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

# FORM 10-Q

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

**For the quarterly period ended June 30, 2013**

| Commission File Number | Exact Name of Registrant as Specified in its Charter, State or Other Jurisdiction of Incorporation, Address of Principal Executive Offices, Zip Code and Telephone Number (Including Area Code) | I.R.S. Employer Identification Number |
|---|---|---|
| 333-147019, 333-182599, and 333-179941-01 | **PROSPER MARKETPLACE, INC.**<br>a Delaware corporation<br>101 Second Street, 15th Floor<br>San Francisco, CA 94105<br>Telephone: (415)593-5400 | **73-1733867** |
| 333-179941 | **PROSPER FUNDING LLC**<br>a Delaware limited liability company<br>101 Second Street, 15th Floor<br>San Francisco, CA 94105<br>Telephone: (415)593-5479 | **45-4526070** |

Indicate by check mark whether each registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months and (2) has been subject to such filing requirements for the past 90 days.

| | |
|---|---|
| Prosper Marketplace, Inc. | Yes ☒ No ☐ |
| Prosper Funding LLC | Yes ☒ No ☐ |

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

| | |
|---|---|
| Prosper Marketplace, Inc. | Yes ☒ No ☐ |
| Prosper Funding LLC | Yes ☒ No ☐ |

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

| | Large Accelerated Filer | Accelerated Filer | Non-Accelerated Filer | Smaller Reporting Company |
|---|---|---|---|---|
| Prosper Marketplace, Inc. | ☐ | ☐ | ☐ | ☒ |
| Prosper Funding LLC | ☐ | ☐ | ☐ | ☒ |

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

| | |
|---|---|
| Prosper Marketplace, Inc. | Yes ☐ No ☒ |
| Prosper Funding LLC | Yes ☐ No ☒ |

**Prosper Funding LLC** meets the conditions set forth in General Instruction H(1)(a) and (b) of Form 10-Q and is therefore filing this Form 10-Q with the reduced disclosure format specified in General Instruction H(2) of Form 10-Q.

| Registrant | Number of Shares of Common Stock of the Registrant Outstanding at Aug 13, 2013 |
|---|---|
| Prosper Marketplace, Inc. | 65,708,365<br>($.001 par value) |
| Prosper Funding LLC | None |

THIS COMBINED FORM 10-Q IS SEPARATELY FILED BY PROSPER MARKETPLACE, INC. AND PROSPER FUNDING LLC. INFORMATION CONTAINED HEREIN RELATING TO ANY INDIVIDUAL REGISTRANT IS FILED BY SUCH REGISTRANT ON ITS OWN BEHALF. EACH REGISTRANT MAKES NO REPRESENTATION AS TO INFORMATION RELATING TO THE OTHER REGISTRANT.

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**Forward-Looking Statements**

This Quarterly Report on Form 10-Q includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934 (the "Exchange Act"). Forward-looking statements include all statements that do not relate solely to historical or current facts, and can generally be identified by the use of words such as "may," "believe," "will," "expect," "project," "estimate," "intend," "anticipate," "plan," "continue" or similar expressions. In particular, information appearing under "Prosper Marketplace, Inc. Notes to Condensed Consolidated Financial Statements," "Prosper Funding LLC Notes to Condensed Financial Statements" and "Management's Discussion and Analysis of Financial Condition and Results of Operations" includes forward-looking statements. Forward-looking statements inherently involve many risks and uncertainties that could cause actual results to differ materially from those projected in these statements. Where, in any forward-looking statement, Prosper Funding LLC ("Prosper Funding") or Prosper Marketplace, Inc. ("PMI" and, collectively with Prosper Funding, the "Registrants") expresses an expectation or belief as to future results or events, such expectation or belief is based on the current plans and expectations of Prosper Funding and PMI's respective managements, expressed in good faith and is believed to have a reasonable basis. Nevertheless, there can be no assurance that the expectation or belief will result or be achieved or accomplished. The following include some but not all of the factors that could cause actual results or events to differ materially from those anticipated:

- the performance of the Borrower Payment Dependent Notes or "Notes", which, in addition to being speculative investments, are special, limited obligations that are not secured, guaranteed or insured;
- Prosper Funding's ability to make payments on the Notes, including in the event that borrowers fail to make payments on the corresponding loans;
- the reliability of the information about borrowers that is supplied by borrowers;
- Prosper Funding and PMI's ability to service the loans, and their ability or the ability of a third party debt collector to pursue collection against any borrower, including in the event of fraud or identity theft;
- credit risks posed by the credit worthiness of borrowers, the lack of a maximum debt-to-income ratio for borrowers, and the effectiveness of the Registrants' credit rating systems;
- actions by some borrowers to defraud lender members and risks associated with identity theft;
- Prosper Funding and PMI's limited operational history and lack of significant historical performance data about borrower performance;
- the impact of current economic conditions on the performance of the Notes and loss rates of the Notes;
- payments by borrowers on the loans in light of the facts that the loans do not impose restrictions on borrowers and do not include cross-default provisions;
- Prosper Funding and PMI's compliance with applicable local, state and federal law, including the Investment Advisers Act of 1940, the Investment Company Act of 1940 and other laws;
- potential efforts by state regulators or litigants to characterize Prosper Funding or PMI, rather than WebBank, as the lender of the loans originated through the platform;
- the application of federal and state bankruptcy and insolvency laws to borrowers and to Prosper Funding and PMI;
- the impact of borrower delinquencies, defaults and prepayments on the returns on the Notes;
- the lack of a public trading market for the Notes and any inability to resell the Notes on the Note Trader platform;
- the federal income tax treatment of an investment in the Notes and the PMI Management Rights;

- Prosper Funding and PMI’s ability to prevent security breaches, disruptions in service, and comparable events that could compromise the personal and confidential information held on their data systems, reduce the attractiveness of the platform or adversely impact their ability to service loans;
- the resolution of any litigation involving PMI, including any state or federal securities litigation; and
- Prosper Funding’s ability to compete successfully in the peer-to-peer and consumer lending industry.

There may be other factors that may cause actual results to differ materially from the forward-looking statements in this Quarterly Report on Form 10-Q. Prosper Funding and PMI can give no assurances that any of the events anticipated by the forward-looking statements will occur or, if any of them does, what impact they will have on Prosper Funding or PMI’s results of operations and financial condition. You should carefully read the factors described in the “Risk Factors” section of our Annual Report on Form 10-K for a description of certain risks that could, among other things, cause Prosper Funding and PMI’s actual results to differ from these forward-looking statements.

All forward-looking statements speak only as of the date of this Quarterly Report on Form 10-Q and are expressly qualified in their entirety by the cautionary statements included in this Quarterly Report on Form 10-Q. Prosper Funding and PMI undertake no obligation to update or revise forward-looking statements that may be made to reflect events or circumstances that arise after the date made or to reflect the occurrence of unanticipated events, other than as required by law.

**WHERE YOU CAN FIND MORE INFORMATION**

The Registrants file annual, quarterly and current reports and other information with the SEC. You can inspect, read and copy these reports and other information at the SEC’s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. You can obtain information regarding the operation of the SEC’s Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC also maintains a website at www.sec.gov that makes available reports, proxy statements and other information regarding issuers that file electronically.

**PART I. Financial Information**
**Item 1. Condensed Consolidated Financial Statements**

**Prosper Marketplace, Inc.**
**Condensed Consolidated Balance Sheets**
(Unaudited)
(in thousands, except for share and per share amounts)

| | June 30, 2013 | December 31, 2012 |
|---|---|---|
| **Assets** | | |
| Cash and Cash Equivalents | $10,515 | $2,300 |
| Restricted Cash | 7,288 | 5,949 |
| Short Term Investments | - | 1,000 |
| Receivables | 132 | 92 |
| Loans Held for Investment at Fair Value | 152 | 175 |
| Borrower Loans Receivable at Fair Value | 187,125 | 166,900 |
| Property and Equipment, net | 2,178 | 1,530 |
| Prepaid and Other Assets | 1,227 | 376 |
| **Total Assets** | $208,617 | $178,322 |
| | | |
| **Liabilities and Stockholders' Equity** | | |
| Accounts Payable | $1,055 | $1,787 |
| Accrued Liabilities | 3,616 | 2,979 |
| Class Action Settlement Liability | 10,000 | - |
| Notes at Fair Value | 187,489 | 167,478 |
| Loan Loss Reserve | 165 | 41 |
| **Total Liabilities** | 202,325 | 172,285 |
| | | |
| Commitments and contingencies (see Note 10) | | |
| | | |
| **Stockholders' Equity** | | |
| Convertible preferred stock – Series A-F ($0.001 par value; zero and 71,958,130 shares authorized, issued and outstanding as of June 30, 2013 and December 31, 2012, respectively) | - | 72 |
| Convertible preferred stock – Series A '13 ($0.001 par value; 138,681,680 and zero shares authorized, issued and outstanding as of June 30, 2013 and December 31, 2012, respectively) | 139 | - |
| Convertible preferred stock – Series A-1 '13 ($0.001 par value; 51,171,951 and zero shares authorized, issued and outstanding as of June 30, 2013 and December 31, 2012, respectively) | 51 | - |
| Common stock ($0.001 par value; 277,363,460 shares authorized; 65,708,365 issued and outstanding as of June 30, 2013; and 82,630,003 shares authorized; 3,006,745 issued and outstanding as of December 31, 2012) | 68 | 5 |
| Additional Paid in Capital | 103,076 | 83,150 |
| Less: Treasury Stock | (291) | (291) |
| Accumulated Deficit | (96,751) | (76,899) |
| **Total Stockholders' Equity** | 6,292 | 6,037 |
| | | |
| **Total Liabilities and Stockholders' Equity** | $208,617 | $178,322 |

*The accompanying notes are an integral part of these condensed consolidated financial statements.*

**Prosper Marketplace, Inc.**
**Condensed Consolidated Statements of Operations**
(Unaudited)
(in thousands, except for share and per share amounts)

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| **Revenues** | | | | |
| Origination Fees | $3,342 | $1,757 | $4,914 | $3,139 |
| Interest Income on Borrower Loans | 8,578 | 5,780 | 16,309 | 10,410 |
| Interest Expense on Notes | (8,128) | (5,499) | (15,453) | (9,902) |
| Rebates and Promotions | (387) | (265) | (662) | (549) |
| **Total Revenues** | 3,405 | 1,773 | 5,108 | 3,098 |
| **Cost of Revenues** | | | | |
| Cost of Services | (500) | (345) | (982) | (681) |
| Provision for Loan Loss | (50) | (8) | (177) | (11) |
| **Net Revenues** | 2,855 | 1,420 | 3,949 | 2,406 |
| **Operating Expenses** | | | | |
| Compensation and Benefits | 3,270 | 2,350 | 5,775 | 4,807 |
| Marketing and Advertising | 3,878 | 1,127 | 5,451 | 2,401 |
| Depreciation and Amortization | 208 | 168 | 413 | 326 |
| **General and Administrative** | | | | |
| Professional Services | 694 | 639 | 1,382 | 1,633 |
| Facilities and Maintenance | 481 | 301 | 794 | 625 |
| Class Action Settlement | 10,000 | - | 10,000 | - |
| Other | 499 | 381 | 825 | 850 |
| **Total Operating Expenses** | 19,030 | 4,966 | 24,640 | 10,642 |
| **Loss Before Other Income and Expenses** | (16,175) | (3,546) | (20,691) | (8,236) |
| **Other Income and Expenses** | | | | |
| Interest Income | - | 5 | - | 4 |
| Change in fair value of Borrower Loans, Loans Held for Investment and Notes, net | 312 | 241 | 487 | 520 |
| Loss on Impairment of Fixed Assets | (61) | - | (62) | - |
| Other Income | 271 | 43 | 414 | 91 |
| **Total Other Income and Expenses** | 522 | 289 | 839 | 615 |
| **Loss Before Income Taxes** | (15,653) | (3,257) | (19,852) | (7,621) |
| Provision For Income Taxes | - | - | - | - |
| **Net Loss** | $(15,653) | $(3,257) | $(19,852) | $(7,621) |
| **Net loss per share – basic and diluted** | $(0.24) | $(1.12) | $(0.33) | $(2.63) |
| **Weighted average shares - basic and diluted net loss per share** | 65,537,851 | 2,897,859 | 60,202,814 | 2,892,749 |

*The accompanying notes are an integral part of these condensed consolidated financial statements.*

**Prosper Marketplace, Inc.**
**Condensed Consolidated Statements of Stockholders' Equity**
(Unaudited)
(in thousands, except for share and per share amounts)

| | Preferred Stock | | Common Stock | | Treasury Stock | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | **Shares** | **Amount** | **Shares** | **Amount** | **Shares** | **Amount** | **Additional Paid-In Capital** | **Accumulated Deficit** | **Total** |
| **Balance as of January 1, 2013** | 71,958,130 | $72 | 4,829,385 | $5 | (1,822,640) | $(291) | $83,150 | $(76,899) | $6,037 |
| Issuance of convertible preferred stock, Series A'13 | 138,681,680 | $139 | - | - | - | - | 19,810 | - | 19,949 |
| Issuance cost of convertible preferred stock, Series A'13 | | | | | | | (101) | | (101) |
| Issuance of convertible preferred stock, Series A-1'13 | 51,171,951 | 51 | - | - | - | - | - | - | 51 |
| Conversion of Preferred Series A-F | (71,958,130) | (72) | 61,912,702 | 62 | - | - | 10 | - | - |
| Exercise of stock options | - | - | 780,718 | 1 | - | - | 115 | - | 116 |
| Exercise of common stock warrants | - | - | 8,200 | - | - | - | - | - | - |
| Compensation expense | - | - | - | - | - | - | 92 | - | 92 |
| Net loss | - | - | - | - | - | - | - | (19,852) | (19,852) |
| **Balance as of June 30, 2013** | 189,853,631 | $190 | 67,531,005 | $68 | (1,822,640) | $(291) | $103,076 | $(96,751) | $6,292 |

*The accompanying notes are an integral part of these condensed consolidated financial statements.*

**Prosper Marketplace, Inc.**
**Condensed Consolidated Statements of Cash Flows**
(Unaudited)
(in thousands, except for share and per share amounts)

| | For the Six Months Ended June 30, | |
|---|---|---|
| | **2013** | **2012** |
| **Cash flows from operating activities:** | | |
| Net loss | $(19,852) | $(7,621) |
| Adjustments to reconcile net loss to net cash used in operating activities: | | |
| Change in fair value of Borrower Loans | 4,082 | (1,060) |
| Change in fair value of Notes | (4,573) | 532 |
| Depreciation and amortization | 413 | 326 |
| Loan loss Reserve | 124 | 7 |
| Stock-based compensation expense | 92 | 163 |
| Loss on impairment of fixed assets | 62 | – |
| Change in fair value of Loans held for investment | 3 | 8 |
| Issuance of common stock warrants | – | 23 |
| Changes in operating assets and liabilities: | | |
| Class action settlement liability | 10,000 | – |
| Restricted cash | (1,339) | (830) |
| Receivables | (40) | (58) |
| Prepaid and other assets | (851) | (145) |
| Accounts payable and accrued liabilities | (95) | 300 |
| Net cash used in operating activities | (11,974) | (8,355) |
| **Cash flows from investing activities:** | | |
| Origination of Borrower Loans held at fair value | (74,875) | (71,074) |
| Repayment of Borrower Loans held at fair value | 50,568 | 27,990 |
| Purchases of property and equipment | (1,123) | (262) |
| Maturities of short term investments | 1,000 | 5,999 |
| Repayment of Loans held for investment at fair value | 64 | 62 |
| Origination of Loans held for investment at fair value | (44) | (158) |
| Purchases of short term investments | – | (3,000) |
| Net cash used in investing activities | (24,410) | (40,443) |
| **Cash flows from financing activities:** | | |
| Proceeds from issuance of Notes held at fair value | 74,875 | 71,074 |
| Payment of Notes held at fair value | (50,291) | (27,351) |
| Proceeds from issuance of convertible preferred stock | 20,000 | – |
| Principal repayment of notes payable | 116 | – |
| Issuance costs of convertible preferred stock | (101) | – |
| Proceeds from issuance of common stock | – | 3 |
| Net cash provided by financing activities | 44,599 | 43,726 |
| Net increase (decrease) in cash and cash equivalents | 8,215 | (5,072) |
| Cash and cash equivalents at beginning of the period | 2,300 | 9,216 |
| Cash and cash equivalents at end of the period | $10,515 | $4,144 |

*The accompanying notes are an integral part of these condensed consolidated financial statements.*

**Prosper Marketplace, Inc.**
**Notes to Condensed Consolidated Financial Statements**
**(Unaudited)**
(in thousands, except for share and per share amounts)

**1. Organization and Business**

Prosper Marketplace, Inc. ("PMI") was incorporated in the state of Delaware on March 22, 2005. PMI developed and operated a peer-to-peer online credit platform (the "platform") that permitted its borrower members to apply for loans and lender members to purchase notes ("Notes") issued by PMI, the proceeds of which facilitated the funding of specific loans to borrowers. On February 1, 2013, PMI transferred ownership of the platform, including all of the rights related to the operation of the platform, to its wholly-owned subsidiary, Prosper Funding LLC ("Prosper Funding" and, collectively with PMI ("PMI Group"). Since February 1, 2013, all Notes issued and sold through the platform are issued and sold by Prosper Funding. Pursuant to a Loan Account Program Agreement between PMI and WebBank, PMI manages the operation of the platform, as agent of WebBank, in connection with the submission of loan applications by potential borrowers, the making of related loans by WebBank and the funding of such loans by WebBank. Pursuant to an Administration Agreement between Prosper Funding and PMI, PMI manages all other aspects of the platform on behalf of Prosper Funding.

The platform enables borrower members to request and obtain personal, unsecured loans by posting anonymous "listings" on the platform. Loan terms are subject to minimum and maximum loan amounts determined by the borrower's credit bureau score and Prosper score, at interest rates set by PMI. PMI sets the interest rates for borrower loans based on Prosper Ratings, as well as additional factors, such as estimated loss rate, loan terms, general economic environment, previous Prosper loans and competitive conditions. As of June 30, 2013, borrowers could create loan listings from $2 up to $35.

All loans requested and obtained through the platform are unsecured obligations of individual borrower members with a fixed interest rate and loan terms set at three or five years as of June 30, 2013. All loans made through the platform are funded by WebBank, an FDIC-insured, Utah chartered industrial bank. After funding a loan, WebBank sells the loan to PMI (prior to February 1, 2013) or Prosper Funding (on or after February 1, 2013), without recourse to WebBank, in exchange for the principal amount of the loan (the "Borrower Loans"). WebBank does not have any obligation to purchasers of the Notes.

As reflected in the accompanying condensed consolidated financial statements, net losses and negative cash flows were incurred from operations since inception. An accumulated deficit of approximately $96,751 was incurred as of June 30, 2013. At June 30, 2013, approximately $10,515 in cash and cash equivalents was on the condensed consolidated balance sheet. Since its inception, operations have been financed primarily through equity financing from various sources and is dependent upon raising additional capital or debt financing to fund its current operating plan. Failure to obtain sufficient debt and equity financings and, ultimately, to achieve profitable operations and positive cash flows from operations could adversely affect the ability to achieve its business objectives and continue as a going concern. Further, there can be no assurances as to the availability or terms upon which the required financing and capital might be available. On January 15, 2013, PMI entered into a Stock Purchase Agreement with certain new investors and certain of its existing investors (each, a "Share Purchaser" and, collectively, the "Share Purchasers"), pursuant to which PMI issued and sold to such Share Purchasers (either directly or through certain of their respective affiliates) 138,681,680 shares of PMI's Series A preferred stock for an aggregate purchase price of $20,000. See Note 7 *Stockholders' Equity* for additional information.

**2. Summary of Significant Accounting Policies**

**Basis of Presentation**

The unaudited interim condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("US GAAP") and disclosure requirements for interim financial information and the requirements of Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by US GAAP for complete financial statements. The unaudited interim condensed consolidated financial statements should be read in conjunction with the audited financial statements and notes thereto for the year ended December 31, 2012. The balance sheet at December 31, 2012 has been derived from the audited financial statements at that date. Management believes these unaudited interim condensed consolidated financial statements reflect all adjustments, including those of a normal recurring nature, which are necessary for a fair presentation of the results for the interim periods presented. The results of operations for the interim periods are not necessarily indicative of the results that may be expected for the full year of any other interim period.

The accompanying interim condensed consolidated financial statements include the accounts of PMI and its wholly-owned subsidiary Prosper Funding. All intercompany balances and transactions between Prosper Funding and PMI have been eliminated in consolidation.

**Use of Estimates**

The preparation of the interim condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities and the related disclosures at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. These estimates, judgments and assumptions include but are not limited to the following: valuation of borrower loans receivable and associated member payment dependent notes, valuation allowance on deferred tax assets, valuation and amortization periods of intangible assets, provision for loan losses, stock-based compensation expense, and contingent liabilities. Estimates are based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Actual results could differ from those estimates.

**Certain Risks and Concentrations**

In the normal course of its business, two significant types of risk are encountered: credit and regulatory. Financial instruments that potentially subject significant concentrations of credit risk consist primarily of cash, cash equivalents, restricted cash and short term investments. Cash, cash equivalents, restricted cash and short term investments are placed with high-quality financial institutions and is exposed to credit risk in the event of default by these institutions to the extent the amount recorded on the balance sheet exceeds federally insured amounts. Periodic evaluations of the relative credit standing of these financial institutions are performed and no credit losses have been sustained from instruments held at these financial institutions.

To the extent that loan payments are not made, servicing income will be reduced.  Borrower Loans are funded by the Notes and repayment of said Notes is wholly dependent on the repayment of the Borrower Loans associated with the Notes.  As a result, PMI Group does not bear the risk associated with the repayment of principal on loans carried on its condensed consolidated balance sheet.

The PMI Group is subject to various regulatory requirements. The failure to appropriately identify and address these regulatory requirements could result in certain discretionary actions by regulators that could have a material effect on the consolidated financial position and results of operations (See Note 10—Commitments and Contingencies—Securities Law Compliance).

**Cash and Cash Equivalents**

All highly liquid investments with stated maturities of three months or less from date of purchase are classified as cash equivalents. Cash equivalents are recorded at cost, which approximates fair value. Such deposits periodically exceed amounts insured by the FDIC.  Cash and cash equivalents include various unrestricted deposits with highly rated financial institutions in checking, money market and short-term certificate of deposit accounts.

**Restricted Cash**

Restricted cash consists primarily of cash deposits required to support operating activities.

**Short Term Investments**

Short term investments consist of highly liquid instruments with maturity periods greater than three months and less than 12 months.

**Borrower Loans and Notes**

Prior to February 1, 2013, PMI Group issues Notes and purchases Borrower Loans from WebBank, and holds the Borrower Loans until maturity.  The obligation to repay the Notes is conditioned upon the repayment of the associated Borrower Loans.  Borrower Loans and Notes are carried on PMI Group's condensed consolidated balance sheets as assets and liabilities, respectively.  PMI Group has adopted the provisions of ASC Topic 825, *Financial Instruments.*  ASC Topic 825 permits companies to choose to measure certain financial instruments and certain other items at fair value on an instrument-by-instrument basis with unrealized gains and losses on items for which the fair value option has been elected reported in earnings.  The fair value election, with respect to an item, may not be revoked once an election is made.  In applying the provisions of ASC Topic 825, the recorded assets and liabilities are measured using the fair value option in a way that separates these reported fair values from the carrying values of similar assets and liabilities measured with a different measurement attribute.  A specific allowance account is not recorded relating to the Borrower Loans and Notes in which it has elected the fair value option, but rather estimates the fair value of such Borrower Loans and Notes using discounted cash flow methodologies adjusted for the historical payment, loss and recovery rates. An account is considered to be a loss, or charged-off, when it reaches more than 120 days past due.  The aggregate fair value of the Borrower Loans and Notes are reported as separate line items in the assets and liabilities sections of the accompanying balance sheets using the methods described in ASC Topic 820, *Fair Value Measurements and Disclosures*—See Fair Value Measurement.

**Fair Value Measurement**

PMI Group adopted ASC Topic 820, *Fair Value Measurements and Disclosures*, on January 1, 2008, which provides a framework for measuring the fair value of assets and liabilities. ASC Topic 820 also provides guidance regarding a fair value hierarchy, which prioritizes information used to measure fair value and the effect of fair value measurements on earnings and provides for enhanced disclosures determined by the level within the hierarchy of information used in the valuation. ASC Topic 820 applies whenever other standards require (or permit) assets or liabilities to be measured at fair value but does not expand the use of fair value in any new circumstances.

ASC Topic 820 defines fair value in terms of the price that would be received upon the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The price used to measure the fair value is not adjusted for transaction costs while the cost basis of certain financial instruments may include initial transaction costs. Under ASC Topic 820, the fair value measurement also assumes that the transaction to sell an asset occurs in the principal market for the asset or, in the absence of a principal market, the most advantageous market for the asset. The principal market is the market in which the reporting entity would sell or transfer the asset with the greatest volume and level of activity for the asset. In determining the principal market for an asset or liability under ASC Topic 820, it is assumed that the reporting entity has access to the market as of the measurement date. If no market for the asset exists or if the reporting entity does not have access to the principal market, the reporting entity should use a hypothetical market.

Under ASC Topic 820, assets and liabilities carried at fair value in the balance sheets are classified among three levels based on the observability of the inputs used to determine fair value:

Level 1 — The valuation is based on quoted prices in active markets for identical instruments.

Level 2 — The valuation is based on observable inputs such as quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3 — The valuation is based on unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the instrument. Level 3 valuations are typically performed using pricing models, discounted cash flow methodologies, or similar techniques, which incorporate management’s own estimates of assumptions that market participants would use in pricing the instrument or valuations that require significant management judgment or estimation.

Fair value of financial instruments are determined based on the fair value hierarchy established in ASC Topic 820, which requires an entity to maximize the use of quoted prices and observable inputs and to minimize the use of unobservable inputs when measuring fair value. Various valuation techniques are utilized, depending on the nature of the financial instrument, including the use of market prices for identical or similar instruments, or discounted cash flow models. When possible, active and observable market data for identical or similar financial instruments are utilized. Alternatively, fair value is determined using assumptions that management believes a market participant would use in pricing the asset or liability.

Financial instruments consist principally of cash and cash equivalents, restricted cash, short term investments, Borrower Loans receivable, accounts payable and accrued liabilities, Notes and long-term debt. The estimated fair values of cash and cash equivalents, restricted cash, accounts payable and accrued liabilities approximate their carrying values because of their short term nature.

Borrower Loans and Notes are accounted for on a fair value basis.

**Property and Equipment**

Property and equipment consists of computer equipment, office furniture and equipment, and software purchased or developed for internal use. Property and equipment are stated at cost, less accumulated depreciation and amortization, and are computed using the straight-line method based upon estimated useful lives of the assets, which range from three to seven years, commencing once the asset is placed in service. Expenditures are capitalized for replacements and betterments and recognized as expense amounts for maintenance and repairs as incurred.

**Internal Use Software and Website Development**

Internal use software costs and website development costs are accounted for, in accordance with ASC Topic 350-40, *Internal Use Software* and ASC Topic 350-50, *Website Development Cost*s. In accordance with ASC Topic 350-40 and 350-50, the costs to develop software for the website and other internal uses are capitalized when management has authorized and committed project funding, preliminary development efforts are successfully completed, and it is probable that the project will be completed and the software will be used as intended. Capitalized software development costs primarily include software licenses acquired, fees paid to outside consultants, and salaries and payroll related costs for employees directly involved in the development efforts.

