ANNALY CAPITAL MANAGEMENT INC
Form 10-Q
August 04, 2016
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED: JUNE 30, 2016

OR

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

FOR THE TRANSITION PERIOD FROM _______________ TO _________________

COMMISSION FILE NUMBER: 1-13447

ANNALY CAPITAL MANAGEMENT, INC.
(Exact Name of Registrant as Specified in its Charter)

MARYLAND (State or other jurisdiction of incorporation or organization)	22-3479661 (IRS Employer Identification No.)
1211 AVENUE OF THE AMERICAS NEW YORK, NY 10036 (Address of principal executive offices)	10036 (Zip Code)

(212) 696-0100
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant 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

(§232.405 of this chapter) during the preceding 12 months (or for such
shorter period that the registrant was required to submit and post such files).
Yes No

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

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the last practicable date:

Class	Outstanding at July 31, 2016
Common Stock, $.01 par value	995,532,782 (an additional 23,280,779 shares remain to be issued in connection with the previously announced acquisition of Hatteras Financial Corp.)

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PART I - FINANCIAL INFORMATION

PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
(dollars in thousands, except per share data)

	June 30, 2016 (Unaudited)	December 31, 2015 (1)
ASSETS		
Cash and cash equivalents (including cash pledged as collateral of $2,578,551 and $1,584,686, respectively) (2)	$2,735,250	$1,769,258
Investments, at fair value:		
Agency mortgage-backed securities (including pledged assets of $59,749,105 and $60,678,548, respectively)	64,862,992	65,718,224
Agency debentures (including pledged assets of $0 and $0, respectively)	-	152,038
Credit risk transfer securities (including pledged assets of $167,549 and $184,160, respectively)	520,321	456,510
Non-Agency mortgage-backed securities (including pledged assets of $1,057,899 and $744,783, respectively)	1,197,549	906,722
Commercial real estate debt investments (including pledged assets of $4,361,972 and $2,911,828, respectively) (3)	4,361,972	2,911,828
Commercial real estate debt and preferred equity, held for investment (including pledged assets of $654,111 and $578,820, respectively) (4)	1,137,971	1,348,817
Loans held for sale, net	164,175	278,600
Investments in commercial real estate	504,605	535,946
Corporate debt	669,612	488,508
Interest rate swaps, at fair value	146,285	19,642
Other derivatives, at fair value	137,490	22,066
Receivable for investments sold	697,943	121,625
Accrued interest and dividends receivable	227,225	231,336
Other assets	237,959	119,422
Goodwill	71,815	71,815
Intangible assets, net	43,306	38,536
Total assets	$77,716,470	$75,190,893
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities:		
Repurchase agreements	$53,868,385	$56,230,860
Other secured financing	3,588,326	1,845,048
Securitized debt of consolidated VIEs (5)	3,748,289	2,540,711
Participation sold	13,079	13,286
Mortgages payable	327,643	334,707
Interest rate swaps, at fair value	3,208,986	1,677,571

Other derivatives, at fair value	154,017	49,963
Dividends payable	277,479	280,779
Payable for investments purchased	746,090	107,115
Accrued interest payable	159,435	151,843
Accounts payable and other liabilities	62,868	53,088
Total liabilities	66,154,597	63,284,971
Stockholders' Equity:		
7.875% Series A Cumulative Redeemable Preferred Stock:		
7,412,500 authorized, issued and outstanding	177,088	177,088
7.625% Series C Cumulative Redeemable Preferred Stock:		
12,650,000 authorized, 12,000,000 issued and outstanding	290,514	290,514
7.50% Series D Cumulative Redeemable Preferred Stock:		
18,400,000 authorized, issued and outstanding	445,457	445,457
Common stock, par value $0.01 per share, 1,956,937,500 authorized,		
924,929,607 and 935,929,561 issued and outstanding, respectively	9,249	9,359
Additional paid-in capital	14,575,426	14,675,768
Accumulated other comprehensive income (loss)	1,117,046	(377,596)
Accumulated deficit	(5,061,565)	(3,324,616)
Total stockholders' equity	11,553,215	11,895,974
Noncontrolling interest	8,658	9,948
Total equity	11,561,873	11,905,922
Total liabilities and equity	$77,716,470	$75,190,893

(1) Derived from the audited consolidated financial statements at December 31, 2015.

(2) Includes cash of consolidated VIEs of $9.7 million and $48.5 million at June 30, 2016 and December 31, 2015, respectively.

(3) Includes senior securitized commercial mortgage loans of consolidated VIEs carried at fair value of $4.0 billion and $2.6 billion at June 30, 2016 and December 31, 2015, respectively.

(4) Includes senior securitized commercial mortgage loans of a consolidated VIE with a carrying value of $187.2 million and $262.7 million carried at amortized cost, net of an allowance for losses of $0, at June 30, 2016 and December 31, 2015, respectively.

(5) Includes securitized debt of consolidated VIEs carried at fair value of $3.7 billion and $2.4 billion at June 30, 2016 and December 31, 2015, respectively.

See notes to consolidated financial statements.

ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(dollars in thousands, except per share data)
(Unaudited)

	Quarter Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Net interest income:				
Interest income	$457,118	$624,277	$845,261	$1,143,391
Interest expense	152,755	113,072	300,202	242,492
Net interest income	304,363	511,205	545,059	900,899
Realized and unrealized gains (losses):				
Realized gains (losses) on interest rate swaps[1]	(130,762)	(144,465)	(278,237)	(302,704)
Realized gains (losses) on termination of interest rate swaps	(60,064)	-	(60,064)	(226,462)
Unrealized gains (losses) on interest rate swaps	(373,220)	700,792	(1,404,940)	234,590
Subtotal	(564,046)	556,327	(1,743,241)	(294,576)
Net gains (losses) on disposal of investments	12,535	3,833	10,860	66,189
Net gains (losses) on trading assets	81,880	(114,230)	207,069	(121,136)
Net unrealized gains (losses) on financial instruments measured at fair value through earnings	(54,154)	17,581	(54,026)	(15,965)
Impairment of goodwill	-	(22,966)	-	(22,966)
Subtotal	40,261	(115,782)	163,903	(93,878)
Total realized and unrealized gains (losses)	(523,785)	440,545	(1,579,338)	(388,454)
Other income (loss):				
Investment advisory income	-	10,604	-	21,068
Dividend income from affiliate	-	4,318	-	8,636
Other income (loss)	(9,930)	(22,275)	(16,045)	(23,299)
Total other income (loss)	(9,930)	(7,353)	(16,045)	6,405
General and administrative expenses:				
Compensation and management fee	36,048	37,014	73,045	75,643
Other general and administrative expenses	13,173	14,995	24,121	27,304
Total general and administrative expenses	49,221	52,009	97,166	102,947
Income (loss) before income taxes	(278,573)	892,388	(1,147,490)	415,903
Income taxes	(76)	(7,683)	(913)	(7,669)
Net income (loss)	(278,497)	900,071	(1,146,577)	423,572
Net income (loss) attributable to noncontrolling interest	(385)	(149)	(547)	(239)
Net income (loss) attributable to Annaly	(278,112)	900,220	(1,146,030)	423,811
Dividends on preferred stock	17,992	17,992	35,984	35,984

Net income (loss) available (related) to common stockholders	$(296,104)	$882,228	$(1,182,014)	$387,827
Net income (loss) per share available (related) to common stockholders:				
Basic	$(0.32)	$0.93	$(1.28)	$0.41
Diluted	$(0.32)	$0.93	$(1.28)	$0.41
Weighted average number of common shares outstanding:				
Basic	924,887,316	947,731,493	925,850,452	947,700,832
Diluted	924,887,316	947,929,762	925,850,452	947,878,958
Dividends declared per share of common stock	$0.30	$0.30	$0.60	$0.60
Net income (loss)	$(278,497)	$900,071	$(1,146,577)	$423,572
Other comprehensive income (loss):				
Unrealized gains (losses) on available-for-sale securities	483,930	(1,125,043)	1,501,637	(493,571)
Reclassification adjustment for net (gains) losses included in net income (loss)	(7,250)	(3,921)	(6,995)	(66,277)
Other comprehensive income (loss)	476,680	(1,128,964)	1,494,642	(559,848)
Comprehensive income (loss)	$198,183	$(228,893)	$348,065	$(136,276)
Comprehensive income (loss) attributable to noncontrolling interest	(385)	(149)	(547)	(239)
Comprehensive income (loss) attributable to Annaly	198,568	(228,744)	348,612	(136,037)
Dividends on preferred stock	17,992	17,992	35,984	35,984
Comprehensive income (loss) attibutable to common stockholders	$180,576	$(246,736)	$312,628	$(172,021)

