917	38,821	86.4%
Total investment income	$ 1,326,962	$ 736,573	$ 590,389	80.2%

<u>*Interest from portfolio companies*</u> The increase in portfolio interest income is attributable to the fact that there has been an increase in the number of investments that provide the Corporation with current income. The blended rate of the debenture investments originated out of the Corporation during the last two fiscal years is approximately 10.7%.

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
Contract Staffing	5%	141,400	2006
G-Tec	8%	400,000	2004
WineIsIt.com	10%	801,918	2005

<u>*Interest from other investments*</u> The increase in interest income is primarily due to higher cash balances and higher yields on these cash balances. The higher cash balances are a result of portfolio investment repayments and sales of portfolio companies equity instruments and draw downs on the SBA leverage.

<u>*Dividend and other investment income*</u> Dividend income is comprised of distributions from Limited Liability Companies (LLC s) in which the Corporation has invested. The Corporation s investment agreements with certain LLC companies require the entities to distribute funds to the Corporation for payment of income taxes on its allocable share of the entities profits. These dividends will fluctuate based upon the profitability of the entities and the timing of the distributions. Dividend income for the year ended December 31, 2006 consisted of distributions from Gemcor II, LLC (Gemcor) for $375,372, Topps for $37,334, Carolina Skiff LLC (Carolina Skiff) for $18,416 and Vanguard Modular Building Systems (Vanguard) for $1,174.

Dividend income for the year ended December 31, 2005 consisted of distributions from Gemcor for $51,500, Topps for $28,174, Carolina Skiff for $14,082 and Vanguard for $1,174.

<u>*Other income*</u> Other income consists of the revenue associated with the amortization of financing fees charged to the portfolio companies upon successful closing of Rand SBIC financing. The SBA regulations limit the amount of fees that can be charged to a portfolio company, and the Corporation typically charges 1% to 3% to the portfolio concerns.

These fees are amortized ratably over the life of the instrument associated with the fees. The unamortized fees are carried on the balance sheet under Deferred revenue . In addition, other income includes fees charged by the Corporation to its portfolio companies for attendance at the portfolio companies board meetings.

The increase in other income is due to the fact that two of the Corporation s portfolio companies, Concentrix and Innov-X, paid off their debenture instruments early and therefore the remaining unamortized closing fees of $12,000 from Concentrix and $6,800 from Innov-X were brought into income. In addition, the Corporation charged Concentrix an $18,000 prepayment penalty fee that was included in other income. The annualized financing fee income based on the existing portfolio will average $20,000 annually in 2007 and less than $11,000 annually thereafter, based on the deferred revenue balance at December 31, 2006. In addition the board attendance income amounted to $9,000 for the year ended December 31, 2006 and $7,000 for year ended December 31, 2005.

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Comparison of the years ended December 31, 2005 and 2004

	December 31, 2005	December 31, 2004	Increase (Decrease)	% Increase (Decrease)
Interest from portfolio companies	$ 593,125	$ 645,206	$ (52,081)	(8.1)%
Interest from other investments	3,601	2,581	1,020	39.5%
Dividend and other investment income	94,930	64,823	30,107	46.4%
Other income	44,917	45,094	(177)	(0.4)%
Total investment income	$ 736,573	$ 757,704	$ (21,131)	(2.8)%

Interest from portfolio companies Portfolio interest income decreased $52,081 for the year ended December 31, 2005 as compared to the same period in the prior year. This is attributable to the fact that the Corporation ceased accruing interest on two WineIsIt.com (Wineisit) debt instruments in January 2005 in anticipation of a restructuring of the Wineisit balance sheet. The total interest recognized from these two Wineisit notes for the year ended December 31, 2004 was $73,009. During 2005 this portfolio company experienced a decline in business performance and therefore the restructuring has been delayed. These two notes are technically in default due to nonpayment of principal and interest and the Corporation has revised their valuation. See further discussion on this valuation change in the section labeled Net Change in Unrealized Appreciation/Depreciation of Investments .

The current period decrease in portfolio income can also be attributed to the fact that the portfolio income for the year ended December 31, 2004 included $62,703 of income on a $900,000 convertible note from Somerset. This note had stopped accruing interest in September 2003 because it was in default and the Corporation had established a 100% reserve for the total accrued interest of $122,914. In April 2004 Somerset became current on the note, therefore the Corporation recognized all past due interest in the first quarter of 2004.

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

Dividend and other investment income Dividend income for the year ended December 31, 2005 consisted of distributions from Gemcor for $51,500, Topps for $28,174, Carolina Skiff for $14,082 and Vanguard for $1,174.

Dividend income for the year ended December 31, 2004 was comprised of distributions from Topps for $35,195, Carolina Skiff for $28,384 and Vanguard for $1,244.

Other income Other income for the year ended December 31, 2005 decreased slightly. The decrease in financing amortization revenue can be attributed to the fact that several fees became fully amortized in early 2005 due to the instrument maturing. The annualized financing fee income based on the existing portfolio will average $29,000 annually in 2006 and 2007 and less than $10,000 annually thereafter, based on the deferred revenue balance at December 31, 2005. In addition the board attendance income amounted to $7,000 for the year ended December 31, 2005 and $0 for year ended December 31, 2004.

Operating Expenses

Comparison of the years ended December 31, 2006 and 2005

	December 31, 2006	December 31, 2005	Increase	% Increase
Total expenses	$ 1,519,184	$ 1,265,846	$ 253,338	20.0%

Operating expenses predominately consist of interest expense on SBA debentures, employee compensation and benefits, directors fees, shareholder related costs, office expenses, professional fees, and expenses related to identifying and reviewing investment opportunities. The increase in operating expenses during the year ended December 31, 2006 can be primarily attributed to the 70.4% or $195,239 increase in SBA interest expense. The SBA interest expense was $472,526 for the year ended December 31, 2006 and $277,287 for the year ended December 31, 2005. The Corporation has borrowed $8,100,000 from the SBA as of December 31, 2006 at an average borrowing rate, including surcharges, of approximately 5.9%. Interest costs will continue to increase in 2007 and beyond as the

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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, salary expense grew 20.4% or $81,727 from $400,340 for the year ended December 31, 2005 to $482,067 for the year ended December 31, 2006. This increase is due to the officer pay increases and the fact that the executive officer bonuses increased by $50,000 in 2006. Professional fees were $116,068 and $96,917 for the years ended December 31, 2006 and 2005, respectively. This represents an increase of 20% which can be attributed to the escalating legal, audit and tax costs due to the increasingly more complex regulatory environment in which the Corporation operates.

Comparison of the years ended December 31, 2005 and 2004

	December 31, 2005	December 31, 2004	Increase	% Increase
Total expenses	$ 1,265,846	$ 900,812	$ 365,034	40.5%

Operating expenses increased $365,034 or 40.5% during the year ended December 31, 2005 as compared to the same period in the prior year. The increase in operating expenses can mainly be attributed to the establishment of a bad debt reserve for $114,870 on Vanguard, and a 158.2% increase in SBA interest expense.