Costs incurred prior to meeting these criteria, together with costs incurred for training and maintenance, are expensed. Costs incurred for upgrades and enhancements that are considered to be probable to result in additional functionality are capitalized. Capitalized costs are included in property and equipment and amortized to expense using the straight-line method over their expected lives. Software assets are evaluated for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Recoverability of software assets to be held and used is measured by a comparison of the carrying amount of the asset to the future net undiscounted cash flows expected to be generated by the asset. If such software assets are considered to be impaired, the impairment to be recognized is the excess of the carrying amount over the fair value of the software asset.

**Loan Loss Reserve**

PMI Group is obligated to indemnify lenders and or repurchase certain Notes sold to the lenders in the event of violation of applicable federal, state, or local lending laws or verifiable identify theft. The loan loss reserve is estimated based on historical experience and is accrued when the Notes are issued. Indemnified or repurchased Notes are written off at the time of repurchase or at the time an indemnification payment is made.

**Revenue Recognition**

Revenue is recognized in accordance with ASC Topic 605, *Revenue Recognition*. Under ASC Topic 605, revenue is recognized when persuasive evidence of an arrangement exists, services have been rendered, the price of the services is fixed and determinable, and collectability is reasonably assured.

*Origination Fees*

Borrowers pay an origination fee upon the successful closing of a loan. The origination fee is deducted and retained from the loan amount prior to disbursing the net amount to the borrower member. The loan origination fee is determined by the term and credit grade of the loan, and ranges from 1.00% to 4.95% of the original principal amount. Origination fees are not deferred but are recognized at origination of the loan, and direct costs to originate loans are recorded as expenses as incurred since Borrower Loans, Borrower Loans held for investment and Notes are accounted for at fair value.

*Loan Servicing Fees*

Loan servicing fees are accrued daily based on the current outstanding loan principal balance of the Borrower Loans but are not recognized until payment is received due to the uncertainty of collection of borrower loan payments.

*Interest Income on Borrower Loans Receivable and Interest Expense on Notes*

Interest income on Borrower Loans is recognized using the accrual method based on the stated interest rate to the extent that is believed it to be collectable. Interest expense is recorded on the corresponding Notes based on the contractual interest rate. Below is a table that summarizes the gross interest income and expense for the three and six months ended June 30, 2013 and 2012.

| | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| Interest Income on Borrower Loans | $8,578 | $5,780 | $16,309 | $10,410 |
| Interest Expense on Notes | (8,128) | (5,499) | (15,453) | (9,902) |
| Net Interest Income | $450 | $281 | $856 | $508 |

**Marketing and Advertising Expense**

Under the provisions of ASC Topic 720, *Other Expenses,* the costs of advertising are expensed as incurred. Advertising costs were approximately $3,878 and $1,127 for the three months ended June 30, 2013 and 2012, respectively. Advertising costs were approximately $5,451 and $2,401 for the six months ended June 30, 2013 and 2012, respectively.

**Rebate and Promotional Expenses**

Rebates and promotions are accounted for in accordance with ASC Topic 605, *Revenue Recognition*. From time to time rebates and promotions are offered to borrower and lender members. These rebates and promotions are recorded as an offset to revenue if a particular rebate or promotion is earned upon the origination of the loan. Rebates and promotions have in the past been in the form of cash back and other incentives paid to lenders and borrowers.

**Stock-Based Compensation**

Stock-based compensation for employees is accounted for using fair-value-based accounting in accordance with ASC Topic 718, *Stock Compensation*. ASC Topic 718 requires companies to estimate the fair value of stock-based awards on the date of grant using an option-pricing model. The stock-based compensation related to awards that are expected to vest is amortized using the straight line method over the vesting term of the stock-based award, which is generally four years. Expected forfeitures of unvested options are estimated at the time of grant such that expense is recorded only for those stock-based awards that are expected to vest.

Options have been granted to purchase shares of common stock to nonemployees in exchange for services performed which it accounts for in accordance with the provisions of ASC Topic 505-50, *Equity-Based Payments to Non-Employees*. Because ASC Topic 505 requires that nonemployee equity awards be recorded at their fair value, the Black-Scholes model is used to estimate the fair value of options granted to nonemployees at each vesting date until performance is complete to determine the appropriate charge for the services provided. The volatility of the common stock was based on comparative company volatility.

**Net Loss Per Share**

Net loss per share is computed in accordance with ASC Topic 260, *Earnings Per Share*. Under ASC Topic 260, basic net loss per share is computed by dividing net loss per share available to common shareholders by the weighted average number of common shares outstanding for the period and excludes the effects of any potentially dilutive securities. Diluted earnings per share, if presented, would include the dilution that would occur upon the exercise or conversion of all potentially dilutive securities into common stock using the "treasury stock" and/or "if converted" methods as applicable. At June 30, 2013, there were outstanding convertible preferred stock, warrants and options convertible into 138,681,720, 2,187,969 and 7,212,610 common shares, respectively, which may dilute future earnings per share. By reporting a net loss for the three and six months ended June 30, 2013 and 2012, potentially dilutive securities are excluded from the computation of net loss per share, as their effect would be antidilutive.

**Income Taxes**

The asset and liability method is used to account for income taxes as codified in ASC Topic 740, *Income Taxes*. Under this method, deferred income tax assets and liabilities are based on the differences between the financial statements and tax bases of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

Under ASC Topic 740, the policy to include interest and penalties related to gross unrecognized tax benefits within its provision for income taxes did not change.

**Comprehensive Income**

There is no comprehensive income (loss) other than the net income (loss) disclosed in the condensed consolidated statement of operations.

**Recent Accounting Pronouncements**

There have been no recent accounting pronouncements or changes in accounting pronouncements during the six months ended June 30, 2013 that are of significance, or potential significance.

**3. Borrower Loans and Notes Held at Fair Value**

The following tables present the assets and liabilities measured at fair value on a recurring basis at June 30, 2013 and December 31, 2012:

| December 31, 2012 | Level 1 Inputs | Level 2 Inputs | Level 3 Inputs | Fair Value |
|---|---|---|---|---|
| **Assets** | | | | |
| Short term investments | $1,000 | $- | $- | $1,000 |
| Borrower Loans receivable | - | - | 166,900 | 166,900 |
| Borrower Loans held for investment | - | - | 175 | 175 |
| **Liabilities** | | | | |
| Notes | $- | $- | $167,478 | $167,478 |
| **June 30, 2013** | **Level 1 Inputs** | **Level 2 Inputs** | **Level 3 Inputs** | **Fair Value** |
| **Assets** | | | | |
| Borrower Loans receivable | $- | $- | $187,125 | $187,125 |
| Loans held for investment | - | - | 152 | 152 |
| **Liabilities** | | | | |
| Notes | $- | $- | $187,489 | $187,489 |

Short term investments consist of United States Treasuries with maturity periods greater than three months and less than 12 months. In general, fair values determined by Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets or liabilities that PMI Group has the ability to access. PMI Group classifies United States Treasuries as Level 1 assets which it intends to hold until maturity.

As observable market prices are not available for the Borrower Loans and Notes the PMI Group holds, or for similar assets and liabilities, the PMI Group believes the Borrower Loans and Notes should be considered Level 3 financial instruments under ASC Topic 820. In a hypothetical transaction as of the measurement date, PMI Group believes that differences in the principal marketplace in which the loans are originated and the principal marketplace in which it might offer those loans may result in differences between the originated amount of the loans and their fair value as of the transaction date. For Borrower Loans, the fair value is estimated using discounted cash flow methodologies based upon valuation assumptions including prepayment speeds, roll rates, recovery rates and discount rates based on the perceived credit risk within each credit grade.

The obligation to pay principal and interest on any Note is equal to the loan payments, if any, that are received on the corresponding Borrower Loan, net of its servicing fee. The fair value election for Notes and Borrower Loans allows both the assets and the related liabilities to receive similar accounting treatment for expected losses which is consistent with the subsequent cash flows to lenders that are dependent upon borrower payments. As such, the fair value of the Notes is approximately equal to the fair value of the Borrower Loans, adjusted for the servicing fee and the timing of borrower payments subsequently disbursed to Note holders. Any unrealized gains or losses on the Borrower Loans and Notes for which the fair value option has been elected is recorded as a separate line item in the statement of operations. The effective interest rate associated with the Notes is less than the interest rate earned on the Borrower Loans due to the servicing fee. See further in this note for a roll-forward and further discussion of the significant assumptions used to value Borrower Loans and Notes.

The fair value of the Notes and Borrower Loans are estimated using discounted cash flow methodologies based upon a set of valuation assumptions. The main assumptions used to value the Borrower Loans and Notes include prepayment rates derived from historical prepayment rates for each credit score, default rates derived from historical performance, recovery rates and discount rates applied to each credit tranche based on the perceived credit risk of each credit grade. The obligation to pay principal and interest on any Note is equal to the loan payments, if any, received on the corresponding Borrower Loan, net of the servicing fee. As such, the fair value of the Notes is approximately equal to the fair value of the Borrower Loans, adjusted for the servicing fee and the timing of borrower payments subsequently disbursed to the Note holders. The effective interest rate associated with the Notes will be less than the interest rate earned on the Borrower Loans due to the servicing fee.

For Borrower Loans originated and Notes, the following average assumptions to determine the fair value as of June 30, 2013 were used:

| | |
|---|---|
| Monthly prepayment rate speed | 1.53% |
| Recovery rate | 2.60% |
| Discount rate * | 10.50% |

* This is the average discount rate among all of the credit grades

The changes in Level 3 assets measured at fair value on a recurring basis are as follows:

**Fair Value Measurements Using Significant Unobservable Inputs (Level 3)**

| | Borrower Loans | Notes | Loans Held for Investment | Total |
|---|---|---|---|---|
| Balance at January 1, 2012 | $75,763 | $(76,160) | $137 | $(260) |
| Originations | 153,175 | (153,175) | 182 | 182 |
| Principal repayments and credit losses | (66,840) | 65,690 | (133) | (1,283) |
| Change in fair value on Borrower Loans and Notes | 4,802 | (3,833) | - | 969 |
| Change in fair value of loans held for investment | - | - | (11) | (11) |
| Balance at December 31, 2012 | $166,900 | $(167,478) | $175 | $(403) |
| Originations | 74,875 | (74,875) | 44 | 44 |
| Principal repayments and credit losses | (50,568) | 50,291 | (64) | (341) |
| Change in fair value on Borrower Loans and Notes | (4,082) | 4,573 | - | 491 |
| Change in fair value of loans held for investment | - | - | (3) | (3) |
| Balance at June 30, 2013 | $187,125 | $(187,489) | $152 | $(212) |

Due to the recent origination of the Borrower Loans and Notes, the change in fair value attributable to instrument-specific credit risk is immaterial. There were no outstanding Borrower Loans or Notes originated or issued prior to July 13, 2009. Of the Borrower Loans originated from July 13, 2009 to June 30, 2013, 255 loans, which were 90 days or more delinquent, totaled an aggregate principal amount of $1,349 and a fair value of $122 as of June 30, 2013.

No other assets or other liabilities were carried at fair value as of June 30, 2013 and December 31, 2012.

**4. Loans Held for Investment at Fair Value**

As of June 30, 2013, a total of $152 of Borrower Loans originated through the platform is presented as Loans Held for Investment in the accompanying condensed consolidated balance sheets. When a borrower member loan has been funded in whole, or in part, the portion of the borrower's monthly loan payment that corresponds to the percentage of the loan that is funded is retained. In these cases, interest income is recorded on these Borrower Loans.

**Fair Value Measurements Using Significant Unobservable Inputs (Level 3)**

| | Loans Held for Investment |
|---|---|
| Balance at January 1, 2012 | $137 |
| Originations | 182 |
| Principal repayments | (133) |
| Change in fair value of loans held for investment | (11) |
| Balance at December 31, 2012 | $175 |
| Originations | 44 |
| Principal repayments and credit losses | (64) |
| Change in fair value of loans held for investment | (3) |
| Balance at June 30, 2013 | $152 |

Origination fees earned from Borrower Loans funded are initially deferred and subsequently amortized ratably over the term of the Borrower Loan and are reported in the statement of operations as Origination fees.

The fair value of the Borrower Loans held for investment is estimated using the discounted cash flow methodologies based upon a set of valuation assumptions similar to those of all the Borrower Loans, which are set forth in Note 3, as they have similar characteristics and the PMI Group expects these Borrower Loans to behave in a comparable manner. The valuation assumptions used to value these Borrower Loans include prepayment rates, default rates and recovery rates derived from historical loan performance data and discount rates based on credit grade applied to each Borrower Loan.

The fair value adjustment on these Borrower Loans held for investment was $3, which is included in earnings for the six months ended June 30, 2013. As of June 30, 2013, $184 in payments was received on these Borrower Loans. As of June 30, 2013, there was $36 in Borrower Loans held for investment that were charged-off.

**5. Loan Loss Reserve**

Changes in the loan loss reserve are summarized below:

| | |
|---|---|
| Balance at January 1, 2013: | $41 |
| Provision for loan loss | 124 |
| Balance at June 30, 2013: | $165 |

**6. Net Loss Per Share**

Net loss per share is computed in accordance with ASC Topic 260. Under ASC Topic 260, basic net loss per share is computed by dividing net loss per share available to common stockholders by the weighted average number of common shares outstanding for the period and excludes the effects of any potentially dilutive securities. Diluted earnings per share, if presented, would include the dilution that would occur upon the exercise or conversion of all potentially dilutive securities into common stock using the “treasury stock” and/or “if converted” methods as applicable.

Basic and diluted loss per share was calculated as follows:

| | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|
| | **2013** | **2012** | **2013** | **2012** |
| Numerator: | | | | |
| Net loss | $(15,653) | $(3,257) | $(19,852) | $(7,621) |
| Denominator: | | | | |
| Weighted average shares used in computing basic and diluted net loss per share | 65,537,851 | 2,897,859 | 60,202,814 | 2,892,749 |
| Basic and diluted net loss per share | $(0.24) | $(1.12) | $(0.33) | $(2.63) |

Due to losses attributable to common shareholders for each of the periods below, the following potentially dilutive shares are excluded from the diluted net loss per share calculation because they were anti-dilutive under the treasury stock method, in accordance with ASC Topic 260:

| | Three and six months ended June 30, | |
|---|---|---|
| | **2013** | **2012** |
| Excluded Securities: | (shares) | (shares) |
| Convertible preferred stock issued and outstanding | 138,681,720 | 61,958,136 |
| Stock options issued and outstanding | 7,212,610 | 12,406,772 |
| Warrants issued and outstanding | 2,187,969 | 2,380,298 |
| Total common stock equivalents excluded from diluted net loss per common share computation | 148,082,299 | 76,745,206 |

## 7. Stockholders' Equity

### Preferred Stock

Under PMI's certificate of incorporation, preferred stock is issuable in series, and PMI's board of directors (the "Board of Directors") is authorized to determine the rights, preferences, and terms of each series.

In January 2013, PMI issued and sold 138,681,680 shares of new Series A ("Series A") preferred stock in a private placement at a purchase price of $0.144 per share for approximately $20,000. In connection with that sale, PMI issued 51,171,951 shares at par value $0.001 per share of Series A-1 ("Series A-1") convertible preferred stock to certain previous holders of PMI's original Series A, Series B, Series C, Series D, Series E and Series F preferred stock who participated in the sale. Upon issuance of the new Series A and Series A-1 preferred stock, all of PMI's preferred stock existing prior to such issuance was converted into PMI common stock at a 1:1 ratio if the holder of the preferred stock participated in the new Series A preferred stock sale or at a 10:1 ratio if the holder of the preferred stock did not so participate. These securities were sold in reliance on the exemption from the registration requirements of the Securities Act set forth in Section 4(2) of the Securities Act and Regulation D promulgated thereunder regarding sales by an issuer not involving a public offering.

| Convertible Preferred Stock | Par Value | Authorized, Issued and Outstanding shares as of June 30, 2013 | Balance June 30, 2013 | Authorized, Issued and Outstanding shares as of December 31, 2012 |
|---|---|---|---|---|
| Series A | $0.001 | - | $- | 4,023,999 |
| Series B | 0.001 | - | - | 3,310,382 |
| Series C | 0.001 | - | - | 2,063,558 |
| Series D | 0.001 | - | - | 20,340,705 |
| Series E | 0.001 | - | - | 23,222,747 |
| Series E-1 | 0.001 | - | - | 10,000,000 |
| Series F | 0.001 | - | - | 8,996,739 |
| | | - | $- | 71,958,130 |

As of December 31, 2012, the total balance of all convertible preferred stock Series A through F was $72.

*Dividends*

Dividends on shares of the new Series A preferred stock are payable only when, as, and if declared by the Board of Directors. No dividends will be paid with respect to the common stock or Series A-1 preferred stock until any declared dividends on the Series A preferred stock have been paid or set aside for payment to the Series A preferred stock holders. Holders of Series A-1 preferred stock are not entitled to receive dividends in preference and priority to, or on a *pari passu* basis with, the other preferred stock or the common stock. To date, no dividends have been declared on any of PMI's preferred stock or common stock, and there are no dividends in arrears at June 30, 2013.

The holders of PMI's Series D, Series E and Series F preferred stock were entitled to receive an annual dividend per share in an amount equal to 8% times the liquidation preference for such share, payable in preference and priority to any declaration or payment of any distribution on common stock in such calendar year. The right to receive dividends on shares of PMI's Series D, Series E and Series F preferred stock was cumulative from and after the date of issuance of such shares and were payable only when, as, and if declared by the Board of Directors. Holders of PMI's Series E-1 preferred stock were not entitled to receive dividends in preference and priority to, or on a *pari passu* basis with, the other preferred stock or the common stock. Dividends on shares of PMI's Series E-1 preferred stock were payable only when, as, and if declared by the Board of Directors. All shares of PMI's Series D, E, E-1 and F preferred stock were converted to common stock in connection with the January 2013 sale of PMI's new Series A and A-1 preferred stock.

*Conversion*

On January 15, 2013, PMI entered into an equity financing transaction where shares of PMI's preferred stock that were outstanding immediately prior to the financing ("Old Preferred Shares") were converted into shares of PMI common stock. For holders of Old Preferred Shares who participated in the financing in proportion to their pro rata ownership interest in PMI, their Old Preferred Shares converted into common shares at a ratio of 1:1. In addition, each such participating holder received a share of PMI's new Series A-1 preferred stock for every dollar of liquidation preference associated with an Old Preferred Share held by such holder. Each share of Series A-1 preferred stock has a liquidation preference of $1.00 and converts into common stock at a ratio of 1,000,000:1.

Under the terms of PMI's new Series A preferred stock (the "Shares"), the holders of such Shares have the right to convert the Shares into common stock at any time. In addition, the Shares automatically convert into common stock (i) immediately prior to the closing of an IPO that values PMI at least at $200,000 and that results in aggregate proceeds to PMI of at least $40,000 or (ii) upon a written request from the holders of at least 70% of the voting power of the outstanding preferred stock (on an as-converted basis). In addition, if a holder of the Shares has converted any of the Shares, then all of such holder's shares of Series A-1 preferred stock also will be converted upon a liquidation event. In lieu of any fractional shares of common stock to which a holder would otherwise be entitled, PMI shall pay such holder cash in an amount equal to the fair market value of such fractional shares, as determined by PMI's Board of Directors. At present, the new Series A preferred stock converts into PMI common stock at a 1:1 ratio while the Series A-1 preferred stock converts into PMI common stock at a 1,000,000:1 ratio.

*Liquidation Rights*

PMI issued 51,171,951 shares at the par value $0.001 per share of Series A-1 convertible preferred stock to certain previous holders of PMI's preferred stock who participated in the new Series A preferred stock sale. The Series A-1 shares established certain liquidation rights, have no voting rights and are convertible into one share of PMI common stock for every one million shares of Series A-1 preferred stock. PMI allocated the fair value of the shares of Series A-1 preferred stock at the par value of $.001 per share from the proceeds of new Series A preferred stock. Upon issuance of PMI's new Series A and Series A-1 preferred stock, all of PMI's preferred stock existing prior to such issuance was converted into PMI common stock at a 1:1 ratio if the holder of the preferred stock participated in the new Series A preferred stock sale or at a 10:1 ratio if the holder of the preferred stock did not so participate.

*Voting*

Each holder of shares of preferred stock shall be entitled to the number of votes equal to the number of shares of common stock into which such shares of preferred stock could be converted and shall have voting rights and powers equal to the voting rights and powers of the common stock (except as otherwise expressly provided in PMI's Amended and Restated Certificate of Incorporation or as required by law), voting together with the common stock as a single class, and shall be entitled to notice of any stockholders' meeting in accordance with the Bylaws of PMI. The holders of preferred stock shall vote as one class with the holders of the common stock except with respect to certain matters that require separate votes.

**Common Stock**

PMI, through its certificate of incorporation, is the sole issuer of common stock and related options and warrants. PMI was authorized to issue up to 277,363,460 shares of common stock, $0.001 par value, of which 65,708,365 shares were issued and outstanding as of June 30, 2013. As of December 31, 2012, there were 82,630,003 shares of common stock authorized, $0.001 par value, of which 3,006,745 shares were issued and outstanding. Each holder of common stock shall be entitled to one vote for each share of common stock held.

*Common Stock Issued upon Exercise of Stock Options*

For the six months ended June 30, 2013 and 2012, PMI issued 780,718 and 25,000 shares of common stock, respectively, upon the exercise of options for cash proceeds of $116 and $3, respectively.

*Common Stock Issued upon Exercise of Stock Warrants*

For the six months ended June 30, 2013 PMI issued 8,200 shares of common stock upon the exercise of warrants for $0.01 per share.

**8. Stock Option Plan and Compensation**

Incentive stock options are granted to employees at an exercise price not less than 100% of the fair value of PMI's common stock on the date of grant. Non-statutory stock options are granted to consultants and directors at an exercise price not less than 85% of the fair value of PMI's common stock on the date of grant. If options are granted to stockholders who hold 10% or more of PMI's common stock on the option grant date, then the exercise price shall not be less than 110% of the fair value of PMI's common stock on the date of grant. The fair value is based on a good faith estimate by the Board of Directors at the time of each grant. As there is no active trading market for these options, such estimate may ultimately differ from valuations completed by an independent party. The options generally vest over four years, which is the same as the performance period. In no event are options exercisable more than ten years after the date of grant.

At December 31, 2012, there were 15,239,664 stock options available for grant under the 2005 Stock Option Plan (the "Plan"). During the first six months of 2013, the Board of Directors increased the total number of options under the plan by an additional 56,483,417 for a total of 71,723,081 available for grant.

Option activity under the Plan is summarized as follows for the periods below:

| | Options Issued and Outstanding | Weighted-Average Exercise Price |
|---|---|---|
| Balance as of January 1, 2013 | 11,738,168 | $0.20 |
| Options granted (weighted average fair value of $0.01) | 10,091 | $0.17 |
| Options exercised | (780,718) | $0.15 |
| Options canceled | (3,754,931) | $0.23 |
| Balance as of June 30, 2013 | 7,212,610 | $0.19 |
| Options outstanding and exercisable at June 30, 2013 | 5,105,188 | $0.21 |

*Other Information Regarding Stock Options*

Additional information regarding PMI common stock options outstanding as of June 30, 2013 is as follows:

| | Options Outstanding | | | | Options Exercisable | | |
|---|---|---|---|---|---|---|---|
| Range of Exercise Prices | Number Outstanding | Weighted Avg. Remaining Life | Weighted Avg. Exercise Price | Intrinsic Value | Number Exercisable | Weighted Avg. Exercise Price | Intrinsic Value |
| $0.12 - $0.12 | 1,829,872 | 8.21 | 0.12 | $ - | 1,200,890 | 0.12 | $ - |
| $0.17 - $0.17 | 1,953,711 | 8.87 | 0.17 | - | 626,966 | 0.17 | - |
| $0.20 - $0.20 | 3,090,527 | 7.06 | 0.20 | - | 2,945,082 | 0.20 | - |
| $0.25 - $0.25 | 15,000 | 2.05 | 0.25 | - | 15,000 | 0.25 | - |
| $0.50 - $0.50 | 110,000 | 3.18 | 0.50 | - | 110,000 | 0.50 | - |
| $0.56 - $0.56 | 182,500 | 6.21 | 0.56 | - | 176,250 | 0.56 | - |
| $1.94 - $1.94 | 31,000 | 5.55 | 1.94 | - | 31,000 | 1.94 | - |
| $0.12 - $1.94 | 7,212,610 | 7.74 | $0.19 | $ - | 5,105,188 | 0.21 | $ - |

The intrinsic value is calculated as the difference between the value of PMI's common stock at June 30, 2013, which was $0.01 per share, and the exercise price of the options.

No compensation expense is recognized for unvested shares that are forfeited upon termination of service, and the stock-based compensation expense for the three months ended June 30, 2013 and 2012 reflect the expenses that PMI expects to recognize after the consideration of estimated forfeitures.

PMI estimates its forfeiture rate based on an analysis of its actual forfeitures and will continue to evaluate the adequacy of the forfeiture rate based on actual forfeiture experience, analysis of employee turnover behavior, and other factors. The impact from a forfeiture rate adjustment will be recognized in full in the period of adjustment, and if the actual number of future forfeitures differs from that estimate, PMI may be required to record adjustments to stock-based compensation expense in future periods.

The fair value of PMI stock option awards for the three and six months ended June 30, 2013 and 2012 was estimated at the date of grant using the Black-Scholes model with the following average assumptions:

| | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| Volatility of common stock | ** | ** | 73.43% | 77.10% |
| Risk-free interest rate | ** | ** | 0.82% | 0.97% |
| Expected life* | ** | ** | 8.7 years | 5.0 years |
| Dividend yield | ** | ** | 0% | 0% |
| Weighted-average fair value of grants | ** | ** | $0.01 | 0.11 |

*For nonemployee stock option awards, the expected life is the contractual term of the award, which is generally ten years.
**No stock option awards were granted during the three months ended June 30, 2013 and June 30, 2012.

The Black-Scholes model requires the input of highly subjective assumptions, including the expected stock price volatility. Because PMI's equity awards have characteristics significantly different from those of traded options, the changes in the subjective input assumptions can materially affect the fair value estimate.

Total stock-based compensation expense for PMI employees reflected in the statements of operations for the six months ended June 30, 2013 and 2012 is approximately $84 and $169, respectively and $34 and $88 for the three months ended June 30, 2013 and 2012. As of June 30, 2013, the unamortized stock-based compensation expense related to PMI employees' unvested stock-based awards was approximately $92, which will be recognized over the remaining weighted average vesting period of approximately 2.5 years.

**9. Income Taxes**

As part of the process of preparing the condensed consolidated financial statements, PMI Group is required to estimate its income taxes in each of the jurisdictions in which it operates. This process involves determining the income tax expense (benefit) together with calculating the deferred income tax expense (benefit) related to temporary differences resulting from differing treatment of items, such as fair value of loans or deductibility of certain intangible assets, for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within the accompanying balance sheet. PMI Group must then assess the likelihood that the deferred tax assets will be recovered through the generation of future taxable income.

Due to the book and tax net losses incurred during the six months ended June 30, 2013 and 2012, zero income tax expense has been incurred during those periods. In addition, substantial historical losses has been incurred and has maintained a full valuation allowance against its net deferred tax assets because the realization of those deferred tax assets is dependent upon future earnings, and the amount and timing of those earnings, if any is uncertain.

**10. Commitments and Contingencies**

*Future Minimum Lease Payments*

The corporate office and co-location facility is under non-cancelable operating leases that expire in December 2014 and August 2014, respectively.