(1) Consists of interest expense on interest rate swaps.
See notes to consolidated financial statements.
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ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(dollars in thousands, except per share data)
(Unaudited)

	7.875% Series A Cumulative Redeemable Preferred Stock	7.625% Series C Cumulative Redeemable Preferred Stock	7.50% Series D Cumulative Redeemable Preferred Stock	Common stock par value	Additional paid-in capital	Accumulated other comprehensive income (loss)	Accumulated deficit	Total stockholders' equity	Nonco interes
BALANCE, December 31, 2014	$177,088	$290,514	$445,457	$9,476	$14,786,509	$204,883	$(2,585,436)	$13,328,491	$5,290
Net income (loss) attributable to Annaly	-	-	-	-	-	-	423,811	423,811	-
Net income (loss) attributable to noncontrolling interest	-	-	-	-	-	-	-	-	(239
Unrealized gains (losses) on available-for-sale securities	-	-	-	-	-	(493,571)	-	(493,571)	-
Reclassification adjustment for net (gains) losses included in net income (loss)	-	-	-	-	-	(66,277)	-	(66,277)	-
Stock compensation expense	-	-	-	-	1,024	-	-	1,024	-
Net proceeds from direct purchase and dividend reinvestment	-	-	-	2	1,144	-	-	1,146	-
Equity contributions from (distributions to) noncontrolling interest	-	-	-	-	-	-	-	-	(245
Preferred Series A dividends, declared $0.984 per share	-	-	-	-	-	-	(7,296)	(7,296)	-
Preferred Series C dividends,	-	-	-	-	-	-	(11,438)	(11,438)	-

declared $0.953 per share									
Preferred Series D dividends, declared $0.938 per share	-	-	-	-	-	-	(17,250)	(17,250)	-
Common dividends declared, $0.60 per share	-	-	-	-	-	-	(568,641)	(568,641)	-
BALANCE, June 30, 2015	$177,088	$290,514	$445,457	$9,478	$14,788,677	$(354,965)	$(2,766,250)	$12,589,999	$4,80
BALANCE, December 31, 2015	$177,088	$290,514	$445,457	$9,359	$14,675,768	$(377,596)	$(3,324,616)	$11,895,974	$9,94
Net income (loss) attributable to Annaly	-	-	-	-	-	-	(1,146,030)	(1,146,030)	-
Net income (loss) attributable to noncontrolling interest	-	-	-	-	-	-	-	-	(547
Unrealized gains (losses) on available-for-sale securities	-	-	-	-	-	1,501,637	-	1,501,637	-
Reclassification adjustment for net (gains) losses included in net income (loss)	-	-	-	-	-	(6,995)	-	(6,995)	-
Stock compensation expense	-	-	-	-	1,084	-	-	1,084	-
Net proceeds from direct purchase and dividend reinvestment	-	-	-	1	1,175	-	-	1,176	-
Buyback of common stock	-	-	-	(111)	(102,601)	-	-	(102,712)	-
Equity contributions from (distributions to) noncontrolling interest	-	-	-	-	-	-	-	-	(743
Preferred Series A dividends, declared $0.984 per share	-	-	-	-	-	-	(7,296)	(7,296)	-

Preferred Series C dividends, declared $0.953 per share	-	-	-	-	-	-	(11,438)	(11,438)	-
Preferred Series D dividends, declared $0.938 per share	-	-	-	-	-	-	(17,250)	(17,250)	-
Common dividends declared, $0.60 per share	-	-	-	-	-	-	(554,935)	(554,935)	-
BALANCE, June 30, 2016	$177,088	$290,514	$445,457	$9,249	$14,575,426	$1,117,046	$(5,061,565)	$11,553,215	$8,65

See notes to consolidated financial statements
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ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(dollars in thousands)
(Unaudited)

	Six Months Ended June 30, 2016	2015
Cash flows from operating activities:		
Net income (loss)	$(1,146,577)	$423,572
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Amortization of Residential Investment Securities premiums and discounts, net	621,146	378,814
Amortization of commercial real estate investment premiums and discounts, net	(1,552)	(581)
Amortization of intangibles	7,621	3,586
Amortization of deferred financing costs	1,019	4,561
Amortization of net origination fees and costs, net	(2,868)	(2,350)
Amortization of contingent beneficial conversion feature and equity component of Convertible Senior Notes	-	12,246
Depreciation expense	10,684	5,687
Net gain on sale of commercial real estate	(821)	-
Net gain on sale of commercial loans held for sale	67	100
Net loss on sale of commerical real estate debt investments	165	-
Net (gains) losses on sales of Residential Investment Securities	(10,271)	(66,289)
Stock compensation expense	1,084	1,024
Impairment of goodwill	-	22,966
Unrealized (gains) losses on interest rate swaps	1,404,940	(234,590)
Net unrealized (gains) losses on financial instruments measured at fair value through earnings	54,026	15,965
Equity in net income from unconsolidated joint ventures	4,417	-
Net (gains) losses on trading assets	(207,069)	121,136
Proceeds from sale of loans held for sale	114,358	-
Proceeds from repurchase agreements of RCap	1,076,600,000	895,400,000
Payments on repurchase agreements of RCap	(1,075,750,000)	(900,650,000)
Proceeds from reverse repurchase agreements	29,700,000	26,925,000
Payments on reverse repurchase agreements	(29,700,000)	(26,825,000)
Net payments on derivatives	196,016	(116,122)
Net change in:		
Due to / from brokers	(5)	-
Other assets	(65,653)	(15,686)
Accrued interest and dividends receivable	3,202	45,897
Receivable for investment advisory income	-	(187)
Accrued interest payable	7,592	(48,857)
Accounts payable and other liabilities	24,331	13,952
Net cash provided by (used in) operating activities	1,865,852	(4,585,156)
Cash flows from investing activities:		
Payments on purchases of Residential Investment Securities	(7,088,346)	(8,638,138)
Proceeds from sales of Residential Investment Securities	4,008,291	18,278,224
Principal payments on Agency mortgage-backed securities	4,615,505	5,342,053
Payments on purchases of corporate debt	(245,447)	(187,035)
Principal payments on corporate debt	65,804	42,352