The Corporation s management reviewed the interest receivable from Vanguard and believed that the collectibilty of this receivable was in doubt and therefore reserved for all of the receivable balance. The portfolio company continued to perform well and was then investigating sale opportunities. The Corporation ceased accruing interest revenue on this instrument in 2003.

The SBA borrowings increased $3,700,000 during the year ended December 31, 2005 and the SBA interest expense increased $169,880 from $107,407 for the year ended December 31, 2004 to $277,287 for the year ended December 31, 2005. The SBA borrowing rates, which included an SBA annual charge, averaged 5.8% in 2005. The SBA annual charge during 2005 decreased from 0.887% to 0.855%. The 2004 SBA borrowing rates averaged 5.4% and the overall combined SBA borrowing rate on the $7,200,000 outstanding leverage at December 31, 2004 was 5.6%. 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.

Increases in salaries and professional costs contributed to the remaining increase in operating expense during the year ended December 31, 2005. Professional fees increased $33,323 or 52.4% during the year ended December 31, 2005 due to the additional accounting and legal expenses related to the increasingly more complex regulatory environment in which the Corporation operates.

Net Realized Gains and Losses on Investments

Comparison of the years ended December 31, 2006 and 2005

	December 31, 2006	December 31, 2005	Increase	% Increase

Net Realized Gain (Loss)	$ 3,456,441	$ (382,353)	$ 3,838,794	1,004.0%

During the year ended December 31, 2006, the Corporation sold a portion of its shares in Innov-X and recognized a realized gain of $2,280,682 on the sale. A portion of the proceeds from the sale of Innov-X is an escrow receivable in the amount of $711,249 which is expected to be collected in early 2008. This escrow receivable is included in the other asset line on the financial statements.

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

During the year ended December 31, 2005, the Corporation recognized a realized loss of ($382,353) on its investment in D Lisi Food Systems, Inc. (D Lisi).

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Comparison of the years ended December 31, 2005 and 2004

	December 31, 2005	December 31, 2004	Decrease	% Decrease
Net Realized (Loss) Gain	$ (382,353)	$ 26,727	$ 3,838,794	1,530.6%

During the year ended December 31, 2005, the Corporation realized a loss of ($382,353) on its investment in D Lisi. The D Lisi investment of $400,000 was written down to zero in the third quarter of 2004 due to the fact that it filed for bankruptcy protection on August 13, 2004. The final bankruptcy proceeds were distributed in July 2005 and resulted in a realized loss of ($382,353).

During the year ended December 31, 2004, the Corporation realized a $32,956 gain on the sale of the remaining Advanced Digital Information Corporation (ADIC) stock. In addition, the Corporation realized a ($6,229) loss on its investment in Clearview Cable.

Net Change in Unrealized Appreciation/(Depreciation) of Investments

For the years ended December 31, 2006 and 2005

	December 31, 2006	December 31, 2005	Increase	% Increase
Net Change in Unrealized Appreciation (Depreciation)	$ 9,958,053	$ 244,020	$ 9,714,033	3,980.8%

The Corporation recorded a net increase in unrealized appreciation on investments of $9,958,053 during the year ended December 31, 2006, as compared to an increase of $244,020 during the year ended December 31, 2005. The increase in unrealized appreciation (depreciation) on investments of $9,958,053 is due to the following valuation changes made by the Corporation:

	December 31, 2006
Increase Innov-X valuation	$ 7,761,700
Increase Synacor valuation	2,809,849
Increase Carolina Skiff valuation	189,000
Vanguard Sale	135,000
Decrease G-Tec valuation	(102,000)
Decrease USTec valuation	(164,000)
Remove Minrad unrealized appreciation	(199,578)
Decrease Wineisit valuation	(471,918)
Total Change in net Unrealized Appreciation during the year ended December 31, 2006	$ 9,958,053

In accordance with its valuation policy, the Corporation increased the value of its holdings in Innov-X and Synacor based on significant equity financings at higher valuations by new non-strategic outside investors for each of these portfolio companies.

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

The Corporation liquidated its holdings in Minrad and Vanguard during 2006 and therefore any unrealized appreciation (depreciation) was reclassified to a realized gain (loss).

The WineIsIt and G-Tec investments were revalued during the year ended December 31, 2006 after a review by the Corporation s management which identified that the business of each of these portfolio companies had

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deteriorated since the time of the original funding, as compared to their original plan. The portfolio companies remain in operation and are developing new business strategies.

The USTec valuation was based on a subsequent event that occurred in January 2007 where the portfolio company was sold and the Corporation recognized a loss.

For the years ended December 31, 2005 and 2004

	December 31, 2005	December 31, 2004	Increase	% Increase
Net Change in Unrealized Appreciation (Depreciation)	$ 244,020	$ (206,737)	$ 450,737	218.0%

The Corporation recorded a decrease in unrealized depreciation on investments before income tax expense of $244,020 during the year ended December 31, 2005, as compared to an increase of $(206,737) during the year ended December 31, 2004. The decrease in unrealized depreciation on investments during the year ended December 31, 2005 is due to the following valuation changes made by the Corporation:

	December 31, 2005
Reclass D Lisi unrealized loss to realized loss	$ 400,000
Increase Topps valuation	332,000
Increase Minrad valuation	272,000
Increase Carolina Skiff valuation	38,000
Decrease Kionix valuation	(284,477)
Decrease Wineisit valuation	(250,000)
Decrease Vanguard valuation	(135,000)
Decrease Ultra-Scan valuation	(73,174)
Decrease Somerset Gas valuation	(50,349)
Decrease Photonics valuation	(4,980)
Total Change in net Unrealized Appreciation during the year ended December 31, 2005	$ 244,020

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

The Corporation recognized appreciation of $272,000 on its 667,981 shares of Minrad. Minrad is traded under the symbol BUF on the Amex stock exchange. The Corporation s Minrad shares were restricted under SEC Rule 144. During the year ended December 31, 2005, Minrad s securities traded between $1.25 and $7.00 per share. The Corporation s policy is to record the valuation of our publicly held securities on a mark to market basis. The Minrad s shares were therefore valued at $1.65 per share at December 31, 2005, which was the average closing price for the last three trading days of the year.

Kionix was revalued during the second quarter of 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.

The WineIsIt investment was revalued during the year ended December 31, 2005 after a review by management which identified that Wineisit s business had deteriorated since the time of the original funding, as compared to their original plan.

The Corporation s investment in Vanguard was written down to $135,000 during the year ended December 31, 2005 based on a financial review of the portfolio company.

The Ultrascan and Somerset investment valuations were adjusted based on recent rounds of financing that lowered the per share prices.

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

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

Net Increase (decrease) in Net Assets from Operations

The Corporation accounts for its operations 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. During the year ended December 31, 2006, the net increase was $8,166,471, as compared to net decreases in net assets from operations of ($411,120) in 2005 and ($211,434) in 2004.

