TWO HARBORS INVESTMENT CORP.
Form 10-Q
November 03, 2016

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

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FORM 10-Q

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QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarterly Period Ended: September 30, 2016

Commission File Number 001-34506

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TWO HARBORS INVESTMENT CORP.
(Exact Name of Registrant as Specified in Its Charter)

| Maryland | 27-0312904 |
|---|---|
| (State or Other Jurisdiction of Incorporation or Organization) | (I.R.S. Employer Identification No.) |

| 590 Madison Avenue, 36th Floor New York, New York | 10022 |
|---|---|
| (Address of Principal Executive Offices) | (Zip Code) |

(612) 629-2500
(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o
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 x No o
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes o No x
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.
As of November 2, 2016 there were 347,643,717 shares of outstanding common stock, par value $.01 per share, issued and outstanding.

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PART I. FINANCIAL INFORMATION
Item 1. Financial Statements
TWO HARBORS INVESTMENT CORP.
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands, except share data)

| | September 30, 2016 (unaudited) | December 31, 2015 |
|---|---|---|
| ASSETS | | |
| Available-for-sale securities, at fair value | $14,284,625 | $7,825,320 |
| Residential mortgage loans held-for-sale, at fair value | 723,174 | 811,431 |
| Residential mortgage loans held-for-investment in securitization trusts, at fair value | 3,620,037 | 3,173,727 |
| Commercial real estate assets | 1,114,548 | 660,953 |
| Mortgage servicing rights, at fair value | 455,629 | 493,688 |
| Cash and cash equivalents | 688,418 | 737,831 |
| Restricted cash | 264,872 | 262,562 |
| Accrued interest receivable | 67,089 | 49,970 |
| Due from counterparties | 56,095 | 17,206 |
| Derivative assets, at fair value | 199,013 | 271,509 |
| Other assets | 326,396 | 271,575 |
| Total Assets [(1)] | $21,799,896 | $14,575,772 |
| LIABILITIES AND STOCKHOLDERS’ EQUITY | | |
| Liabilities | | |
| Repurchase agreements | $10,637,373 | $5,008,274 |
| Collateralized borrowings in securitization trusts, at fair value | 3,375,906 | 2,000,110 |
| Federal Home Loan Bank advances | 4,000,000 | 3,785,000 |
| Revolving credit facilities | 30,000 | — |
| Derivative liabilities, at fair value | 39,918 | 7,285 |
| Due to counterparties | 78,179 | 34,294 |
| Dividends payable | 79,956 | 92,016 |
| Other liabilities | 80,323 | 72,232 |
| Total Liabilities [(1)] | 18,321,655 | 10,999,211 |
| Stockholders’ Equity | | |
| Preferred stock, par value $0.01 per share; 50,000,000 shares authorized; no shares issued and outstanding | — | — |
| Common stock, par value $0.01 per share; 900,000,000 shares authorized and 347,635,488 and 353,906,807 shares issued and outstanding, respectively | 3,476 | 3,539 |
| Additional paid-in capital | 3,655,854 | 3,705,519 |
| Accumulated other comprehensive income | 538,443 | 359,061 |
| Cumulative earnings | 1,696,630 | 1,684,755 |
| Cumulative distributions to stockholders | (2,416,162) | (2,176,313) |
| Total Stockholders’ Equity | 3,478,241 | 3,576,561 |
| Total Liabilities and Stockholders’ Equity | $21,799,896 | $14,575,772 |

(1) The condensed consolidated balance sheets include assets of consolidated variable interest entities, or VIEs, that can only be used to settle obligations of these VIEs, and liabilities of the consolidated VIEs for which creditors do not have recourse to Two Harbors Investment Corp. At September 30, 2016 and December 31, 2015, assets of the VIEs totaled $3,686,340 and $3,237,918, and liabilities of the VIEs totaled $3,398,215 and $2,017,677,

respectively. See Note 3 - Variable Interest Entities for additional information.
The accompanying notes are an integral part of these condensed consolidated financial statements.

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TWO HARBORS INVESTMENT CORP.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(in thousands, except share data)