Purchases of commercial real estate debt investments	(76,862)	(276,918)
Sales of commercial real estate debt investments	-	41,016
Purchase of securitized loans at fair value	(1,489,268)	(2,574,353)
Origination of commercial real estate investments, net	(189,020)	(180,531)
Proceeds from sale of commercial real estate investments	12,750	46,806
Principal payments on commercial real estate debt investments	61,601	1,616
Principal payments on securitized loans at fair value	52,407	-
Principal payments on commercial real estate investments	402,459	321,050
Purchase of investments in real estate	(1,187)	(121)
Investment in unconsolidated joint venture	(559)	(12,410)
Distributions in excess of cumulative earnings from unconsolidated joint ventures	2,117	-
Purchase of equity securities	(88,062)	(8,130)
Proceeds from sales of equity securities	16,112	-
Net cash provided by (used in) investing activities	58,295	12,195,481
Cash flows from financing activities:		
Proceeds from repurchase agreements	85,723,588	105,819,378
Principal payments on repurchase agreements	(88,936,063)	(114,471,752)
Payments on maturity of convertible senior notes	-	(857,541)
Proceeds from other secured financing	2,146,084	203,200
Payments on other secured financing	(402,806)	-
Proceeds from issuance of securitized debt	1,381,640	2,382,810
Principal repayments on securitized debt	(163,472)	(37,915)
Principal repayments on securitized loans	-	50
Payment of deferred financing cost	(3,076)	(641)
Net proceeds from direct purchases and dividend reinvestments	1,176	1,144
Principal payments on participation sold	(153)	(147)
Principal payments on mortgages payable	(7,399)	(165)
Distributions to noncontrolling interests	(743)	(245)
Net payment on share repurchase	(102,712)	-
Dividends paid	(594,219)	(604,587)
Net cash provided by (used in) financing activities	(958,155)	(7,566,411)
Net (decrease) increase in cash and cash equivalents	965,992	43,914
Cash and cash equivalents, beginning of period	1,769,258	1,741,244
Cash and cash equivalents, end of period	$2,735,250	$1,785,158
	-	-
Supplemental disclosure of cash flow information:		
Interest received	$1,456,076	$1,541,718
Dividends received	$-	$8,366
Investment advisory income received	$-	$20,881
Interest paid (excluding interest paid on interest rate swaps)	$282,146	$218,272
Net interest paid on interest rate swaps	$281,120	$305,327
Taxes paid	$591	$1,901
Noncash investing activities:		
Receivable for investments sold	$697,943	$247,361
Payable for investments purchased	$746,090	$673,933
	$1,494,642	$(559,848)

Net change in unrealized gains (losses) on available-for-sale securities, net of reclassification adjustment	$-	$-
Noncash financing activities:		
Dividends declared, not yet paid	$277,479	$284,331

See notes to consolidated financial statements.

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ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. DESCRIPTION OF BUSINESS

Annaly Capital Management, Inc. (the "Company" or "Annaly") is a Maryland corporation that commenced operations on February 18, 1997. The Company owns a portfolio of real estate related investments, including mortgage pass-through certificates, collateralized mortgage obligations, Agency debentures, credit risk transfer ("CRT") securities, other securities representing interests in or obligations backed by pools of mortgage loans, commercial real estate assets and corporate debt. The Company's principal business objectives are to generate net income for distribution to its stockholders from its investments and capital preservation. The Company is externally managed by Annaly Management Company LLC (the "Manager").
The Company's business operations are primarily comprised of the following:

- Annaly, the parent company, which invests primarily in Agency mortgage-backed securities and related derivatives to hedge these investments. Its portfolio also includes residential credit investments such as CRT and non-Agency mortgage-backed securities.
- Annaly Commercial Real Estate Group, Inc. ("ACREG," formerly known as CreXus Investment Corp.), a wholly-owned subsidiary that was acquired during the second quarter of 2013 which specializes in acquiring, financing and managing commercial real estate loans and other commercial real estate debt, commercial mortgage-backed securities and other commercial real estate-related assets.
- Annaly Middle Market Lending LLC ("MML," formerly known as Charlesfort Capital Management LLC), a wholly-owned subsidiary which engages in corporate middle market lending transactions.
- RCap Securities, Inc. ("RCap"), a wholly-owned subsidiary, which operates as a broker-dealer and is a member of the Financial Industry Regulatory Authority ("FINRA").

The Company has elected to be taxed as a Real Estate Investment Trust ("REIT") as defined under the Internal Revenue Code of 1986, as amended, and regulations promulgated thereunder (the "Code").

2. BASIS OF PRESENTATION

The accompanying consolidated financial statements and related notes of the Company have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP").

The accompanying consolidated financial statements and related notes are unaudited and should be read in conjunction with the audited consolidated financial statements included in the Company's most recent annual report on Form 10-K. The consolidated financial information as of December 31, 2015 has been derived from audited consolidated financial statements not included herein.

In the opinion of management, all normal, recurring adjustments have been included for a fair presentation of this interim financial information. Interim period operating results may not be indicative of the operating results for a full year.

3. SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation – The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries and consolidated variable interest entities. All intercompany balances and transactions have been eliminated in consolidation. The Company reclassified previously presented financial information so that amounts previously presented conform to the current period presentation.
The Company has evaluated all of its investments in legal entities in order to determine if they are variable interests in Variable Interest Entities ("VIEs"). A VIE is defined as an entity in which equity investors (i) do not have the characteristics of a controlling financial interest, and/or (ii) do not have sufficient equity at risk for the entity to

finance its activities without additional subordinated financial support from other parties. A variable interest is an investment or other interest that will absorb portions of a VIE's expected losses or receive portions of the entity's expected residual returns. A VIE is required to be consolidated by its primary beneficiary, which is defined as the party that (i) has the power to direct the activities that most significantly impact the VIE's economic performance and (ii) has the obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE.

ANNALY CAPITAL MANAGEMENT, INC. AND SUBSIDIARIES
Item 1. Financial Statements
To assess whether the Company has the power to direct the activities of a VIE that most significantly impact the VIE's economic performance, the Company considers all facts and circumstances, including the Company's role in establishing the VIE and the Company's ongoing rights and responsibilities. This assessment includes first, identifying the activities that most significantly impact the VIE's economic performance; and second, identifying which party, if any, has power over those activities. In general, the parties that make the most significant decisions affecting the VIE or have the right to unilaterally remove those decision makers are deemed to have the power to direct the activities of a VIE.

To assess whether the Company has the obligation to absorb losses of the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE, the Company applies significant judgment and considers all of its economic interests, including debt and equity investments and other arrangements deemed to be variable interests, both explicit and implicit, in the VIE. This assessment requires that the Company applies judgment in determining whether these interests, in the aggregate, are considered potentially significant to the VIE. Factors considered in assessing significance include: the design of the VIE, including its capitalization structure; subordination of interests; payment priority; relative share of interests held across various classes within the VIE's capital structure; and the reasons why the interests are held by the Company.

The Company performs ongoing reassessments of whether changes in the facts and circumstances regarding the Company's involvement with a VIE causes the Company's consolidation conclusion regarding the VIE to change.

Cash and Cash Equivalents – Cash and cash equivalents include cash on hand, cash held in money market funds on an overnight basis and cash pledged as collateral with counterparties. Cash deposited with clearing organizations is carried at cost, which approximates fair value. The Company also maintains collateral in the form of cash on margin with counterparties to its interest rate swaps and other derivatives. RCap is a member of various clearing organizations with which it maintains cash required to conduct its day-to-day clearance activities. Cash and securities deposited with clearing organizations and collateral held in the form of cash on margin with counterparties to the Company's interest rate swaps and other derivatives totaled approximately $2.6 billion and $1.6 billion at June 30, 2016 and December 31, 2015, respectively.
Fair Value Measurements – The Company reports various financial instruments at fair value. A complete discussion of the methodology utilized by the Company to estimate the fair value of certain financial instruments is included in these Notes to Consolidated Financial Statements.

Revenue Recognition – The revenue recognition policy by asset class is discussed below.

Agency Mortgage-Backed Securities, Agency Debentures, Non-Agency Mortgage-Backed Securities and CRT Securities – The Company invests in mortgage pass-through certificates, collateralized mortgage obligations and other mortgage-backed securities representing interests in or obligations backed by pools of mortgage loans and certificates guaranteed by the Government National Mortgage Association ("Ginnie Mae"), the Federal Home Loan Mortgage Corporation ("Freddie Mac") or the Federal National Mortgage Association ("Fannie Mae") (collectively, "Agency mortgage-backed securities"). These Agency mortgage-backed securities may include forward contracts for Agency mortgage-backed securities purchases or sales of a generic pool, on a to-be-announced basis ("TBA securities"). The Company also invests in Agency debentures issued by the Federal Home Loan Banks, Freddie Mac and Fannie Mae, as well as CRT securities. CRT securities are risk sharing instruments issued by Fannie Mae and Freddie Mac, and similarly structured transactions arranged by third party market participants. CRT securities are designed to synthetically transfer mortgage credit risk from Fannie Mae, Freddie Mac and/or third parties to private investors. The Company also invests in non-Agency mortgage-backed securities, such as those issued in non-performing loan ("NPL") and re-performing loan ("RPL") securitizations.
Agency mortgage-backed securities, Agency debentures, non-Agency mortgage-backed securities and CRT securities are referred to herein as "Residential Investment Securities." Although the Company generally intends to hold most of

its Residential Investment Securities until maturity, it may, from time to time, sell any of its Residential Investment Securities as part of the overall management of its portfolio. Residential Investment Securities classified as available-for-sale are reported at fair value with unrealized gains and losses reported as a component of other comprehensive income (loss) unless the Company has elected the fair value option, where the unrealized gains and losses on these financial instruments are recorded through earnings (e.g., interest-only securities). The fair value of Residential Investment Securities classified as available-for-sale is estimated by management and is compared to independent sources for reasonableness. Residential Investment Securities transactions are recorded on trade date, including TBA

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securities that meet the regular-way securities scope exception from derivative accounting. Gains and losses on sales of Residential Investment Securities are recorded on trade date based on the specific identification method.