The net increase in net assets from operations for the year ended December 31, 2006 is due to the $9,431,273 net realized and unrealized gain on investments. The net decrease in net assets from operations in 2005 can primarily be attributed to the net investment loss of ($175,179), a realized loss on investments of ($382,353) and an unrealized gain on investments after tax of 146,412. The 2004 decrease is primarily due to the net investment loss of ($112,384) and the increase in unrealized depreciation after tax of ($125,777).

Liquidity and Capital Resources

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

As of December 31, 2006, the Corporation s total liquidity, consisting of cash and cash equivalents, was $4,299,852.

Net cash used in operating activities has averaged approximately $345,000 over the last three years and management anticipates cash will continue to be utilized at similar levels. The cash flow may fluctuate based on possible expenses associated with compliance with new regulations.

The Corporation realized approximately $2,500,000 in net cash flow from investing activities in fiscal 2006. The Corporation has experienced an average net use of cash in the investing activities of approximately $3 million over the two years prior. The Corporation will generally use cash in investing activities as it builds its portfolio utilizing its available SBA financing and proceeds from prior liquidations of portfolio investments. The Corporation anticipates that it will continue to make new investments and may experience a net use of cash over the next two years. In addition, significant liquidating events within the Corporation s investment portfolio are difficult to determine with any certainty.

As of December 31, 2006 the Corporation had paid $100,000 to the SBA to reserve its approved $10,000,000 leverage. The leverage commitment expires on September 30, 2008. The Corporation has drawn down $8,100,000 of this leverage as of December 31, 2006. Management expects that it will not be necessary to draw down the SBA leverage in 2007, and the large cash balance and expected investment payoffs will be adequate to fund new investments and operating activities. It is anticipated that the remaining $1,900,000 in SBA leverage will be drawn down in fiscal year 2008 prior to the expiration of the commitment and will be available to fund operations and new investments.

Management believes that the cash and cash equivalents at December 31, 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 over the next twelve months.

The following table summarizes the cash to be received over the next five years from portfolio companies based on contractual obligations as of December 31, 2006. These payments represent scheduled principal and interest payments that are contained in the investment documents of each portfolio company.

	Cash Receipts due by year				
	2007	2008	2009	2010	2011 and beyond
Scheduled Cash Receipts from Portfolio Companies	$ 2,300,000	$ 655,000	$ 675,000	$ 2,700,000	$ 576,000

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

Disclosure of Contractual Obligations

The following table shows the Corporation s contractual obligations at December 31, 2006. The Corporation does not have any capital lease obligations or other long-term liabilities reflected on its balance sheet.

	Payments due by period				
	Total	Less than 1 Year	1-3 Years	4-5 Years	More than 5 yrs
SBA Debentures	$ 8,100,000	$ 0	$ 0	$ 0	$ 8,100,000
Operating Lease Obligations (Rent of office space)	$ 63,600	$ 15,360	$ 48,240	$ 0	$ 0
Total	$ 8,163,600	$ 15,360	$ 48,240	$ 0	$ 8,100,000

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

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

At times a portion of the Corporation s portfolio may include marketable securities traded in the over-the-counter market. In addition, there may be a portion of the Corporation s portfolio for which no regular trading market exists. In order to realize the full value of a security, the market must trade in an orderly fashion or a willing purchaser must be available when a sale is to be made. Should an economic or other event occur that would not allow 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 December 31, 2006, the Corporation did not have any off-balance sheet investments or hedging investments.

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Item 8. *Financial Statements and Supplementary Data*

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

Statements of Financial Position as of December 31, 2006 and 2005

Statements of Operations for the three years in the period ended December 31, 2006

Statements of Changes in Net Assets for the three years in the period ended December 31, 2006

Statements of Cash Flows for the three years in the period ended December 31, 2006

Schedule of Portfolio Investments as of December 31, 2006

Schedules of Selected Per Share Data and Ratios for the five years in the period ended December 31, 2006

Notes to the Consolidated Financial Statements

Supplemental Schedule of Consolidated Changes in Investments at Cost and Realized Gain for the year ended December 31, 2006

Report of Independent Registered Public Accounting Firm

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RAND CAPITAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
December 31,

	2006	2005
Assets		
Investments at fair value (identified cost: 2006 $14,033,789; 2005 $13,712,890)	**$ 23,649,814**	$ 13,370,862
Cash and cash equivalents	**4,299,852**	1,209,839
Interest receivable (net of allowance: 2006 $122,000; 2005 $236,870)	**507,242**	297,619
Deferred tax asset		846,000
Income tax receivable		15,582
Other assets	**1,007,036**	323,703
Total assets	**$ 29,463,944**	$ 16,063,605
Liabilities and Stockholders Equity (net assets)		
Liabilities:		
Debentures guaranteed by the SBA	**$ 8,100,000**	$ 7,200,000
Deferred tax liability	**3,808,000**	
Income tax payable	**410,575**	
Accounts payable and accrued expenses	**317,359**	167,788
Deferred revenue	**45,605**	79,883
Total liabilities	**12,681,539**	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)	**(6,253,128)**	(4,988,326)
Undistributed net realized gain on investments	**9,763,366**	6,306,925
Net unrealized appreciation (depreciation) on investments	**5,769,615**	(205,217)
Treasury stock, at cost, 44,100 shares	**(47,206)**	(47,206)
Net assets (per share 2006 $2.93, 2005 $1.51)	**16,782,405**	8,615,934
Total liabilities and stockholders equity (net assets)	**$ 29,463,944**	$ 16,063,605

See accompanying notes

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RAND CAPITAL CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
For The Years Ended December 31, 2006, 2005 and 2004

	2006	2005	2004
Investment income:			
Interest from portfolio companies	**$ 757,824**	$ 593,125	$ 645,206
Interest from other investments	**53,104**	3,601	2,581
Dividend and other investment income	**432,296**	94,930	64,823
Other income	**83,738**	44,917	45,094
	1,326,962	736,573	757,704
Operating expenses:			
Salaries	**482,067**	400,340	380,154
Employee benefits	**101,785**	99,569	85,200
Directors fees	**59,500**	54,200	45,100
Professional fees	**116,068**	96,917	63,594
Stockholders and office operating	**108,687**	115,386	116,032
Insurance	**43,674**	46,017	46,062
Corporate development	**54,233**	51,875	44,723
Other operating	**10,769**	9,385	13,454
	976,783	873,689	794,319
Interest on SBA obligations	**472,526**	277,287	107,407
Bad debt expense (recovery)	**69,875**	114,870	(914)
Total expenses	**1,519,184**	1,265,846	900,812
Investment (loss) before income taxes	**(192,222)**	(529,273)	(143,108)
Current income tax expense	**401,801**	23,514	24,316
Deferred income tax expense (benefit)	**670,779**	(377,608)	(55,040)
Net investment (loss)	**(1,264,802)**	(175,179)	(112,384)
Realized and unrealized gain (loss) on investments:			
Net realized gain (loss) on sales and dispositions	**3,456,441**	(382,353)	26,727
Unrealized appreciation (depreciation) on investments:			
Beginning of year	**(342,028)**	(586,048)	(379,737)
End of year	**9,616,025**	(342,028)	(586,048)
Change in unrealized appreciation (depreciation) before income taxes	**9,958,053**	244,020	(206,737)
Deferred income tax expense (benefit)	**3,983,221**	97,608	(80,960)
Net increase (decrease) in unrealized appreciation	**5,974,832**	146,412	(125,777)