Future minimum rental payments under these leases as of June 30, 2013 are as follows:

| | |
|---|---|
| 2013 | $296 |
| 2014 | 501 |
| Total future operating lease obligations | $797 |

Rental expense under premises-operating lease arrangements was $201 and $337 for the three and six months ended June 30, 2013 and $129 and $264 for the corresponding periods during 2012, respectively.

PMI Group amended and restated an agreement with WebBank, an FDIC-insured Utah-chartered industrial bank, under which all loans originated through the platform are made by WebBank under its bank charter. The arrangement allows for loans to be offered to borrowers at uniform nationwide terms. PMI Group is required to pay the greater of a monthly minimum fee or a fee calculated based on a certain percentage of monthly loan origination volume.

PMI Group has an agreement with a third party broker-dealer in which the third party agreed to operate and maintain the Note Trader Platform for the secondary trading of PMI Group Notes. PMI Group is required to pay the third party broker-dealer an agreed upon monthly fee which equals the difference between the minimum monthly fee and the transaction fees collected by the third party provider during that month.

*Securities Law Compliance*

From inception through October 16, 2008, PMI sold approximately $178,000 of borrower loans to lender members through the old platform structure, whereby PMI assigned promissory notes directly to lender members. PMI did not register the offer and sale of the promissory notes corresponding to these loans under the Securities Act or under the registration or qualification provisions of any state securities laws. The question of whether or not the operation of the platform during this period constituted an offer or sale of "securities" involved a complicated factual and legal analysis and was uncertain. If the sales of promissory notes offered through the platform during this period were viewed as a securities offering, PMI would have failed to comply with the registration and qualification requirements of federal and state laws and lender members who hold these promissory notes may be entitled to rescission of unpaid principal, plus statutory interest. Generally, the federal statute of limitations for noncompliance with the requirement to register securities under the Securities Act is one year from the violation, although the statute of limitations period under various state laws may be for a longer period of time.

PMI's decision to restructure the platform and cease sales of promissory notes offered through the platform effective October 16, 2008 limited this contingent liability to the period covering its activities prior to October 16, 2008.

On April 21, 2009, PMI and the North American Securities Administrators Association ("NASAA") reached agreement on the terms of a model consent order between PMI and the states in which PMI offered loan notes for sale prior to November 2008. The consent order involves payment by PMI of up to an aggregate of $1,000 in penalties, which have been allocated among the states based on PMI's promissory note sale transaction volume in each state prior to November 2008. A state that enters into a consent order receives its portion of the $1,000 in exchange for its agreement to terminate, or refrain from initiating, any investigation of PMI's note sale activities prior to November 2008. Penalties are paid promptly after a state enters into a consent order. NASAA has recommended that each state enter into a consent order. However, no state is obliged to do so, and there is no deadline by which a state must make its decision. PMI is not required to pay any portion of the penalty to those states that do not elect to enter into a consent order. If a state does not enter into a consent order, it is free to pursue its own remedies against PMI, subject to any applicable statute of limitations. As of June 30, 2013, PMI Group has entered into consent orders with thirty-four states and has paid an aggregate of $466 in penalties to those states.

As of June 30, 2013 and December 31, 2012, PMI Group had accrued approximately $248 and $248, respectively, in connection with the contingent liability associated with the states that have not entered into consent orders, in accordance with ASC Topic 450, *Contingencies*. The methodology applied to estimate the accrual was to divide the $1,000 maximum fee pro-rata by state, using PMI's note sales from inception through November 2008. A weighting was then applied by state to each state that has not entered into a consent order, assigning likelihood that the penalty will be claimed. In estimating the probability of a claim being made by a state, PMI Group considered factors such as the standard terms of the consent orders; whether the state ever gave any indication of concern regarding the sale of promissory notes through the platform; the probability of a state electing not to enter into a consent order in order to pursue its own litigation against PMI; whether the penalty is sufficient to compensate a state for the cost of processing the settlement consent order; and finally the impact that current economic conditions have had on state governments. PMI Group will continue to evaluate this accrual and related assumptions as new information becomes known.

In 2008 plaintiffs filed a class action lawsuit ("Hellum Litigation") against PMI and certain of its executive officers and directors in the Superior Court of California, County of San Francisco, California ("Superior Court"). The suit was brought on behalf of all promissory note purchasers on the platform from January 1, 2006 through October 14, 2008. The lawsuit alleged that PMI offered and sold unqualified and unregistered securities in violation of the California and federal securities laws. The lawsuit sought class certification, damages and the right of rescission against PMI and the other named defendants, as well as treble damages against PMI and the award of attorneys' fees, experts' fees and costs, and pre-judgment and post-judgment interest.

As described in Note 13, Subsequent Events, on July 19, 2013 solely to avoid the costs, risks and uncertainties inherent in litigation, and without admitting any liability or wrongdoing, the parties to the Hellum Litigation pending before the Superior Court, entered into a Stipulation and Agreement of Compromise, Settlement, and Release (the "Settlement") setting forth an agreement to settle all claims related thereto. In connection with the Settlement, PMI agreed to pay, and took the charge on the income statement, the plaintiffs an aggregate amount of $10,000, payable into four annual installments of $2,000 in 2013, $2,000 in 2014, $3,000 in 2015 and $3,000 in 2016. The settlement is subject to final approval by the Superior Court. Subject to satisfaction of the conditions set forth in the Settlement, the defendants will be released by the plaintiffs from all claims concerning or arising out of the offering of promissory notes on the platform from January 1, 2006 through October 14, 2008.

As a result of the settlement, PMI recorded a reserve for class action settlement liability of $10,000 in the condensed consolidated balance sheet as of June 30, 2013.

**11. Related Parties**

PMI Group's executive officers, directors who are not executive officers, and certain affiliates participate on PMI Group's lending platform by placing bids and purchasing Notes. The aggregate amount of Notes and Borrower Loans purchased and the income earned by parties deemed to be affiliates and related parties of PMI Group as of June 30, 2013 and 2012 are summarized below:

| Related Party | Aggregate Amount of Borrower Loans and Notes Purchased June 30, | | Income Earned on Borrower Loans and Notes for the six months ended June 30, | |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| Executive officers and management | $722 | $179 | $142 | $8 |
| Directors | 4,323 | 2,930 | 25 | 145 |
| Affiliate | - | 1,161 | - | 61 |
| | $5,045 | $4,270 | $167 | $214 |

The Notes and Borrower Loans were obtained on terms and conditions that were not more favorable than those obtained by other Note and Borrower Loan purchasers. Of the total aggregate amount of Notes and Borrower Loans purchased since inception approximately $308 or 6% and $179 or 4% of principal has been charged off through June 30, 2013 and 2012, respectively. The revenue earned is approximately $9 and $11 in servicing fee revenue related to these Notes and Borrower Loans for the six months ended June 30, 2013 and 2012, respectively.

**12. Post-retirement Benefit Plans**

PMI has a 401(k) plan that covers all employees meeting certain eligibility requirements. The 401(k) plan is designed to provide tax-deferred retirement benefits in accordance with the provisions of Section 401(k) of the Internal Revenue Code. Eligible employees may defer up to 90% of eligible compensation up to the annual maximum as determined by the Internal Revenue Service. PMI's contributions to the plan are discretionary. PMI has not made any contributions to the plan to date.

**13. Subsequent Events**

On July 17, 2013, Kenneth Niewald was appointed Chief Financial Officer of PMI.

On July 19, 2013, PMI agreed to enter into a Stipulation and Agreement of Compromise, Settlement, and Release (the "Settlement") related to the action captioned *Christian Hellum, David Booth, Brian Russom, and Michael del Greco, individually and on behalf of all others similarly situated, v. Prosper Marketplace, Inc., a Delaware Corporation, Christian Larsen, Ed Giedgowd, Kirk T. Inglis, Doug Fuller, James W. Breyer, Larry W. Cheng, Robert C. Kagle, and John and Jane Does 1-100*, No. CGC-08-482329, which is currently pending in the Superior Court. In exchange for a full release of the Claims as to all class members against all defendants, and subject to Court approval, PMI agreed to pay settlement consideration in the total amount of $10,000 according to the following schedule: (i) $2,000 within 10 days of entry of an order by the Court granting preliminary approval of the settlement ("Preliminary Approval"); (ii) $2,000 on the one-year anniversary of Preliminary Approval; (iii) $3,000 on the two-year anniversary of Preliminary Approval; and (iv) $3,000 on the three-year anniversary of Preliminary Approval. See Note 10 *Commitments and Contingencies.*

The 2005 Stock Plan (the "Plan") was amended and restated on July 19, 2013 to increase the maximum aggregate number of shares that may be issued under the Plan from 71,723,081 shares to 94,359,621. On August 1, 2013, a Form S-8 registering the shares reserved for issuance under the Plan was filed with the SEC. On August 5, 2013, the California Department of Business Oversight approved the amendment to qualification of the Plan.

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**Schedule I**

**Prosper Funding LLC**
**Condensed Balance Sheets**
(Unaudited)
(amounts in thousands)

| | June 30, 2013 | December 31, 2012 |
|---|---|---|
| **Assets** | | |
| Cash and Cash Equivalents | $3,510 | $5 |
| Restricted Cash | 4,119 | - |
| Loans Held for Investment at Fair Value | 152 | - |
| Borrower Loans Receivable at Fair Value | 187,125 | - |
| Property and Equipment, net | 1,023 | - |
| Intercompany Receivable | 71 | - |
| **Total Assets** | $196,000 | $5 |
| | | |
| **Liabilities and Member's Equity** | | |
| Accounts Payable | $24 | $- |
| Accrued Liabilities | 1,185 | - |
| Notes at Fair Value | 187,489 | - |
| Loan Loss Reserve | 165 | - |
| **Total Liabilities** | 188,863 | - |
| | | |
| **Member's Equity** | | |
| Member's Equity | 6,075 | 210 |
| Retained Earnings (Accumulated Deficit) | 1,062 | (205) |
| **Total Member's Equity** | 7,137 | 5 |
| **Total Liabilities and Member's Equity** | $196,000 | $5 |

*The accompanying notes are an integral part of these condensed financial statements.*

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**Prosper Funding LLC**
**Condensed Statements of Operations**
(Unaudited)
(amounts in thousands)

| | Three months ended June 30, 2013 | Three months ended June 30, 2012 | Six months ended June 30, 2013 | From February 17, 2012 (date of inception) to June 30, 2012 |
|---|---|---|---|---|
| **Revenues** | | | | |
| Administration Fee Revenue | $1,528 | $- | $2,135 | $- |
| Interest Income on Borrower Loans | 8,578 | - | 13,651 | - |
| Interest Expense on Notes | (8,128) | - | (12,946) | - |
| **Total Revenues** | 1,978 | - | 2,840 | - |
| | | | | |
| **Cost of Revenues** | | | | |
| Cost of Services | (338) | - | (563) | - |
| Provision for Loan Losses | (50) | - | (149) | - |
| **Net revenues** | 1,590 | - | 2,128 | - |
| | | | | |
| **Operating Expenses** | | | | |
| Administration Fee Expense | 631 | - | 1,012 | - |
| Depreciation and Amortization | 124 | - | 207 | - |
| Professional Services | 5 | 17 | 20 | 82 |
| Other Operating Expenses | 50 | - | 94 | 59 |
| **Total Operating Expenses** | 810 | 17 | 1,333 | 141 |
| **Income (Loss) Before Other Income and Expenses** | 780 | (17) | 795 | (141) |
| | | | | |
| **Other Income and Expenses** | | | | |
| Change in FV on Borrower Loans, Loans Held for Investment and Notes, net | 312 | - | 487 | - |
| Other Expense | (14) | - | (15) | - |
| **Total Other Income and Expenses, net** | 298 | - | 472 | - |
| | | | | |
| **Income (Loss) Before Income Taxes** | $1,078 | $(17) | $1,267 | $(141) |
| Provision For Income Taxes | - | - | - | - |
| **Total Net Income (Loss)** | $1,078 | $(17) | $1,267 | $(141) |

*The accompanying notes are an integral part of these condensed financial statements.*

**Prosper Funding LLC**
**Condensed Statements of Cash Flows**
(Unaudited)
(amounts in thousands)

| | Six Months Ended June 30, 2013 | From February 17, 2012 (date of inception) to June 30, 2012 |
|---|---|---|
| **Cash flows from operating activities:** | | |
| Net Income (loss) | $1,267 | $(141) |
| Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities: | | |
| Change in fair value of Notes | (4,573) | – |
| Change in fair value of Borrower Loans | 4,082 | – |
| Depreciation and amortization | 207 | – |
| Loan loss Reserve | 124 | – |
| Change in fair value of Loans held for investment | 3 | – |
| Changes in operating assets and liabilities: | | – |
| Restricted cash | 25 | – |
| Accounts payable and accrued liabilities | 430 | – |
| Net Intercompany Payable | (71) | – |
| Net cash provided by (used in) operating activities | 1,494 | (141) |
| **Cash flows from investing activities:** | | |
| Origination of Borrower Loans held at fair value | (65,053) | – |
| Repayment of Borrower Loans held at fair value | 44,190 | – |
| Purchases of property and equipment | (509) | – |
| Repayment of Loans held for investment at fair value | 49 | – |
| Origination of Loans held for investment at fair value | (29) | – |
| Net cash used in investing activities | (21,352) | – |
| **Cash flows from financing activities:** | | |
| Proceeds from issuance of Notes held at fair value | 65,053 | – |
| Payment of Notes held at fair value | (43,565) | – |
| Net cash included in transfer of assets from PMI | 1,875 | – |
| Proceeds from Member's equity | – | 146 |
| Net cash provided by financing activities | 23,363 | 146 |
| Net increase in cash and cash equivalents | 3,505 | 5 |
| Cash and cash equivalents at beginning of the period | 5 | – |
| Cash and cash equivalents at end of the period | $3,510 | $5 |

*The accompanying notes are an integral part of these condensed financial statements.*

**Prosper Funding LLC**
**Notes to Condensed Financial Statements**
(Unaudited)
(amounts in thousands)

## 1. Organization and Business

Prosper Funding LLC ("Prosper Funding") was formed in the state of Delaware in February 2012 as a limited liability company with the sole equity member being Prosper Marketplace, Inc. ("PMI").

Prosper Funding was formed by PMI to hold borrower loans and issue borrower payment dependent notes through the platform.  Although Prosper Funding is consolidated with PMI for accounting and tax purposes, Prosper Funding has been organized and is operated in a manner that is intended to minimize the likelihood that it would be substantively consolidated with PMI in a bankruptcy proceeding.  Prosper Funding's intention is to minimize the likelihood that its assets would be subject to claims by PMI's creditors if PMI were to file for bankruptcy, as well as to minimize the likelihood that Prosper Funding will become subject to bankruptcy proceedings directly.  Prosper Funding seeks to achieve this by placing certain restrictions on its activities and implementing certain formal procedures designed to expressly reinforce its status as a distinct corporate entity from PMI.

On January 22, 2013, PMI entered into an Asset Transfer Agreement with Prosper Funding (the "Asset Transfer Agreement"), pursuant to which PMI transferred substantially all of its remaining assets to Prosper Funding, including (i) all outstanding notes issued by PMI under the Indenture dated June 15, 2009 between PMI and Wells Fargo Bank, as trustee, (ii) all borrower loans held by PMI, (iii) all lender/borrower/group leader registration agreements related to the notes or the borrower loans, and (iv) all documents and information related to the foregoing, effective February 1, 2013.

Prosper Funding commenced operations as of February 1, 2013 when PMI transferred ownership of the platform, including all of the rights related to the operation of the platform, to Prosper Funding. Since February 1, 2013, all notes issued and sold through the platform are issued, sold and serviced by Prosper Funding (together with the notes transferred from PMI, the "Notes").  Pursuant to a Loan Account Program Agreement between PMI and WebBank, PMI manages the operation of the platform, as agent of WebBank, in connection with the submission of loan applications by potential borrowers, the making of related loans by WebBank and the funding of such loans by WebBank. Pursuant to an Administration Agreement between Prosper Funding and PMI, PMI manages all other aspects of the platform on behalf of Prosper Funding.

All loans requested and obtained through the platform are unsecured obligations of individual borrower members with a fixed interest rate and loan terms set at three or five years as of June 30, 2013. All loans made through the platform are funded by WebBank, an FDIC-insured, Utah chartered industrial bank.  After funding a loan, WebBank sells the loan to Prosper Funding, without recourse to WebBank, in exchange for the principal amount of the loan (together with the borrower loans transferred from PMI, the "Borrower Loans"). WebBank does not have any obligation to purchasers of the Notes.

## 2. Summary of Significant Accounting Policies

### Basis of Presentation

Prosper Funding's unaudited interim condensed financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("US GAAP") and disclosure requirements for interim financial information and the requirements of Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by US GAAP for complete financial statements. The unaudited interim condensed financial statements should be read in conjunction with the audited financial statements and notes thereto for the year ended December 31, 2012. The balance sheet at December 31, 2012 has been derived from the audited financial statements at that date. Management believes these unaudited interim condensed financial statements reflect all adjustments, including those of a normal recurring nature, which are necessary for a fair presentation of the results for the interim periods presented. The results of operations for the interim periods are not necessarily indicative of the results that may be expected for the full year or any other interim period.

**Use of Estimates**

The preparation of Prosper Funding's condensed financial statements in conformity with accounting principles generally accepted in the United States requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities and the related disclosures at the date of the condensed financial statements and the reported amounts of revenues and expenses during the reporting periods. These estimates, judgments and assumptions include but are not limited to the following: valuation of Borrower Loans receivable and associated Notes, valuation allowance on deferred tax assets, valuation and amortization periods of intangible assets, provision for loan loss and contingent liabilities. Prosper Funding bases its estimates on historical experience from all Borrower Loans, and on various other assumptions that it believes to be reasonable under the circumstances. Actual results could differ from those estimates.

**Certain Risks and Concentrations**

In the normal course of its business, Prosper Funding encounters two significant types of risk: credit and regulatory. Financial instruments that potentially subject Prosper Funding to significant concentrations of credit risk consist primarily of cash, cash equivalents, restricted cash and short term investments. Prosper Funding places cash, cash equivalents, restricted cash and short term investments with high-quality financial institutions and is exposed to credit risk in the event of default by these institutions to the extent the amount recorded on the balance sheet exceeds federally insured amounts. Prosper Funding also performs periodic evaluations of the relative credit standing of these financial institutions and has not sustained any credit losses from instruments held at these financial institutions.

To the extent that loan payments are not made, servicing income will be reduced. Borrower Loans were funded by the Notes and repayment of said Notes is wholly dependent on the repayment of the Borrower Loans associated with the Notes. As a result, Prosper Funding does not bear the risk associated with the repayment of principal on loans carried on its condensed balance sheet.

Prosper Funding is subject to various regulatory requirements. The failure to appropriately identify and address these regulatory requirements could result in certain discretionary actions by regulators that could have a material effect on Prosper Funding's financial position and results of operations.

**Cash and Cash Equivalents**

Cash equivalents are recorded at cost, which approximates fair value. Such deposits periodically exceed amounts insured by the FDIC.

**Restricted Cash**

Restricted cash consists primarily of cash deposits required to support operating activities.

**Borrower Loans and Notes**

Prosper Funding has adopted the provisions of ASC Topic 825, *Financial Instruments.* ASC Topic 825 permits companies to choose to measure certain financial instruments and certain other items at fair value on an instrument-by-instrument basis with unrealized gains and losses on items for which the fair value option has been elected reported in earnings. The fair value election, with respect to an item, may not be revoked once an election is made. In applying the provisions of ASC Topic 825, Prosper Funding has recorded assets and liabilities measured using the fair value option in a way that separates these reported fair values from the carrying values of similar assets and liabilities measured with a different measurement attribute. Prosper Funding does not record a specific allowance account related to the Borrower Loans and Notes in which it has elected the fair value option, but rather estimates the fair value of the Borrower Loans and Notes using discounted cash flow methodologies adjusted for historical payment, loss and recovery rates of Borrower Loans. An account is considered to be a loss, or charged-off, when it reaches more than 120 days past due. Prosper Funding has reported the aggregate fair value of the Borrower Loans and Notes as separate line items in the assets and liabilities sections of the accompanying balance sheets using the methods described in ASC Topic 820, *Fair Value Measurements and Disclosures*—See Fair Value Measurement.

Prosper Funding purchases Borrower Loans from WebBank and, if issuing Notes to lender members to fund its purchase of Borrower Loans, holds the Borrower Loans until maturity, except as may otherwise be determined in connection with the servicing of any Borrower Loan. Prosper Funding's obligation to repay the Notes is conditioned upon the repayment of the associated Borrower Loan owned by Prosper Funding. Prosper Funding carries the Borrower Loans and Notes on its balance sheet as assets and liabilities, respectively. Prosper Funding also purchases Borrower Loans from WebBank and immediately sells them to certain qualified lender members.

*Fair Value Measurement*

Prosper Funding follows ASC Topic 820, *Fair Value Measurements and Disclosures*, which provides guidance regarding a fair value hierarchy, which prioritizes information used to measure fair value and the effect of fair value measurements on earnings and provides for enhanced disclosures determined by the level within the hierarchy of information used in the valuation. ASC Topic 820 applies whenever other standards require (or permit) assets or liabilities to be measured at fair value but does not expand the use of fair value in any new circumstances.

ASC Topic 820 defines fair value in terms of the price that would be received upon the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The price used to measure the fair value is not adjusted for transaction costs while the cost basis of certain financial instruments may include initial transaction costs. Under ASC Topic 820, the fair value measurement also assumes that the transaction to sell an asset occurs in the principal market for the asset or, in the absence of a principal market, the most advantageous market for the asset. The principal market is the market in which the reporting entity would sell or transfer the asset with the greatest volume and level of activity for the asset. In determining the principal market for an asset or liability under ASC Topic 820, it is assumed that the reporting entity has access to the market as of the measurement date. If no market for the asset exists or if the reporting entity does not have access to the principal market, the reporting entity should use a hypothetical market.

Under ASC Topic 820, assets and liabilities carried at fair value in the balance sheets are classified among three levels based on the observability of the inputs used to determine fair value:

Level 1 — The valuation is based on quoted prices in active markets for identical instruments.

Level 2 — The valuation is based on observable inputs such as quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3 — The valuation is based on unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the instrument. Level 3 valuations are typically performed using pricing models, discounted cash flow methodologies, or similar techniques, which incorporate management's own estimates of assumptions that market participants would use in pricing the instrument or valuations that require significant management judgment or estimation.

Fair value of financial instruments are determined based on the fair value hierarchy established in ASC Topic 820, which requires an entity to maximize the use of quoted prices and observable inputs and to minimize the use of unobservable inputs when measuring fair value. Various valuation techniques are utilized, depending on the nature of the financial instrument, including the use of market prices for identical or similar instruments, or discounted cash flow models. When possible, active and observable market data for identical or similar financial instruments are utilized. Alternatively, fair value is determined using assumptions that management believes a market participant would use in pricing the asset or liability.

Financial instruments consist principally of cash and cash equivalents, restricted cash, short term investments, Borrower Loans receivable, accounts payable and accrued liabilities, Notes and long-term debt. The estimated fair values of cash and cash equivalents, restricted cash, accounts payable and accrued liabilities approximate their carrying values because of their short term nature.

Borrower Loans and Notes are accounted for on a fair value basis.

**Internal Use Software and Website Development**

Internal use software costs and website development costs are accounted for in accordance with ASC Topic 350-40, *Internal Use Software*, and ASC Topic 350-50, *Website Development Cost*s. In accordance with ASC Topic 350-40 and 350-50, the costs to develop software for Prosper Funding's website and other internal uses are capitalized when management has authorized and committed project funding, preliminary development efforts are successfully completed, and it is probable that the project will be completed and the software will be used as intended. Capitalized software development costs primarily include software licenses acquired, fees paid to outside consultants, salaries and payroll related costs for PMI employees directly involved in the development efforts.

Costs incurred prior to meeting these criteria, together with costs incurred for training and maintenance, are expensed. Costs incurred for upgrades and enhancements that are considered to be probable to result in additional functionality are capitalized. Capitalized costs are included in property and equipment and amortized to expense using the straight-line method over their expected lives. Prosper Funding evaluates its software assets for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Recoverability of software assets to be held and used is measured by a comparison of the carrying amount of the asset to the future net undiscounted cash flows expected to be generated by the asset. If such software assets are considered to be impaired, the impairment to be recognized is the excess of the carrying amount over the fair value of the software asset.

**Loan Loss Reserve**

Prosper Funding is obligated to indemnify lenders and or repurchase certain Notes sold to the lenders in the event of violation of applicable federal, state, or local lending laws, or verifiable identify theft. The loan loss reserve is estimated based on historical experience and is accrued when the Notes are issued. Indemnified or repurchased Notes are written off at the time of repurchase or at the time an indemnification payment is made.

**Revenue Recognition**

Revenue is recognized in accordance with ASC Topic 605, *Revenue Recognition*. Revenue is recognized when persuasive evidence of an arrangement exists, services have been rendered, the price of the services is fixed and determinable, and collectability is reasonably assured.

*Administration Agreement License Fees*

Prosper Funding primarily generates revenues through license fees it earns through an Administration Agreement with PMI. The Administration Agreement contains a license granted by Prosper Funding to PMI that entitles PMI to use the platform for and in relation to: (i) PMI’s performance of its duties and obligations under the Administration Agreement relating to corporate administration, loan platform services, loan and note servicing and marketing, and (ii) PMI’s performance of its duties and obligations to WebBank in relation to loan origination and funding.

*Loan Servicing Fees*

Loan servicing fees are accrued daily based on the current outstanding loan principal balance of the Borrower Loan but are not recognized until payment is received due to the uncertainty of collection of borrower loan payments.

*Interest Income on Borrower Loans Receivable and Interest Expense on Notes*

Interest income on Borrower Loans is recognized using the accrual method based on the stated interest rate to the extent that is believed it to be collectable. Interest expense is recorded on the corresponding Notes based on the contractual interest rate. Below is a table that summarizes the gross interest income and expense for the three and six months ended 2013 and 2012.

| | Three months ended June 30, | | Six months ended June 30, | From February 17, 2012 (date of inception) to June 30, |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| Interest Income on Borrower Loans | $8,578 | $- | $13,651 | $- |
| Interest Expense on Notes | (8,128) | - | (12,946) | - |
| Net Interest Income (Expense) on Loans & Notes | $450 | $- | $705 | $- |

**Comprehensive Income**

There is no comprehensive income (loss) other than the net income (loss) disclosed in the condensed statement of operations.

**Recent Accounting Pronouncements**

There have been no recent accounting pronouncements or changes in accounting pronouncements during the six months ended June 30, 2013 that are of significance, or potential significance.

**3. Borrower Loans and Notes Held at Fair Value**

The following tables present the assets and liabilities measured at fair value on a recurring basis at June 30, 2013.

| June 30, 2013 | Level 1 Inputs | Level 2 Inputs | Level 3 Inputs | Fair Value |
|---|---|---|---|---|
| **Assets** | | | | |
| Borrower Loans receivable | $- | $- | $187,125 | $187,125 |
| Loans held for investment | - | - | 152 | 152 |
| **Liabilities** | | | | |
| Notes | $- | $- | $187,489 | $187,489 |

As observable market prices are not available for the Borrower Loans and Notes Prosper Funding holds, or for similar assets and liabilities, the Prosper Funding believes the Borrower Loans and Notes should be considered Level 3 financial instruments under ASC Topic 820. In a hypothetical transaction as of the measurement date, Prosper Funding believes that differences in the principal marketplace in which the loans are originated and the principal marketplace in which it might offer those loans may result in differences between the originated amount of the loans and their fair value as of the transaction date. For Borrower Loans, the fair value is estimated using discounted cash flow methodologies based upon valuation assumptions including prepayment speeds, roll rates, recovery rates and discount rates based on the perceived credit risk within each credit grade.