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| Interest income: | (unaudited) | | (unaudited) | |
| Available-for-sale securities | $ 111,393 | $ 116,318 | $ 292,333 | $ 369,972 |
| Trading securities | — | — | — | 8,676 |
| Residential mortgage loans held-for-sale | 7,627 | 9,479 | 19,789 | 21,268 |
| Residential mortgage loans held-for-investment in securitization trusts | 33,495 | 24,841 | 100,765 | 64,908 |
| Commercial real estate assets | 15,907 | 1,947 | 40,279 | 2,841 |
| Cash and cash equivalents | 440 | 249 | 1,235 | 667 |
| Total interest income | 168,862 | 152,834 | 454,401 | 468,332 |
| Interest expense: | | | | |
| Repurchase agreements | 27,056 | 18,235 | 65,782 | 58,198 |
| Collateralized borrowings in securitization trusts | 26,422 | 15,562 | 70,965 | 39,401 |
| Federal Home Loan Bank advances | 6,744 | 3,282 | 18,804 | 8,012 |
| Revolving credit facilities | 128 | — | 128 | — |
| Total interest expense | 60,350 | 37,079 | 155,679 | 105,611 |
| Net interest income | 108,512 | 115,755 | 298,722 | 362,721 |
| Other-than-temporary impairments: | | | | |
| Total other-than-temporary impairment losses | (1,015) | (238) | (1,822) | (535) |
| Other income (loss): | | | | |
| Gain on investment securities | 28,290 | 64,123 | 66,095 | 263,512 |
| Gain (loss) on interest rate swap and swaption agreements | 5,584 | (171,656) | (132,608) | (253,147) |
| Loss on other derivative instruments | (12,028) | (455) | (44,064) | (2,972) |
| (Loss) gain on residential mortgage loans held-for-sale | (889) | 16,040 | 17,648 | 18,300 |
| Servicing income | 38,708 | 32,010 | 108,657 | 94,613 |
| Loss on servicing asset | (33,451) | (61,549) | (211,426) | (96,317) |
| Other income (loss) | 5,757 | 2,201 | (977) | (16,265) |
| Total other income (loss) | 31,971 | (119,286) | (196,675) | 7,724 |
| Expenses: | | | | |
| Management fees | 11,387 | 12,617 | 35,268 | 38,024 |
| Securitization deal costs | 2,080 | 2,676 | 6,241 | 7,771 |
| Servicing expenses | 9,073 | 7,234 | 24,510 | 19,849 |
| Other operating expenses | 14,780 | 16,150 | 47,280 | 48,032 |
| Restructuring charges | 1,189 | — | 1,189 | — |
| Total expenses | 38,509 | 38,677 | 114,488 | 113,676 |
| Income (loss) before income taxes | 100,959 | (42,446) | (14,263) | 256,234 |
| Benefit from income taxes | (16,827) | (7,656) | (26,138) | (25,270) |
| Net income (loss) | $ 117,786 | $ (34,790) | $ 11,875 | $ 281,504 |
| Basic and diluted earnings (loss) per weighted average common share | $ 0.34 | $ (0.09) | $ 0.03 | $ 0.77 |
| Dividends declared per common share | $ 0.23 | $ 0.26 | $ 0.69 | $ 0.78 |
| | 347,627,226 | 367,365,973 | 348,218,234 | 366,985,731 |

Basic and diluted weighted average number of shares of common
stock outstanding

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

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TWO HARBORS INVESTMENT CORP.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS), continued
(in thousands, except share data)

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| | (unaudited) | | (unaudited) | |
| Comprehensive income (loss): | | | | |
| Net income (loss) | $117,786 | $(34,790) | $11,875 | $281,504 |
| Other comprehensive income (loss), net of tax: | | | | |
| Unrealized gain (loss) on available-for-sale securities | 18,746 | (58,031) | 179,382 | (282,788) |
| Other comprehensive income (loss) | 18,746 | (58,031) | 179,382 | (282,788) |
| Comprehensive income (loss) | $136,532 | $(92,821) | $191,257 | $(1,284) |

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

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TWO HARBORS INVESTMENT CORP.
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(in thousands, except share data)

| | Common Stock | | | | | | |
|---|---|---|---|---|---|---|---|
| | Shares | Amount | Additional Paid-in Capital | Accumulated Other Comprehensive Income (unaudited) | Cumulative Earnings | Cumulative Distributions to Stockholders | Total Stockholders' Equity |
| Balance, December 31, 2014 | 366,395,920 | $3,664 | $3,811,027 | $ 855,789 | $1,195,536 | $(1,797,974) | $4,068,042 |
| Cumulative effect of adoption of new accounting principle | — | — | — | — | (2,991) | — | (2,991) |
| Adjusted balance, January 1, 2015 | 366,395,920 | 3,664 | 3,811,027 | 855,789 | 1,192,545 | (1,797,974) | 4,065,051 |
| Net income | — | — | — | — | 281,504 | — | 281,504 |
| Other comprehensive loss before reclassifications, net of tax | — | — | — | (54,805) | — | — | (54,805) |
| Amounts reclassified from accumulated other comprehensive income, net of tax | — | — | — | (227,983) | — | — | (227,983) |
| Net other comprehensive loss, net of tax | — | — | — | (282,788) | — | — | (282,788) |
| Issuance of common stock, net of offering costs | 54,088 | 1 | 403 | — | — | — | 404 |
| Repurchase of common stock | (1,391,887) | (14) | (12,462) | — | — | — | (12,476) |
| Common dividends declared | — | — | — | — | — | (286,323) | (286,323) |
| Non-cash equity award compensation | 1,098,638 | 11 | 7,355 | — | — | — | 7,366 |
| Balance, September 30, 2015 | 366,156,759 | $3,662 | $3,806,323 | $ 573,001 | $1,474,049 | $(2,084,297) | $3,772,738 |
| | | | | | | | |
| Balance, December 31, 2015 | 353,906,807 | $3,539 | $3,705,519 | $ 359,061 | $1,684,755 | $(2,176,313) | $3,576,561 |
| Net income | — | — | — | — | 11,875 | — | 11,875 |
| Other comprehensive income before reclassifications, net of tax | — | — | — | 232,212 | — | — | 232,212 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Amounts reclassified from accumulated other comprehensive income, net of tax | — | — | — | (52,830 ) | — | — | (52,830 ) |
| Net other comprehensive income, net of tax | — | — | — | 179,382 | — | — | 179,382 |
| Issuance of common stock, net of offering costs | 43,764 | — | 356 | — | — | — | 356 |
| Repurchase of common stock | (8,020,000 ) | (80 ) | (61,227 ) | — | — | — | (61,307 ) |
| Common dividends declared | — | — | — | — | — | (239,849 ) | (239,849 ) |
| Non-cash equity award compensation | 1,704,917 | 17 | 11,206 | — | — | — | 11,223 |
| Balance, September 30, 2016 | 347,635,488 | $3,476 | $3,655,854 | $ 538,443 | $1,696,630 | $(2,416,162 ) | $3,478,241 |