Net realized and unrealized gain (loss) on investments		**9,431,273**		(235,941)		(99,050)
Net increase (decrease) in net assets from operations	**$**	**8,166,471**	$	(411,120)	$	(211,434)
Weighted average shares outstanding		5,718,934		5,718,934		5,718,934
Basic and diluted net increase (decrease) in net assets from operations per share	$	1.43	$	(0.07)	$	(0.04)

See accompanying notes

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RAND CAPITAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS
For The Years Ended December 31, 2006, 2005 and 2004

	2006	2005	2004
Net assets at beginning of period	**$ 8,615,934**	$ 9,027,054	$ 9,238,488
Net investment (loss)	**(1,264,802)**	(175,179)	(112,384)
Net realized gain (loss) on sales and dispositions of investments	**3,456,441**	(382,353)	26,727
Net increase (decrease) in unrealized appreciation	**5,974,832**	146,412	(125,777)
Net increase (decrease) in net assets from operations	**8,166,471**	(411,120)	(211,434)
Net assets at end of period	**$ 16,782,405**	**$ 8,615,934**	**$ 9,027,054**

See accompanying notes.

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RAND CAPITAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
For The Years Ended December 31, 2006, 2005 and 2004

	2006	2005	2004
Cash flows from operating activities:			
Net increase (decrease) in net assets from operations	**$ 8,166,471**	$ (411,120)	$ (211,434)
Adjustments to reconcile net increase (decrease) in net assets to net cash used in operating activities:			
Depreciation and amortization	**26,672**	23,297	14,890
Change in interest receivable allowance		114,870	(914)
(Increase) decrease in unrealized appreciation of investments	**(9,958,053)**	(244,020)	206,737
Deferred tax expense (benefit)	**4,654,000**	(280,000)	(136,000)
Net realized (gain) loss on portfolio investments	**(3,456,441)**	382,353	(26,727)
Non-cash conversion of debenture interest	**(34,356)**	(30,852)	(138,319)
Changes in operating assets and liabilities:			
(Increase) decrease in interest receivable	**(209,623)**	(151,999)	75,158
Decrease (increase) in other assets	**42,440**	(48,207)	(29,504)
Increase in accounts payable and accrued liabilities	**560,246**	34,891	33,001
(Decrease) increase in deferred revenue	**(34,278)**	(3,275)	36,405
Total adjustments	**(8,409,393)**	(202,942)	34,727
Net cash used in operating activities	**(242,922)**	(614,062)	(176,707)
Cash flows from investing activities:			
Investments originated	**(3,383,769)**	(2,605,260)	(4,464,000)
Proceeds from sale of portfolio investments	**4,374,762**	17,647	86,813
Proceeds from loan repayments	**1,473,322**	181,271	572,824
Capital expenditures	**(12,255)**	(4,001)	(6,232)
Net cash provided by (used in) investing activities	**2,452,060**	(2,410,343)	(3,810,595)
Cash flows from financing activities:			
Proceeds from SBA debenture	**900,000**	3,700,000	3,500,000
Origination costs to SBA	**(19,125)**	(92,500)	(87,500)
Purchase of SBA commitment			(50,000)
Net cash provided by financing activities	**880,875**	3,607,500	3,362,500
Net increase (decrease) in cash and cash equivalents	**3,090,013**	583,095	(624,802)
Cash and cash equivalents:			
Beginning of year	**1,209,839**	626,744	1,251,546
End of year	**$ 4,299,852**	$ 1,209,839	$ 626,744

See accompanying notes

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RAND CAPITAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED SCHEDULE OF PORTFOLIO INVESTMENTS
December 31, 2006

Company and Business	Type of Investment	(b) Date Acquired	(c) Equity	Cost	(d) Value	Per Share of Rand
Adampluseve, LLC (g) New York, NY. Luxury sports wear company for men and women. www.adampluseve.com	$561,000 Senior Subordinated note at 10% due July 14, 2011. Warrants to purchase approximately 2.5% of Company.	7/14/06	3%	$ 566,667	$ 566,667	.10
APF Group, Inc. (e) (g) (h) 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	$584,328 Consolidated Senior Subordinated note at 12.74% due June 30, 2011. Warrants to purchase 10.2941 shares of common stock.	7/8/04	6%	586,488	586,488	.10
Carolina Skiff LLC (e) (g) 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	1,227,000	.21
Contract Staffing 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
EmergingMed.com, Inc. (g) New York, NY. Cancer clinical trial matching and referral service. www.emergingmed.com	$500,000 Senior subordinated note at 10% due December 19, 2010. Warrants to purchase 5% of the Company.	12/19/05	5%	500,000	500,000	.09
Gemcor II, LLC (e) (g) (h) West Seneca, NY. Designs and sells automatic riveting	$250,000 Subordinated note at 8% due June 28, 2010	6/28/04	31%	722,933	722,933	.13

machines used in the assembly of aircraft components. www.gemcor.com	with warrant to purchase 6.25 membership units. 25 membership units.					
G-TEC Natural Gas Systems Buffalo, NY. Manufactures and distributes systems that allow natural gas to be used as an alternative fuel to gases. www.gas-tec.com	33.057% Class A membership interest. 8% cumulative dividend.	8/31/99	33%	400,000	198,000	.03
Innov-X Systems, Inc. (e) (g) Woburn, MA. Manufactures portable x-ray fluorescence (XRF) analyzers used in metals/alloy analysis. www.innovxsys.com	2,642 Series A Convertible Preferred stock. Warrants for 21,596 common shares.	9/27/04	9%	1,000,000	8,761,700	1.53

RAND CAPITAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED SCHEDULE OF PORTFOLIO INVESTMENTS
December 31, 2006 (Continued)