The obligation to pay principal and interest on any Note is equal to the loan payments, if any, that are received on the corresponding Borrower Loan, net of its servicing fee. The fair value election for Notes and Borrower Loans allows both the assets and the related liabilities to receive similar accounting treatment for expected losses which is consistent with the subsequent cash flows to lenders that are dependent upon borrower payments. As such, the fair value of the Notes is approximately equal to the fair value of the Borrower Loans, adjusted for the servicing fee and the timing of borrower payments subsequently disbursed to Note holders. Any unrealized gains or losses on the Borrower Loans and Notes for which the fair value option has been elected is recorded as a separate line item in the statement of operations. The effective interest rate associated with the Notes is less than the interest rate earned on the Borrower Loans due to the servicing fee. See further in this note for a roll-forward and further discussion of the significant assumptions used to value Borrower Loans and Notes.

The fair value of the Notes and Borrower Loans are estimated using discounted cash flow methodologies based upon a set of valuation assumptions. The main assumptions used to value the Borrower Loans and Notes include prepayment rates derived from historical prepayment rates for each credit score, default rates derived from historical performance, recovery rates and discount rates applied to each credit tranche based on the perceived credit risk of each credit grade. The obligation to pay principal and interest on any Note is equal to the loan payments, if any, received on the corresponding Borrower Loan, net of the servicing fee. As such, the fair value of the Notes is approximately equal to the fair value of the Borrower Loans, adjusted for the servicing fee and the timing of borrower payments subsequently disbursed to the Note holders. The effective interest rate associated with the Notes will be less than the interest rate earned on the Borrower Loans due to the servicing fee.

For Borrower Loans originated and Notes, the following average assumptions were used to determine the fair value as of June 30, 2013:

| | |
|---|---|
| Monthly prepayment rate speed | 1.53% |
| Recovery rate | 2.60% |
| Discount rate * | 10.50% |

* This is the average discount rate among all of the credit grades

The changes in Level 3 assets measured at fair value on a recurring basis are as follows:

**Fair Value Measurements Using Significant Unobservable Inputs (Level 3)**

| | Borrower Loans | Notes | Loans Held for Investment | Total |
|---|---|---|---|---|
| Balance at January 1, 2013 | $- | $- | $- | $- |
| Assets transferred on February 1, 2013 | 170,344 | (170,574) | 175 | (55) |
| Originations | 65,053 | (65,053) | 29 | 29 |
| Principal repayments and credit losses | (44,190) | 43,565 | (49) | (674) |
| Change in fair value on Borrower Loans and Notes | (4,082) | 4,573 | - | 491 |
| Change in fair value of loans held for investment | - | - | (3) | (3) |
| Balance at June 30, 2013 | $187,125 | $(187,489) | $152 | $(212) |

Due to the recent origination of the Borrower Loans and Notes, the change in fair value attributable to instrument-specific credit risk is immaterial. Prosper Funding had no outstanding Borrower Loans or Notes originated or issued prior to July 13, 2009. Of the Borrower Loans originated from July 13, 2009 to June 30, 2013, 255 loans, which were 90 days or more delinquent, totaled an aggregate principal amount of $1,349 and a fair value of $122 as of June 30, 2013.

No other assets or other liabilities were carried at fair value as of June 30, 2013.

**4. Loans Held for Investment at Fair Value**

As of June 30, 2013, Prosper Funding retained a total of $152 of loans originated through the platform. When a borrower member loan has been funded in whole, or in part, by Prosper Funding, Prosper Funding retains the portion of the borrower's monthly loan payment that corresponds to the percentage of the loan that Prosper Funding funded. In these cases, Prosper Funding records interest income on these loans.

**Fair Value Measurements Using Significant Unobservable Inputs (Level 3)**

| | Loans Held for Investment |
|---|---|
| Balance at January 1, 2013 | $- |
| Assets transferred on February 1, 2013 | 175 |
| Originations | 29 |
| Principal repayments and credit losses | (49) |
| Change in fair value of loans held for investment | (3) |
| Balance at June 30, 2013 | $152 |

Prosper Funding estimates the fair value of the Borrower Loans held for investment using discounted cash flow methodologies based upon a set of valuation assumptions similar to those of all Borrower Loans, which are set forth in Note 3, as they have similar characteristics and Prosper Funding expects these Borrower Loans to behave in a comparable manner. The valuation assumptions Prosper Funding used to value these Borrower Loans include prepayment rates, default rates and recovery rates derived from historical loan performance data and discount rates based on credit grade applied to each loan.

The fair value adjustment on these Borrower Loans held for investment was $3, which is included in earnings for the six months ended June 30, 2013. As of June 30, 2013 Prosper Funding had received $184 in payments on these Borrower Loans. As of June 30, 2013, there was $36 in Borrower Loans held for investment that were charged-off.

**5. Loan Loss Reserve**

Changes in Prosper Funding's loan loss reserve are summarized below:

| | |
|---|---|
| Balance at January 1, 2013: | $- |
| Assets transferred on February 1, 2013 | 41 |
| Provision for loan loss | 124 |
| Balance at June 30, 2013: | $165 |

**6. Member's Equity**

Prosper Funding is a wholly owned subsidiary of PMI and PMI has made all capital infusions related to the formation and initial operating expenses of Prosper Funding LLC.

**7. Subsequent Events**

Prosper Funding has evaluated subsequent events for disclosure and recognition and noted no matters that require disclosure herein.

**Item 2.**

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION

*This management's discussion and analysis of consolidated financial condition and results of operations, or MD&A, contains forward-looking statements that involve risks and uncertainties. Please see "Forward-Looking Statements" in this Quarterly Report on Form 10-Q for a discussion of the uncertainties, risks and assumptions associated with these statements. This discussion should be read in conjunction with PMI Group's historical condensed consolidated financial statements and related notes thereto, Prosper Funding's condensed financial statements and related notes thereto and the other disclosures contained elsewhere in this Quarterly Report on Form 10-Q. The results of operations for the periods reflected herein are not necessarily indicative of results that may be expected for future periods, and PMI Group's consolidated actual results may differ materially from those discussed in the forward-looking statements as a result of various factors, including but not limited to those included elsewhere in this Quarterly Report on Form 10-Q and those included in the "Risk Factors" section and elsewhere in PMI Group's Annual Report on Form 10-K.*

**PROSPER MARKETPLACE, INC.**
(in thousands, except for share and per share amounts)

### Overview

Prosper Marketplace, Inc. ("PMI") developed and began operating a peer-to-peer online credit platform (the "platform") in 2006 that permitted its borrower members to apply for loans and lender members to purchase notes issued by PMI, the proceeds of which facilitated the funding of specific loans to borrowers. On February 1, 2013, PMI transferred ownership of the platform, including all of the rights related to the operation of the platform, to its wholly-owned subsidiary, Prosper Funding LLC ("Prosper Funding" and, collectively with PMI, the "PMI Group"). Beginning February 1, 2013, all notes issued and sold through the platform are issued, sold and serviced by Prosper Funding (together with the notes transferred to Prosper Funding, the "Notes"). Pursuant to an Administration Agreement between PMI and Prosper Funding, PMI manages all aspects of the platform on behalf of Prosper Funding. Pursuant to a Loan Account Program Agreement between PMI and WebBank, PMI manages the operation of the platform, as agent of WebBank, in connection with the submission of loan applications by potential borrowers, the making of related loans by WebBank and the funding of such loans by WebBank.

The platform enables borrower members to request and obtain personal, unsecured loans (together with the notes transferred to Prosper Funding, the"Borrower Loans") by posting anonymous "listings" on the platform indicating the principal amount of the desired loan. PMI assigns a Prosper Rating consisting of letter grades, based in part on the borrower's credit score, to each member who requested a borrower loan. Borrower members' Prosper Rating, credit score range, debt-to-income ratios and other credit data are displayed with their listings and are available for viewing by lender members on an anonymous basis.

Listings are automatically allocated to one of two lender member funding channels, based upon a random allocation methodology: (i) the first channel allows lender members to commit to purchase Notes from Prosper Funding, the payments of which are dependent on the payments made on the corresponding Borrower Loan (the "Note Channel"); and (ii) the second channel allows lender members to commit to purchase 100% of a Borrower Loan directly from Prosper Funding (the "Whole Loan Channel"). The random allocation methodology ensures that there is a fair initial distribution of listings between the two channels. If, however, a listing is not funded through the Whole Loan Channel within the first hour of its posting, the listing will be removed from the Whole Loan Channel and posted to the Note Channel for the remainder of its listing period. Such listing will include a designation indicating that it came from the Whole Loan Channel. The Whole Loan Channel was launched in April 2013 and is only available to certain accredited investor and institutional lender members and is becoming a growing part of Prosper Funding's business. Lender members who participate in the Whole Loan Channel are required to enter into a purchase and servicing agreement with Prosper Funding that specifies the parties' rights and obligations with regard to the sale of Borrower Loans through the Whole Loan Channel and which names Prosper Funding the servicer of such loans.

Borrower Loans originated to borrower members are made by WebBank, an FDIC-insured, Utah-chartered industrial bank, and sold to Prosper Funding. WebBank sells the loan to Prosper Funding, without recourse to WebBank, in exchange for the principal amount of the Borrower Loan. WebBank does not have any obligation to the purchasers of the Notes or subsequent purchasers of the Borrower Loans. PMI verifies the identity of 100% of borrowers using a variety of methods including credit bureau data, other electronic data sources and offline documentary procedures. PMI verifies income and/or employment on a subset of borrowers based on a proprietary algorithm. The intention of the algorithm is to verify income or employment in cases where the self-reported income of the borrower is highly determinative of the borrower's risk rating.

Prior to February 1, 2013, PMI derived operating revenue from WebBank. Upon funding a Borrower Loan, WebBank charged the borrower an origination fee equal to a specified percentage of the principal amount of such Borrower Loan. WebBank, in turn, paid PMI amounts equal to the origination fees as compensation for loan origination activities. PMI also charged lender members a servicing fee equal to an annualized rate set at a percentage of the outstanding principal balance of the corresponding Borrower Loan, which PMI deducted from each lender member's share of the Borrower Loan payments.

As of February 1, 2013, concurrent with transfer of the platform, PMI continues to receive origination fees directly from WebBank as compensation for its loan origination activities, while PFL charges the servicing fees to lender members. PMI derives additional revenue from the fees it receives from Prosper Funding for the services it provides pursuant to the Administration Agreement. Prosper Funding has agreed to compensate PMI for its various roles and related services under the Administration Agreement including corporate administration, loan platform servicing, and loan and note servicing fees. Prosper Funding primarily generates revenues through license fees it earns through the Administration Agreement with PMI and the servicing fee it charges lender members.

**Operating History**

The platform was launched on February 13, 2006 and enables borrower members to request and obtain personal, unsecured loans between $2 and $35 by posting anonymous "listings" indicating the principal amount of the desired loan. Borrower Loan terms are subject to minimum and maximum loan amounts determined by the borrower's Prosper Score created using proprietary models that include numerous factors, at interest rates set by PMI. Interest rates are set for borrower loans based on a Prosper Score, as well as additional factors, such as estimated loss rate, loan terms, general economic environment, previous loans obtained through the platform and competitive conditions. As of June 30, 2013, the platform had facilitated 78,195 Borrower Loans since its launch totaling an aggregate principal amount of approximately $549,997. The platform has a limited operating history and PMI has incurred net losses since its inception. Our net loss was $15,653 and $3,257 for the three months ended June 30, 2013 and 2012, respectively and $19,852 and $7,621 for the six months ended June 30, 2013 and 2012, respectively.

PMI Group funds its operations primarily with proceeds from equity financings, which are described below under "Liquidity and Capital Resources." The operating plan calls for a continuation of the current strategy of increasing borrower and lender transaction volume and improving the efficiency of the platform to increase revenue until profitability is reached.

**Trends and Uncertainties**

The peer-to-peer lending industry remains a very innovative and unique industry, and the application of federal and state laws in areas such as securities and consumer finance to the industry is still evolving. PMI Group will continue to monitor this evolution actively in order to identify and respond quickly to any legislative or regulatory developments that may affect the platform.

During the first half of 2013, the platform increased its origination and funding volume consistently in terms of both units and total dollar amounts. PMI Group hopes to continue this trend of growth as both the borrower and lender bases continue to strengthen and become more familiar with the platform. Over time PMI Group expects the lender base to grow as the platform gains more exposure to potential lenders and establishes PMI Group Notes as a viable investment alternative.

In February 2012, PMI formed Prosper Funding to hold Borrower Loans and issue Notes. Prosper Funding has been organized and operates in a manner that is intended to minimize the likelihood that Prosper Funding would be substantively consolidated with PMI in a bankruptcy proceeding. PMI is the sole equity member of Prosper Funding. Prosper Funding commenced operations on February 1, 2013.

**Critical Accounting Policies and Estimates**

Management's discussion and analysis of the consolidated financial condition and results of operations is based on the condensed consolidated financial statements, which has prepared in accordance with U.S. generally accepted accounting principles. The preparation of condensed consolidated financial statements requires management to make estimates, judgments and assumptions that affect the reported amounts of assets and liabilities, revenues and expenses and the related disclosures. Estimates are based on historical experience and on various other assumptions that PMI Group believes to be reasonable under the circumstances. Actual results could differ from those estimates. Significant accounting policies which include revenue recognition, stock-based compensation, provision for loan losses and income taxes are more fully described in Note 2 to Prosper Marketplace, Inc.'s condensed consolidated financial statements included elsewhere in this quarterly report.

Critical accounting policies are those policies that PMI Group believes present the most complex or subjective measurements and have the most potential to impact its financial position and operating results. While all decisions regarding accounting policies are important, the PMI Group believes that the following policies could be considered critical.

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***Fair Value Measurement***

PMI Group determines the fair values of its financial instruments based on the fair value hierarchy established in Accounting Standards Codification ("ASC") Topic 820, *Fair Value Measurements and Disclosures*, which requires an entity to maximize the use of quoted prices and observable inputs and to minimize the use of unobservable inputs when measuring fair value. PMI Group uses various valuation techniques depending on the nature of the financial instrument, including the use of market prices for identical or similar instruments, or discounted cash flow models. When possible, active and observable market data for identical or similar financial instruments are utilized. Alternatively, PMI Group determines fair value using assumptions that it believes a market participant would use in pricing the asset or liability.

The estimated fair values of cash and cash equivalents, restricted cash, accounts payable and accrued liabilities approximate their carrying values because of their short-term nature. Short term investments, Borrower Loans held for investment, Borrower Loans, and Notes are accounted for on a fair value basis. For additional information and discussion regarding significant accounting policies surrounding fair value measurement, see Note 2, Note 3 and Note 4 to Prosper Marketplace, Inc.'s condensed consolidated financial statements included elsewhere in this quarterly report.

***Borrower Loans and Notes***

Overall, if the fair value of the Borrower Loans decrease or increase due to any changes in the PMI Group's assumptions, there will also be a corresponding decrease or increase in the fair value of the linked Notes. As a result, the effect on the PMI Group's earnings of adverse changes in key assumptions is mitigated.

As the PMI Group receives scheduled payments of principal and interest on the Borrower Loans it in turn makes principal and interest payments on the Notes. These principal payments reduce the carrying value of the Borrower Loans and Notes. If the PMI Group does not receive payments on the Borrower Loans, the PMI Group is not obligated to and does not make payments on the Notes. The fair value of a Note is approximately equal to the fair value of the corresponding Borrower Loan, less the service fee. If the fair value of the Borrower Loan decreases due to the PMI Group's expectation regarding both the likelihood of default of the loan and the amount of loss in the event of default, there is also a corresponding decrease in the fair value of the Note (an unrealized gain related to the Note and an unrealized loss related to the Borrower Loan).

Key economic assumptions and the sensitivity of the current fair value to immediate adverse changes in those assumptions at June 30, 2013 for Borrower Loans and Notes are presented in the following table:

| | Borrower Loans | Notes |
|---|---|---|
| **Discount rate assumption:** | 10.50% | 10.50% |
| Decrease in fair value and income (loss) to earnings from: | | |
| 100 basis point increase | $186,043 | $183,829 |
| 200 basis point increase | 183,991 | 181,796 |
| Increase in fair value and income (loss) to earnings from: | | |
| 100 basis point decrease | $190,309 | $188,056 |
| 200 basis point decrease | 192,528 | 190,254 |
| | | |
| **Default rate assumption:** | | |
| Decrease in fair value and income (loss) to earnings from: | | |
| 10% higher default rates | $186,061 | $183,850 |
| 20% higher default rates | 183,733 | 181,546 |
| Increase in fair value and income (loss) to earnings from: | | |
| 10% lower default rates | $190,172 | $187,917 |
| 20% lower default rates | 192,184 | 189,908 |

For additional information and discussion, see Note 2 and Note 3 to Prosper Marketplace, Inc.'s condensed consolidated financial statements included elsewhere in this quarterly report.

**Results of Operations**

**Revenues**

***Origination Fees***

The PMI Group charges an origination fee equal to a specified percentage of the aggregate principal balance of the Borrower Loan based on the Prosper Rating and terms of the loan. Origination fees are charged by WebBank and the PMI Group receives amounts equal to those fees as compensation for marketing and underwriting activities.

Prior to April 2012, the PMI Group maintained a single origination fee of 0.50% for AA loans, 3.95% for loans rated A or B and 4.95% for loans rated C to HR . In April 2012, the schedule was updated to include the loan terms when determining loan origination fees.

| | Jan - Apr 2012 | Apr 2012 - May 2013 | | |
|---|---|---|---|---|
| Prosper Rating | All Loans | 1 Year Loan * | 3 Year Loan | 5 Year Loan |
| AA | 0.50% | 0.50% | 1.95% | 4.95% |
| A | 3.95% | 1.95% | 3.95% | 4.95% |
| B | 3.95% | 2.95% | 4.95% | 4.95% |
| C - HR | 4.95% | 3.95% | 4.95% | 4.95% |

* In April 2013, we stopped offering 1 year loans with no change to 3 year loan or 5 year loan origination fee structure.

In May 2013, the schedule was updated to reflect an origination fee range based on credit profile of the lowest risk customers:

| | May 2013 - Jun 2013 | |
|---|---|---|
| Prosper Rating | 3 Year Loan | 5 Year Loan |
| AA | 1.00% - 1.95% | 1.95% - 4.95% |
| A | 3.95% | 4.95% |
| B | 4.95% | 4.95% |
| C - HR | 4.95% | 4.95% |

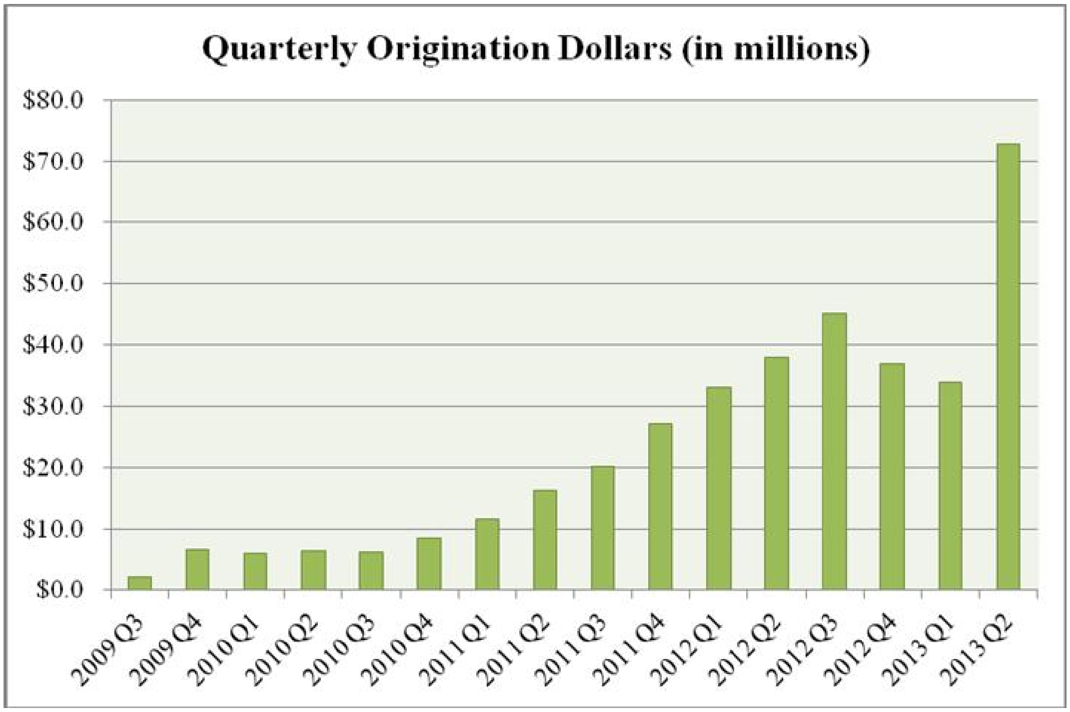
Origination fees for the three months ended June 30, 2013 and 2012 were $3,342 and $1,757, respectively, representing an increase of $1,585, or 90%, which was primarily due to the PMI Group's higher origination volume during 2013. Origination fees for the six months ended June 30, 2013 and 2012 were $4,914 and $3,139, respectively, representing an increase of $1,775, or 57%, which was primarily due to the PMI Group's higher origination volume during 2013.

***Origination Volume***

From inception to June 30, 2013, the PMI Group has originated a total of 78,195 in borrower loans totaling $549,997.

The PMI Group originated 7,099 Borrower Loans totaling $72,777 during the second quarter of 2013, compared to 5,061 Borrower Loans totaling $38,010 originated during the second quarter of 2012. This represented a "unit" or loan, increase of 40.3% and a dollar increase of 91.5% over the corresponding periods in 2012.

The PMI Group originated 10,715 Borrower Loans totaling $106,720 during the first six months of 2013, compared to 9,496 Borrower Loans totaling $71,074 originated during the first six months of 2012. This represented a "unit" or loan, increase of 13% and a dollar increase of 50% over the corresponding periods in 2012.




The increase in volume experienced in the second quarter of 2013 is primarily related to marketing efforts focused on bringing in new lenders and borrowers. In January 2013, PMI Group announced bankruptcy remoteness covering all lenders. In February 2013 there was an equity financing along with a new management team. Lenders, liquidity and loan originations have increased since these announcements. In the second quarter of 2013, PMI Group increased marketing campaigns to attract new borrowers and introduced the whole loan product, which in turn, has increased loan origination volumes. The decrease that occurred between Q3 2012 and Q1 2013 was due to lack of liquidity.

***Interest Income on Borrower Loans and Interest Expense on Notes***

The PMI Group recognizes interest income on Borrower Loans using the accrual method based on the stated interest rate to the extent that they believe it to be collectable. The PMI Group records interest expense on the corresponding Note based on the contractual interest rate.

The following table summarizes interest income on borrower loans and interest expense on notes for the three and six months ended June 30, 2013 and 2012.

| | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|
| | **2013** | **2012** | **2013** | **2012** |
| Interest Income on Borrower Loans | $8,578 | $5,780 | $16,309 | $10,410 |
| Interest Expense on Notes | (8,128) | (5,499) | (15,453) | (9,902) |
| Net Interest Income | $450 | $281 | $856 | $508 |

Increases in interest income on Borrower Loans and interest expense on Notes is driven by the increase in the amount of loans that the PMI Group originated through the platform for the three and six months ended June 30, 2013 and 2012.

***Rebates and Promotions***

Rebates and promotions are accounted for in accordance with ASC Topic 605, *Revenue Recognition*. From time to time, rebates and promotions are offered to its borrower and lender members. Rebates and promotions are recorded as an offset to revenue if a particular rebate or promotion was earned directly upon the origination of the loan. Rebates and promotions are generally in the form of cash back and other incentives paid to lenders and borrowers.

For the three months ended June 30, 2013 and 2012, the PMI Group incurred expenses related to rebates and promotions extended to borrowers and lenders of $387 and $265, respectively, which represented an increase of $122 or 46%. For the six months ended June 30, 2013 and 2012, the PMI Group incurred expenses related to rebates and promotions extended to borrowers and lenders of $662 and $549, respectively, which represented an increase of $113 or 20%.

**Cost of Revenues**

***Cost of Services***

Cost of services consists primarily of credit bureau fees, payments which are due to strategic partners, collection expenses, and other expenses directly related to loan originations, funding and servicing. Cost of services expenses were $500 and $345 for the three months ended June 30, 2013 and 2012, respectively, representing an increase of 45%. Cost of services expenses were $982 and $681 for the six months ended June 30, 2013 and 2012, respectively, representing an increase of 44%. The primary driver for the increase was due to an increase in strategic partnership fees due to the renegotiation of the PMI Group's contract with WebBank.

***Provision for Loan Loss***

Under the terms of the Notes and Lender Registration Agreements, the PMI Group may, in certain circumstances, become obligated to repurchase a Note from a lender or indemnify a lender against loss on a Note. Generally these circumstances include the occurrence of verifiable identity theft, the failure to properly follow loan listing or bidding protocols, and a violation of the applicable federal/state/local lending laws. The provision for loan loss is evaluated at least once a quarter and represents an estimate based on the rate of historical loan losses as a percentage of originations (which generally occur within six to nine months of origination). The provision for loan loss may include a judgmental management adjustment due to the limited operating history, changes in current economic conditions, the risk of new and as of yet undetected fraud schemes, origination unit and dollar volumes and the lack of industry comparables. Based on the analysis of the historical provision, the Note provision for loan loss was $50 and $8 for the three months ended June 30, 2013 and 2012, respectively. The provision for loan loss was $177 and $11 for the six months ended June 30, 2013 and 2012, respectively.

**Other Income and Expenses**

***Change in Fair Value of Borrower Loans and Notes, net***

The total fair value adjustment was $4,082 and $4,573 for Borrower Loans and Notes, respectively, resulting in a net unrealized loss of $491 for the six months ended June 30, 2013. The total fair value adjustment was $1,060 and $532 for Borrower Loans and Notes, respectively, resulting in a net unrealized loss of $528 for the six months ended June 30, 2012. These amounts are included as a component of other income (expense) in the PMI Group's condensed consolidated statement of operations.

***Insurance Recoveries***

PMI and certain of its executive officers and directors were the subject of a class action lawsuit brought on behalf of all promissory note purchasers on the platform from January 1, 2006 through October 14, 2008 that alleged that PMI offered and sold unqualified and unregistered securities in violation of the California and federal securities law. During the first quarter of 2011 the Superior Court of California issued a final statement of decision finding that Greenwich Insurance Company, PMI's insurance carrier with respect to the class action lawsuit, had a duty to defend the suit and requiring that Greenwich pay PMI's past and future defense costs in the suit up to $2,000. During 2011, Greenwich made aggregate payments to PMI in the amount of $2,000 to reimburse PMI for the defense costs it had incurred in the class action suit. On October 2, 2012, Greenwich made an additional payment of $143 to PMI for pre-judgment interest. Please see Note 10 *Commitments and Contingencies* in the notes to Prosper Marketplace, Inc.'s condensed consolidated financial statements contained elsewhere in this quarterly report.

***Other Income***

Other income consists primarily of credit referral fees, where partner companies pay the PMI Group an agreed upon amount for referrals of customers from the website. Other income was $271 for the three months ended June 30, 2013 versus $43 at June 30, 2012, which represented an increase of 530%. Other income was $414 for the six months ended June 30, 2013 versus $91 at June 30, 2012, which represented an increase of 355%. The increase in credit referrals during these periods was due to the addition of new partners as well as increased traffic to existing credit referral partners.