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

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TWO HARBORS INVESTMENT CORP.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

| | Nine Months Ended September 30, | |
|---|---|---|
| | 2016 | 2015 |
| Cash Flows From Operating Activities: | (unaudited) | |
| Net income | $11,875 | $281,504 |
| Adjustments to reconcile net income to net cash used in operating activities: | | |
| Amortization of premiums and discounts on investment securities and commercial real estate assets, net | 29,469 | 32,556 |
| Other-than-temporary impairment losses | 1,822 | 535 |
| Realized and unrealized gains on investment securities, net | (66,095) | (263,512) |
| Gain on residential mortgage loans held-for-sale | (17,648) | (18,300) |
| Loss on residential mortgage loans held-for-investment and collateralized borrowings in securitization trusts | 5,173 | 19,441 |
| Loss on servicing asset | 211,426 | 96,317 |
| Loss on termination and option expiration of interest rate swaps and swaptions | 119,548 | 124,984 |
| Unrealized (gain) loss on interest rate swaps and swaptions | (5,080) | 55,079 |
| Unrealized loss (gain) on other derivative instruments | 2,025 | (15,563) |
| Equity based compensation | 11,223 | 7,366 |
| Depreciation of fixed assets | 981 | 1,002 |
| Purchases of residential mortgage loans held-for-sale | (1,159,782) | (2,166,494) |
| Proceeds from sales of residential mortgage loans held-for-sale | 95,331 | 137,612 |
| Proceeds from repayment of residential mortgage loans held-for-sale | 117,092 | 80,152 |
| Net change in assets and liabilities: | | |
| (Increase) decrease in accrued interest receivable | (17,119) | 9,279 |
| Increase in deferred income taxes, net | (24,581) | (19,592) |
| Decrease (increase) in income taxes receivable | 3,667 | (6,854) |
| Increase in prepaid and fixed assets | (62) | (221) |
| Decrease in other receivables | 5,721 | 8,563 |
| Increase in servicing advances | (8,965) | (3,465) |
| Increase (decrease) in accrued interest payable | 11,084 | (4,780) |
| Decrease in income taxes payable | (70) | (1,215) |
| (Decrease) increase in accrued expenses and other liabilities | (2,923) | 6,324 |
| Net cash used in operating activities | $(675,888) | $(1,639,282) |

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

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TWO HARBORS INVESTMENT CORP.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS, continued
(in thousands)

| | Nine Months Ended September 30, | |
|---|---|---|
| | 2016 | 2015 |
| Cash Flows From Investing Activities: | (unaudited) | |
| Purchases of available-for-sale securities | $(13,734,884) | $(1,732,979) |
| Proceeds from sales of available-for-sale securities | 6,567,992 | 3,666,974 |
| Principal payments on available-for-sale securities | 910,386 | 918,798 |
| (Purchases) short sales of derivative instruments, net | (13,953) | 3,592 |
| Proceeds from sales (payments for termination) of derivative instruments, net | 3,209 | (93,352) |
| Proceeds from sales of trading securities | — | 2,004,375 |
| Proceeds from repayment of residential mortgage loans held-for-investment in securitization trusts | 649,134 | 435,967 |
| Originations and purchases of commercial real estate assets, net of deferred fees | (463,680) | (290,683) |
| Proceeds from repayment of commercial real estate assets | 15,296 | — |
| Purchases of mortgage servicing rights, net of purchase price adjustments | (208,474) | (75,011) |
| Proceeds from sales of mortgage servicing rights | 41,844 | — |
| Purchases of Federal Home Loan Bank stock | (11,206) | (53,640) |
| Increase (decrease) in due to counterparties, net | 4,996 | (57,265) |
| Increase in restricted cash | (2,310) | (47,258) |
| Net cash (used in) provided by investing activities | (6,241,650) | 4,679,518 |
| Cash Flows From Financing Activities: | | |
| Proceeds from repurchase agreements | 70,805,165 | 37,275,034 |
| Principal payments on repurchase agreements | (65,176,066) | (42,224,569) |
| Proceeds from issuance of collateralized borrowings in securitization trusts | 1,875,371 | 1,104,093 |
| Principal payments on collateralized borrowings in securitization trusts | (568,485) | (309,341) |
| Proceeds from Federal Home Loan Bank advances | 215,000 | 1,415,000 |
| Principal payments on Federal Home Loan Bank advances | — | (205,000) |
| Proceeds from revolving credit facilities | 30,000 | — |
| Proceeds from issuance of common stock, net of offering costs | 356 | 404 |
| Repurchase of common stock | (61,307) | (3,683) |
| Dividends paid on common stock | (251,909) | (286,127) |
| Net cash provided by (used in) financing activities | 6,868,125 | (3,234,189) |
| Net decrease in cash and cash equivalents | (49,413) | (193,953) |
| Cash and cash equivalents at beginning of period | 737,831 | 1,005,792 |
| Cash and cash equivalents at end of period | $688,418 | $811,839 |

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

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TWO HARBORS INVESTMENT CORP.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS, continued
(in thousands)