The Company elected the fair value option for interest-only mortgage-backed securities, non-Agency mortgage-backed securities and certain CRT securities. Interest-only securities and inverse interest-only securities are collectively referred to as "interest-only securities." These interest-only mortgage-backed securities represent the Company's right to receive a specified proportion of the contractual interest flows of specific mortgage-backed securities. Interest-only mortgage-backed securities, non-Agency mortgage-backed securities and certain CRT securities are measured at fair value with changes in fair value recorded as Net unrealized gains (losses) on financial instruments measured at fair value through earnings in the Company's Consolidated Statements of Comprehensive Income (Loss). The interest-only securities are included in Agency mortgage-backed securities at fair value on the accompanying Consolidated Statements of Financial Condition.

The Company recognizes coupon income, which is a component of interest income, based upon the outstanding principal amounts of the Residential Investment Securities and their contractual terms. In addition, the Company amortizes or accretes premiums or discounts into interest income for its Agency mortgage-backed securities, excluding interest-only securities, considering estimates of future principal prepayment in the calculation of the effective yield because they are probable and the timing and amount of prepayments can be reasonably estimated. The Company recalculates the effective yield as differences between anticipated and actual prepayments occur. Using third-party model and market information to project future cash flows and expected remaining lives of securities, the effective interest rate determined for each security is applied as if it had been in place from the date of the security's acquisition. The amortized cost of the investment is then adjusted to the amount that would have existed had the new effective yield been applied since the acquisition date. The adjustment to amortized cost is offset with a charge or credit to interest income. Changes in interest rates and other market factors will impact prepayment speed projections and the amount of premium amortization recognized in any given period.

Premiums or discounts associated with the purchase of Agency interest-only securities and residential credit securities are amortized or accreted into interest income based upon current expected future cash flows with any adjustment to yield made on a prospective basis.

Interest income for Agency debentures is recognized by applying the interest method using contractual cash flows without estimating prepayments.

The table below summarizes the interest income recognition methodology for Residential Investment Securities:

	Interest Income Methodology
Agency	
Fixed-rate pass-through[(1)]	Effective yield[(3)]
Adjustable-rate pass-through[(1)]	Effective yield[(3)]
CMO[(1)]	Effective yield[(3)]
Debentures[(1)]	Contractual Cash Flows
Interest-only[(2)]	Prospective
Residential Credit	
CRT[(2)]	Prospective
Legacy [(2)]	Prospective
NPL/RPL [(2)]	Prospective
New issue [(2)]	Prospective
New issue interest-only [(2)]	Prospective

(1) Changes in fair value are recognized in Other comprehensive income (loss) on the accompanying Consolidated Statements of Comprehensive Income (Loss).
(2) Changes in fair value are recognized in Net unrealized gains (losses) on financial instruments measured at fair value through earnings on the accompanying Consolidated Statements of Comprehensive Income (Loss).
(3) Effective yield is recalculated for differences between estimated and actual prepayments and the amortized cost is adjusted as if the new effective yield had been applied since inception.

Equity Securities – The Company may invest in equity securities that are classified as available-for-sale or trading. Equity securities classified as available-for-sale are reported at fair value, based on market quotes, with unrealized gains and losses reported as a component of other comprehensive income (loss). Equity securities classified as trading are reported at fair value, based on market quotes, with unrealized gains and losses reported in the Consolidated Statements of Comprehensive Income (Loss) as Net gains (losses) on trading assets. Dividends are recorded in earnings based on the declaration date.

Derivative Instruments – The Company may use a variety of derivative instruments to economically hedge some of its exposure to market risks, including interest rate and prepayment risk. These instruments include, but are not limited to, interest rate swaps, options to enter into interest rate swaps (“swaptions”), TBA contracts without intent to accept delivery ("TBA derivatives"), options on TBA contracts ("MBS options") and U.S. Treasury and Eurodollar futures contracts. The Company may also invest in other types of mortgage derivatives such as interest-only securities and synthetic total return swaps, such as the Markit IOS Synthetic Total Return Swap Index. Derivatives are accounted for in accordance with the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 815, Derivatives and Hedging, which requires recognition of all derivatives as either assets or liabilities at fair value in the Consolidated Statements of Financial Condition with changes in fair value recognized in the Consolidated Statements of Comprehensive Income (Loss). None of the Company's derivative transactions have been designated as hedging instruments for accounting purposes.

Some derivative agreements contain provisions that allow for netting or setting off by counterparty; however, the Company elected to present related assets and liabilities on a gross basis in the Consolidated Statements of Financial Condition.

Interest rate swap agreements - Interest rate swaps are the primary instrument used to mitigate interest rate risk. In particular, the Company uses interest rate swaps to manage its exposure to changing interest rates on its repurchase agreements by economically hedging cash flows associated with these borrowings. Swap agreements may or may not be cleared through a derivatives clearing organization ("DCO"). Uncleared swaps are fair valued using internal pricing models and compared to the counterparty market values. Centrally cleared swaps are fair valued using the DCO's market values.

Interest rate swaptions - Interest rate swaptions are purchased/sold to mitigate the potential impact of increases or decreases in interest rates. Interest rate swaptions provide the option to enter into an interest rate swap agreement for a predetermined notional amount, stated term and pay and receive interest rates in the future. They are not centrally cleared. The premium paid/received for interest rate swaptions is reported as an asset/liability in the Consolidated Statements of Financial Condition. The difference between the premium and the fair value of the swaption is reported in Net gains (losses) on trading assets in the Consolidated Statements of Comprehensive Income (Loss). If a swaption expires unexercised, the realized gain (loss) on the swaption would be equal to the premium received/paid. If the Company sells or exercises a swaption, the realized gain or loss on the swaption would be equal to the difference between the cash received or the fair value of the underlying interest rate swap received and the premium paid.
The fair value of interest rate swaptions is estimated using internal pricing models and compared to the counterparty market value.

TBA Dollar Rolls - TBA dollar roll transactions are accounted for as a series of derivative transactions. The fair value of TBA derivatives is based on similar methods used to value Agency mortgage-backed securities with gains and losses recorded in Net gains (losses) on trading assets in the Consolidated Statements of Comprehensive Income (Loss).

MBS Options – MBS options are generally options on TBA contracts, which help manage mortgage market risks and volatility while providing the potential to enhance returns. MBS options are over-the-counter traded instruments and those written on current-coupon mortgage-backed securities are typically the most liquid. MBS options are measured at fair value using internal pricing models and compared to the counterparty market value at the valuation date with gains and losses recorded in Net gains (losses) on trading assets in the Consolidated Statements of Comprehensive Income (Loss).
Futures Contracts - Futures contracts are derivatives that track the prices of specific assets. Short sales of futures contracts help mitigate the potential impact of changes in interest rates on the portfolio performance. The Company maintains margin accounts that are settled daily with Futures Commission Merchants ("FCMs"). The margin requirement varies based on the market value of the open positions and the equity retained in the account. Futures

contracts are fair valued based on exchange pricing with gains and losses recorded in Net gains (losses) on trading assets in the Consolidated Statements of Comprehensive Income (Loss).
Repurchase Agreements – The Company finances the acquisition of a significant portion of its Agency mortgage-backed securities with repurchase agreements. The Company examines each of the specified criteria in ASC 860, Transfers and Servicing, at the inception of each transaction and has determined that each of the financings meet the specified criteria in this guidance.