Company and Business	Type of Investment	(b) Date Acquired	(c) Equity	Cost	(d) Value	Per Share of Rand
Kionix, Inc. Ithaca, NY. Develops innovative MEMS based technology applications. www.kionix.com	30,241 shares Series B preferred stock. 696,296 shares Series C preferred stock. (g) 2,862,091 shares Series A preferred stock. 714,285 shares Series B preferred stock.	5/17/02	2%	1,506,044	1,221,567	.21
New Monarch Machine Tool, Inc. (e) (g) (h) 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	11%	692,662	692,662	.12
Niagara Dispensing Technologies, Inc. (g) 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
Photonic Products Group, Inc (OTC:PHPG.OB) (a) (i) (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	133,220	.02
RAMSCO (e) (g) (h) Albany, NY. Distributor of water, sanitary, storm sewer and specialty construction materials to the contractor, highway and municipal	$916,947.23 notes at 13% due November 18, 2007. Warrants to purchase 12.5% of common shares.	11/19/02	13%	819,428	819,428	.14

construction markets. www.ramsco.com						
Rocket Broadband Networks, Inc. (g) Rochester, NY. Communications service provider of satellite TV, broadband internet and VoIP digital phone targeting multiple dwelling units. www.rocketbroadband.com	533,827 Series A Preferred shares.	12/20/05	8%	400,000	400,000	.07
Somerset Gas Transmission Company, LLC Columbus, OH. Natural gas transportation company. www.somersetgas.com	26.5337 Units.	7/10/02	2%	719,097	786,748	.14

RAND CAPITAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED SCHEDULE OF PORTFOLIO INVESTMENTS
December 31, 2006 (Continued)

Company and Business	Type of Investment	(b) Date Acquired	(c) Equity	Cost	(d) Value	Per Share of Rand
Synacor Inc. (e) (g) Buffalo, NY. Develops provisioning platforms for aggregation and delivery of content for broadband access providers. www.synacor.com	200,000 shares of Series B preferred stock. 78,186 Series A preferred shares. 80,126 Series C preferred shares. Warrants for 299,146 common shares.	11/18/02	4%	999,478	3,818,000	.67
Topps Meat Company LLC (e) (g) 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
Ultra Scan Corporation Amherst, NY. Biometrics application developer of ultrasonic fingerprint technology. www.ultra-scan.com	536,596 common shares, 107,104 Series A-1 preferred shares. (g) 95,284 Series A-1 preferred shares.	12/11/92	4%	938,164	1,203,000	.21
UStec, Inc. 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. (g) $350,000 Senior Subordinated Convertible Debentures at 6% due February 2, 2008.	6/26/98	<1%	450,500	311,000	.06
WineIsIt.com, Corp. (e) Amherst, NY. Marketing company specializing in customer loyalty programs supporting the wine and	$20,000 note at 12% due April 26, 2007. (g) $500,000 Senior Subordinated note at 10% due December	12/18/02	2%	821,918	100,000	.02

spirit industry. www.wineisit.com	17, 2009. $250,000 note at 10% due April 16, 2005. Warrants to purchase 100,000 shares Class B common stock.				
Other Investments	Other	Various	519,010	33,001	.02
	Total portfolio investments		$ 14,033,789	$ 23,649,814	$ 4.14

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RAND CAPITAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED SCHEDULE OF PORTFOLIO INVESTMENTS
December 31, 2006 (Continued)
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 December 31, 2006 restricted securities represented 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 Corporation holds an equity interest of less than one percent.

(d) The Corporation has adopted the SBA s valuation guidelines for SBIC s, which describe the policies and procedures used in valuing investments. These valuation guidelines are similar to the accounting principals generally accepted in the United States of America. 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 that 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 December 31, 2006, the aggregate cost of investment securities approximated $14.0 million. Net unrealized appreciation aggregated approximately $9.6 million of which $11.5 million related to appreciated investment securities and $1.9 million related to depreciated investment securities.

(g) Rand Capital SBIC, L.P. investment.

(h) Reduction in cost and value reflects current principal repayment.

(i) Publicly owned company.

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RAND CAPITAL CORPORATION AND SUBSIDIARIES

SCHEDULES OF SELECTED PER SHARE DATA AND RATIOS
For the Five Years Ended December 31, 2006, 2005, 2004, 2003 and 2002

Selected data for each share of capital stock outstanding throughout the five most current years is as follows:

	Year Ended December 31,				
	2006	**2005**	**2004**	**2003**	**2002**
Income from investment operations(1):					
Investment income	$ 0.23	$ 0.13	$ 0.13	$ 0.08	$ 0.05
Expenses	0.26	0.22	0.16	0.16	0.15
Investment (loss) before income taxes	(0.03)	(0.09)	(0.03)	(0.08)	(0.10)
Income tax expense (benefit)	0.19	(0.06)	(0.01)	(0.03)	0.03
Net investment (loss)	(0.22)	(0.03)	(0.02)	(0.05)	(0.13)
Net realized and unrealized gain (loss) on investments	1.65	(0.04)	(0.02)	0.00	0.05
Increase (decrease) in net asset value	1.43	(0.07)	(0.04)	(0.05)	(.08)
Net asset value, beginning of year	1.51	1.58	1.62	1.67	1.75
Net asset value, end of year	$ 2.93	$ 1.51	$ 1.58	$ 1.62	$ 1.67
Per share market value, end of year	$ 3.50	$ 1.34	$ 1.56	$ 1.45	$ 1.03
Total return based on market value	161.2%	(14.1)%	7.6%	40.8%	(18.9)%
Total return based on net asset value	94.0%	(4.6)%	(2.5)%	(3.0)%	(4.6)%
Supplemental data:					
Ratio of expenses before income taxes to average net assets	11.96%	14.35%	9.86%	10.01%	8.73%
Ratio of expenses including taxes to average net assets	20.41%	10.34%	9.53%	8.45%	10.16%

Ratio of net investment loss to average net assets	(9.96)%	(1.99)%	(1.23)%	(3.67)%	(7.51)%
Portfolio turnover	18.1%	21.6%	50.4%	24.3%	65.4%
Net assets end of year	$ 16,782,405	$ 8,615,934	$ 9,027,054	$ 9,238,488	$ 9,604,634
Weighted average shares outstanding at end of year	5,718,934	5,718,934	5,718,934	5,722,776	5,759,260

(1) Per share data are based on weighted average shares outstanding and results are rounded.

RAND CAPITAL CORPORATION AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Summary of Significant Accounting Policies

Nature of Business Rand Capital Corporation (Rand) was founded in 1969 and is headquartered in Buffalo, New York. Rand s investment strategy is to seek capital appreciation through venture capital investments in small, unseasoned, developing companies, primarily in the northeastern United States.

Rand continues to operate as a publicly-held venture capital company, listed on the NASDAQ Small Cap Market under the symbol RAND .

Effective August 16, 2002, Rand made an election, following an authorized vote of its stockholders, to become a Business Development Company, or BDC . Generally, 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. Prior to this election, Rand operated as a diversified closed-end management investment company registered under the Investment Company Act of 1940.

During the first quarter of 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. Simultaneously with the formation of Rand SBIC, Rand Capital Management, LLC (Rand Management), also a wholly-owned subsidiary, was formed to act as the general partner of Rand SBIC. On January 25, 2002, Rand transferred $5 million in cash to Rand SBIC to serve as regulatory capital. On August 16, 2002, Rand received notification that its Small Business Investment Company (SBIC) application had been approved and licensed 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. As of December 31, 2006, the Corporation had drawn down $8,100,000 on its leverage commitments (see Note 4).