**Operating Expenses**

All employees of the PMI Group are employed by PMI. Compensation and benefits expense were $3,270 and $5,775 for the three and six months ended June 30, 2013, respectively. In comparison, compensation and benefits expense were $2,350 and $4,807 for the three and six months ended June 30, 2012, respectively. The increase of $920 for the three months and $968 for the six months was largely due to PMI's steadily increasing its employee headcount, which in turn resulted in increased payroll costs such as salary and wages, payroll taxes, healthcare, and accrued vacation. PMI increased its headcount across its marketing and operations during this period in response to increased volume demands. PMI intends to continue to increase headcount as the platform's lender and borrower bases grow and PMI carries out its business plan; however, PMI expects its ongoing investment in the platform and website to improve operating expense efficiency going forward. In addition, spending increased related to the use of contract labor, bonus expense, variable pay expense and overtime during 2013 over the corresponding periods in 2012. During 2013, PMI experienced a decrease in the amount of salaries capitalized related to the development of internal use software which contributed to the overall increase in compensation and benefits.

As of June 30, 2013, PMI had 75 full-time employees compared to 70 full-time employees as of June 30, 2012.

| | June 30, 2013 | June 30, 2012 |
|---|---|---|
| Sales, Marketing and Customer Service | 39 | 31 |
| Engineering | 23 | 25 |
| Administration | 13 | 14 |
| **Total Headcount** | **75** | **70** |

Marketing and advertising costs consist primarily of affiliate marketing, search engine marketing, online and offline campaigns, email marketing, public relations, and direct mail marketing. Marketing and advertising costs were $3,878 and $1,127 for the three months ended June 30, 2013 and 2012, respectively, representing an increase of 244% Marketing and advertising costs were $5,451 and $2,401 for the six months ended June 30, 2013 and 2012, respectively, representing an increase of 127%. This increase was largely due to increased efforts with various marketing programs in order to increase borrower volume. The PMI Group placed an increased emphasis on direct mail marketing campaigns in order to increase its brand awareness and drive borrower volume. Affiliate marketing expense is deployed through direct partnerships with other websites that send qualified individuals seeking loan options to the platform. Increased costs associated with search engine marketing are specifically related to increased volume and systematic testing to attract new borrowers through search engines. Each marketing effort is measured, analyzed and optimized to improve scale and efficiency. Through optimization of our marketing efforts, we will shift marketing costs to more efficient channels to balance the mix of growth and efficiency in its marketing activities in subsequent quarters.

Depreciation and amortization expense was $208 and $168 for the three months ended June 30, 2013 and 2012, representing an increase of 24% compared to the prior year period. Depreciation and amortization expense was $413 and $326 for the six months ended June 30, 2013 and 2012, representing an increase of 27% compared to the prior year period. The increase in overall depreciation and amortization expense was primarily due to the capitalization of various internally developed software projects placed in service in 2012, which in turn increased depreciation expense taken on those assets during the three and six months ended June 30, 2013.

**General and Administrative Expenses**

Professional service expenses are comprised of legal expenses, audit and accounting fees, consulting services and other outside costs. Professional service expenses were $694 and $639 for the three months ended June 30, 2013 and 2012, respectively, representing an increase of 9%. Professional service expenses were $1,382 and $1,633 for the six months ended June 30, 2013 and 2012, respectively, representing a decrease of 15%. This change was primarily due to an increase in legal fees related to activity in the PMI class action lawsuit and consulting fees.

Facilities and maintenance expenses consist primarily of rent paid for the PMI Group's corporate office lease and data co-location facility, network and power usage costs, software licenses and subscriptions, and hardware and software maintenance and support. Facilities and maintenance expenses were $481 and $301 for the three months ended June 30, 2013 and 2012, respectively. Facilities and maintenance expenses were $794 and $625 for the six months ended June 30, 2013 and 2012, respectively.

PMI recorded a reserve for class action settlement liability of $10,000 in the condensed consolidated statements of operations for the three and six months ended June 30, 2013.

Other general and administrative expenses consist of bank service charges, NASAA state penalty settlement expenses, travel and entertainment expenses, taxes and licenses costs, communications costs, recruiting costs and other miscellaneous expenses. Other general and administrative expenses were $499 and $381 for the three months ended June 30, 2013 and 2012, respectively, representing an increase of 31%. Other general and administrative expenses were $825 and $850 for the six months ended June 30, 2013 and 2012, respectively, representing a decrease of 2.9%. This change is primarily due to lower recruiting costs offset by higher license costs.

**Liquidity and Capital Resources**

The following table summarizes the cash flow for the six months ended June 30, 2013 and 2012, respectively:

| | For the six months ended June 30, 2013 | For the six months ended June 30, 2012 |
|---|---|---|
| Net Loss | $(19,852) | $(7,621) |
| | | |
| Net cash used in operating activities | (11,974) | (8,355) |
| Net cash used in investing activities | (24,410) | (40,443) |
| Net cash provided by financing activities | 44,599 | 43,726 |
| | | |
| Net increase (decrease) in cash and cash equivalents | 8,215 | (5,072) |
| Cash and cash equivalents at the beginning of the period | 2,300 | 9,216 |
| Cash and cash equivalents at the end of the period | $10,515 | $4,144 |

PMI has incurred operating losses since its inception. The negative cash flows from operations were $11,974 and $8,355 for the six months ended June 30, 2013 and 2012, respectively. As reflected in the accompanying condensed consolidated financial statements, the accumulated deficit is approximately $96,751 as of June 30, 2013.

At June 30, 2013, the PMI Group had approximately $10,515 in available cash and cash equivalents. Since its inception, the PMI Group has financed its operations primarily through equity financing from various sources. The PMI Group is dependent upon raising additional capital or debt financing to fund its current operating plan, however the PMI Group believes that its current cash position is sufficient to meet its current liquidity needs.

Net cash used in operating activities was $11,974 and $8,355 for the six months ended June 30, 2013 and 2012, respectively. The increase in cash used in operating activities was primarily attributable to the net loss offset by the class action settlement liability.

Net cash used in investing activities was $24,410 and $40,443 for the six months ended June 30, 2013 and 2012, respectively. The primary driver for the change is due to increase in borrower loan originations offset by increased repayments of borrower loans held at fair value.

Net cash provided by financing activities was $44,599 and $43,726 for the six months ended June 30, 2013 and 2012, respectively. Net cash provided by financing activities during 2013 consisted of proceeds from the issuance of convertible preferred stock, proceeds from the issuance of Notes and repayments of Notes held at fair value.

In January 2013, PMI issued and sold 138,681,680 shares of new Series A preferred stock ("new Series A") in a private placement at a purchase price of $0.144 per share for approximately $20,000. In connection with that sale, PMI issued 51,171,951 shares at par value $0.001 per share of Series A-1 convertible preferred stock to certain previous holders of PMI's Series A, Series B, Series C, Series D, Series E and Series F preferred stock who participated in the sale. The new Series A securities were sold in reliance on the exemption from the registration requirements of the Securities Act set forth in Section 4(2) of the Securities Act and Regulation D promulgated thereunder regarding sales by an issuer not involving a public offering.

In connection with the new Series A sale, shares of PMI's preferred stock that were outstanding immediately prior to the sale ("Old Preferred Shares") were converted into shares of PMI common stock. For holders of Old Preferred Shares who participated in the sale in proportion to their pro rata ownership interest in PMI, their Old Preferred Shares converted into common shares at a ratio of 1:1. In addition, each such participating holder received a share of PMI's new Series A-1 preferred stock for every dollar of liquidation preference associated with an Old Preferred Share held by such holder. Each share of Series A-1 preferred stock has a liquidation preference of $1.00 and converts into common stock at a ratio of 1,000,000:1.

On July 19, 2013 solely to avoid the costs, risks and uncertainties inherent in litigation, and without admitting any liability or wrongdoing, the parties to the Hellum Litigation pending before the Superior Court of California, County of San Francisco, California, entered into a Stipulation and Agreement of Compromise, Settlement, and Release (the "Settlement") setting forth an agreement- to settle all claims related thereto. In connection with the Settlement, PMI agreed to pay the plaintiffs an aggregate amount of $10,000, payable in four annual installments of $2,000 in 2013, $2,000 in 2014, $3,000 in 2015 and $3,000 in 2016. The settlement is subject to final approval by the Superior Court. Subject to satisfaction of the conditions set forth in the Settlement, the defendants will be released by the plaintiffs from all claims concerning or arising out of the offering of promissory notes on the platform from January 1, 2006 through October 14, 2008. For more information, see Note 10 of Prosper Marketplace, Inc.'s condensed consolidated financial statements located elsewhere in this report.

**Income Taxes**

The PMI Group incurred no income tax provision for the three and six months ended June 30, 2013 and 2012. Given the PMI Group's history of operating losses and inability to achieve profitable operations, it is difficult to accurately forecast how future results will be affected by the realization and use of net operating loss carry forwards.

**Off-Balance Sheet Arrangement*s***

There are no off-balance sheet arrangements as of June 30, 2013.

**Additional Information about the Platform**

***Comparing Estimated Loss Rates to Actual Losses***

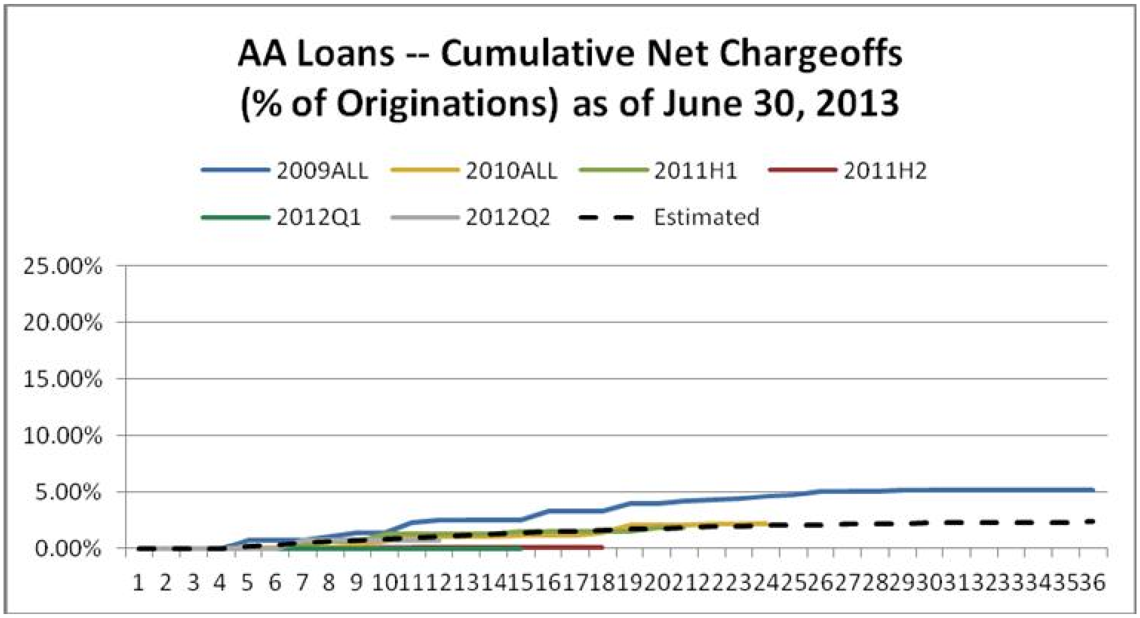
Loan performance is reviewed on a monthly basis to determine how loss rate estimates compare to the actual performance of loans. As part of this monthly review, the processes for calculating and assigning loss rates and Prosper Ratings described in the preceding sections are reassessed to ensure continued accuracy. The graphs below show the estimated versus actual cumulative dollar loss rates by Prosper Rating for Borrower Loans booked from July 13, 2009 through June 30, 2013. Performance is as of June 30, 2013. The loss performance is tracked by vintage and factors in aging. Accordingly, each line represents all loans originated in a given period that have been outstanding at least 12 months. In addition, data for a point along the x axis is only included if the entire vintage is at least that mature.

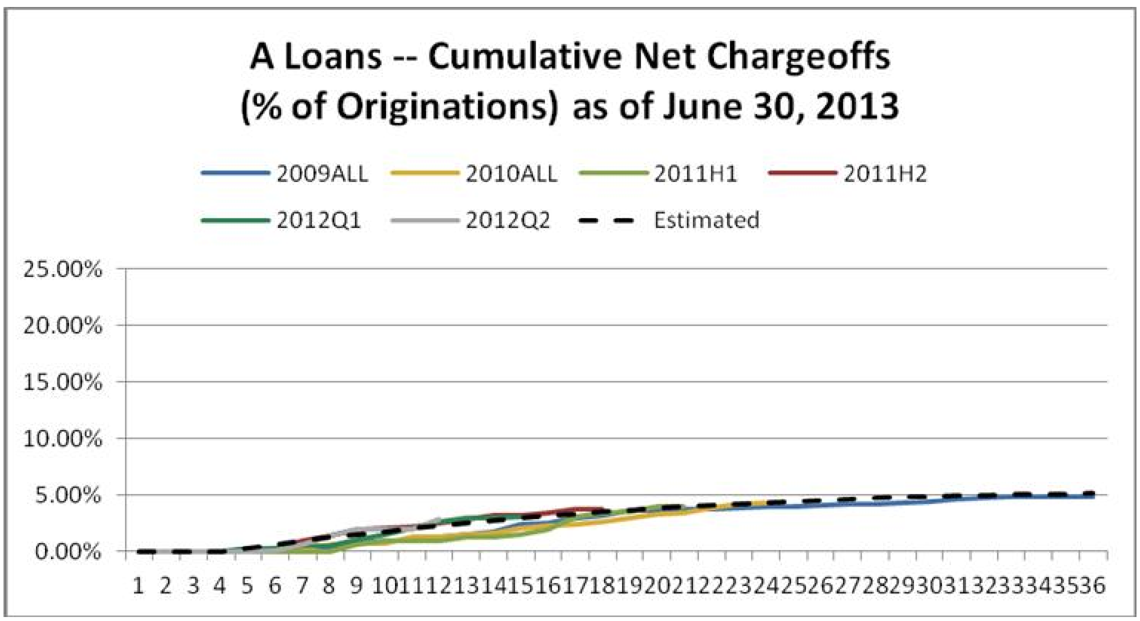
Vintages generally contain enough loan volume for their performance curves to be meaningful. In order to increase the significance of the curves presented, Borrower Loans originated from July 13, 2009 through December 31, 2010 have been aggregated into annual vintages. Borrower Loans originated in 2011 are aggregated into half-year vintages. Only the first two quarters of 2012 originations are mature enough to be shown.

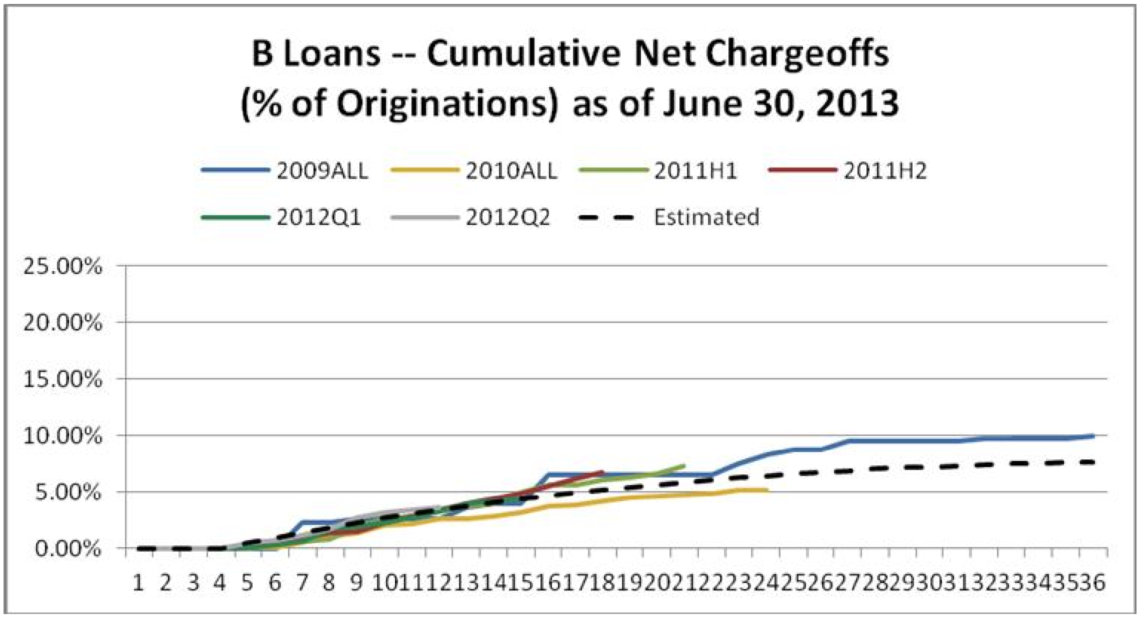
The graphs below show cumulative net charge-offs for Borrower Loans as a percentage of originations for each Prosper Rating presented by origination vintage from July 13, 2009 to June 30, 2012 as compared to the estimates provided to investors at the time the loans were originated. The estimates do not represent updated loss forecasts. This information is provided as a helpful way of comparing actual losses with such estimates, but it is only one of many important factors to consider in evaluating the suitability of Notes as investments. Other important factors to consider include, but are not limited to, early loan prepayment, severity and timing of the charge-off, and recovery and timing of payment post default.

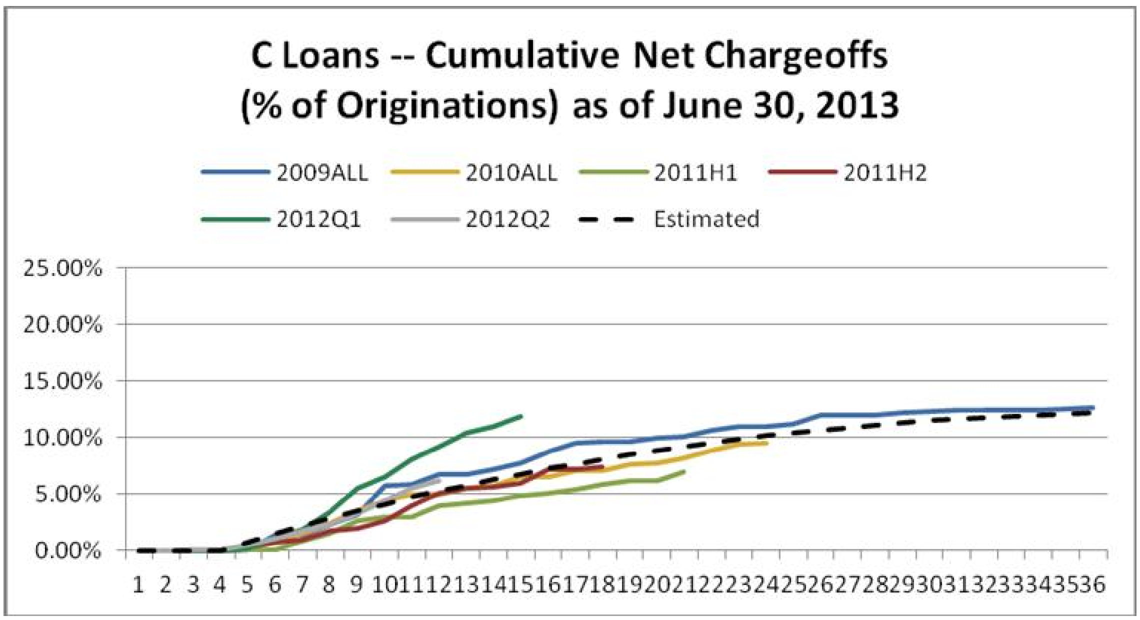
The PMI Group's participation in funding loans on the platform from time to time has had, and will continue to have, no effect on the income and employment verification process, the selection of loan requests verified or the frequency of income and employment verification.

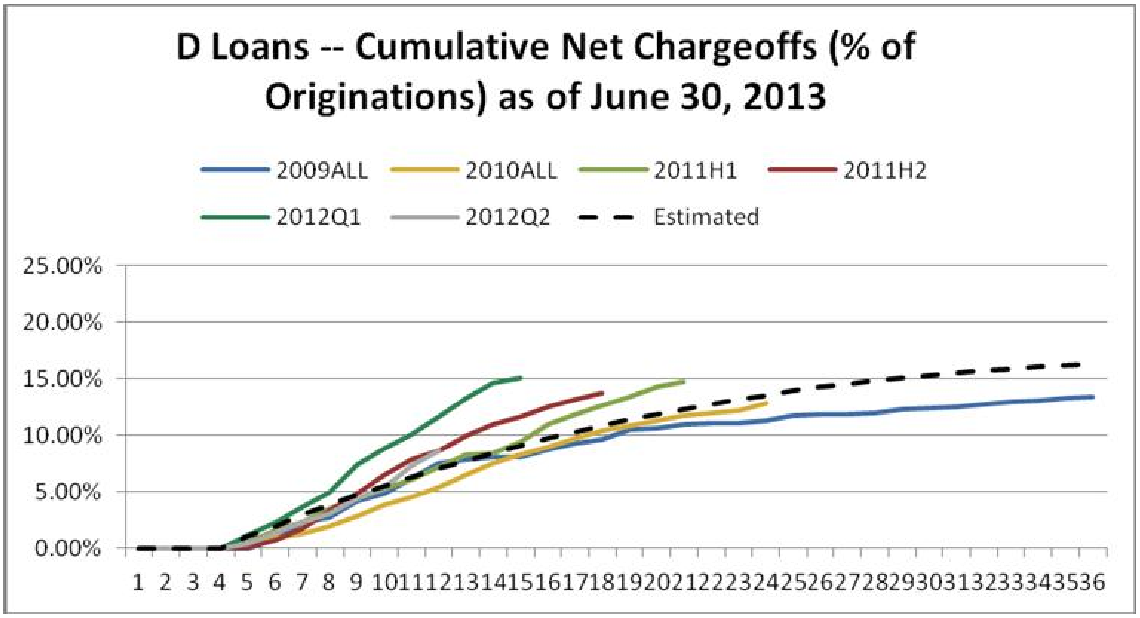
The graphs below show cumulative net charge-offs for Borrower Loans as a percentage of originations for each Prosper Rating presented by origination vintage from July 13, 2009 to June 30, 2012.

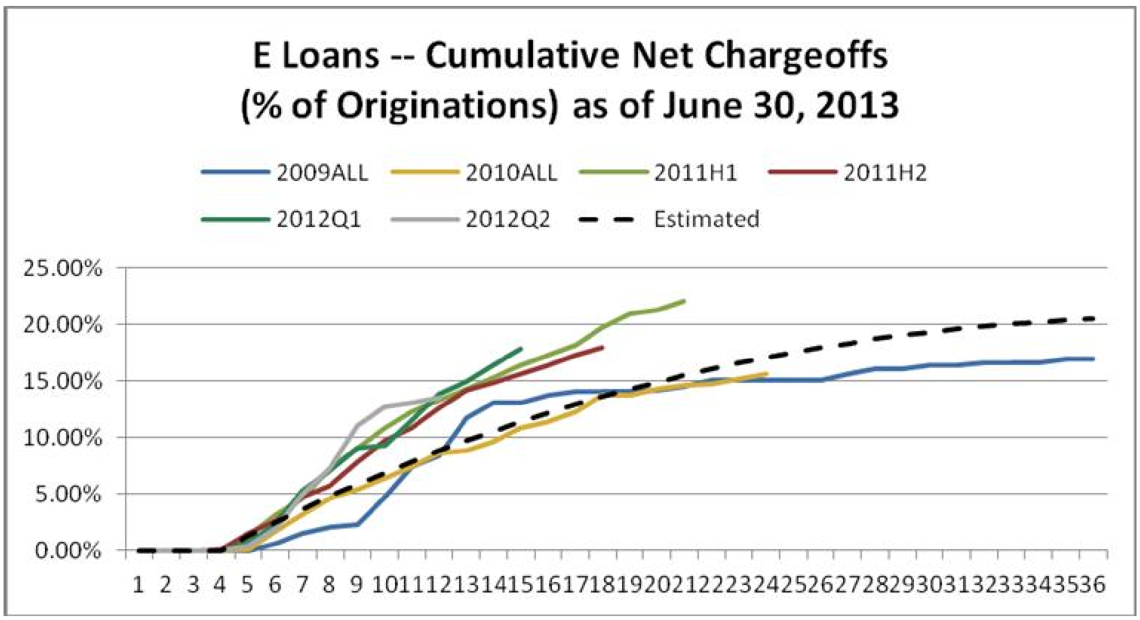

AA Loans -- Cumulative Net Chargeoffs
(% of Originations) as of June 30, 2013
2009ALL
2010ALL
2011H1
2011H2
2012Q1
2012Q2
Estimated
25.00%
20.00%
15.00%
10.00%
5.00%
0.00%
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25 26 27 28 29 30 31 32 33 34 35 36

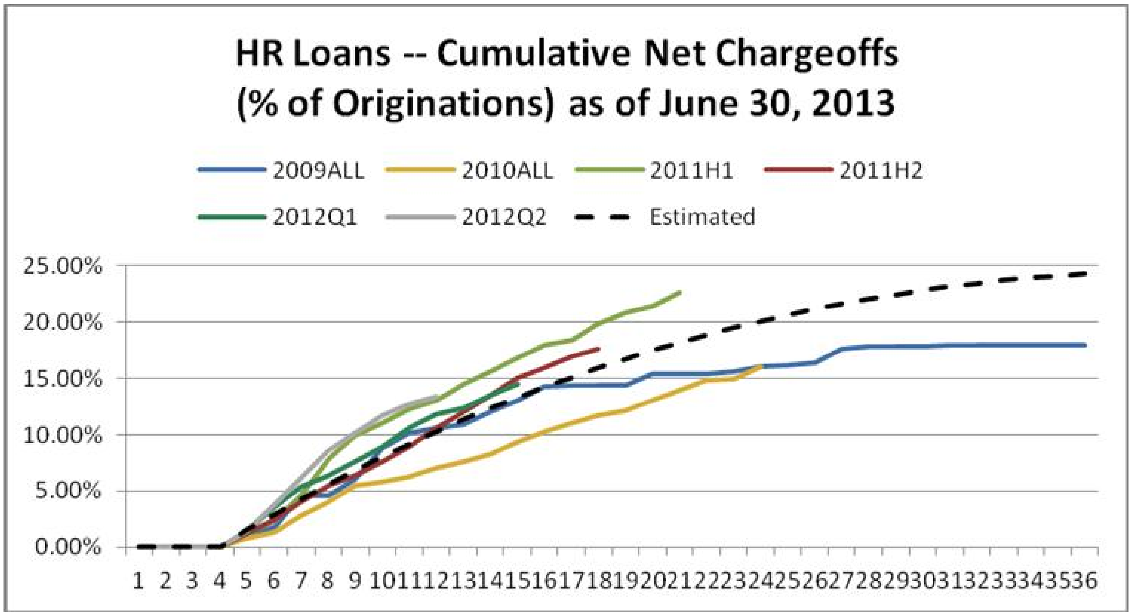

A Loans -- Cumulative Net Chargeoffs
(% of Originations) as of June 30, 2013
2009ALL
2010ALL
2011H1
2011H2
2012Q1
2012Q2
Estimated
25.00%
20.00%
15.00%
10.00%
5.00%
0.00%
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25 26 27 28 29 30 31 32 33 34 35 36


B Loans -- Cumulative Net Chargeoffs
(% of Originations) as of June 30, 2013
2009ALL
2010ALL
2011H1
2011H2
2012Q1
2012Q2
Estimated
25.00%
20.00%
15.00%
10.00%
5.00%
0.00%
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25 26 27 28 29 30 31 32 33 34 35 36


C Loans -- Cumulative Net Chargeoffs
(% of Originations) as of June 30, 2013
2009ALL
2010ALL
2011H1
2011H2
2012Q1
2012Q2
Estimated
25.00%
20.00%
15.00%
10.00%
5.00%
0.00%
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25 26 27 28 29 30 31 32 33 34 35 36


D Loans -- Cumulative Net Chargeoffs (% of Originations) as of June 30, 2013
2009ALL
2010ALL
2011H1
2011H2
2012Q1
2012Q2
Estimated
25.00%
20.00%
15.00%
10.00%
5.00%
0.00%
1 2 3 4 5 6 7 8 9 101112131415161718192021222324252627282930313233343536


E Loans -- Cumulative Net Chargeoffs (% of Originations) as of June 30, 2013
2009ALL
2010ALL
2011H1
2011H2
2012Q1
2012Q2
Estimated
25.00%
20.00%
15.00%
10.00%
5.00%
0.00%
1 2 3 4 5 6 7 8 9 101112131415161718192021222324252627282930313233343536




**Note**: Estimated lines represent the high end of the estimated loss rate range for each Prosper Rating, except for HR, where the high end of the range is 100% and the estimated curve was set at 24.75% cumulative principal loss.