Reverse repurchase agreements and repurchase agreements with the same counterparty and the same maturity are presented net in the Consolidated Statements of Financial Condition when the terms of the agreements meet the criteria to permit netting. The Company reports cash flows on repurchase agreements as financing activities in the Consolidated Statements of Cash Flows. The Company reports cash flows on reverse repurchase and repurchase agreements entered into by RCap as operating activities in the Consolidated Statements of Cash Flows.

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Goodwill and Intangible Assets – The Company's acquisitions are accounted for using the acquisition method. Under the acquisition method, net assets and results of operations of acquired companies are included in the consolidated financial statements from the date of acquisition. The purchase prices are allocated to the assets acquired, including identifiable intangible assets, and the liabilities assumed based on their estimated fair values at the date of acquisition. The excess of purchase price over the fair value of the net assets acquired is recognized as goodwill. Conversely, any excess of the fair value of the net assets acquired over the purchase price is recognized as a bargain purchase gain.
The Company tests goodwill for impairment on an annual basis and at interim periods when events or circumstances may make it more likely than not that an impairment has occurred. If a qualitative analysis indicates that there may be an impairment, a quantitative analysis is performed. The quantitative impairment test for goodwill utilizes a two-step approach, whereby the Company compares the carrying value of each identified reporting unit to its fair value. If the carrying value of the reporting unit is greater than its fair value, the second step is performed, where the implied fair value of goodwill is compared to its carrying value. The Company recognizes an impairment charge for the amount by which the carrying amount of goodwill exceeds its fair value. An impairment of the goodwill associated with the Company's acquisition of Fixed Income Discount Advisory Company ("FIDAC") was recorded during the year ended December 31, 2015.
Intangible assets with an estimated useful life are amortized over their expected useful lives.

Convertible Senior Notes – The Company recorded the 4% Convertible Senior Notes and 5% Convertible Senior Notes (collectively, the "Convertible Senior Notes") at their contractual amounts, adjusted by the effects of a beneficial conversion feature and a contingent beneficial conversion feature (collectively, the "Conversion Features"). The Conversion Features' intrinsic value is included in "Additional paid-in capital" on the Company's Consolidated Statements of Financial Condition and reduces the recorded liability amount associated with the Convertible Senior Notes. A Conversion Feature may be recognized as a result of adjustments to the conversion price for dividends declared to common stockholders. The 4% and 5% Convertible Senior Notes matured in February 2015 and May 2015, respectively.

Stock Based Compensation – The Company is required to measure and recognize in the consolidated financial statements the compensation cost relating to share-based payment transactions. The Company recognizes compensation expense on a straight-line basis over the requisite service period for the entire award.
Income Taxes – The Company has elected to be taxed as a REIT and intends to comply with the provisions of the Code, with respect thereto. Accordingly, the Company will not be subject to federal income tax to the extent of its distributions to stockholders and as long as certain asset, income and stock ownership tests are met. The Company and certain of its direct and indirect subsidiaries, including FIDAC, RCap and certain subsidiaries of ACREG, have made separate joint elections to treat these subsidiaries as taxable REIT subsidiaries ("TRSs"). As such, each of these TRSs is taxable as a domestic C corporation and subject to federal, state and local income taxes based upon their taxable income.
The provisions of ASC 740, Income Taxes, ("ASC 740") clarify the accounting for uncertainty in income taxes recognized in financial statements and prescribe a recognition threshold and measurement attribute for uncertain tax positions taken or expected to be taken on a tax return. ASC 740 also requires that interest and penalties related to unrecognized tax benefits be recognized in the financial statements. The Company does not have any unrecognized tax benefits that would affect its financial position. Thus, no accruals for penalties and interest were necessary as of June 30, 2016 and December 31, 2015.

Use of Estimates – The preparation of the consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Commercial Real Estate Investments

Commercial Real Estate Debt Investments - The Company's commercial real estate debt investments are comprised of commercial mortgage-backed securities and loans held by consolidated collateralized financing entities. Commercial mortgage-backed securities are classified as available-for-sale and reported at fair value with unrealized gains and losses reported as a component of other comprehensive income (loss). Management evaluates commercial mortgage-backed securities for other-than-temporary impairment at least quarterly. See the "Commercial Real Estate Investments" Note for additional information regarding the consolidated collateralized financing entities.

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Commercial Real Estate Loans – The Company's commercial real estate loans are comprised of fixed-rate and adjustable-rate loans. The Company designates loans as held for investment if it has the intent and ability to hold the loans until maturity or payoff. The difference between the principal amount of a loan and proceeds at acquisition is recorded as either a discount or premium. Commercial real estate loans that are designated as held for investment and are originated or purchased by the Company are carried at their outstanding principal balance, net of unamortized origination fees and costs, premiums or discounts, less a reserve for estimated losses if necessary.
If the Company intends to sell or securitize the loans and the financing vehicle is not expected to be consolidated, they are classified as held for sale. Commercial real estate loans that are designated as held for sale are carried at the lower of amortized cost or fair value and recorded as Loans held for sale in the accompanying Consolidated Statements of Financial Condition. Any origination fees and costs or purchase premiums or discounts are deferred and recognized upon sale. The Company determines the fair value of commercial real estate loans held for sale on an individual loan basis. The Company has elected the fair value option for multi-family mortgage loans held in securitization trusts that it was required to consolidate. Preferred equity interests are designated as held for investment and are carried at their outstanding principal balance, net of unamortized origination fees and costs, premiums or discounts, less a reserve for estimated losses if necessary. See "Commercial Real Estate Investments" Note for additional information.
Investments in Commercial Real Estate – Investments in commercial real estate are carried at historical cost less accumulated depreciation. Historical cost includes all costs necessary to bring the asset to the condition and location necessary for its intended use, including financing during the construction period. Costs directly related to acquisitions deemed to be business combinations are expensed. Ordinary repairs and maintenance which are not reimbursed by tenants are expensed as incurred. Major replacements and improvements that extend the useful life of the asset are capitalized and depreciated over their useful life.
Investments in commercial real estate are depreciated using the straight-line method over the estimated useful lives of the assets, summarized as follows:

Category	Term
Building	30 - 40 years
Site improvements	1 - 28 years

The Company follows the acquisition method of accounting for acquisitions of operating real estate held for investment, where the purchase price of operating real estate is allocated to tangible assets such as land, building, site improvements and other identified intangibles such as above/below market and in-place leases.

The Company applies the equity method of accounting for its investments in joint ventures where it is not considered to have a controlling financial interest. Under the equity method of accounting, the Company will recognize its share of earnings or losses of the investee in the period in which they are reported by the investee. The Company also considers whether there are any indicators of other-than-temporary impairment of joint ventures accounted for under the equity method.

The Company evaluates whether real estate acquired in connection with a foreclosure ("REO") or UCC/deed in lieu of foreclosure (herein collectively referred to as a foreclosure) constitutes a business and whether business combination accounting is applicable. Upon foreclosure of a property, the excess of the carrying value of a loan, if any, over the estimated fair value of the property, less estimated costs to sell, is charged to provision for loan losses.

Investments in commercial real estate, including REO, that do not meet the criteria to be classified as held for sale are separately presented in the Consolidated Statements of Financial Condition as held for investment. Real estate held for sale is reported at the lower of its carrying value or its estimated fair value less estimated costs to sell. Once a property is determined to be held for sale, depreciation is no longer recorded.

The Company's real estate portfolio (REO and real estate held for investment) is reviewed on a quarterly basis, or more frequently as necessary, to assess whether there are any indicators that the value of its operating real estate may be impaired or that its carrying value may not be recoverable. A property's value is considered impaired if the Company's estimate of the aggregate future undiscounted cash flows to be generated by the property is less than the carrying value of the property. In conducting this review, the Company considers U.S. macroeconomic factors, including real estate sector conditions, together with asset specific and other factors. To the extent impairment has occurred and is considered to be other than temporary, the loss will be measured as the excess of the carrying amount of the property over the calculated fair value of the property.