| | Nine Months Ended September 30, | |
|---|---|---|
| | 2016 | 2015 |
| Supplemental Disclosure of Cash Flow Information: | (unaudited) | |
| Cash paid for interest | $77,142 | $73,187 |
| Cash (received) paid for taxes | $(5,154) | $2,389 |
| Noncash Activities: | | |
| Transfers of residential mortgage loans held-for-sale to residential mortgage loans held-for-investment in securitization trusts | $1,031,707 | $1,705,885 |
| Transfers of residential mortgage loans held-for-sale to other receivables for foreclosed government-guaranteed loans | $14,200 | $12,764 |
| Transfer of fair value of mortgage servicing rights to fair value of Ginnie Mae residential mortgage loans held-for-sale upon buyout | $5,973 | $15,077 |
| Additions to mortgage servicing rights due to sale of residential mortgage loans held-for-sale | $764 | $1,568 |
| Cumulative-effect adjustment to equity for adoption of new accounting principle | $— | $(2,991) |
| Shares repurchase payable at end of period | $— | $8,793 |
| Dividends declared but not paid at end of period | $79,956 | $95,459 |
| Reconciliation of residential mortgage loans held-for-sale: | | |
| Residential mortgage loans held-for-sale at beginning of period | $811,431 | $535,712 |
| Purchases of residential mortgage loans held-for-sale | 1,159,782 | 2,166,494 |
| Transfers to residential mortgage loans held-for-investment in securitization trusts | (1,031,707) | (1,705,885) |
| Transfers to other receivables for foreclosed government-guaranteed loans | (14,200) | (12,764) |
| Transfer of fair value of mortgage servicing rights to fair value of Ginnie Mae residential mortgage loans held-for-sale upon buyout | (5,973) | (15,077) |
| Proceeds from sales of residential mortgage loans held-for-sale | (95,331) | (137,612) |
| Proceeds from repayment of residential mortgage loans held-for-sale | (117,092) | (80,152) |
| Realized and unrealized gains on residential mortgage loans held-for-sale | 16,264 | 17,292 |
| Residential mortgage loans held-for-sale at end of period | $723,174 | $768,008 |

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

TWO HARBORS INVESTMENT CORP.
Notes to the Condensed Consolidated Financial Statements (unaudited)

## Note 1. Organization and Operations

Two Harbors Investment Corp., or the Company, is a Maryland corporation focused on investing in, financing and managing residential mortgage-backed securities, or RMBS, residential mortgage loans, mortgage servicing rights, or MSR, commercial real estate and other financial assets. The Company is externally managed and advised by PRCM Advisers LLC, or PRCM Advisers, which is a subsidiary of Pine River Capital Management L.P., or Pine River, a global multi-strategy asset management firm. The Company's common stock is listed on the NYSE under the symbol "TWO".

The Company was incorporated on May 21, 2009, and commenced operations as a publicly traded company on October 28, 2009, upon completion of a merger with Capitol Acquisition Corp., or Capitol, which became a wholly owned indirect subsidiary of the Company as a result of the merger.

The Company has elected to be treated as a real estate investment trust, or REIT, as defined under the Internal Revenue Code of 1986, as amended, or the Code, for U.S. federal income tax purposes. As long as the Company continues to comply with a number of requirements under federal tax law and maintains its qualification as a REIT, the Company generally will not be subject to U.S. federal income taxes to the extent that the Company distributes its taxable income to its stockholders on an annual basis and does not engage in prohibited transactions. However, certain activities that the Company may perform may cause it to earn income which will not be qualifying income for REIT purposes. The Company has designated certain of its subsidiaries as taxable REIT subsidiaries, or TRSs, as defined in the Code, to engage in such activities, and the Company may in the future form additional TRSs.

## Note 2. Basis of Presentation and Significant Accounting Policies

### Consolidation and Basis of Presentation

The interim unaudited condensed consolidated financial statements of the Company have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission, or SEC. Certain information and note disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles, or U.S. GAAP, have been condensed or omitted according to such SEC rules and regulations. However, management believes that the disclosures included in these interim condensed consolidated financial statements are adequate to make the information presented not misleading. The accompanying condensed consolidated financial statements should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2015. In the opinion of management, all normal and recurring adjustments necessary to present fairly the financial condition of the Company at September 30, 2016 and results of operations for all periods presented have been made. The results of operations for the three and nine months ended September 30, 2016 should not be construed as indicative of the results to be expected for future periods or the full year.

The condensed consolidated financial statements of the Company have been prepared on the accrual basis of accounting in accordance with U.S. GAAP. The preparation of financial statements in conformity with U.S. GAAP requires us to make a number of significant estimates and assumptions. These estimates include estimates of fair value of certain assets and liabilities, amount and timing of credit losses, prepayment rates, the period of time during which the Company anticipates an increase in the fair values of real estate securities sufficient to recover unrealized losses in those securities, and other estimates that affect the reported amounts of certain assets and liabilities and disclosure of contingent assets and liabilities as of the date of the condensed consolidated financial statements and the reported amounts of certain revenues and expenses during the reported period. It is likely that changes in these estimates (e.g., valuation changes due to supply and demand, credit performance, prepayments, interest rates, or other reasons) will occur in the near term. The Company's estimates are inherently subjective in nature and actual results could differ from its estimates and the differences may be material.

The condensed consolidated financial statements of the Company include the accounts of all subsidiaries; inter-company accounts and transactions have been eliminated. Certain prior period amounts have been reclassified to conform to the current period presentation. The Company's Chief Investment Officer manages the investment portfolio as a whole and resources are allocated and financial performance is assessed on a consolidated basis.

All trust entities in which the Company holds investments that are considered VIEs for financial reporting purposes were reviewed for consolidation under the applicable consolidation guidance. Whenever the Company has both the power to direct the activities of a trust that most significantly impact the entity's performance, and the obligation to absorb losses or the right to receive benefits of the entity that could be significant, the Company consolidates the trust.