In aggregate, the 2011 through 2012H1 vintages are on track for higher cumulative losses than those experienced for the 2009H2 and 2010 vintages. The increase in losses is explained both due to the riskier customer mix in 2011 and 2012 as well as worse than estimated performance in the riskier (C-HR) rating grades.

In instances where a material variance relative to estimates exists, analysis is conducted to understand the reason for the variance and the credit policy is adjusted to bring loan losses back in-line with estimates. For instance, many of the higher risk (C-HR) applicants from 2011 and 2012 would currently either be given a worse rating or would not be allowed to post a listing were they to apply for a loan today under the current credit policy.

Please note that the historical performance of Borrower Loans may not be indicative of the future performance of Borrower Loans. See “Item 1A. Risk Factors—Risks Related to Prosper Funding and PMI, the Platform and Prosper Funding and PMI’s Ability to Service the Notes” in the PMI Group’s Form 10-K filed on March 19, 2013 for more information.

***Loan Originations***

The tables below show loan volume, origination amount, average credit scores and other pertinent data by Prosper Rating for originations from July 13, 2009 to June 30, 2013:

| Prosper Rating | Number | Amount | Weighted Average Borrower Rate | Weighted Average Estimated Loss | Weighted Average Lender Yield | Average Experian ScorexPlus Score | Weighted Average Borrower APR |
|---|---|---|---|---|---|---|---|
| AA | 3,126 | $33,039 | 8.66% | 1.45% | 7.66% | 797 | 9.72% |
| A | 7,458 | $74,938 | 11.83% | 3.00% | 10.83% | 752 | 14.26% |
| B | 7,546 | $74,136 | 16.57% | 5.34% | 15.57% | 723 | 19.31% |
| C | 8,408 | $73,828 | 21.05% | 7.69% | 20.05% | 707 | 24.19% |
| D | 10,029 | $66,702 | 25.59% | 10.64% | 24.59% | 693 | 28.96% |
| E | 6,433 | $26,973 | 30.45% | 14.11% | 29.45% | 673 | 34.22% |
| HR | 6,182 | $21,243 | 31.85% | 17.46% | 30.85% | 689 | 35.67% |
| Total | 49,182 | $370,859 | 19.31% | 7.27% | 18.31% | 712 | 22.16% |

The tables below show loan volume, origination amount, average credit scores and other pertinent data by Prosper Rating for originations from April 1, 2013 to June 30, 2013:

| Prosper Rating | Number | Amount | Weighted Average Borrower Rate | Weighted Average Estimated Loss | Weighted Average Lender Yield | Average Experian ScorexPlus Score | Weighted Average Borrower APR |
|---|---|---|---|---|---|---|---|
| AA | 341 | $4,134 | 7.85% | 1.63% | 6.85% | 787 | 9.33% |
| A | 1,229 | $16,033 | 11.65% | 3.29% | 10.65% | 752 | 14.16% |
| B | 1,585 | $20,377 | 15.91% | 5.15% | 14.91% | 733 | 18.70% |
| C | 1,764 | $19,684 | 20.20% | 7.47% | 19.20% | 706 | 23.23% |
| D | 1,160 | $8,751 | 24.46% | 10.44% | 23.46% | 688 | 27.74% |
| E | 851 | $3,187 | 28.25% | 13.25% | 27.25% | 678 | 31.78% |
| HR | 169 | $611 | 31.33% | 15.74% | 30.33% | 696 | 35.35% |
| Total | 7,099 | $72,777 | 17.37% | 6.25% | 16.37% | 717 | 20.19% |

## PROSPER FUNDING LLC

### Overview

Prosper Funding LLC (“Prosper Funding”) was formed in the state of Delaware in February 2012 as a limited liability company with its sole equity member being PMI. Prosper Funding was formed by PMI to hold borrower loans and issue borrower payment dependent notes through the platform. Although Prosper Funding is consolidated with PMI for accounting and tax purposes, Prosper Funding has been organized and is operated in a manner that is intended to minimize the likelihood that it would be substantively consolidated with PMI in a bankruptcy proceeding. Prosper Funding’s intention is to minimize the likelihood that its assets would be subject to claims by PMI’s creditors if PMI were to file for bankruptcy, as well as to minimize the likelihood that Prosper Funding will become subject to bankruptcy proceedings directly. Prosper Funding seeks to achieve this by placing certain restrictions on its activities and implementing certain formal procedures designed to expressly reinforce its status as a distinct corporate entity from PMI.

On January 22, 2013, PMI entered into an Asset Transfer Agreement with Prosper Funding (the “Asset Transfer Agreement”), pursuant to which PMI transferred substantially all of its remaining assets to Prosper Funding, including (i) all outstanding notes issued by PMI under the Indenture dated June 15, 2009 between PMI and Wells Fargo Bank, as trustee, (ii) all borrower loans held by PMI, (iii) all lender/borrower/group leader registration agreements related to the notes or the borrower loans, and (iv) all documents and information related to the foregoing, effective February 1, 2013.

On February 1, 2013, PMI made a capital contribution in excess of $3,000 to Prosper Funding and Prosper Funding commenced operations. Since February 1, 2013, all notes are issued, sold and serviced through the platform by Prosper Funding (together with the notes transferred from PMI, the “Notes”). Pursuant to an Administration Agreement between Prosper Funding and PMI, PMI manages all other aspects of the platform on behalf of Prosper Funding.

All loans requested and obtained through the platform are unsecured obligations of individual borrower members with a fixed interest rate and loan terms set at three or five years as of June 30, 2013. All loans made through the platform are funded by WebBank, an FDIC-insured, Utah chartered industrial bank. After funding a loan, WebBank sells the loan to Prosper Funding, without recourse to WebBank, in exchange for the principal amount of the loan (together with the borrower loans transferred from PMI, the “Borrower Loans”). WebBank does not have any obligation to purchasers of the Notes.

Prosper Funding entered into an Administration Agreement with PMI pursuant to which PMI has agreed to provide certain administrative services relating to the platform. The Administration Agreement contains a license granted by Prosper Funding to PMI that entitles PMI to use the platform for and in relation to: (i) PMI’s performance of its duties and obligations under the Administration Agreement relating to corporate administration, loan platform services, loan and note servicing and marketing, and (ii) PMI’s performance of its duties and obligations to WebBank in relation to loan origination and funding. The license is terminable in whole or in part in relation to failure by PMI to pay the licensing fee or the termination of PMI as the provider of some or all of the aforementioned services.

### Trends and Uncertainties

The performance of current and future Borrower Loans may not be consistent with the historical trends demonstrated by prior Borrower Loans. During 2013, Prosper Funding increased its origination volume consistently in terms of both units and total dollar amounts and hopes to continue that trend of growth into the future. Over time, Prosper Funding expects its lender base to grow as it gains more exposure to potential borrowers and lenders and establishes its Notes as a viable investment alternative. Prosper Funding expects the growth of its lender base will contribute to increased origination volume.

Prosper Funding’s operating plan calls for a strategy of increasing transaction volume, borrower focused marketing and improving the efficiency of the platform to increase revenue. Prosper Funding will generate revenue through license fees earned under the Administration Agreement and servicing fees from lender members which are described more fully in the Prosper Funding LLC Notes to Condensed Financial Statements included elsewhere in this quarterly report.

The peer-to-peer lending industry remains a very innovative and unique industry. The application of federal and state laws in areas such as securities and consumer finance to Prosper Funding’s business is still evolving. Prosper Funding will continue to monitor this evolution actively in order to identify and respond quickly to any legislative or regulatory developments that may impact the platform.

***Fair Value Measurement***

Upon commencement of operations on February 1, 2013, Prosper Funding began to purchase Borrower Loans originated through the platform and issue Notes, which are accounted for on a fair value basis.

Prosper Funding determines the fair values of its financial instruments based on the fair value hierarchy established in Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 820, *Fair Value Measurements and Disclosures,* which requires an entity to maximize the use of quoted prices and observable inputs and to minimize the use of unobservable inputs when measuring fair value. Prosper Funding uses various valuation techniques depending on the nature of the financial instrument, including the use of market prices for identical or similar instruments, or discounted cash flow models. When possible, active and observable market data for identical or similar financial instruments are utilized. Alternatively, Prosper Funding may determine fair value using assumptions that it believes a market participant would use in pricing the asset or liability.

The estimated fair values of cash and cash equivalents, restricted cash, accounts payable and accrued liabilities approximate their carrying values because of their short-term nature. Short term investments, Borrower Loans held for investment, Borrower Loans, and Notes are accounted for on a fair value basis. For additional information and discussion regarding significant accounting policies surrounding fair value measurement, see Note 2, Note 3 and Note 4 to Prosper Funding's condensed financial statements included elsewhere in this quarterly report.

***Borrower Loans and Notes***

Prosper Funding purchases Borrower Loans from WebBank and, if issuing Notes to lender members to fund its purchase of Borrower Loans, holds the Borrower Loans until maturity, except as may otherwise be determined in connection with the servicing of any Borrower Loan. The obligation to repay the Notes is conditioned upon the repayment of the associated Borrower Loan owned by Prosper Funding. Prosper Funding carries the Borrower Loans and Notes on its balance sheet as assets and liabilities, respectively. Prosper Funding also purchases Borrower Loans from WebBank and immediately sells them to certain qualified lender members.

Prosper Funding has adopted the provisions of ASC Topic 825, *Financial Instruments.* ASC Topic 825 permits companies to choose to measure certain financial instruments and certain other items at fair value. The standard requires that unrealized gains and losses on items for which the fair value option has been elected be reported in earnings. Prosper Funding applies the provisions of ASC Topic 825 to the Borrower Loans and Notes issued on an instrument by instrument basis. The aggregate fair value of the Borrower Loans and Notes are reported as separate line items in the assets and liabilities sections of the balance sheet using the methods described in ASC Topic 820.

Prosper Funding determines the fair value of the Borrower Loans and Notes in accordance with the fair value hierarchy established in ASC Topic 820, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. As observable market prices are not available for the Borrower Loans and Notes Prosper Funding holds or for similar assets and liabilities, Prosper Funding believes that the Borrower Loans and Notes should be considered Level 3 financial instruments under ASC Topic 820. ASC Topic 820 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date.

In a hypothetical transaction as of the measurement date, Prosper Funding believes that differences in the principal marketplace in which the Borrower Loans are originated and the principal marketplace in which it might offer those Borrower Loans may result in differences between the originated amount of the Borrower Loans and their fair value as of the transaction date. Changes in the fair value of Borrower Loans and Notes subject to the provisions of ASC Topic 820 are recognized in earnings; fees and costs associated with the acquisition of Borrower Loans are recognized as incurred. Prosper Funding estimates the fair value of the Borrower Loans and Notes using a discounted cash flow methodology based upon a set of valuation assumptions it believes market participants would use for similar assets and liabilities. The main assumptions used to value the Borrower Loans and Notes include default rates, discount rates applied to each credit tranche/grade, prepayment rates, and recovery rates based upon historical data for Borrower Loans and Notes originated in prior periods.

Overall, if the fair value of the Borrower Loans decrease or increase due to any changes in Prosper Funding's assumptions, there will also be a corresponding decrease or increase in the fair value of the linked Notes. As a result, the effect on Prosper Funding's earnings of adverse changes in key assumptions is mitigated. However, the impact of these changes in fair value could have a material adverse impact on lender members' investments in the Notes.

As Prosper Funding receives scheduled payments of principal and interest on the Borrower Loans it in turn makes principal and interest payments on the Notes. These principal payments reduce the carrying value of the Borrower Loans and Notes. If Prosper Funding does not receive payments on the Borrower Loans, it is not obligated to and will not make payments on the Notes. The fair value of a Note is approximately equal to the fair value of the corresponding Borrower Loan, less a servicing fee charged to Note holders. If the fair value of the Borrower Loan decreases due to Prosper Funding's expectation regarding both the likelihood of default of the loan and the amount of loss in the event of default, there will also be a corresponding decrease in the fair value of the Note (an unrealized gain related to the Note and an unrealized loss related to the Borrower Loan).

Overall, if the fair value of the Borrower Loans decrease or increase due to any changes in the PMI Group's assumptions, there will also be a corresponding decrease or increase in the fair value of the linked Notes. As a result, the effect on the PMI Group's earnings of adverse changes in key assumptions is mitigated.

As the PMI Group receives scheduled payments of principal and interest on the Borrower Loans it in turn makes principal and interest payments on the Notes. These principal payments reduce the carrying value of the Borrower Loans and Notes. If the PMI Group does not receive payments on the Borrower Loans, the PMI Group is not obligated to and does not make payments on the Notes. The fair value of a Note is approximately equal to the fair value of the corresponding Borrower Loan, less the service fee. If the fair value of the Borrower Loan decreases due to the PMI Group's expectation regarding both the likelihood of default of the loan and the amount of loss in the event of default, there is also a corresponding decrease in the fair value of the Note (an unrealized gain related to the Note and an unrealized loss related to the Borrower Loan).

Key economic assumptions and the sensitivity of the current fair value to immediate adverse changes in those assumptions at June 30, 2013 for Borrower Loans and Notes are presented in the following table:

| | Borrower Loans | Notes |
|---|---|---|
| **Discount rate assumption:** | 10.50% | 10.50% |
| Decrease in fair value and income (loss) to earnings from: | | |
| 100 basis point increase | $186,043 | $183,829 |
| 200 basis point increase | 183,991 | 181,796 |
| Increase in fair value and income (loss) to earnings from: | | |
| 100 basis point decrease | $190,309 | $188,056 |
| 200 basis point decrease | 192,528 | 190,254 |
| | | |
| **Default rate assumption:** | | |
| Decrease in fair value and income (loss) to earnings from: | | |
| 10% higher default rates | $186,061 | $183,850 |
| 20% higher default rates | 183,733 | 181,546 |
| Increase in fair value and income (loss) to earnings from: | | |
| 10% lower default rates | $190,172 | $187,917 |
| 20% lower default rates | 192,184 | 189,908 |

For additional information and discussion, see Note 2 and Note 3 to Prosper Funding's condensed financial statements included elsewhere in this report.

**Results of Operations**

**Revenues**

***Revenue Recognition***

Prosper Funding's revenue recognition policy is in accordance with ASC Topic 605, *Revenue Recognition*. Under ASC Topic 605, revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the price of the services is fixed and determinable and collectability is reasonably assured.

*Administration Fee Revenue*

Prosper Funding primarily generates revenues through license fees it earns through an Administration Agreement with PMI. The Administration Agreement contains a license granted by Prosper Funding to PMI that entitles PMI to use the platform for and in relation to: (i) PMI's performance of its duties and obligations under the Administration Agreement relating to corporate administration, loan platform services, loan and note servicing and marketing, and (ii) PMI's performance of its duties and obligations to WebBank in relation to loan origination and funding. For the three months ended June 30, 2013, Prosper Funding received $1,528 in administration fee revenue from PMI. For the six months ended June 30, 2013, Prosper Funding received $2,135 in administration fee revenue from PMI.

*Loan Servicing Fees*

Loan servicing revenue includes monthly loan servicing fees and non-sufficient funds ("NSF") fees on Borrower Loans. Loan servicing fees are accrued daily based on the current outstanding loan principal balance of the Borrower Loan but are not recognized until payment is received due to the uncertainty of collection of Borrower Loan payments. Prosper Funding's servicing fee is currently equal to 1.0% of the outstanding principal balance of the corresponding Borrower Loan.

*Interest Income on Borrower Loans and Interest Expense on Notes*

Prosper Funding recognizes interest income on Borrower Loans using the accrual method based on the stated interest rate to the extent that Prosper Funding believes it to be collectable. Prosper Funding records interest expense on the corresponding Note based on the contractual interest rate.

| | Three months ended June 30, | | Six months ended June 30, | From February 17, 2012 (date of inception) to June 30, |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| Interest Income on Borrower Loans | $8,578 | $- | $13,651 | $- |
| Interest Expense on Notes | (8,128) | - | (12,946) | - |
| Net Interest Income (Expense) on Loans & Notes | $450 | $- | $705 | $- |

The overall increase in net interest income for the three and six months ended June 30, 2013 was driven by the rise in the amount of Borrower Loans that Prosper Funding owned and serviced at any given point.

**Cost of Revenues**

***Cost of Services***

Prosper Funding also incurs certain recurring expenses relating to fees under the Administration Agreement with PMI, as well as its agreements with WebBank, Wells Fargo, FOLIO*fn* Investments, Inc. and CSC Logic, Inc. In addition, Prosper Funding incurs certain ongoing expenses related to collateral requirements under its agreements with WebBank and Wells Fargo Bank. During the three month period ending June 30, 2013, Prosper Funding incurred $338 in cost of services. During the period from commencement of operations on February 1, 2013 through June 30, 2013, Prosper Funding incurred $563 in cost of services.

***Provision for Loan Loss***

Under the terms of the Notes and Lender Registration Agreements, the PMI Group may, in certain circumstances, become obligated to repurchase a Note from a lender or indemnify a lender against loss on a Note. Generally these circumstances include the occurrence of verifiable identity theft, the failure to properly follow loan listing or bidding protocols, and a violation of the applicable federal/state/local lending laws. The provision for loan loss is evaluated at least once a quarter and represents an estimate based on the rate of historical loan losses as a percentage of originations (which generally occur within six to nine months of origination). The provision for loan loss may include a judgmental management adjustment due to the limited operating history, changes in current economic conditions, the risk of new and as of yet undetected fraud schemes, origination unit and dollar volumes and the lack of industry comparables. Based on the analysis of the historical provision, the provision for loan loss was $50 for the three months ended June 30, 2013. The provision for loan loss was $149 for the six months ended June 30, 2013.

**Other Income and Expenses**

***Change in Fair Value of Borrower Loans and Notes, net***

The total fair value adjustment was $4,082 and $4,573 for Borrower Loans and Notes, respectively, resulting in a net unrealized gain of $491 for the six months ended June 30, 2013. The amounts are included as a component of other income (expense) in the condensed consolidated statement of operations. Since Prosper Funding did not commence operations until 2013, there were no fair value adjustments in 2012.

**Operating Expenses**

*Administration Fee Expense*

Pursuant to an Administration Agreement between Prosper Funding and PMI, PMI manages the platform on behalf of Prosper Funding. Accordingly, each month, Prosper Funding is required to pay PMI certain corporate administration fees and other variable fees based on funding volume and servicing activities.

*Professional Services*

Professional service expenses are comprised of legal expenses, audit and accounting fees, consulting services and other outside costs. Professional service expenses were $5 and $17 for the three months ended June 30, 2013 and 2012, respectively, representing a decrease of $12. Professional service expenses were $20 and $82 for the six months ended June 30, 2013 and 2012, respectively, representing a decrease of $62. The decrease was primarily due to legal fees related to the formation of Prosper Funding diminished.

*Other Operating Expense*

Other expenses consist primarily of bank service charges. Other expenses were $50 and zero for the three months ended June 30, 2013 and 2012, respectively, representing an increase of $50. Other expenses were $94 and $59 for the six months ended June 30, 2013 and 2012, respectively, representing an increase of $35. This increase is primarily due to bank service charges.

Prosper Funding incurs certain fees relating to registering or qualifying its offering and sale of Notes with federal and state securities regulators, as well as additional fees relating to obtaining other licenses and permits that are necessary to the operation of its business. In addition, Prosper Funding incurs certain ongoing expenses related to collateral requirements under its agreements with WebBank and Wells Fargo Bank.

Prosper Funding also incurs certain recurring expenses relating to fees under the Administration Agreement with PMI, as well as its agreements with WebBank, Wells Fargo, FOLIO*fn* Investments, Inc. and CSC Logic, Inc. Prosper Funding will also incur additional expense to the extent it is required to repurchase any Notes or indemnify Note holders in regard to any Notes. It will pay these recurring expenses from license fees and servicing fees that it earns in connection with the license contained in the Administration Agreement and the servicing of Borrower Loans and Notes. Prosper Funding expects that the combination of the initial capital contributions described above and ongoing fee revenue will be sufficient for it to meet ongoing cash requirements and sustain its operations.

**Income Taxes**

Prosper Funding incurred no income tax provision for the three and six months ended June 30, 2013. Prosper Funding is a US disregarded entity and the income and loss is included in the return of its parent, PMI. Given PMI’s history of operating losses and inability to achieve profitable operations, it is difficult to accurately forecast how PMI and Prosper Funding’s results will be affected by the realization and use of net operating loss carry forwards.

**Liquidity and Capital Resources**

The following table summarizes the cash flow for the six months ended June 30, 2013 and 2012, respectively:

| | For the six months ended June 30, 2013 | From February 17, 2012 (date of inception) to June 30, 2012 |
|---|---|---|
| Net Loss | **$1,267** | **$(141)** |
| | | |
| Net cash provided by operating activities | 1,494 | (141) |
| Net cash used in investing activities | (21,352) | - |
| Net cash provided by financing activities | 23,363 | 146 |
| | | |
| Net Increase (decrease) in cash and cash equivalents | 3,505 | 5 |
| Cash and cash equivalents at the beginning of the period | 5 | - |
| Cash and cash equivalents at the end of the period | $3,510 | $5 |

Prosper Funding has positive cash flow since commencement of operations and anticipates that it will continue to be cash flow positive through the end of 2013. Prosper Funding has positive cash flows from operations of $1,494 for the six months ended June 30, 2013. At June 30, 2013, Prosper Funding had $3,510 in available cash and cash equivalents. Since its inception, Prosper Funding has financed its operations primarily through capital infusions from its parent, PMI. Prosper Funding believes that its current cash position is sufficient to meet its current liquidity needs.

Net cash provided by operating activities was $1,494 for the six months ended June 30, 2013. The cash provided by operating activities was primarily attributable to license fees Prosper Funding received offset by fees incurred related to certain recurring expenses under the Administration Agreement with PMI, as well as its agreements with WebBank, Wells Fargo, FOLIO*fn* Investments, Inc. and CSC Logic, Inc. Prosper Funding will also incur additional expense to the extent it is required to repurchase any Notes or indemnify Note holders in regard to any Notes.

Net cash used in investing activities was $21,352 for the six months ended June 30, 2013. Net cash provided by investing activities primarily consisted of repayments of Borrower Loans held at fair value and Borrower Loan originations at fair value.

Net cash provided by financing activities was $23,363 for the six months ended June 30, 2013. Net cash provided by financing activities mainly consisted of capital infusions contributed by PMI, proceeds from issuance of Notes and payments of Notes.

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

*Not applicable for smaller reporting companies.*

**Item 4. Controls and Procedures**

**Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures**

Each Registrant maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in such Registrant's Exchange Act Reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and that such information is accumulated and communicated to the management of such Registrant, including such Registrant's principal executive officer ("PEO") and principal financial officer ("PFO"), as appropriate, to allow for timely decisions regarding required disclosure. Disclosure controls and procedures, no matter how well designed and operated, can provide only reasonable assurance that the objectives of the control system are met. Such Registrant's disclosure controls and procedures were designed to provide reasonable assurance of achieving their stated objectives. Under the supervision, and with the participation, of management, including the PEO and the PFO, each Registrant has evaluated the effectiveness of the design and operation of its disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of June 30, 2013, following the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control—Integrated Framework, and with further guidance for internal controls for small business provided by the SEC's Interpretive Guidance in Release No. 34-55929. Based upon this evaluation, the PEO and the PFO of such Registrant have concluded that these disclosure controls and procedures are effective to provide reasonable assurance that material information relating to such Registrant and its subsidiaries that is required to be disclosed in reports filed with, or submitted to, the SEC under the Exchange Act (i) is recorded, processed, summarized and reported within the time periods specified by the SEC rules and forms, and (ii) is accumulated and communicated to management, including its PEO and PFO, as appropriate to allow timely decisions regarding required disclosure.

Under the supervision and with the participation of management, including the PEO and PFO of each Registrant, each such Registrant has evaluated changes in internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during each Registrant's most recent fiscal quarter, and has concluded there was no change in such Registrant's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, such Registrant's internal control over financial reporting.

The Dodd-Frank Wall Street Reform and Consumer Protection Act exempts any company that is not a "large accelerated filer" or an "accelerated filer" (as defined by SEC rules) from the requirement that such company obtain an external audit of the effectiveness of its internal control over financial reporting pursuant to Section 404(b) of the Sarbanes-Oxley Act. As a result, each of the Registrants is exempt from the requirement that it include in its Annual Report on Form 10-K an attestation report on internal control over financial reporting by an independent registered public accounting firm; however, management's annual report on internal control over financial reporting, pursuant to Section 404(a) of the Sarbanes-Oxley Act, is still required with respect to each Registrant.

# PART II. OTHER INFORMATION

## Item 1. Legal Proceedings

See Note 10: " Commitments and Contingencies" of PMI's Notes to Condensed Consolidated Financial Statements contained in Part I, Item 1 of this report for information regarding

- PMI's NASAA settlement agreement,
- Litigation between PMI and its insurer, and
- Class action litigation involving PMI.

This information is incorporated into this Item by reference.

Because of the nature and inherent uncertainties of litigation, should the outcome of any legal actions be unfavorable, the PMI Group may be required to pay damages and other expenses, which could have a material adverse effect on the PMI Group's consolidated financial position and results of operations. The PMI Group is not currently subject to any material legal proceedings other than the matters referenced above. Except for those matters, the PMI Group is not aware of any litigation matters that have had, or are expected to have, a material adverse effect on the PMI Group.

This Item should be read in conjunction with the Legal Proceedings disclosures in our Annual Report on Form 10-K for the year ended December 31, 2012 (Part I, Item 3).