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Revenue Recognition – Commercial Real Estate Investments - Interest income is accrued based on the outstanding principal amount of the commercial real estate loans and preferred equity interests held for investment (collectively referred to as “CRE Debt and Preferred Equity Investments”) and their contractual terms. Premiums and discounts associated with the purchase of CRE Debt and Preferred Equity Investments are amortized or accreted into interest income over the projected lives of the CRE Debt and Preferred Equity Investments using the interest method.

Corporate Debt
Corporate Loans – The Company’s investments in corporate debt that are loans are designated as held for investment when the Company has the intent and ability to hold the investment until maturity or payoff. These investments are carried at their principal balance outstanding plus any premiums or discounts less allowances for loan losses. Interest income from coupon payments is accrued based upon the outstanding principal amounts of the debt and its contractual terms. Premiums and discounts are amortized or accreted into interest income using the interest method. These investments typically take the form of senior secured loans primarily in first lien and second lien loans. The Company’s senior secured loans generally have stated maturities of three to eight years. In connection with these senior secured loans the Company receives a security interest in certain of the assets of the borrower and such assets support repayment of such loans. Senior secured loans are generally exposed to the least amount of credit risk given their seniority to scheduled principal and interest and priority of security in the assets of the borrower. To date, the majority of the Company’s investments have been funded term loans versus debt securities.
Corporate Debt Securities – The Company’s investments in corporate debt securities are designated as held-to-maturity when the Company has the intent and ability to hold the investments until maturity. These investments are carried at their principal balance outstanding plus any premiums or discounts less other-than-temporary impairment. Interest income from coupon payments is accrued based upon the outstanding principal amounts of the debt and its contractual terms. Premiums and discounts are amortized or accreted into interest income using the interest method.
Other-Than-Temporary Impairment – Management evaluates available-for-sale securities and held-to-maturity debt securities for other-than-temporary impairment at least quarterly, and more frequently when economic or market conditions warrant such evaluation. When the fair value of an available-for-sale security is less than its amortized cost, the security is considered impaired. For available-for-sale securities that are impaired, the Company determines if it (1) has the intent to sell the security, (2) is more likely than not that it will be required to sell the security before recovery of its amortized cost basis, or (3) does not expect to recover the entire amortized cost basis of the security. Further, the security is analyzed for credit loss (the difference between the present value of cash flows expected to be collected and the amortized cost basis). The credit loss, if any, will then be recognized in the Consolidated Statements of Comprehensive Income (Loss), while the balance of losses related to other factors will be recognized as a component of other comprehensive income (loss). If the fair value is less than the cost of a held-to-maturity security, the Company performs an analysis to determine whether it expects to recover the entire cost basis of the security. There was no other-than-temporary impairment recognized for the quarters ended June 30, 2016 and 2015.

Allowance for Losses – The Company evaluates the need for a loss reserve on its CRE Debt and Preferred Equity Investments and its corporate loans. A provision for losses related to CRE Debt and Preferred Equity Investments and corporate loans, including those accounted for under ASC 310-30, Loans and Debt Securities Acquired with Deteriorated Credit Quality, may be established when it is probable the Company will not collect amounts contractually due or all amounts previously estimated to be collectable. Management assesses the credit quality of the portfolio and adequacy of loan loss reserves on a quarterly basis, or more frequently as necessary. Significant judgment is required in this analysis. Depending on the expected recovery of its investment, the Company considers the estimated net recoverable value of the CRE Debt and Preferred Equity Investments as well as other factors, including but not limited to the fair value of any collateral, the amount and the status of any senior debt, the prospects for the borrower and the competitive landscape where the borrower conducts business. To determine if loan loss allowances are required on investments in corporate debt, the Company reviews the monthly and/or quarterly financial

statements of the borrowers, verifies loan compliance packages if applicable and analyzes current results relative to budgets and sensitivities performed at inception of the investment. Because these determinations are based upon projections of future economic events, which are inherently subjective, the amounts ultimately realized may differ materially from the carrying value as of the reporting date.
The Company may be exposed to various levels of credit risk depending on the nature of its investments and credit enhancements, if any, supporting its assets. The Company’s core investment process includes procedures related to the initial approval and periodic monitoring of credit risk and other risks associated with each investment.

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The Company's investment underwriting procedures include evaluation of the underlying borrowers' ability to manage and operate their respective properties or companies. Management reviews loan-to-value metrics upon either the origination or the acquisition of a new investment but generally does not update the loan-to-value metrics in the course of quarterly surveillance. Management generally reviews the most recent financial information produced by the borrower, which may include, but is not limited to, net operating income ("NOI"), debt service coverage ratios, property debt yields (net cash flow or NOI divided by the amount of outstanding indebtedness), loan per unit and rent rolls relating to each of the Company's CRE Debt and Preferred Equity Investments, and may consider other factors management deems important. Management also reviews market pricing to determine each borrower's ability to refinance their respective assets at the maturity of each loan. Management also reviews economic trends, both macro and those affecting the property specifically, and the supply and demand of competing projects in the sub-market in which each subject property is located. Management monitors the financial condition and operating results of its corporate borrowers and continually assesses the future outlook of the borrower's financial performance in light of industry developments, management changes and company-specific considerations.

In connection with the quarterly surveillance review process, CRE Debt and Preferred Equity Investments are assigned an internal risk rating. Effective December 31, 2015, the loan risk ratings were enhanced and considered guidance provided by the Office of the Comptroller of the Currency for commercial real estate lending. The initial internal risk ratings ("Initial Ratings") are based on loan-to-values and the NOI debt yields of the underlying collateral of the Company's CRE Debt and Preferred Equity Investments and based upon leverage and cash flow coverages of the borrowers' debt and operating obligations. The final internal risk ratings are influenced by other quantitative and qualitative factors that can result in an adjustment to the Initial Ratings, subject to review and approval by the respective committee. The internal risk rating categories include "Performing", "Performing - Closely Monitored", "Performing - Special Mention", "Substandard", "Doubtful" or "Loss". Performing loans meet all present contractual obligations. Performing - Closely Monitored loans meet all present contractual obligations, are transitional or could be exhibiting some weakness in both leverage and liquidity. Performing - Special Mention loans meet all present contractual obligations, but exhibit potential weakness that deserves management's close attention and if uncorrected, may
result in deterioration of repayment prospects. Substandard loans are inadequately protected by sound worth and paying capacity of the obligor or of the collateral pledged with a distinct possibility that loss will be sustained if some of the deficiencies are not corrected. Doubtful loans are Substandard loans whereby collection of all contractual principal and interest is highly questionable or improbable. Loss loans are considered uncollectible. The presentation of prior period internal risk ratings have been revised to conform to the current period presentation.

The Company did not have any impaired loans, nonaccrual loans, or loans in default as all of the loans were performing as of June 30, 2016 and December 31, 2015. Accordingly, no allowance for loan losses was deemed necessary as of June 30, 2016 and December 31, 2015.

Broker Dealer Activities

In January 2014, RCap ceased its trading activity in U.S. Treasury securities, derivatives and securities borrowed and loaned transactions.

Reverse Repurchase Agreements – RCap enters into reverse repurchase agreements and repurchase agreements as part of its matched book trading activity. Reverse repurchase agreements are recorded on settlement date at the contract amount and are collateralized by mortgage-backed or other securities. Margin calls are made by RCap as necessary based on the daily valuation of the underlying collateral as compared to the contract price. RCap generates income from the spread between what is earned on the reverse repurchase agreements and what is paid on the matched repurchase agreements. RCap's policy is to obtain possession of collateral with a market value in excess of the principal amount loaned under reverse repurchase agreements. To ensure that the market value of the underlying collateral remains sufficient, collateral is valued daily, and RCap requires counterparties to deposit additional collateral, when necessary. All reverse repurchase activities are transacted under master repurchase agreements that give RCap the right, in the event of default, to liquidate collateral held and in some instances, to offset receivables and payables with the same counterparty. Substantially all of RCap's reverse repurchase activity is with affiliated entities.