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.

Certain investment agreements require the portfolio companies to meet certain financial and non-financial covenants. At December 31, 2006 certain of Rand s portfolio investments were in violation of its loan covenants. Management of the Corporation is pursuing compliance and has considered this in determining the appropriateness of the carrying value of the investment.

Amounts reported as realized gains and losses are measured by the difference between the proceeds from the 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 also regulated by the SBA s Accounting Standards and Financial Reporting Requirements for Small Business Investments Companies. Under these rules interest income cannot be recognized

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RAND CAPITAL CORPORATION AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

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.

Original Issue Discount Investments may create original issue discount or OID income. This situation arises when the Corporation purchases a warrant and a note from a portfolio company simultaneously. The transaction requires an allocation of a portion of the purchase price to the warrant and reduces the note or debt instrument by the equal amount in the form of a note discount or OID. The note is then reported net of the OID and the OID, therefore, is amortized into interest income over the life of the loan. The Corporation has recorded one original issue discount during the year ended December 31, 2006 in the amount of approximately $68,000 and has recognized $5,557 in OID income for the year ended December 31, 2006. The unamortized OID as of December 31, 2006 amounted to $62,333.

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 during the year ended December 31, 2006 was $26,591 ($17,272 in 2005; $0 in 2004). Annual amortization expense for the next five years is estimated to average $31,000 per year.

Deferred Revenue The Corporation charges application and closing fees in connection with its investments. These fees are deferred and amortized into income over the life of the debt or equity investment. Deferred fees amortized into income for the years ended December 31, 2006, 2005 and 2004 amounted to $50,277, $37,916 and $42,094, respectively. Deferred revenue amortization income is estimated to be $21,000 in 2007, and less than $11,000 annually thereafter, based on the deferred revenue balance at December 31, 2006.

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 years ended December 31, 2006, 2005 and 2004 amounted to $11,097, ($27,517) and ($42,273), respectively. Interest paid during the years ended December 31, 2006, 2005 and 2004 amounted to $392,080, $216,068 and $44,564, respectively. During 2006, 2005 and 2004, the Corporation converted $34,356, $30,852 and $138,319, respectively, of interest receivable into equity investments. During the year ended December 31, 2006 the Corporation recorded an escrow receivable of $711,249 in connection with the recognized gain on the sale of an investment.

Concentration of Credit and Market Risk Financial instruments that potentially subject the Corporation to concentrations of credit risk consisted of cash and cash equivalents. Cash is invested with banks in amounts, which, at times, exceed insurable limits. Management does not anticipate non-performance by the banks.

As of December 31, 2006, 67% of the Corporation s total investment value was held in five notes and equity securities. As of December 31, 2005, 52% of the Corporation s total investment value was held in seven notes and equity securities.

Accounting Estimates The preparation of 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 disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Recent Accounting Pronouncements - In June 2006 the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*. This Interpretation clarifies that management is expected to evaluate an income tax position taken or expected to be taken for the likelihood of realization before recording any amounts for such position in the financial statements. FIN 48 also requires expanded disclosure with respect to income tax positions taken that are not certain to be realized. This Interpretation is effective for fiscal years beginning after December 15,

RAND CAPITAL CORPORATION AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

2006, and will require management to evaluate every open tax position that exists in every jurisdiction on the date of initial adoption. Certain disclosures are required in Form 10-Q in the period of adoption of FIN 48 which would be the March 31, 2007 Form 10-Q.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements.* SFAS No. 157 defines fair value, establishes a framework for measuring fair value and requires enhanced disclosures about fair value measurements. SFAS No. 157 requires companies to disclose the fair value of their financial instruments according to a fair value hierarchy as defined in the standard. Additionally, companies are required to provide enhanced disclosure regarding financial instruments in one of the categories (level 3), including a reconciliation of the beginning and ending balances separately for each major category of assets and liabilities. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The adoption of SFAS No. 157 will have an impact on the Company s consolidated financial statements from a disclosure standpoint.

In September 2006, the SEC issued Staff Accounting Bulletin No. 108, *Considering the Effects of Prior Year Misstatements When Quantifying Misstatements in Current Year Financial Statements* . Due to diversity in practice among registrants, SAB 108 expresses SEC staff views regarding the process by which misstatements in financial statements are evaluated for purposes of determining whether financial statement restatement is necessary. SAB 108 is effective for fiscal years ending after November 15, 2006. The adoption of SAB 108 did not have an impact on the Company s consolidated financial statements.

Note 2. Other Assets

At December 31, 2006 and 2005 other assets was comprised of the following:

	2006	2005
Escrow receivable from Innov-X	$ 711,249	
Deferred debenture costs	247,410	254,876
Dividend receivables	19,254	58,494
Operating receivables	16,228	3,846
Property, plant and equipment (net)	12,895	6,487
Total other assets	$ 1,007,036	$ 323,703

In December 2006 the Corporation sold a portion of its shares in Innov-X. As part of the sale a percentage of the proceeds were to be held in an escrow account which the Corporation has recorded as a receivable. The amount is expected to be released from escrow in fiscal year 2008.

Note 3. Income Taxes

Deferred tax assets and liabilities are recorded for temporary differences between the financial statement and tax bases of assets and liabilities using the tax rate expected to be in effect when the taxes are actually paid or recovered.

RAND CAPITAL CORPORATION AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The tax effect of the major temporary difference and carryforwards that give rise to the Corporation s net deferred tax (liabilities) assets at December 31, 2006 and 2005 are approximately as follows:

	2006	2005
Operations	$ (125,000)	$ 54,000
Investments	(3,846,000)	137,000
Tax credit carryforwards	163,000	
Net operating loss carryforwards		655,000
Deferred tax (liability) asset, net	$ (3,808,000)	$ 846,000

The Company assesses annually the recoverability of its deferred tax asset to determine if a valuation allowance is necessary. In performing this assessment, it considers estimated future taxable income and ongoing tax planning strategies. No allowance was deemed necessary for 2006 and 2005.

The components of income tax expense (benefit) reported in the statements of operations are as follows for the years ended December 31:

	2006	2005	2004
Current:			
Federal	$ 398,154	$	$
State	3,647	23,514	24,316
	401,801	23,514	24,316
Deferred:			
Federal	3,956,000	(112,000)	(85,000)
State	698,000	(168,000)	(51,000)
	4,654,000	(280,000)	(136,000)
Total	$ 5,055,801	$ (256,486)	$ (111,684)

A reconciliation of the expense (benefit) for income taxes at the federal statutory rate to the expense reported is as follows:

	2006	2005	2004
Net investment gain (loss) and realized gain (loss) before income tax expense (benefit)	$ 13,222,272	$ (667,606)	$ (323,118)
Expected tax expense (benefit) at statutory rate	$ 4,495,572	$ (226,986)	$ (109,860)
State net of federal effect	793,336	(40,057)	(19,387)
Tax credits and other	(233,107)	(4,443)	17,563
Total	$ 5,055,801	$ (271,486)	$ (111,684)

At December 31, 2006 the Corporation no longer had any federal net operating loss carryforwards, state net operating loss carryforwards or capital loss carryforwards. For state tax purposes the Corporation had a Qualified Emerging Technology Company (QETC) tax credit carryforward of $247,300 at December 31, 2006 which does not have an expiration date. At December 31, 2005, the Corporation had federal net operating loss carryforwards of $1,351,000, state net operating loss carryforwards of $1,365,000 and capital loss carryforwards of $382,000.