## Item 1A. Risk Factors

*Not applicable for smaller reporting companies.*

## Item 2. Unregistered Sale of Equity Securities and Use of Proceeds

On January 15, 2013, PMI entered into a Stock Purchase Agreement with certain new investors and certain of its existing investors (each, a "Share Purchaser" and, collectively, the "Share Purchasers"), pursuant to which, PMI issued and sold to such Share Purchasers (either directly or through certain of their respective affiliates) 138,681,680 shares of PMI's new Series A preferred stock (the "Shares") for an aggregate purchase price of $20,000. In connection with that sale, PMI also issued 51,171,951 shares at the par value $0.001 per share of Series A-1 convertible preferred stock to certain previous holders of PMI's preferred stock who participated in the sale. The Series A-1 shares established certain liquidation rights, have no voting rights and are convertible into one share of PMI common stock for every one million shares of Series A-1 preferred stock. PMI allocated the fair value of the shares of Series A-1 preferred stock at the par value of $.001 per share from the proceeds of Series A preferred stock. Upon issuance of PMI Series A and Series A-1 preferred stock, all of PMI's preferred stock existing prior to such issuance was converted into PMI common stock at a 1:1 ratio if the holder of the preferred stock participated in the new Series A preferred stock sale or at a 10:1 ratio if the holder of the existing preferred stock did not so participate.

INFORMATION FOR THIS ITEM IS NOT REQUIRED FOR PROSPER FUNDING BECAUSE IT MEETS THE CONDITIONS SET FORTH IN GENERATION INSTRUCTION H(1)(a) AND (b) OF FORM 10-Q AND THEREFORE IS FILING THIS FORM WITH A REDUCED FILING FORMAT.

## Item 3. Defaults upon Senior Securities

Not applicable.

## Item 4. Mine Safety Disclosures

Not applicable.

## Item 5. Other Information

Not applicable.

## Item 6. Exhibits

The exhibits listed on the accompanying Exhibit Index are filed or incorporated by reference as a part of this report and such Exhibit Index is incorporated herein by reference.

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

PROSPER MARKETPLACE, INC.
PROSPER FUNDING LLC

| | |
|---|---|
| Date: August 14, 2013 | /s/ Stephan Vermut<br>Stephan Vermut<br>Chief Executive Officer of Prosper Marketplace, Inc.<br>Chief Executive Officer of Prosper Funding LLC<br>(*principal executive officer*) |
| Date: August 14, 2013 | /s/ Kenneth L. Niewald<br>Kenneth L. Niewald<br>Chief Financial Officer of Prosper Marketplace, Inc.<br>Treasurer of Prosper Funding LLC<br>(*principal financial and accounting officer*) |

EXHIBIT INDEX

| Exhibit Number | Exhibit Description |
|---|---|
| 3.1 | Third Amended and Restated Limited Liability Company Agreement of Prosper Funding, dated June 4, 2013 (incorporated by reference to Exhibit 3.1 of the Current Report on Form 8-K, filed June 5, 2013 by Prosper Funding and PMI) |
| 3.2 | Amended and Restated Certificate of Incorporation of PMI(incorporated by reference to Exhibit 3.1 of the Registration Statement on Form S-8, filed August 1, 2013 by and PMI) |
| 3.3 | Prosper Funding Certificate of Formation (incorporated by reference to Exhibit 3.2 of the Registration Statement on Form S-1/A, filed April 23, 2012 by Prosper Funding and PMI) |
| 3.4 | Bylaws of PMI, dated March 22, 2005 (incorporated by reference to Exhibit 3.2 of the Registration Statement on Form S-1, filed October 30, 2007 by PMI) |
| 4.1 | First Supplemental Indenture, dated May 10, 2013, between Prosper Funding LLC and Wells Fargo Bank, National Association |
| 10.1 | Form of Prosper Funding Borrower Registration Agreement (incorporated by reference to Exhibit 10.1 of Post-Effective Amendment No. 2 to the Registration Statement on Form S-1, filed April 24, 2013 by Prosper Funding and PMI) |
| 10.2 | Form of Lender Registration Agreement (incorporated by reference to Exhibit 10.2 of Post-Effective Amendment No. 2 to the Registration Statement on Form S-1, filed April 24, 2013 by Prosper Funding and PMI) |
| 10.3 | Amended and Restated Services Indemnity Agreement, between Prosper Funding LLC, Prosper Marketplace, Inc., Global Securitization Services, LLC, Bernard J. Angelo and David V. DeAngelis, dated May 30, 2013 (incorporated by reference to Exhibit 10.1 of the Current Report on Form 8-K, filed June 5, 2013 by Prosper Funding and PMI) |
| 31.1 | Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, with respect to PMI’s Quarterly Report on Form 10-Q for the quarter ended June 30, 2013. |
| 31.2 | Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, with respect to PMI’s Quarterly Report on Form 10-Q for the quarter ended June 30, 2013. |
| 31.3 | Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, with respect to Prosper Funding’s Quarterly Report on Form 10-Q for the quarter ended June 30, 2013. |
| 31.4 | Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, with respect to Prosper Funding’s Quarterly Report on Form 10-Q for the quarter ended June 30, 2013. |
| 32.1 | Certification of Principal Executive Officer and Principal Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, with respect to PMI’s Quarterly Report on Form 10-Q for the quarter ended June 30, 2013. |
| 32.2 | Certification of Principal Executive Officer and Principal Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, with respect to Prosper Funding’s Quarterly Report on Form 10-Q for the quarter ended June 30, 2013. |
| 101.INS | XBRL Instance Documents |
| 101.SCH | XBRL Taxonomy Extension Schema Document |
| 101.CAL | Taxonomy Extension Calculation Linkbase Document |
| 101.LAB | Taxonomy Extension Label Linkbase Document |
| 101.PRE | Taxonomy Extension Presentation Linkbase Document |
| 101.DEF | Taxonomy Extension Definition Linkbase Document |

**Exhibit 3.2**

**CERTIFICATE OF AMENDMENT TO**

**AMENDED AND RESTATED CERTIFICATE OF INCORPORATION OF**

**PROSPER MARKETPLACE, INC.**

Prosper Marketplace, Inc., a corporation duly organized and existing under the General Corporation Law of the State of Delaware, does hereby certify that:.

**First**: The name of corporation is Prosper Marketplace, Inc.

**Second**: The corporation's original certificate of incorporation was filed with the Secretary of State of the State of Delaware on March 22, 2005, under the name of JC Capital Solutions, Inc. The corporation changed its name to P2P Credit, Inc. pursuant to an amended and restated certificate of incorporation filed with the Secretary of State of the State of Delaware on April 20, 2005; to CircleOne Holdings, Inc. pursuant to an amended certificate of incorporation filed with the Secretary of State of the State of Delaware on October 17, 2005; and to Prosper Marketplace, Inc. pursuant to an amended and restated certificate of incorporation filed with the Secretary of State of the State of Delaware on February 6, 2006.

**Third**: The amended and restated certificate of incorporation of the corporation is hereby amended by deleting Article IV thereof and inserting the following in lieu thereof:

ARTICLE IV

The total number of shares of stock that the corporation shall have authority to issue is 489,853,631, consisting of 300,000,000 shares of Common Stock, $0.001 par value per share, and 189,853,631 shares of Preferred Stock, $0.001 par value per share, 138,681,680 of which are designated as "**Series A Preferred Stock**" and 51,171,951 of which are designated as "**Series A-1 Preferred Stock**."

**Fourth**: The foregoing amendment was duly adopted in accordance with the provisions of Sections 242 and 228 (by the written consent of the stockholders of the corporation) of the General Corporation Law of the State of Delaware.

**In Witness Whereof**, Prosper Marketplace, Inc. has caused this Certificate of Amendment to be executed by its duly authorized officer on this 19th day of July, 2013.

/s/ Sachin Adarkar

Name: Sachin Adarkar
Title: General Counsel & Secretary

**AMENDED AND RESTATED CERTIFICATE OF INCORPORATION OF PROSPER MARKETPLACE, INC.**

ARTICLE I

The name of the Corporation is Prosper Marketplace, Inc.

ARTICLE II

The purpose of the Corporation is to engage in any lawful act or activity for which corporations may be organized under the General Corporation Law of Delaware.

ARTICLE III

The address of the Corporation's registered office in the State of Delaware is 615 South DuPont Highway, City of Dover, County of Kent, 19901. The name of the registered agent at such address is National Corporate Research, Ltd.

ARTICLE IV

The total number of shares of stock that the corporation shall have authority to issue is 467,217,091, consisting of 277,363,460 shares of Common Stock, $0.001 par value per share, and 189,853,631 shares of Preferred Stock, $0.001 par value per share, 138,681,680 of which are designated as "**Series A Preferred Stock**" and 51,171,951 of which are designated as "**Series A-1 Preferred Stock**."

ARTICLE V

1. Definitions. For purposes of this ARTICLE V, the following definitions shall apply:

(a) "**Conversion Price**" shall mean $0.144215155 per share for the Series A Preferred Stock and $0.10 per share for the Series A-1 Preferred Stock (subject to adjustment from time to time for Recapitalizations and as otherwise set forth elsewhere herein).

(b) "**Convertible Securities**" shall mean any evidences of indebtedness, shares or other securities convertible into or exchangeable for Common Stock.

(c) "**Corporation**" shall mean Prosper Marketplace, Inc.

(d) "**Distribution**" shall mean the transfer of cash or other property without consideration whether by way of dividend or otherwise, other than dividends on Common Stock payable in Common Stock, or the purchase or redemption of shares of the Corporation for cash or property other than: (i) repurchases of Common Stock issued to or held by employees, officers, directors or consultants of the Corporation or its subsidiaries upon termination of their employment or services pursuant to agreements providing for the right of said repurchase, (ii) repurchases of Common Stock issued to or held by employees, officers, directors or consultants of the Corporation or its subsidiaries pursuant to rights of first refusal contained in agreements providing for such right, (iii) repurchase of capital stock of the Corporation in connection with the settlement of disputes with any stockholder that is approved by the Board of Directors or (iv) any other repurchase or redemption of capital stock of the Corporation approved by the Board of Directors.

(e) “**Liquidation Preference**” shall mean $0.144215155 per share for the Series A Preferred Stock and $1.00 per share for the Series A-1 Preferred Stock (subject to adjustment from time to time for Recapitalizations as set forth elsewhere herein).

(f) “**Options**” shall mean rights, options or warrants to subscribe for, purchase or otherwise acquire Common Stock or Convertible Securities.

(g) “**Original Issue Price**” shall mean $0.144215155 per share for the Series A Preferred Stock and $0.0000001 per share for the Series A-1 Preferred Stock (subject to adjustment from time to time for Recapitalizations as set forth elsewhere herein).

(h) “**Preferred Stock**” shall mean the Series A Preferred Stock and Series A-1 Preferred Stock.

(i) “**Recapitalization**” shall mean any stock dividend, stock split, combination of shares, reorganization, recapitalization, reclassification or other similar event.

2. Dividends. No Distributions shall be made with respect to the Common Stock until all declared dividends (if any) on the Series A Preferred Stock have been paid or set aside for payment to the Series A Preferred Stock holders. After payment of such dividends, any additional dividends or distributions shall be distributed among all holders of Common Stock and Preferred Stock in proportion to the number of shares of Common Stock that would be held by each such holder if all shares of Preferred Stock were converted to Common Stock at the then effective conversion rate.

3. Liquidation Rights.

(a) Liquidation Preference. In the event of any Liquidation Event (as defined below), either voluntary or involuntary, distributions shall be made in the following manner:

(i) The holders of Series A Preferred Stock shall be entitled to receive, prior and in preference to any Distribution of the proceeds of such Liquidation Event (the “**Proceeds**”) to the holders of Series A-1 Preferred Stock or Common Stock by reason of their ownership of such stock, an amount per share for each share of Series A Preferred Stock held by them equal to the sum of (A) the Liquidation Preference specified for such share of Series A Preferred Stock and (B) all declared but unpaid dividends (if any) on such share of Series A Preferred Stock. If upon such Liquidation Event, the assets of the Corporation legally available for distribution to the holders of the Series A Preferred Stock are insufficient to permit the payment to such holders of the full amounts specified in this Section 3(a)(i), then the entire assets of the Corporation legally available for distribution shall be distributed with equal priority and pro rata among the holders of the Series A Preferred Stock in proportion to the full amounts they would otherwise be entitled to receive pursuant to this Section 3(a)(i).

(ii) After the payment or setting aside for payment to the holders of Series A Preferred Stock of the full amounts specified in 3(a)(i) above, the holders of Series A-1 Preferred Stock shall be entitled to receive, prior and in preference to any Distribution of Proceeds to the holders of Common Stock by reason of their ownership of such stock, an amount per share for each share of Series A-1 Preferred Stock held by them equal to the sum of (A) the Liquidation Preference specified for such share of Series A-1 Preferred Stock and (B) all declared but unpaid dividends (if any) on such share of Series A-1 Preferred Stock. If upon such Liquidation Event, the assets of the Corporation legally available for distribution to the holders of the Series A-1 Preferred Stock are insufficient to permit the payment to such holders of the full amounts specified in this Section 3(a)(ii), then the remaining assets of the Corporation legally available for distribution shall be distributed with equal priority and pro rata among the holders of the Series A-1 Preferred Stock in proportion to the full amounts they would otherwise be entitled to receive pursuant to this Section 3(a)(ii).

(b) Remaining Assets. After the payment or setting aside for payment to the holders of Series A Preferred Stock and Series A-1 Preferred Stock of the full amounts specified in Sections 3(a)(i) and 3(a)(ii) above, the entire remaining Proceeds legally available for distribution shall be distributed pro rata to the holders of Series A Preferred Stock and Common Stock in proportion to the number of shares of Common Stock held by them (assuming for this purpose that all outstanding shares of Series A Preferred Stock had been converted into shares of Common Stock at the then effective Conversion Rate (as defined below) for Series A Preferred Stock immediately prior to such Liquidation Event); *provided*, *however*, that the maximum aggregate amount per share of Series A Preferred Stock which the holders of Series A Preferred Stock shall be entitled to receive pursuant to Sections 3.1(a)(i) and 3.1(b) is three (3) times the Original Issue Price for the Series A Preferred Stock.

(c) Shares not Treated as Both Preferred Stock and Common Stock in any Distribution. Subject to the rights of holders of Series A Preferred Stock to participate in the distribution of remaining assets as set forth in Section 3(b) above, shares of Preferred Stock shall not be entitled to be converted into shares of Common Stock in order to participate in any Distribution, or series of Distributions, as shares of Common Stock, without first foregoing participation in the Distribution, or series of Distributions, as shares of Preferred Stock.

(d) Liquidation Event. A "**Liquidation Event**" shall be deemed to be occasioned by, or to include, each of the following events unless the holders of at least seventy percent (70%) of the voting power of all then outstanding shares of Series A Preferred Stock and Series A-1 Preferred Stock, voting as a single class on an as converted basis, elect otherwise by written notice sent to the Corporation at least 5 days prior to the effective date of any such event: (i) the acquisition of the Corporation by another entity by means of any transaction or series of related transactions (including, without limitation, any stock acquisition, reorganization, merger or consolidation but excluding any sale of stock for capital raising purposes) other than a transaction or series of transactions in which the holders of the voting securities of the Corporation outstanding immediately prior to such transaction continue to retain in the same relative proportions as to each other (either by such voting securities remaining outstanding or by such voting securities being converted into voting securities of the surviving entity), as a result of shares in the Corporation held by such holders prior to such transaction, at least fifty percent (50%) of the total voting power represented by the voting securities of the Corporation or such surviving entity outstanding immediately after such transaction or series of transactions; (ii) a sale, lease, transfer, exclusive license or other conveyance (in a single transaction or series of related transactions) of all or substantially all of the assets of the Corporation and its subsidiaries taken as a whole; (iii) the sale or disposition (whether by merger or otherwise) of one or more subsidiaries of the Corporation if substantially all of the assets of the Corporation and its subsidiaries taken as a whole are held by such subsidiary or subsidiaries, except where such sale, lease, transfer, exclusive license or other disposition is to the Corporation or to a wholly owned subsidiary of the Corporation; or (iv) any liquidation, dissolution or winding up of the Corporation, whether voluntary or involuntary.

(e) Valuation of Non-Cash Consideration. If any Proceeds distributed to stockholders in connection with any Liquidation Event are other than cash, then the value of such assets shall be their fair market value as determined in good faith by the Board of Directors, except that any publicly-traded securities to be distributed to stockholders in a Liquidation Event shall be valued as follows:

(i) Securities not subject to an investment letter:

(1) If the securities are then traded on a national securities exchange or the Nasdaq Stock Market (or a similar national quotation system), then the value of the securities shall be deemed to be the average of the closing prices of the securities on such exchange or system over the twenty (20) trading day period ending five (5) trading days prior to the Distribution; or

(2) if the securities are actively traded over-the-counter, then the value of the securities shall be deemed to be the average of the closing bid prices of the securities over the twenty (20) trading day period ending five (5) trading days prior to the Distribution.

(ii) The method of valuation of securities subject to an investment letter shall be to make an appropriate discount from the market value determined as above in (i)(1), or (2) to reflect the approximate fair market value thereof, as mutually determined by the Corporation and the holders of at least a majority of the voting power of all then outstanding shares of such Preferred Stock.

(iii) The foregoing methods for valuing non-cash consideration to be distributed in connection with a Liquidation Event shall, upon approval by the stockholders of the definitive agreements governing a Liquidation Event, be superseded by any determination of such value set forth in the definitive agreements governing such Liquidation Event.

In the event of a merger or other acquisition of the Corporation by another entity, the Distribution date shall be deemed to be the date such transaction closes.

4. Conversion. The holders of the Preferred Stock shall have conversion rights as follows:

(a) Right to Convert. Each share of Preferred Stock shall be convertible, at the option of the holder thereof, at any time after the date of issuance of such share at the office of the Corporation or any transfer agent for the Preferred Stock, into that number of fully-paid, nonassessable shares of Common Stock determined by dividing the Original Issue Price for the relevant series by the Conversion Price for such series. (The number of shares of Common Stock into which each share of Preferred Stock of a series may be converted is hereinafter referred to as the "**Conversion Rate**" for each such series.) Upon any decrease or increase in the Conversion Price for any series of Preferred Stock, as described in this Section 4, the Conversion Rate for such series shall be appropriately increased or decreased.

(b) Automatic Conversion. Each share of Preferred Stock shall automatically be converted into fully-paid, non-assessable shares of Common Stock at the then effective Conversion Rate for such share (i) immediately prior to the closing of an underwritten initial public offering at a price per share (prior to underwriting commissions and expenses) that values the Corporation at least $200,000,000 in an offering with aggregate proceeds to the Corporation of not less than $40,000,000 (before deducting underwriters commissions and expenses), pursuant to an effective registration statement filed under the Securities Act of 1933, as amended (the "**Securities Act**"), covering the offer and sale of the Corporation's Common Stock, or (ii) upon the receipt by the Corporation of a written request for such conversion from the holders of at least seventy percent (70%) of the voting power of all then outstanding shares of Preferred Stock on an as converted basis (the "**Required Vote**"), or, if later, the effective date for conversion specified in such requests. In addition, if and when a Liquidation Event occurs in which any of a holder's shares of Series A Preferred Stock have been converted into Converted Stock then all shares of Series A-1 Preferred Stock held by such holder shall automatically be converted into fully-paid, non-assessable shares of Common Stock at the then effective Conversion Rate for such shares immediately prior to such Liquidation Event. Each of the events referred to in this Section 4(b) is referred to herein as an "**Automatic Conversion Event**."

(c) Mechanics of Conversion. No fractional shares of Common Stock shall be issued upon conversion of Preferred Stock. In lieu of any fractional shares to which the holder would otherwise be entitled, the Corporation shall pay cash equal to such fraction multiplied by the then fair market value of a share of Common Stock as determined by the Board of Directors. For such purpose, all shares of Preferred Stock held by each holder of Preferred Stock shall be aggregated, and any resulting fractional share of Common Stock shall be paid in cash. Before any holder of Preferred Stock shall be entitled to convert the same into full shares of Common Stock, and to receive certificates therefor, such holder shall either (A) surrender the certificate or certificates therefor, duly endorsed, at the office of the Corporation or of any transfer agent for the Preferred Stock or (B) notify the Corporation or its transfer agent that such certificates have been lost, stolen or destroyed and execute an agreement satisfactory to the Corporation to indemnify the Corporation from any loss incurred by it in connection with such certificates, and shall give written notice to the Corporation at such office that such holder elects to convert the same; *provided*, *however*, that on the date of an Automatic Conversion Event, the outstanding shares of Preferred Stock being thereby converted shall be converted automatically without any further action by the holders of such shares and whether or not the certificates representing such shares are surrendered to the Corporation or its transfer agent; *provided further*, *however*, that the Corporation shall not be obligated to issue certificates evidencing the shares of Common Stock issuable upon such Automatic Conversion Event unless either the certificates evidencing such shares of Preferred Stock are delivered to the Corporation or its transfer agent as provided above, or the holder notifies the Corporation or its transfer agent that such certificates have been lost, stolen or destroyed and executes an agreement satisfactory to the Corporation to indemnify the Corporation from any loss incurred by it in connection with such certificates. On the date of the occurrence of an Automatic Conversion Event, each holder of record of shares of Preferred Stock being thereby converted shall be deemed to be the holder of record of the Common Stock issuable upon such conversion, notwithstanding that the certificates representing such shares of Preferred Stock shall not have been surrendered at the office of the Corporation, that notice from the Corporation shall not have been received by any holder of record of shares of Preferred Stock, or that the certificates evidencing such shares of Common Stock shall not then be actually delivered to such holder.

(d) Adjustments to Conversion Price for Diluting Issues.

(i) Special Definition. For purposes of this paragraph 4(d), "**Additional Shares of Common**" shall mean all shares of Common Stock issued (or, pursuant to paragraph 4(d)(iii), deemed to be issued) by the Corporation after the filing of this Amended and Restated Certificate of Incorporation, other than issuances or deemed issuances of:

(1) Common Stock and options, warrants or other rights to purchase Common Stock issued to employees, officers or directors of, or consultants or advisors to the Corporation or any subsidiary pursuant to restricted stock purchase agreements, stock option plans or similar arrangements approved by the Board of Directors of the Corporation;

(2) shares of Common Stock issued upon the exercise or conversion of Options or Convertible Securities outstanding as of the date of the filing of this Amended and Restated Certificate of Incorporation;

(3) shares of Common Stock issued or issuable as a dividend or distribution on Series A Preferred Stock in accordance with the provisions of Section 2 hereof or pursuant to any event for which adjustment is made pursuant to paragraph 4(e), 4(f) or 4(g) hereof;

(4) shares of Common Stock issued in an initial registered public offering under the Securities Act in which all Preferred Stock converts to Common Stock;

(5) shares of Common Stock issued or issuable pursuant to the acquisition of another corporation by the Corporation by merger, purchase of substantially all of the assets or other reorganization or to a joint venture agreement, provided, that such issuances are approved by the Board of Directors;

(6) shares of Common Stock issued or issuable pursuant to a strategic transaction, other than for primarily equity financing purposes, provided, that such issuances are approved by the Board of Directors;

(7) shares of Common Stock issued or issuable to banks, equipment lessors or other financial institutions pursuant to a debt financing or commercial leasing transaction other than for primarily equity financing purposes approved by the Board of Directors;

(8) shares of Common Stock issued or issuable in connection with any settlement of any action, suit, proceeding or litigation approved by the Board of Directors;

(9) shares of Common Stock issued or issuable in connection with sponsored research, collaboration, technology license, development, OEM, marketing or other similar agreements or strategic partnerships approved by the Board of Directors;

(10) shares of Common Stock issued or issuable to suppliers or third party service providers in connection with the provision of goods or services pursuant to transactions approved by the Board of Directors;

(11) shares of Series A Preferred Stock issued pursuant to that certain Series A Preferred Stock Purchase Agreement dated on or around the date of filing of this Amended and Restated Certificate of Incorporation (the "**Purchase Agreement**"), and shares of Common Stock issued upon conversion thereof;

(12) shares of Series A-1 Preferred Stock issued pursuant to the Purchase Agreement, and shares of Common Stock issued upon conversion thereof; and

(13) securities deemed issued pursuant to the operation of paragraph (iii) below.

(ii) No Adjustment of Conversion Price. No adjustment in the Conversion Price of a particular series of Preferred Stock shall be made in respect of the issuance of Additional Shares of Common unless the consideration per share (as determined pursuant to paragraph 4(d)(v)) for an Additional Share of Common issued or deemed to be issued by the Corporation is less than the Conversion Price in effect on the date of, and immediately prior to such issue, for such series of Preferred Stock.

(iii) Deemed Issue of Additional Shares of Common. In the event the Corporation at any time or from time to time after the date of the filing of this Amended and Restated Certificate of Incorporation shall issue any Options or Convertible Securities or shall fix a record date for the determination of holders of any class of securities entitled to receive any such Options or Convertible Securities, then the maximum number of shares (as set forth in the instrument relating thereto without regard to any provisions contained therein for a subsequent adjustment of such number) of Common Stock issuable upon the exercise of such Options or, in the case of Convertible Securities, the conversion or exchange of such Convertible Securities or, in the case of Options for Convertible Securities, the exercise of such Options and the conversion or exchange of the underlying securities, shall be deemed to have been issued as of the time of such issue or, in case such a record date shall have been fixed, as of the close of business on such record date, provided that in any such case in which shares are deemed to be issued:

(1) no further adjustment in the Conversion Price of any series of Preferred Stock shall be made upon the subsequent issue of Convertible Securities or shares of Common Stock in connection with the exercise of such Options or conversion or exchange of such Convertible Securities;

(2) if such Options or Convertible Securities by their terms provide, with the passage of time or otherwise, for any change in the consideration payable to the Corporation or in the number of shares of Common Stock issuable upon the exercise, conversion or exchange thereof (other than a change pursuant to the anti-dilution provisions of such Options or Convertible Securities such as this Section 4(d) or pursuant to Recapitalization provisions of such Options or Convertible Securities such as Sections 4(e), 4(f) and 4(g) hereof), the Conversion Price of each series of Preferred Stock and any subsequent adjustments based thereon shall be recomputed to reflect such change as if such change had been in effect as of the original issue thereof (or upon the occurrence of the record date with respect thereto);

(3) no readjustment pursuant to clause (2) above shall have the effect of increasing the Conversion Price of a series of Preferred Stock to an amount above the Conversion Price that would have resulted from any other issuances of Additional Shares of Common and any other adjustments provided for herein between the original adjustment date and such readjustment date;

(4) upon the expiration of any such Options or any rights of conversion or exchange under such Convertible Securities which shall not have been exercised, the Conversion Price of each Series of Preferred Stock computed upon the original issue thereof (or upon the occurrence of a record date with respect thereto) and any subsequent adjustments based thereon shall, upon such expiration, be recomputed as if:

(a) in the case of Convertible Securities or Options for Common Stock, the only Additional Shares of Common issued were the shares of Common Stock, if any, actually issued upon the exercise of such Options or the conversion or exchange of such Convertible Securities and the consideration received therefor was the consideration actually received by the Corporation for the issue of such exercised Options plus the consideration actually received by the Corporation upon such exercise or for the issue of all such Convertible Securities which were actually converted or exchanged, plus the additional consideration, if any, actually received by the Corporation upon such conversion or exchange; and

(b) in the case of Options for Convertible Securities, only the Convertible Securities, if any, actually issued upon the exercise thereof were issued at the time of issue of such Options, and the consideration received by the Corporation for the Additional Shares of Common deemed to have been then issued was the consideration actually received by the Corporation for the issue of such exercised Options, plus the consideration deemed to have been received by the Corporation (determined pursuant to Section 4(d)(v)) upon the issue of the Convertible Securities with respect to which such Options were actually exercised; and

(5) if such record date shall have been fixed and such Options or Convertible Securities are not issued on the date fixed therefor, the adjustment previously made in the Conversion Price which became effective on such record date shall be canceled as of the close of business on such record date, and thereafter the Conversion Price shall be adjusted pursuant to this paragraph 4(d)(iii) as of the actual date of their issuance.