Recent Accounting Pronouncements

The following table provides a brief description of recent accounting pronouncements that could potentially impact the Company's consolidated financial statements:

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Standard	Description	Date of Adoption	Effect on the financial statements or other significant matters
Standards that are not yet adopted			
ASU 2016-13 Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments	This ASU updates the existing incurred loss model to a current expected credit loss model for financial assets and net investments in leases that are not accounted for at fair value through earnings. The amendments affect loans, debt securities, trade receivables, net investments in leases, off balance sheet credit exposures and any other financial assets not excluded from the scope. There are also changes to the accounting for available for sale debt securities.	January 1, 2020 (early adoption permitted)	The Company is assessing the impact to the consolidated financial statements.
ASU 2016-02 Leases (Topic 842)	The amendments require lessees to recognize a right-of-use asset and a liability to make lease payments in the statement of financial position for most leases. The accounting for lessors is largely unchanged.	January 1, 2019 (early adoption permitted)	Not expected to have a significant impact to the consolidated financial statements.
ASU 2016-01 Financial Instruments - Overall (Subtopic 825-10) Recognition and Measurement of Financial Assets and Financial Liabilities	The amendments address certain aspects of recognition, measurement, presentation, and disclosure of financial instruments.	January 1, 2018 (early adoption permitted for a provision related presentation of instrument-specific credit risk of liabilities accounted for under the fair value option)	Expected to impact disclosures only and not have a significant impact to the consolidated financial statements.
ASU 2014-15, Presentation of Financial Statements – Going Concern (Subtopic 205-04) Disclosure of Uncertainties about an Entity’s Ability to Continue as a Going Concern	This ASU requires management to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company’s ability to continue as a going concern within one year after the date the financial statements are issued.	January 1, 2017 (early adoption permitted)	Not expected to have an impact to the consolidated financial statements.
ASU 2014-09, Revenue from Contracts with Customers	This guidance applies to contracts with customers to transfer goods or services and contracts to transfer nonfinancial assets unless those	January 1, 2018	Not expected to have a significant impact to the consolidated

	contracts are within the scope of other standards (for example, lease transactions).		financial statements.
Standard	Description	Date of Adoption	Effect on the financial statements or other significant matters
Standards that were adopted			
ASU 2015-16 Business Combinations (Topic 805) Simplifying the Accounting Measurement-Period Adjustments	This amendment removes the requirement to present adjustments to provisional amounts retrospectively. The update requires that an acquirer record, in the same period's financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change to provisional amounts.	January 1, 2016 (early adoption permitted)	Did not have a significant impact to the consolidated financial statements.
ASU 2015-15, Interest - Imputation of Interest (Subtopic 835-30) Simplifying the Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements - Amendments to SEC Paragraphs Pursuant to Staff Announcement at June 18, 2015 EITF Meeting (SEC Update)	This amendment provides SEC guidance that it would not object to filers presenting debt issue costs related to line-of-credit arrangements as an asset and ratably amortizing the costs over the term of the arrangement.	June 18, 2015 (early adoption permitted)	Did not have an impact to the consolidated financial statements.
ASU 2015-10, Technical Corrections and Improvements	This perpetual project updates the Codification for technical corrections and improvements.	January 1, 2016 (early adoption permitted), for amendments subject to transition guidance	Did not have a significant impact to the consolidated financial statements.
ASU 2015-08, Business Combinations Topic 805 Pushdown Accounting Amendments to SEC Paragraphs Pursuant to Staff Accounting Bulletin No. 115	This update amends the codification for SEC Staff Bulletin No. 115	November 18, 2014	Did not have a significant impact to the consolidated financial statements.
ASU 2015-07, Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)	This update removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share practical expedient and also removes certain disclosure requirements for these investments.	January 1, 2016 (early adoption permitted)	Did not have an impact to the consolidated financial statements.

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Standard	Description	Date of Adoption	Effect on the financial statements or other significant matters
ASU 2015-05, Customer's Accounting for Fees Paid in a Cloud Computing Arrangement	This update clarifies that customers should determine whether a cloud computing arrangement includes the license of software by applying the same guidance cloud service providers use. The guidance also eliminates the current requirement that customers analogize to the leasing standard when determining the asset acquired in a software licensing arrangement.	January 1, 2016 (early adoption permitted)	Did not have a significant impact to the consolidated financial statements.
ASU 2015-03, Interest - Imputation of Interest (Subtopic 835-30) Simplifying the Presentation of Debt Issuance Costs	This ASU requires that debt issue costs are presented in the balance sheet as a direct deduction from the carrying amount of that debt liability. The recognition and measurement of debt issue costs are not affected.	January 1, 2016 (early adoption permitted)	Impacted presentation only and did not have a significant impact to the consolidated financial statements.
ASU 2015-02, Consolidation (Topic 810) Amendments to the Consolidation Analysis	This update affects the following areas of the consolidation analysis: limited partnerships and similar entities, evaluation of fees paid to a decision maker or service provider as a variable interest and in determination of the primary beneficiary, effect of related parties on the primary beneficiary determination and for certain investment funds.	January 1, 2016 (early adoption permitted)	Did not have a significant impact to the consolidated financial statements.
ASU 2015-01, Income Statement - Extraordinary and Unusual Items (Subtopic 225-20)	This update eliminates from GAAP the concept of extraordinary items.	January 1, 2016 (early adoption permitted)	Did not have an impact to the consolidated financial statements.
ASU 2014-16, Derivatives and Hedging (Topic 815) Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share is More Akin to Debt or Equity	This ASU provides additional guidance for evaluating whether conversion rights, redemption rights, voting rights, liquidation rights and dividend payment preferences and other features embedded in a share, including preferred stock, contain embedded derivatives requiring bifurcation. The update requires that an entity determine the nature of the host contract by considering all stated and implied terms and features in a hybrid instrument.	January 1, 2016 (early adoption permitted)	Did not have a significant impact to the consolidated financial statements.
ASU 2014-13, Consolidation (Topic 810) Measuring the Financial Assets and the Financial	This update provides a practical expedient to measure the fair value of the financial assets and financial liabilities of	January 1, 2015 (early adoption	The Company early adopted this ASU and applied the guidance to

Liabilities of a Consolidated Collateralized Financing Entity	a consolidated collateralized financing entity, which the reporting entity has elected to or is required to measure on a fair value basis.	permitted)	commercial mortgage backed securitization transactions. See "Commercial Real Estate Investments" footnote for further disclosure.
ASU 2014-11, Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosure	This update makes limited amendments to the guidance in ASC 860 on accounting for certain repurchase agreements.	January 1, 2015	Impacted disclosures only and did not have a significant impact to the consolidated financial statements.
ASU 2014-08, Presentation of Financial Statements (Topic 205) and Property, Plant and Equipment (Topic 360) Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity	This ASU raises the threshold for a disposal to be treated as discontinued operations.	April 1, 2015	Did not have a significant impact to the consolidated financial statements.
ASU 2014-04 Receivables–Troubled Debt Restructurings by Creditors, Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure	This update clarifies that an in substance repossession or foreclosure has occurred, and a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, when the creditor obtains legal title to the property upon completion of a foreclosure or the borrower conveys all interest in the property to the creditor through a deed in lieu of foreclosure or similar arrangement.	January 1, 2015	Did not have a significant impact to the consolidated financial statements.