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TWO HARBORS INVESTMENT CORP.
Notes to the Condensed Consolidated Financial Statements (unaudited)

Significant Accounting Policies
Included in Note 2 to the Consolidated Financial Statements of the Company’s 2015 Annual Report on Form 10-K is a summary of the Company’s significant accounting policies. Provided below is a summary of additional accounting policies that are significant to the Company’s consolidated financial condition and results of operations for the nine months ended September 30, 2016.
Revolving Credit Facilities
To finance MSR, the Company enters into revolving credit facilities collateralized by pledged MSR. Borrowings under these revolving credit facilities are generally short-term debt, which expire within one year. The Company’s revolving credit facilities generally bear interest rates of a specified margin over one-month LIBOR and are uncommitted. Borrowings under revolving credit facilities are treated as collateralized financing transactions and are carried at contractual amounts, as specified in the respective agreements.
Offsetting Assets and Liabilities
Certain of the Company’s repurchase agreements are governed by underlying agreements that provide for a right of setoff in the event of default of either party to the agreement. The Company also has netting arrangements in place with all derivative counterparties pursuant to standard documentation developed by the International Swap and Derivatives Association, or ISDA, or central clearing exchange agreements, in the case of centrally cleared interest rate swaps. Additionally, the Company and the counterparty or clearing agency are required to post cash collateral based upon the net underlying market value of the Company’s open positions with the counterparty.
Under U.S. GAAP, if the Company has a valid right of setoff, it may offset the related asset and liability and report the net amount. The Company presents repurchase agreements subject to master netting arrangements or similar agreements on a gross basis, and derivative assets and liabilities subject to such arrangements on a net basis, based on derivative type and counterparty, in its condensed consolidated balance sheets. Separately, the Company presents cash collateral subject to such arrangements on a net basis, based on counterparty, in its condensed consolidated balance sheets. However, the Company does not offset financial assets and liabilities with the associated cash collateral on its condensed consolidated balance sheets.
The following tables present information about the Company’s assets and liabilities that are subject to master netting arrangements or similar agreements and can potentially be offset on the Company’s condensed consolidated balance sheets as of September 30, 2016 and December 31, 2015:

| | September 30, 2016 | | | | | |
|---|---|---|---|---|---|---|
| | | | | Gross Amounts Not Offset with Financial Assets (Liabilities) in the Condensed Consolidated Balance Sheets [1] | | |
| (in thousands) | Gross Amounts of Recognized Assets (Liabilities) | Gross Amounts Offset in the Condensed Consolidated Balance Sheets | Net Amounts of Assets (Liabilities) Presented in the Condensed Consolidated Balance Sheets | Financial Instruments | Cash Collateral (Received) Pledged | Net Amount |
| Assets | | | | | | |
| Derivative assets | $298,389 | $ (99,376 ) | $199,013 | $(39,918 ) | $ — | $159,095 |
| Total Assets | $298,389 | $ (99,376 ) | $199,013 | $(39,918 ) | $ — | $159,095 |
| Liabilities | | | | | | |

| | | | | | | |
|---|---|---|---|---|---|---|
| Repurchase agreements | $(10,637,373) | $ — | $(10,637,373) | $10,637,373 | $ — | $— |
| Derivative liabilities | (139,294) | 99,376 | (39,918) | 39,918 | — | — |
| Total Liabilities | $(10,776,667) | $ 99,376 | $(10,677,291) | $10,677,291 | $ — | $— |

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| December 31, 2015 | | | | | | |
|---|---|---|---|---|---|---|
| | | | | Gross Amounts Not Offset with Financial Assets (Liabilities) in the Condensed Consolidated Balance Sheets (1) | | |
| (in thousands) | Gross Amounts of Recognized Assets (Liabilities) | Gross Amounts Offset in the Condensed Consolidated Balance Sheets | Net Amounts of Assets (Liabilities) Presented in the Condensed Consolidated Balance Sheets | Financial Instruments | Cash Collateral (Received) Pledged | Net Amount |
| Assets | | | | | | |
| Derivative assets | $325,755 | $ (54,246 ) | $271,509 | $(7,285 ) | $ — | $264,224 |
| Total Assets | $325,755 | $ (54,246 ) | $271,509 | $(7,285 ) | $ — | $264,224 |
| Liabilities | | | | | | |
| Repurchase agreements | $(5,008,274) | $ — | $(5,008,274 ) | $5,008,274 | $ — | $— |
| Derivative liabilities | (61,531 ) | 54,246 | (7,285 ) | 7,285 | — | — |
| Total Liabilities | $(5,069,805) | $ 54,246 | $(5,015,559 ) | $5,015,559 | $ — | $— |

(1) Amounts presented are limited in total to the net amount of assets or liabilities presented in the condensed consolidated balance sheets by instrument. Excess cash collateral or financial assets that are pledged to counterparties may exceed the financial liabilities subject to a master netting arrangement or similar agreement, or counterparties may have pledged excess cash collateral to the Company that exceed the corresponding financial assets. These excess amounts are excluded from the table above, although separately reported within restricted cash, due from counterparties, or due to counterparties in the Company's condensed consolidated balance sheets.

Recently Issued and/or Adopted Accounting Standards

Revenue from Contracts with Customers

In May 2014, the Financial Accounting Standards Board, or FASB, issued ASU No. 2014-09, which is a comprehensive revenue recognition standard that supersedes virtually all existing revenue guidance under U.S. GAAP. The standard's core principle is that an entity will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. As a result of the issuance of ASU No. 2015-14 in August 2015 deferring the effective date of ASU No. 2014-09 by one year, the ASU is effective for annual periods, and interim periods within those annual periods, beginning on or after December 15, 2017, with early adoption prohibited. The Company has determined this ASU will not have a material impact on the Company's financial condition or results of operations.

Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern

In August 2014, the FASB issued ASU No. 2014-15, which requires management to evaluate whether there are conditions and events that raise substantial doubt about the entity's ability to continue as a going concern for both annual and interim reporting periods. The update requires certain disclosures if management concludes that substantial doubt exists and plans to alleviate that doubt. The ASU is effective for annual periods ending after December 15, 2016, and for both annual and interim periods thereafter, with early adoption permitted.