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RAND CAPITAL CORPORATION AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 4. SBA Debenture Obligations

Rand SBIC paid a non-refundable commitment fee of $100,000 to the SBA to reserve $10,000,000 of its approved SBA Guaranteed Debenture leverage. This fee was paid in two installments of $50,000 each in July 2003 and August 2004. The fee represents 1% of the face amount of the leverage reserved under the commitment and is a partial prepayment of the SBA s nonrefundable 3% leverage draw fees. As of December 31, 2006, Rand SBIC has debentures payable to and guaranteed by the SBA totaling $8,100,000 ($7,200,000 at December 31, 2005) against this commitment. The debenture terms require semiannual payments of interest at annual interest rates ranging from 4.12% to 5.995%, plus an annual charge that ranged from .855% to .887% during the year ended December 31, 2006. The debentures outstanding at December 31, 2006 mature from 2014 to 2016.

Note 5. Stockholders Equity (Net Assets)

At December 31, 2006 and 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 26, 2007.

Summary of change in equity accounts:

	Accumulated Net Investment Loss	Undistributed Net Realized Gain (Loss) on Investments	Net unrealized Appreciation (Depreciation) on Investments
Balance, December 31, 2004	$ (4,813,146)	$ 6,689,278	$ (351,629)
Net (decrease) increase in net assets from operations	(175,180)	(382,353)	146,412
Balance, December 31, 2005	$ (4,988,326)	$ 6,306,925	$ (205,217)
Net (decrease) increase in net assets from operations	(1,264,802)	3,456,441	5,974,832
Balance, December 31, 2006	$ (6,253,128)	$ 9,763,366	$ 5,769,615

Note 6. Stock Option Plans

In July 2001, the stockholders of the Corporation authorized the establishment of an Employee Stock Option Plan (the Plan). The Plan provides for the award of options to purchase up to 200,000 common shares to eligible employees. In 2002, the Corporation placed the Plan on inactive status as it developed a new profit sharing plan for the Corporation s employees in connection with the establishment of its SBIC subsidiary. As of December 31, 2006 and 2005, 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.

Note 7. Employee Benefit Plans

The Corporation has a defined contribution 401(k) Plan. The Plan provides a base contribution of 1% for eligible employees and also provides up to 5% matching contributions. Plan expense was $22,073, $21,847 and $20,304 during the years ended December 31, 2006, 2005 and 2004, respectively.

In 2002, the Corporation established a Profit Sharing Plan for its executive officers in accordance with of the Section 57(n) of the Investment Company Act of 1940 (the 1940 Act).There were no contributions to the Plan during the years ended 2006, 2005 and 2004

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RAND CAPITAL CORPORATION AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 8. Commitments and Contingencies

The Corporation has an agreement which provides health benefits for the spouse of a former officer of the Corporation. Remaining payments projected to be paid to the surviving spouse have been fully accrued. Total accrued health benefits under this agreement at December 31, 2006 and 2005 were $27,142 and, $34,333, respectively.

The Corporation has a lease for office space which expires in December 2010. Rent expense under this operating lease was approximately $16,000 for the year ended December 31, 2006 ($17,000 for 2005 and $17,000 for 2004). The future operating lease obligation for the next 4 years is approximately $16,000 per year.

Note 9. Subsequent Events

Subsequent to the year ended December 31, 2006, two portfolio companies repaid their debenture instruments totaling $825,000 to the Corporation.

Note 10. Quarterly Operations and Earnings Data Unaudited

	4th Quarter	3rd Quarter	2nd Quarter	1st Quarter
2006				
Investment income	$ 506,419	$ 406,127	$ 213,171	$ 201,245
Net increase in net assets from operations	7,653,329	81,037	238,475	193,630
Basic and diluted net increase in net assets from operations per share	1.34	0.01	0.04	0.04
2005				
Investment income	$ 229,858	$ 171,004	$ 178,059	$ 157,653
Net (decrease) increase in net assets from operations	(301,949)	(41,711)	(173,607)	106,147
Basic and diluted net (decrease) increase in net assets from operations per share	(0.05)	(0.01)	(0.03)	0.02

Note 11. Allowance for Doubtful Accounts

The Corporation maintains an allowance for doubtful accounts for estimated losses from interest payments due from portfolio investments. The allowance for doubtful accounts is based on a review of the overall condition of the accounts receivable balances and a review of past due amounts. Changes in the allowance for doubtful accounts consist of the following:

	2006	2005	2004
Balance at beginning of year	$ (236,870)	$ (122,000)	$ (122,914)

Provision for losses		(114,870)	(122,000)
Recoveries/Sales	114,870		122,914
Balance at end of year	$ (122,000)	$ (236,870)	$ (122,000)

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RAND CAPITAL CORPORATION AND SUBSIDIARIES

SCHEDULE OF CONSOLIDATED CHANGES IN INVESTMENTS AT COST AND REALIZED GAIN
For the Year Ended December 31, 2006

	Cost Increase (Decrease)	Realized Gain (Loss)
New and additions to previous investments		
Innov-X	$ 1,000,000	
Adam+Eve	561,000	
Synacor	507,999	
Niagara Dispensing	500,000	
New Monarch	300,000	
Kionix	243,704	
Rocket Broadband	195,918	
Innov-X	55,148	
Synacor	21,479	
Wineisit	20,000	
Photonics	10,000	
Adam+Eve	5,667	
New Monarch	2,877	
	3,423,792	
Investments sold/liquidated		
Minrad stock sales	(919,422)	$ 1,256,759
Concentrix payback	(600,000)	
Innovex debt repayment	(600,000)	
Synacor repayment	(350,000)	
Vanguard sale	(270,000)	(81,000)
New Monarch repayment	(135,214)	
Ramsco repayment	(97,519)	
Innov-X sold shares	(90,148)	2,280,682
Gemcor repayment	(27,067)	
APF repayment	(8,106)	
Takeform, Inc. repayment	(5,417)	
	(3,102,893)	3,456,441
Net change in investments at Cost and Realized gain	$ 320,899	$ 3,456,441

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders
Rand Capital Corporation and Subsidiaries