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4. RESIDENTIAL INVESTMENT SECURITIES

The following tables present the Company's Residential Investment Securities portfolio carried at fair value as of June 30, 2016 and December 31, 2015:

	June 30, 2016						
	Principal / Notional	Remaining Premium	Remaining Discount	Amortized Cost	Unrealized Gains(1)	Unrealized Losses(1)	Estimated Fair Value
Agency	(dollars in thousands)						
Fixed-rate pass-through	$55,843,681	$3,073,647	$(2,017)	$58,915,311	$1,080,129	$(55,271)	$59,940,169
Adjustable-rate pass-through	2,906,239	62,572	(5,173)	2,963,638	77,317	-	3,040,955
CMO	473,489	9,860	(430)	482,919	15,080	(252)	497,747
Debentures	-	-	-	-	-	-	-
Interest-only	9,061,768	1,572,531	-	1,572,531	18,835	(207,245)	1,384,121
Total Agency investments	$68,285,177	$4,718,610	$(7,620)	$63,934,399	$1,191,361	$(262,768)	$64,862,992
Residential Credit							
CRT	$519,387	$1,878	$(12,415)	$508,850	$12,476	$(1,005)	$520,321
Legacy(2)	690,679	815	(91,368)	600,126	12,553	(924)	611,755
NPL/RPL	374,096	65	(1,240)	372,921	1,785	(82)	374,624
New issue	194,334	973	(373)	194,934	4,444	-	199,378
New issue interest-only	1,020,183	17,223	-	17,223	-	(5,431)	11,792
Total residential credit investments	$2,798,679	$20,954	$(105,396)	$1,694,054	$31,258	$(7,442)	$1,717,870
Total Residential Investment Securities	$71,083,856	$4,739,564	$(113,016)	$65,628,453	$1,222,619	$(270,210)	$66,580,862

	December 31, 2015						
	Principal / Notional	Remaining Premium	Remaining Discount	Amortized Cost	Unrealized Gains(1)	Unrealized Losses(1)	Estimated Fair Value
Agency	(dollars in thousands)						
Fixed-rate pass-through	$57,339,705	$3,270,521	$(2,832)	$60,607,394	$400,350	$(824,862)	$60,182,882
Adjustable-rate pass-through	2,894,192	61,781	(6,427)	2,949,546	70,849	(10,317)	3,010,078
CMO	964,095	27,269	(477)	990,887	9,137	(12,945)	987,079
Debentures	158,802	-	(648)	158,154	-	(6,116)	152,038
Interest-only	9,499,332	1,634,312	-	1,634,312	18,699	(114,826)	1,538,185
Total Agency investments	$70,856,126	$4,993,883	$(10,384)	$66,340,293	$499,035	$(969,066)	$65,870,262
Residential Credit							
CRT	$476,084	$2,225	$(12,840)	$465,469	$250	$(9,209)	$456,510

Legacy[2]	378,527	773	(37,150)	342,150	698	(1,140)	341,708
NPL/RPL	354,945	19	(1,270)	353,694	19	(1,172)	352,541
New issue	197,695	566	-	198,261	-	(1,060)	197,201
New issue interest-only	811,245	15,430	-	15,430	-	(158)	15,272
Total residential credit securities	$2,218,496	$19,013	$(51,260)	$1,375,004	$967	$(12,739)	$1,363,232
Total Residential Investment Securities	$73,074,622	$5,012,896	$(61,644)	$67,715,297	$500,002	$(981,805)	$67,233,494

(1) Unrealized gains and losses on Agency investments, excluding interest-only investments, are reported as a component of other comprehensive income (loss). Unrealized gains and losses on residential credit investments and Agency interest-only investments are generally reported in Net unrealized gains (losses) on financial instruments measured at fair value through earnings in the Consolidated Statements of Comprehensive Income (Loss).
(2) Legacy residential credit refers to securities whose underlying collateral was securitized prior to 2009.

The following tables present the Company's Agency mortgage-backed securities portfolio by issuing Agency concentration as of June 30, 2016 and December 31, 2015:

Investment Type	June 30, 2016	December 31, 2015
	(dollars in thousands)	
Fannie Mae	$42,009,658	$42,647,075
Freddie Mac	22,769,693	22,960,595
Ginnie Mae	83,641	110,554
Total	$64,862,992	$65,718,224

Actual maturities of the Company's Residential Investment Securities portfolio are generally shorter than stated contractual maturities because actual maturities of the portfolio are affected by periodic payments and prepayments of principal on underlying mortgages. The
following table summarizes the Company's available-for-sale Residential Investment Securities as of June 30, 2016 and December 31, 2015, according to their estimated weighted average life classifications:

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Weighted Average Life	June 30, 2016 Estimated Fair Value	June 30, 2016 Amortized Cost	December 31, 2015 Estimated Fair Value	December 31, 2015 Amortized Cost
	(dollars in thousands)			
Less than one year	$83,514	$84,500	$37,862	$37,850
Greater than one year through five years	53,216,416	52,372,346	20,278,111	20,066,435
Greater than five years through ten years	13,272,846	13,163,536	46,473,701	47,174,319
Greater than ten years	8,086	8,071	443,820	436,693
Total	$66,580,862	$65,628,453	$67,233,494	$67,715,297

The weighted average lives of the Agency mortgage-backed securities at June 30, 2016 and December 31, 2015 in the table above are based upon projected principal prepayment rates. The actual weighted average lives of the Agency mortgage-backed securities could be materially longer or shorter than projected.
The following table presents the gross unrealized losses and estimated fair value of the Company’s Agency mortgage-backed securities by length of time that such securities have been in a continuous unrealized loss position at June 30, 2016 and December 31, 2015.

	June 30, 2016 Estimated Fair Value(1)	June 30, 2016 Gross Unrealized Losses(1)	June 30, 2016 Number of Securities(1)	December 31, 2015 Estimated Fair Value(1)	December 31, 2015 Gross Unrealized Losses(1)	December 31, 2015 Number of Securities(1)
	(dollars in thousands)					
Less than 12 Months	$467	$ (3)	1	$20,072,072	$ (164,259)	463
12 Months or More	9,608,938	(55,520)	81	21,705,764	(689,981)	189
Total	$9,609,405	$ (55,523)	82	$41,777,836	$ (854,240)	652

(1) Excludes interest-only mortgage-backed securities.

The decline in value of these securities is solely due to market conditions and not the quality of the assets. Substantially all of the Agency mortgage-backed securities are “AAA” rated or carry an implied “AAA” rating. The investments are not considered to be other-than-temporarily impaired because the Company currently has the ability and intent to hold the investments to maturity or for a period of time sufficient for a forecasted market price recovery up to or beyond the cost of the investments, and it is not more likely than not that the Company will be required to sell the investments before recovery of the amortized cost bases, which may be maturity. Also, the Company is guaranteed payment of the principal amount of the securities by the respective issuing government agency.
During the quarter and six months ended June 30, 2016, the Company disposed of $1.8 billion and $5.2 billion of Residential Investment Securities, respectively, resulting in a net realized gain of $11.9 million and $10.3 million, respectively.

During the quarter and six months ended June 30, 2015, the Company disposed of $2.5 billion and $17.4 billion of Residential Investment Securities, respectively, resulting in a net realized gain of $3.9 million and $66.3, respectively.

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5. COMMERCIAL REAL ESTATE INVESTMENTS

On December 11, 2015, the Company originated a $335.0 million recapitalization financing with respect to eight class A/B office properties in Orange County, California.

As of December 31, 2015, such financing is comprised of a $280.0 million senior mortgage loan ($278.6 million, net of origination fees), and mezzanine debt with an initial principal balance of $55.0 million ($52.7 million, net of origination fees) and a future funding component of $30.0 million. The senior loan was held
for sale as of December 31, 2015. In April 2016, the Company sold $115.0 million ($114.3 million, net of origination fees) of the senior loan to an unrelated third party at carrying value, accordingly, no gain or loss was recorded in connection with the sale. The balance of the senior loan of $165.0 million ($164.2 million, net of origination fees) remains held for sale as of June 30, 2016.

The following tables present commercial real estate investments held for investment at June 30, 2016 and December 31, 2015.

CRE Debt and Preferred Equity Investments

	June 30, 2016				December 31, 2015			
	Outstanding Principal	Carrying Value[(1)]	Percentage of Loan Portfolio[(2)]		Outstanding Principal	Carrying Value[(1)]	Percentage of Loan Portfolio[(2)]	
	(dollars in thousands)							
Senior mortgages	$480,665	$478,260	42.0	%	$387,314	$385,838	28.6	%
Senior securitized mortgages(3)	187,322	187,246	16.4	%	263,072	262,703	19.4	%
Mezzanine loans	466,844							