Recognition and Measurement of Financial Assets and Financial Liabilities

In January 2016, the FASB issued ASU No. 2016-01, which changes how entities measure certain equity investments and present changes in the fair value of financial liabilities measured under the fair value option that are attributable to their own credit. The ASU requires certain recurring disclosures and is effective for annual periods, and interim periods within those annual periods, beginning on or after December 15, 2017, with early adoption permitted. The Company has determined this ASU will not have a material impact on the Company’s financial condition or results of operations.

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Lease Classification and Accounting
In February 2016, the FASB issued ASU No. 2016-02, which requires lessees to recognize on their balance sheets both a lease liability for the obligation to make lease payments and a right-of-use asset for the right to use the underlying asset for the lease term. The ASU is effective for annual periods, and interim periods within those annual periods, beginning on or after December 15, 2018, with early adoption permitted. The Company has determined this ASU will not have a material impact on the Company's financial condition or results of operations.
Measurement of Credit Losses on Financial Instruments
In June 2016, the FASB issued ASU No. 2016-13, which changes the impairment model for most financial assets and certain other instruments. Allowances for credit losses on AFS debt securities will be recognized, rather than direct reductions in the amortized cost of the investments. The new model also requires the estimation of lifetime expected credit losses and corresponding recognition of allowance for losses on trade and other receivables, held-to-maturity debt securities, loans, and other instruments held at amortized cost. The ASU requires certain recurring disclosures and is effective for annual periods, and interim periods within those annual periods, beginning on or after December 15, 2019, with early adoption permitted for annual periods, and interim periods within those annual periods, beginning on or after December 15, 2018. The Company is evaluating the adoption of this ASU.
Classification of Certain Cash Receipts and Cash Payments
In August 2016, the FASB issued ASU No. 2016-15, which clarifies how entities should classify certain cash receipts and cash payments and how the predominance principle should be applied on the statement of cash flows. The ASU is effective for annual periods, and interim periods within those annual periods, beginning on or after December 15, 2017, with early adoption permitted. The Company has determined this ASU will not have an impact on the Company's financial condition or results of operations but may impact the presentation of the condensed consolidated statements of cash flows.

Note 3. Variable Interest Entities
The Company purchases subordinated debt and excess servicing rights from securitization trusts sponsored by either third parties or the Company's subsidiaries. Additionally, the Company is the sole certificate holder of a trust entity that holds a commercial real estate loan. All of these trusts are considered VIEs for financial reporting purposes and, thus, were reviewed for consolidation under the applicable consolidation guidance. Because the Company has both the power to direct the activities of the trusts that most significantly impact the entities' performance, and the obligation to absorb losses or the right to receive benefits of the entities that could be significant, the Company consolidates the trusts. As the Company is required to reassess VIE consolidation guidance each quarter, new facts and circumstances may change the Company's determination. A change in the Company's determination could result in a material impact to the Company's condensed consolidated financial statements during subsequent reporting periods.
The following table presents a summary of the assets and liabilities of all consolidated trusts as reported on the condensed consolidated balance sheets as of September 30, 2016 and December 31, 2015:

| (in thousands) | September 30, 2016 | December 31, 2015 |
|---|---|---|
| Residential mortgage loans held-for-investment in securitization trusts | $ 3,620,037 | $ 3,173,727 |
| Commercial real estate assets | 45,837 | 45,698 |
| Accrued interest receivable | 20,466 | 18,493 |
| Total Assets | $ 3,686,340 | $ 3,237,918 |
| Collateralized borrowings in securitization trusts | $ 3,375,906 | $ 2,000,110 |
| Accrued interest payable | 9,457 | 5,943 |
| Other liabilities | 12,852 | 11,624 |
| Total Liabilities | $ 3,398,215 | $ 2,017,677 |

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The Company is not required to consolidate VIEs for which it has concluded it does not have both the power to direct the activities of the VIEs that most significantly impact the entities' performance, and the obligation to absorb losses or the right to receive benefits of the entities that could be significant. The Company's investments in these unconsolidated VIEs include non-Agency RMBS, which are classified within available-for-sale securities, at fair value on the condensed consolidated balance sheets. As of September 30, 2016 and December 31, 2015, the carrying value, which also represents the maximum exposure to loss, of all non-Agency RMBS in unconsolidated VIEs was $1.8 billion and $1.9 billion, respectively.

Note 4. Available-for-Sale Securities, at Fair Value

The Company holds AFS investment securities which are carried at fair value on the condensed consolidated balance sheets. AFS securities exclude the retained interests from the Company's on-balance sheet securitizations, as they are eliminated in consolidation in accordance with U.S. GAAP. The following table presents the Company's AFS investment securities by collateral type as of September 30, 2016 and December 31, 2015:

| (in thousands) | September 30, 2016 | December 31, 2015 |
|---|---|---|
| Agency | | |
| Federal Home Loan Mortgage Corporation | $ 1,808,122 | $ 1,678,814 |
| Federal National Mortgage Association | 10,393,094 | 3,602,348 |
| Government National Mortgage Association | 235,600 | 691,728 |
| Non-Agency | 1,847,809 | 1,852,430 |
| Total available-for-sale securities | $ 14,284,625 | $ 7,825,320 |

At September 30, 2016 and December 31, 2015, the Company pledged AFS securities with a carrying value of $14.3 billion and $7.8 billion, respectively, as collateral for repurchase agreements and advances from the Federal Home Loan Bank of Des Moines, or the FHLB. See Note 15 - Repurchase Agreements and Note 17 - Federal Home Loan Bank of Des Moines Advances.