We have audited the accompanying consolidated statements of financial position of Rand Capital Corporation and Subsidiaries (the Corporation) as of December 31, 2006 and 2005, including the consolidated schedule of portfolio investments as of December 31, 2006, and the related consolidated statements of operations, cash flows and changes in net assets for each of the three years in the period ended December 31, 2006, and the selected per share data and ratios for each of the five years in the period then ended. These consolidated financial statements and the selected per share data and ratios are the responsibility of the Corporation s management. Our responsibility is to express an opinion on these consolidated financial statements and selected per share data and ratios based on our 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 audit to obtain reasonable assurance about whether the financial statements and selected per share data and ratios are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company s internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. Our procedures included examination or confirmation of securities owned as of December 31, 2006 and 2005. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements and selected per share data and ratios referred to above present fairly, in all material respects, the financial position of the Corporation as of December 31, 2006 and 2005, the results of their operations, their cash flows and the changes in their net assets for each of the three years in the period ended December 31, 2006, and the selected per share data and ratios for each of the five years in the period then ended, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 1, the investment securities included in the consolidated financial statements valued at $23,649,814 (141% of net assets) and $13,370,862 (155% of net assets) as of December 31, 2006 and 2005, respectively, include securities valued at $23,516,594 and $12,128,642, respectively, whose fair values have been estimated by the Board of Directors in the absence of readily ascertainable market value. We have reviewed the procedures used by the Directors in preparing the valuations of investment securities and have inspected the underlying documentation, and in the circumstances we believe the procedures are reasonable and the documentation appropriate. Those estimated values may differ from the values that would have been used had a ready market for the investments existed.

Our audits were made for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The supplementary schedule of consolidated changes in investments at cost and realized loss for the year ended December 31, 2006 is presented for purposes of additional analysis and is not a required part of the basic consolidated financial statements. The supplemental schedule is the responsibility of Corporation s management. Such schedule has been subjected to the auditing procedures applied in the audits of the basic consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic consolidated financial statements taken as a whole.

/s/ Freed Maxick & Battaglia, CPA s, PC

Buffalo, New York
March 23, 2007

Item 9. ***Changes in and Disagreements with Accountants on Accounting and Financial Disclosure***

None

Item 9A. ***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 Annual Report on Form 10-K. Based on that evaluation, our principal executive officer and principal financial officer have concluded that as of that 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 or in other factors that could significantly affect those controls subsequent to our evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Item 9B. ***Other Information***

None

Part III

Item 10. ***Directors, Executive Officers, and Corporate Governance***

Information in response to this Item is incorporated herein by reference to the information under the headings ELECTION OF DIRECTORS , COMMITTEES AND MEETING DATA, and Section 16(a) Beneficial Ownership Compliance provided in the Corporation s definitive Proxy Statement for its Annual Meeting of Shareholders to be held April 26, 2007, to be filed under Regulation 14A (the 2007 Proxy Statement).

The Corporation has adopted a written code of ethics and officer Code of Ethics that applies to our principal executive officer, principal financial officer, and controller, and a Business Ethics Policy applicable to the Corporation s directors, officers and employees. The Corporation s Code of Ethics and Business Ethics Policy are available, free of charge, in the Governance section of the Corporation s website located at www.randcapital.com.

Item 11. ***Executive Compensation***

Information in response to this Item is incorporated herein by reference to the information provided in the Corporation s 2007 Proxy Statement under the headings COMPENSATION DISCUSSION AND ANALYSIS and DIRECTOR COMPENSATION.

Item 12. ***Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters***

Information in response to this Item is incorporated herein by reference to the information provided in the Corporation s 2007 Proxy Statement under the heading BENEFICIAL OWNERSHIP OF SHARES.

Item 13. ***Certain Relationships and Related Transactions and Director Independence***

Information in response to this Item is incorporated herein by reference to the information in the Corporation s 2007 Proxy Statement under the heading DIRECTOR INDEPENDENCE.

Item 14. ***Principal Accounting Fees and Services***

Information concerning the Corporation s independent auditors, the audit committee s pre-approval policy for audit services and our principal accountant fees and services is contained in the Corporation s 2007 Proxy Statement under the heading INDEPENDENT ACCOUNTANT FEES .

Part IV

Item 15. ***Exhibits, Financial Statement Schedules***

(a) The following documents are filed as part of this report and included in Item 8:

(1) CONSOLIDATED FINANCIAL STATEMENTS

Statements of Financial Position as of December 31, 2006 and 2005

Statements of Operations for the three years in the period ended December 31, 2006

Statements of Changes in Net Assets for the three years in the period ended December 31, 2006

Statements of Cash Flows for the three years in the period ended December 31, 2006

Schedule of Portfolio Investments as of December 31, 2006

Schedules of Selected Per Share Data and Ratios for the five years in the period ended December 31, 2006

Notes to the Consolidated Financial Statements

Supplemental Schedule of Consolidated Changes in Investments at Cost and Realized Gain for the year ended December 31, 2006

Report of Independent Registered Public Accounting Firm

(2) FINANCIAL STATEMENT SCHEDULES

The required financial statement Schedule II Valuation and Qualifying Accounts has been omitted because the information required is included in the note 10 to the consolidated financial statements.

(b) 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 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 Formation of 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.

(10.5) Limited Liability Corporation Agreement of Rand Capital Management, LLC incorporated by reference to Exhibit 10.3 to the Corporation s Form 10-K filed for the year ended December 31, 2001.

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(10.6) Certificate of Formation of Rand Capital Management, LLC incorporated by reference to Exhibit 10.3 to the Corporation s Form 10-K filed for the year ended December 31, 2001.

(10.8) Profit Sharing Plan incorporated by reference to Exhibit 10.8 to the Corporation s Form 10-K filed for the year ended December 31, 2002.*

(21) Subsidiaries of the Corporation filed on the Corporation s Form 10-K filed December 31, 2001.

(31.1) Certification of Principal 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 Principal 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

* 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-K to be signed on its behalf by the undersigned thereunto duly authorized.

Date: March 22, 2007
RAND CAPITAL CORPORATION

By: /s/ Allen F. Grum

Allen F. Grum, President

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report on Form 10-K has been signed below by the following persons on behalf of the Corporation in the capacities and on the date indicated.

Signature	Title	
(i) Principal Executive Officer:		
/s/ Allen F. Grum	President	March 22, 2007
Allen F. Grum		
(ii) Principal Accounting & Financial Officer:		
/s/ Daniel P. Penberthy	Treasurer	March 22, 2007
Daniel P. Penberthy		
(iii) Directors:		
/s/ Allen F. Grum	Director	March 22, 2007
Allen F. Grum		
/s/ Erland E. Kailbourne	Director	March 22, 2007
Erland E. Kailbourne		
/s/ Ross B. Kenzie	Director	March 22, 2007
Ross B. Kenzie		
/s/ Willis S. McLeese	Director	March 22, 2007
Willis S. McLeese		
/s/ Reginald B. Newman II	Director	March 22, 2007

Reginald B. Newman II		
/s/ Jayne K. Rand	Director	March 22, 2007
Jayne K. Rand		
/s/ Robert M. Zak	Director	March 22, 2007
Robert M. Zak		