(iv) Adjustment of Conversion Price Upon Issuance of Additional Shares of Common. In the event the Corporation shall issue Additional Shares of Common (including Additional Shares of Common deemed to be issued pursuant to paragraph 4(d)(iii)) without consideration or for a consideration per share less than the applicable Conversion Price of a series of Preferred Stock in effect on the date of and immediately prior to such issue, then, the Conversion Price of the affected series of Preferred Stock shall be reduced, concurrently with such issue, to a price (calculated to the nearest cent) determined by multiplying such Conversion Price by a fraction, the numerator of which shall be the number of shares of Common Stock outstanding immediately prior to such issue plus the number of shares which the aggregate consideration received by the Corporation for the total number of Additional Shares of Common so issued would purchase at such Conversion Price, and the denominator of which shall be the number of shares of Common Stock outstanding immediately prior to such issue plus the number of such Additional Shares of Common so issued. Notwithstanding the foregoing, the Conversion Price shall not be reduced at such time if the amount of such reduction would be less than $0.01, but any such amount shall be carried forward, and a reduction will be made with respect to such amount at the time of, and together with, any subsequent reduction which, together with such amount and any other amounts so carried forward, equal $0.01 or more in the aggregate. For the purposes of this Subsection 4(d)(iv), all shares of Common Stock issuable upon conversion of all outstanding shares of Preferred Stock and the exercise and/or conversion of any other outstanding Convertible Securities and all outstanding Options shall be deemed to be outstanding.

(v) Determination of Consideration. For purposes of this Subsection 4(d), the consideration received by the Corporation for the issue (or deemed issue) of any Additional Shares of Common shall be computed as follows:

(1) Cash and Property. Such consideration shall:

(a) insofar as it consists of cash, be computed at the aggregate amount of cash received by the Corporation before deducting any reasonable discounts, commissions or other expenses allowed, paid or incurred by the Corporation for any underwriting or otherwise in connection with such issuance;

(b) insofar as it consists of property other than cash, be computed at the fair market value thereof at the time of such issue, as determined in good faith by the Board of Directors; and

(c) in the event Additional Shares of Common are issued together with other shares or securities or other assets of the Corporation for consideration which covers both, be the proportion of such consideration so received, computed as provided in clauses (a) and (b) above, as reasonably determined in good faith by the Board of Directors.

(2) Options and Convertible Securities. The consideration per share received by the Corporation for Additional Shares of Common deemed to have been issued pursuant to paragraph 4(d)(iii) shall be determined by dividing

(x) the total amount, if any, received or receivable by the Corporation as consideration for the issue of such Options or Convertible Securities, plus the minimum aggregate amount of additional consideration (as set forth in the instruments relating thereto, without regard to any provision contained therein for a subsequent adjustment of such consideration) payable to the Corporation upon the exercise of such Options or the conversion or exchange of such Convertible Securities, or in the case of Options for Convertible Securities, the exercise of such Options for Convertible Securities and the conversion or exchange of such Convertible Securities by

(y) the maximum number of shares of Common Stock (as set forth in the instruments relating thereto, without regard to any provision contained therein for a subsequent adjustment of such number) issuable upon the exercise of such Options or the conversion or exchange of such Convertible Securities.

(e) Adjustments for Subdivisions or Combinations of Common Stock. In the event the outstanding shares of Common Stock shall be subdivided (by stock split, by payment of a stock dividend or otherwise), into a greater number of shares of Common Stock, the Conversion Price of each series of Preferred Stock in effect immediately prior to such subdivision shall, concurrently with the effectiveness of such subdivision, be proportionately decreased. In the event the outstanding shares of Common Stock shall be combined (by reclassification or otherwise) into a lesser number of shares of Common Stock, the Conversion Prices in effect immediately prior to such combination shall, concurrently with the effectiveness of such combination, be proportionately increased.

(f) Adjustments for Subdivisions or Combinations of Preferred Stock. In the event the outstanding shares of Preferred Stock or a series of Preferred Stock shall be subdivided (by stock split, by payment of a stock dividend or otherwise), into a greater number of shares of Preferred Stock, the Conversion Price, the Original Issue Price and the Liquidation Preference of the affected series of Preferred Stock in effect immediately prior to such subdivision shall, concurrently with the effectiveness of such subdivision, be proportionately decreased. In the event the outstanding shares of Preferred Stock or a series of Preferred Stock shall be combined (by reclassification or otherwise) into a lesser number of shares of Preferred Stock, the Conversion Price, the Original Issue Price and the Liquidation Preference of the affected series of Preferred Stock in effect immediately prior to such combination shall, concurrently with the effectiveness of such combination, be proportionately increased.

(g) Adjustments for Reclassification, Exchange and Substitution. Subject to Section 3 above, if the Common Stock issuable upon conversion of the Preferred Stock shall be changed into the same or a different number of shares of any other class or classes of stock, whether by capital reorganization, reclassification or otherwise (other than a subdivision or combination of shares provided for above), then, in any such event, in lieu of the number of shares of Common Stock which the holders would otherwise have been entitled to receive each holder of such Preferred Stock shall have the right thereafter to convert such shares of Preferred Stock into a number of shares of such other class or classes of stock which a holder of the number of shares of Common Stock deliverable upon conversion of such series of Preferred Stock immediately before that change would have been entitled to receive in such reorganization or reclassification, all subject to further adjustment as provided herein with respect to such other shares.

(h) Certificate as to Adjustments. Upon the occurrence of each adjustment or readjustment of the Conversion Price pursuant to this Section 4, the Corporation at its expense shall promptly compute such adjustment or readjustment in accordance with the terms hereof and furnish to each holder of Preferred Stock a certificate setting forth such adjustment or readjustment and showing in detail the facts upon which such adjustment or readjustment is based. The Corporation shall, upon the written request at any time of any holder of Preferred Stock, furnish or cause to be furnished to such holder a like certificate setting forth (i) such adjustments and readjustments, (ii) the Conversion Price at the time in effect and (iii) the number of shares of Common Stock and the amount, if any, of other property which at the time would be received upon the conversion of Preferred Stock.

(i) Waiver of Adjustment of Conversion Price. Notwithstanding anything herein to the contrary, any downward adjustment of the Conversion Price of any series of Preferred Stock may be waived by the consent or vote of the holders of at least seventy percent (70%) of the outstanding shares of such series, either before or after the issuance causing the adjustment. Any such waiver shall bind all future holders of shares of such series of Preferred Stock.

(j) Reservation of Stock Issuable Upon Conversion. The Corporation shall at all times reserve and keep available out of its authorized but unissued shares of Common Stock solely for the purpose of effecting the conversion of the shares of the Preferred Stock, such number of its shares of Common Stock as shall from time to time be sufficient to effect the conversion of all then outstanding shares of the Preferred Stock; and if at any time the number of authorized but unissued shares of Common Stock shall not be sufficient to effect the conversion of all then outstanding shares of the Preferred Stock, the Corporation will take such corporate action as may, in the opinion of its counsel, be necessary to increase its authorized but unissued shares of Common Stock to such number of shares as shall be sufficient for such purpose.

5. Voting.

(a) Restricted Class Voting. Except as otherwise expressly provided herein or as required by law, the holders of Preferred Stock and the holders of Common Stock shall vote together and not as separate classes.

(b) No Series Voting. Other than as provided herein or required by law, there shall be no series voting.

(c) Preferred Stock. Each holder of Preferred Stock shall be entitled to the number of votes equal to the number of shares of Common Stock into which the shares of Preferred Stock held by such holder could be converted as of the record date in accordance with the provisions of Section 4 hereof. The holders of shares of the Preferred Stock shall be entitled to vote on all matters on which the Common Stock shall be entitled to vote. Holders of Preferred Stock shall be entitled to notice of any stockholders' meeting in accordance with the Bylaws of the Corporation. Fractional votes shall not, however, be permitted and any fractional voting rights resulting from the above formula (after aggregating all shares into which shares of Preferred Stock held by each holder could be converted), shall be disregarded.

(d) Election of Directors. So long as at least 10,000,000 shares (as adjusted for Recapitalizations) of Series A Preferred Stock remain outstanding, the holders of shares of Series A Preferred Stock, voting as a separate class, shall be entitled to elect one (1) member of the Corporation's Board of Directors at each meeting or pursuant to each consent of the Corporation's stockholders for the election of directors, and so long as at least 10,000,000 shares (as adjusted for Recapitalizations) of Series A-1 Preferred Stock remain outstanding, the holders of shares of Series A-1 Preferred Stock, voting as a separate class, shall be entitled to elect one (1) member of the Corporation's Board of Directors at each meeting or pursuant to each consent of the Corporation's stockholders for the election of directors Any additional members of the Corporation's Board of Directors shall be elected by the holders of Common Stock, Series A Preferred Stock and Series A-1 Preferred Stock, voting together as a single class, on an as converted basis. If a vacancy on the Board of Directors is to be filled by the Board of Directors, only directors elected by the same class or classes of stockholders as those who would be entitled to vote to fill such vacancy shall vote to fill such vacancy.

(e) Adjustment in Authorized Common Stock. Notwithstanding the provisions of Section 242(b)(2) of the General Corporation Law of the State of Delaware to the contrary, the number of authorized shares of Common Stock may be increased or decreased (but not below the number of shares of Common Stock then outstanding) by an affirmative vote of the holders of a majority of the votes applicable to the then outstanding stock of the Corporation.

(f) Common Stock. Each holder of shares of Common Stock shall be entitled to one vote for each share thereof held.

6. Amendments and Changes.

(a) As long as at least 10,000,000 shares (as adjusted for Recapitalizations) of the Preferred Stock shall be issued and outstanding, the Corporation shall not (by amendment, consolidation, merger or otherwise), without first obtaining (in addition to any other vote required by law or this Amended and Restated Certificate of Incorporation) the approval by vote or written consent as provided by law of the holders of at least seventy percent (70%) of the voting power of all then outstanding shares of Preferred Stock:

(i) amend, alter or repeal any provision of this Amended and Restated Certificate of Incorporation or the Bylaws of the Corporation, whether by merger or otherwise, if such action would adversely alter the rights, preferences, privileges or powers of, or restrictions provided for the benefit of the Preferred Stock or any series thereof;

(ii) increase or decrease (other than decreases resulting from conversion of the Preferred Stock) the authorized number of shares of Common Stock or Preferred Stock or any series thereof;

(iii) authorize or create (by reclassification, merger or otherwise), or permit any subsidiary to authorize or create, any new class or series of shares having rights, preferences or privileges with respect to dividends, redemption or payments upon liquidation senior to or on a parity with any series of Preferred Stock or having voting rights other than those granted to the Preferred Stock generally;

(iv) take any action, or permit any subsidiary to take any action, resulting in the repurchase or redemption of shares of Common Stock or Preferred Stock, other than the repurchase of shares of Common Stock or Preferred Stock issued to or held by employees, officers, directors or consultants of or to the Corporation or any of its subsidiaries upon termination of their employment or services approved by the Board of Directors or pursuant to agreements providing for the right of such repurchase between the Corporation and such persons;

(v) consummate a Liquidation Event;

(vi) declare or pay, or permit any subsidiary to declare or pay, any Distribution with respect to the Preferred Stock or Common Stock of the Corporation or the capital stock of any subsidiary, unless such Distribution is made to the Corporation or any of its wholly owned subsidiaries;

(vii) take any action resulting in the increase or decrease of the authorized size of the Board of Directors;

(viii) create, or hold capital stock in, any subsidiary that is not wholly owned (either directly or through one or more other subsidiaries) by the Corporation, or sell, transfer or otherwise dispose of any capital stock of any direct or indirect subsidiary of the Corporation, or permit any direct or indirect subsidiary to sell, lease, transfer, exclusively license or otherwise dispose (in a single transaction or series of related transactions) all or substantially all of the assets of such subsidiary, unless such sale, transfer, license or disposal is to the Corporation or any of its wholly owned subsidiaries; or

(ix) amend this Section 6(a).

7. Redemption. The Preferred Stock is not redeemable.

8. Notices. Any notice required by the provisions of this ARTICLE V to be given to the holders of Preferred Stock shall be deemed given if deposited in the United States mail, postage prepaid, and addressed to each holder of record at such holder’s address appearing on the books of the Corporation.

ARTICLE VI

The Corporation is to have perpetual existence.

ARTICLE VII

Elections of directors need not be by written ballot unless a stockholder demands election by written ballot at the meeting and before voting begins or unless the Bylaws of the Corporation shall so provide.

ARTICLE VIII

Unless otherwise set forth herein, the number of directors which constitute the Board of Directors of the Corporation shall be designated in the Bylaws of the Corporation.

ARTICLE IX

Except as set forth herein, in furtherance and not in limitation of the powers conferred by statute, the Board of Directors of the Corporation is expressly authorized to make, alter, amend or repeal the Bylaws of the Corporation.

ARTICLE X

1. To the fullest extent permitted by the Delaware General Corporation Law as the same exists or as may hereafter be amended, a director of the Corporation shall not be personally liable to the Corporation or its stockholders for monetary damages for a breach of fiduciary duty as a director.

2. The Corporation may indemnify to the fullest extent permitted by law any person made or threatened to be made a party to an action or proceeding, whether criminal, civil, administrative or investigative, by reason of the fact that he, his testator or intestate is or was a director, officer or employee of the Corporation or any predecessor of the Corporation or serves or served at any other enterprise as a director, officer or employee at the request of the Corporation or any predecessor to the Corporation.

3. Neither any amendment nor repeal of this ARTICLE X, nor the adoption of any provision of the Corporation’s Certificate of Incorporation inconsistent with this ARTICLE X, shall eliminate or reduce the effect of this ARTICLE X, in respect of any matter occurring, or any action or proceeding accruing or arising or that, but for this ARTICLE X, would accrue or arise, prior to such amendment, repeal or adoption of an inconsistent provision.

ARTICLE XI

Meetings of stockholders may be held within or without the State of Delaware, as the Bylaws may provide. The books of the Corporation may be kept (subject to any provision contained in the statutes) outside of the State of Delaware at such place or places as may be designated from time to time by the Board of Directors or in the Bylaws of the Corporation.

The Corporation renounces any interest or expectancy of the Corporation in, or in being offered an opportunity to participate in, or in being informed about, an Excluded Opportunity. An “**Excluded Opportunity**” is any matter, transaction or interest that is presented to, or acquired, created or developed by, or which otherwise comes into the possession of, (i) any director of the Corporation who is not an employee of the Corporation or any of its subsidiaries, or (ii) any holder of Preferred Stock or any affiliate, partner, member, director, stockholder, employee, agent or other related person of any such holder, other than someone who is an employee of the Corporation or any of its subsidiaries (collectively, “**Covered Persons**”), unless such matter, transaction or interest is presented to, or acquired, created or developed by, or otherwise comes into the possession of, a Covered Person expressly and solely in such Covered Person’s capacity as a director of the Corporation.

**Exhibit 4.1**

**FIRST SUPPLEMENTAL INDENTURE**

This FIRST SUPPLEMENTAL INDENTURE (this "Supplemental Indenture"), dated as of May 10, 2013 and effective as of the Effective Time (as defined in Section 3 (a) below), is entered into by and among Prosper Funding LLC, a Delaware limited liability company ("Prosper Funding"), and Wells Fargo Bank, National Association, a national banking association incorporated and existing under the laws of the United States of America, as trustee (the "Trustee"). Capitalized terms used herein and not otherwise defined have the meanings ascribed thereto in the Indenture specified below to which this Supplemental Indenture relates.

**WITNESSETH:**

WHEREAS, Prosper Funding and the Trustee have heretofore entered into that Amended and Restated Indenture, dated as of January 22, 2013 (the "Indenture"), providing for the issuance from time to time of special limited obligations of Prosper Funding referred to as Borrower Payment Dependent Notes (referred to herein collectively as the "Securities"), to be issued in series as provided therein;

WHEREAS, Section 8.01 of the Indenture sets forth certain circumstances under which Prosper Funding and the Trustee may execute an indenture supplemental to the Indenture without consent of holders of Securities, including "(e) to cure any ambiguity, defect or inconsistency";

WHEREAS, this Supplemental Indenture is an indenture supplemental to the Indenture referred to in Section 8.01(e) of the Indenture, inasmuch as Prosper Funding and the Trustee desire to cure ambiguities and defects in certain definitions and operative provisions of the Indenture to (a) clarify (consistent with provisions already appearing in the Indenture, the Form of Borrower Payment Dependent Note comprising an Exhibit to the Indenture and the Securities already outstanding, and the descriptions thereof appearing in the Registration Statement on Form S-1 (File No. 333-179941 and 333-179941-01) of Prosper Funding and Prosper Marketplace, Inc. that was filed with the U.S. Securities and Exchange Commission on December 20, 2012 and declared effective on December 27, 2012 and the prospectuses and prospectus supplements delivered by Prosper Funding in relation thereto) that direct loans originated through Prosper Funding's online marketplace and funded by the issuance and sale of Securities are collateral securing such Securities, but that loans originated through Prosper Funding's online marketplace and funded from proceeds of other activities of Prosper Funding (including, but not limited to, whole loan sales) do not comprise collateral securing any Securities or other obligations under the Indenture and (b) clarify that the qualification and eligibility of the Trustee may be measured by its capital and surplus or the capital and surplus of a bank holding company that wholly owns the Trustee; and

NOW, THEREFORE, in consideration of the foregoing premises and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto hereby mutually covenant and agree for the equal and ratable benefit of the Holders of the Securities as follows:

1. Amendments of Definitions.

(a) Effective as of the Effective Time, the following defined term not currently appearing in the Indenture is added to the Indenture:
"*Excluded Borrower Loan*" means a loan originated through the Platform that is not funded from proceeds of the sale of any Security, including any loan sold or otherwise transferred or purported to be sold or otherwise transferred by the Company as a whole loan.

(b) Effective as of the Effective Time, the following defined terms appearing in the Indenture are amended and restated in their entirety to read as follows:

"*Borrower Loan*" means a direct loan originated through the Platform that is not an Excluded Borrower Loan.

"*Platform*" means the Company's online marketplace through which an individual who registers with the Company as a borrower can request a loan, and Persons who register with the Company as lenders can (i) facilitate the funding of such loan by committing to purchase Securities of the series corresponding to such loan (in which case such loan will be a Corresponding Borrower Loan), (ii) purchase such loan as a whole loan (in which case such loan will be an Excluded Borrower Loan) or (iii) facilitate the funding of such loan by committing to purchase securities that are not issued pursuant to this Indenture (in which case such loan also will be an Excluded Borrower Loan).

2. Amendments of Operative Provisions.

(a) Effective as of the Effective Time, the final sentence of the first paragraph of Section 6.12 of the Indenture is amended to read as follows:
For the avoidance of doubt, (a) the Excluded Borrower Loans and proceeds thereof do not constitute Collateral under this Indenture and (b) notwithstanding the security interest granted in this Section 6.12 (the "Security Interest"), (i) the Company shall be authorized at all times to (or to cause the Servicer on its behalf to) withdraw from or transfer from (or to instruct the Trustee to withdraw from or transfer from) the Deposit Account the excess of the Borrower Loan Payments over the related Borrower Loan Net Payments (the "Excess Amounts"), and to deposit such amounts into the Fee Account, (ii) the Company shall be authorized at all times to (or to cause the Servicer on its behalf to) withdraw from or transfer from (or to instruct the Trustee to withdraw from or transfer from) the Deposit Account any amounts comprising proceeds of Excluded Borrower Loans and to deposit the same into any other account designated by the Company as the account to which such proceeds should have been deposited and (iii) the Trustee will reasonably promptly upon any instruction from the Company (or the Servicer on its behalf) (A) transfer such Excess Amounts from the Deposit Account to the Fee Account, and (B) transfer such proceeds of Excluded Borrower Loans to the account designated by the Company as the account to which such proceeds should have been deposited.

(b) Effective as of the Effective Time, the following sentence will be added as the final sentence of Section 2.02(b) of the Indenture:

For the avoidance of doubt, neither any Holder of a Security nor the Indenture Trustee on behalf of any Holder of a Security shall have any right, title or interest in, to or under, claim on or recourse against (i) any Excluded Borrower Loan or any proceeds thereof, or (ii) any Borrower Loan that is not the Corresponding Borrower Loan or any proceeds thereof, in either case in relation to the Company's obligations under such Security or under the Indenture in respect of such Security.

(c) Effective as of the Effective Time, clause SECOND of Section 5.10 of the Indenture is amended to read as follows:

SECOND: to the Securityholders for amounts due and unpaid for the Principal and interest on the Securities in respect of which or for the benefit of which any such money has been collected in respect of the related Corresponding Borrower Loan as contemplated by Sections 2.02(b) and 3.01, ratably, without preference or priority of any kind, according to the amounts due and payable on such Securities for Principal and interest, respectively; and

(d) Effective as of the Effective Time, the second sentence of Section 6.10 of the Indenture will be amended to read as follows:

The Trustee (a) shall have a combined capital and surplus of at least $50,000,000 or (b) is a wholly-owned subsidiary of a bank holding company having a consolidated capital and surplus of at least $50,000,000, in each case as set forth in its most recent published annual report of condition.

3. Effective Time; Deliverables.

(a) Subject to Section 3(b), the "Effective Time" shall occur at 12:01 a.m. (Pacific Time) on May 10, 2013, or at such other time and date as may be designated jointly by PMI and Prosper Funding in writing to the Trustee.

(b) The occurrence of the Effective Time shall be conditioned upon delivery to the Trustee, at or prior to the Effective Time, of: (i) a certificate, dated as of the date on which the Effective Time occurs, duly executed by authorized officers of Prosper Funding, in their capacity as such, substantially in the form attached hereto as Exhibit A; and (ii) an opinion of Bingham McCutchen LLP, counsel to Prosper Funding, substantially in the form attached hereto as Exhibit B.

4. Effect of Amendments. The Trustee consents to and authorizes the filing by Prosper Funding or its designees of a UCC-3 financing statement amendment in any and all such jurisdiction(s) as Prosper Funding shall determine as necessary or desirable solely in order to give further effect to this Supplemental Indenture it being understood that no liability or claims against the trustee shall arise from the filing thereof.

5. Separability Clause. In case any provision of this Supplemental Indenture shall be invalid, illegal or unenforceable, the validity, legality and enforceability of the remaining provisions shall not in any way be affected or impaired thereby.

6. Effect of Headings. The section headings herein are for convenience only and shall not affect the construction hereof.

7. Governing Law. THIS SUPPLEMENTAL INDENTURE SHALL BE GOVERNED BY AND CONSTRUED IN ACCORDANCE WITH THE LAWS OF THE STATE OF NEW YORK, AS APPLIED TO CONTRACTS MADE AND PERFORMED WITHIN THE STATE OF NEW YORK, WITHOUT REGARD TO ANY PRINCIPLE OF CONFLICTS OF LAW THAT WOULD REQUIRE OR PERMIT THE APPLICATION OF THE LAWS OF ANY OTHER JURISDICTION.

8. Benefits of Supplemental Indenture. Nothing in this Supplemental Indenture, express or implied, shall give to any person, other than the parties hereto and their successors hereunder and the Holders of Securities, any benefits or any legal or equitable right, remedy or claim under this Supplemental Indenture.

9. Multiple Originals. The exchange of copies of this Supplemental Indenture and of signature pages by facsimile or PDF transmission shall constitute effective execution and delivery of this Supplemental Indenture as to the parties hereto and may be used in lieu of the original Supplemental Indenture for all purposes. Signatures of the parties hereto transmitted by facsimile or PDF transmission shall be deemed to be their original signatures for all purposes.

10. Execution as Supplemental Indenture. This Supplemental Indenture is executed and shall be construed as an indenture supplemental to the Indenture and, as provided in the Indenture, this Supplemental Indenture forms a part thereof.

11. Ratification and Incorporation of Indenture. As supplemented and amended hereby, the Indenture is in all respects ratified and confirmed.

12. Trustee Makes No Representation. The Trustee makes no representation as to the validity or sufficiency of this Supplemental Indenture. The Trustee accepts the amendments of the Indenture effected by this Supplemental Indenture, but on the terms and conditions set forth in the Indenture, including the terms and provisions defining and limiting the liabilities and responsibilities of the Trustee. Without limiting the generality of the foregoing, the Trustee shall not be responsible in any manner whatsoever for or with respect to any of the recitals or statements contained herein, all of which recitals or statements are made solely by Prosper Funding, or for or with respect to (i) the validity or sufficiency of this Supplemental Indenture or any of the terms or provisions hereof, (ii) the proper authorization hereof by Prosper Funding by action or otherwise, (iii) the due execution hereof by Prosper Funding, or (iv) the consequences of any amendment herein provided for, and the Trustee makes no representation with respect to any such matters.

*[Signature Page Follows]*

IN WITNESS WHEREOF, the parties hereto have duly executed this Supplemental Indenture as of the date first above written.

PROSPER FUNDING LLC

By: /s/ Sachin Adarkar
Name: Sachin Adarkar
Title: Secretary

WELLS FARGO BANK, NATIONAL ASSOCIATION, as Trustee

By: /s/ Raymond Delli Colli
Name: Raymond Delli Colli
Title: Vice President

[Signature Page to Supplemental Indenture]

**Exhibit A**

**Officer’s Certificate**

See attached.

**Exhibit B**

**Legal Opinion**

See attached.

**Exhibit 31.1**

**CERTIFICATIONS**

I, Stephan Vermut, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Prosper Marketplace, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 14, 2013

/s/ Stephan Vermut

Stephan Vermut
Chief Executive Officer of Prosper Marketplace, Inc
(*principal executive officer*)

**Exhibit 31.2**

**CERTIFICATIONS**

I, Kenneth L. Niewald, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Prosper Marketplace, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 14, 2013

/s/ Kenneth L. Niewald

Kenneth L. Niewald
Chief Financial Officer of Prosper Marketplace, Inc.
(*principal financial and accounting officer*)

**Exhibit 31.3**

**CERTIFICATIONS**

I, Stephan Vermut, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Prosper Funding LLC

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 14, 2013

/s/ Stephan Vermut

Stephan Vermut
President of Prosper Funding LLC
(*principal executive officer*)

**Exhibit 31.4**

**CERTIFICATIONS**

I, Kenneth L. Niewald, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Prosper Funding LLC;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 14, 2013

/s/ Kenneth L. Niewald
Kenneth L. Niewald
Treasurer of Prosper Funding LLC
(*principal financial and accounting officer)*

**Exhibit 32.1**

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Prosper Marketplace, Inc. ("PMI") on Form 10-Q for the quarter ended March 31, 2013, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), each of the undersigned officers of PMI certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to such officer's knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of PMI.

Date: August 14, 2013

/s/ Stephan Vermut
Stephan Vermut
Chief Executive Officer of Prosper Marketplace, Inc.
(*principal executive officer*)

/s/ Kenneth L. Niewald
Kenneth L. Niewald
Chief Financial Officer of Prosper Marketplace, Inc.
(*principal financial and accounting officer)*

**Exhibit 32.2**

**CERTIFICATION PURSUANT TO**
**18 U.S.C. SECTION 1350**
**AS ADOPTED PURSUANT TO**
**SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Prosper Funding LLC ("Prosper Funding") on Form 10-Q for the quarter ended March 31, 2013, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), each of the undersigned officers of Prosper Funding certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to such officer's knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of Prosper Funding.

Date: August 14, 2013

/s/ Stephan Vermut
Stephan Vermut
President of Prosper Funding LLC
(*principal executive officer*)

/s/ Kenneth L. Niewald
Kenneth L. Niewald
Treasurer of Prosper Funding LLC
(*principal financial and accounting officer)*