At September 30, 2016 and December 31, 2015, the Company did not have any securities purchased from and financed with the same counterparty that did not meet the conditions of ASC 860, Transfers and Servicing, or ASC 860, to be considered linked transactions and, therefore, classified as derivatives.

The following tables present the amortized cost and carrying value (which approximates fair value) of AFS securities by collateral type as of September 30, 2016 and December 31, 2015:

| | September 30, 2016 | | |
|---|---|---|---|
| (in thousands) | Agency | Non-Agency | Total |
| Face Value | $14,254,562 | $2,634,994 | $16,889,556 |
| Unamortized premium | 625,519 | — | 625,519 |
| Unamortized discount | | | |
| Designated credit reserve | — | (352,489 ) | (352,489 ) |
| Net, unamortized | (2,620,684 ) | (789,425 ) | (3,410,109 ) |
| Amortized Cost | 12,259,397 | 1,493,080 | 13,752,477 |
| Gross unrealized gains | 208,319 | 359,748 | 568,067 |
| Gross unrealized losses | (30,900 ) | (5,019 ) | (35,919 ) |
| Carrying Value | $12,436,816 | $1,847,809 | $14,284,625 |

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| | December 31, 2015 | | |
|---|---|---|---|
| (in thousands) | Agency | Non-Agency | Total |
| Face Value | $8,257,030 | $2,655,381 | $10,912,411 |
| Unamortized premium | 394,787 | — | 394,787 |
| Unamortized discount | | | |
| Designated credit reserve | — | (409,077 ) | (409,077 ) |
| Net, unamortized | (2,721,979 ) | (707,021 ) | (3,429,000 ) |
| Amortized Cost | 5,929,838 | 1,539,283 | 7,469,121 |
| Gross unrealized gains | 98,389 | 329,206 | 427,595 |
| Gross unrealized losses | (55,337 ) | (16,059 ) | (71,396 ) |
| Carrying Value | $5,972,890 | $1,852,430 | $7,825,320 |

The following tables present the carrying value of the Company's AFS securities by rate type as of September 30, 2016 and December 31, 2015:

| | September 30, 2016 | | |
|---|---|---|---|
| (in thousands) | Agency | Non-Agency | Total |
| Adjustable Rate | $32,588 | $ 1,545,843 | $1,578,431 |
| Fixed Rate | 12,404,228 | 301,966 | 12,706,194 |
| Total | $12,436,816 | $ 1,847,809 | $14,284,625 |

| | December 31, 2015 | | |
|---|---|---|---|
| (in thousands) | Agency | Non-Agency | Total |
| Adjustable Rate | $108,596 | $ 1,673,038 | $1,781,634 |
| Fixed Rate | 5,864,294 | 179,392 | 6,043,686 |
| Total | $5,972,890 | $ 1,852,430 | $7,825,320 |

The following table presents the Company's AFS securities according to their estimated weighted average life classifications as of September 30, 2016:

| | September 30, 2016 | | |
|---|---|---|---|
| (in thousands) | Agency | Non-Agency | Total |
| ≤ 1 year | $2,186 | $ 67,171 | $69,357 |
| > 1 and ≤ 3 years | 102,324 | 241,346 | 343,670 |
| > 3 and ≤ 5 years | 5,407,166 | 214,452 | 5,621,618 |
| > 5 and ≤ 10 years | 6,923,818 | 957,723 | 7,881,541 |
| > 10 years | 1,322 | 367,117 | 368,439 |
| Total | $12,436,816 | $ 1,847,809 | $14,284,625 |

When the Company purchases a credit-sensitive AFS security at a significant discount to its face value, the Company often does not amortize into income a significant portion of this discount that the Company is entitled to earn because the Company does not expect to collect the entire discount due to the inherent credit risk of the security. The Company may also record an other-than-temporary impairment, or OTTI, for a portion of its investment in the security to the extent the Company believes that the amortized cost will exceed the present value of expected future cash flows. The amount of principal that the Company does not amortize into income is designated as a credit reserve on the security, with unamortized net discounts or premiums amortized into income over time to the extent realizable.

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The following table presents the changes for the nine months ended September 30, 2016 and 2015, of the unamortized net discount and designated credit reserves on non-Agency AFS securities.

| (in thousands) | Nine Months Ended September 30, 2016 Designated Credit Reserve | 2016 Unamortized Net Discount | 2016 Total | 2015 Designated Credit Reserve | 2015 Unamortized Net Discount | 2015 Total |
|---|---|---|---|---|---|---|
| Beginning balance at January 1 | $(409,077) | $(707,021) | $(1,116,098) | $(927,605) | $(967,368) | $(1,894,973) |
| Acquisitions | (45,398) | (140,318) | (185,716) | (274) | (4,293) | (4,567) |
| Accretion of net discount | — | 50,596 | 50,596 | — | 76,861 | 76,861 |
| Realized credit losses | 279 | — | 279 | 13,376 | — | 13,376 |
| Reclassification adjustment for other-than-temporary impairments | (1,226) | — | (1,226) | 1,742 | — | 1,742 |
| Transfers from (to) | 70,371 | (70,371) | — | 85,767 | (85,767) | — |
| Sales, calls, other | 32,562 | 77,689 | 110,251 | 282,821 | 227,078 | 509,899 |
| Ending balance at September 30 | $(352,489) | $(789,425) | $(1,141,914) | $(544,173) | $(753,489) | $(1,297,662) |

The following table presents the components comprising the carrying value of AFS securities not deemed to be other than temporarily impaired by length of time that the securities had an unrealized loss position as of September 30, 2016 and December 31, 2015. At September 30, 2016, the Company held 1,220 AFS securities, of which 80 were in an unrealized loss position for less than twelve consecutive months and 124 were in an unrealized loss position for more than twelve consecutive months. At December 31, 2015, the Company held 1,181 AFS securities, of which 121 were in an unrealized loss position for less than twelve consecutive months and 182 were in an unrealized loss position for more than twelve consecutive months.

| (in thousands) | Unrealized Loss Position for Less than 12 Months Estimated Fair Value | Less than 12 Months Gross Unrealized Losses | 12 Months or More Estimated Fair Value | 12 Months or More Gross Unrealized Losses | Total Estimated Fair Value | Total Gross Unrealized Losses |
|---|---|---|---|---|---|---|
| September 30, 2016 | $2,122,527 | $(12,318) | $551,086 | $(23,601) | $2,673,613 | $(35,919) |
| December 31, 2015 | $1,503,939 | $(26,984) | $1,141,839 | $(44,412) | $2,645,778 | $(71,396) |

Evaluating AFS Securities for Other-Than-Temporary Impairments

In evaluating AFS securities for OTTI, the Company determines whether there has been a significant adverse quarterly change in the cash flow expectations for a security. The Company compares the amortized cost of each security in an unrealized loss position against the present value of expected future cash flows of the security. The Company also considers whether there has been a significant adverse change in the regulatory and/or economic environment as part of this analysis. If the amortized cost of the security is greater than the present value of expected future cash flows using the original yield as the discount rate, an other-than-temporary credit impairment has occurred. If the Company does not intend to sell and will not be more likely than not required to sell the security, the credit loss is recognized in earnings and the balance of the unrealized loss is recognized in either other comprehensive income (loss), net of tax, or gain on investment securities, depending on the accounting treatment. If the Company intends to sell the security or will be more likely than not required to sell the security, the full unrealized loss is recognized in earnings.

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The Company recorded $1.0 million and $1.8 million in other-than-temporary credit impairments during the three and nine months ended September 30, 2016 on one and four non-Agency RMBS, respectively, where the future expected cash flows for each security were less than its amortized cost. As of September 30, 2016, impaired securities with a carrying value of $124.0 million had actual weighted average cumulative losses of 12.0%, weighted average three-month prepayment speed of 6.8%, weighted average 60+ day delinquency of 22.9% of the pool balance, and weighted average FICO score of 666. At September 30, 2016, the Company did not intend to sell the securities and determined that it was not more likely than not that the Company will be required to sell the securities; therefore, only the projected credit loss was recognized in earnings. During the three and nine months ended September 30, 2015, the Company recorded $0.2 million and $0.5 million in other-than-temporary credit impairments on two non-Agency RMBS where the future expected cash flows for the security were less than its amortized cost.
The following table presents the changes in OTTI included in earnings for the three and nine months ended September 30, 2016 and 2015:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| (in thousands) | 2016 | 2015 | 2016 | 2015 |
| Cumulative credit loss at beginning of period | $(6,710) | $(6,622) | $(6,499) | $(8,241) |
| Additions: | | | | |
| Other-than-temporary impairments not previously recognized | (1,015) | (238) | (1,307) | (238) |
| Increases related to other-than-temporary impairments on securities with previously recognized other-than-temporary impairments | — | — | (515) | (297) |
| Reductions: | | | | |
| Decreases related to other-than-temporary impairments on securities paid down | — | — | — | — |
| Decreases related to other-than-temporary impairments on securities sold | — | 361 | 596 | 2,277 |
| Cumulative credit loss at end of period | $(7,725) | $(6,499) | $(7,725) | $(6,499) |

Cumulative credit losses related to OTTI may be reduced for securities sold as well as for securities that mature, are paid down, or are prepaid such that the outstanding principal balance is reduced to zero. Additionally, increases in cash flows expected to be collected over the remaining life of the security cause a reduction in the cumulative credit loss.
Gross Realized Gains and Losses
Gains and losses from the sale of AFS securities are recorded as realized gains (losses) within gain on investment securities in the Company’s condensed consolidated statements of comprehensive income (loss). For the three and nine months ended September 30, 2016, the Company sold AFS securities for $2.8 billion and $6.6 billion with an amortized cost of $2.8 billion and $6.5 billion for net realized gains of $31.8 million and $63.3 million, respectively. For the three and nine months ended September 30, 2015, the Company sold AFS securities for $1.1 billion and $3.7 billion with an amortized cost of $1.0 billion and $3.4 billion for net realized gains of $66.5 million and $259.8 million, respectively.
The following table presents the gross realized gains and losses on sales of AFS securities for the three and nine months ended September 30, 2016 and 2015:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| (in thousands) | 2016 | 2015 | 2016 | 2015 |
| Gross realized gains | $31,942 | $75,427 | $77,836 | $269,314 |

| | | | | |
|---|---|---|---|---|
| Gross realized losses | (164 ) | (8,955 ) | (14,487 ) | (9,511 ) |
| Total realized gains on sales, net | $31,778 | $66,472 | $63,349 | $259,803 |

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Note 5. Residential Mortgage Loans Held-for-Sale, at Fair Value

Residential mortgage loans held-for-sale consists of residential mortgage loans carried at fair value as a result of a fair value option election. The following table presents the carrying value of the Company's residential mortgage loans held-for-sale as of September 30, 2016 and December 31, 2015:

| (in thousands) | September 30, 2016 | December 31, 2015 |
| --- | --- | --- |
| Unpaid principal balance | $ 720,609 | $ 812,661 |
| Fair value adjustment | 2,565 | (1,230 ) |
| Carrying value | $ 723,174 | $ 811,431 |

At September 30, 2016 and December 31, 2015, the Company pledged residential mortgage loans with a carrying value of $632.7 million and $745.5 million, respectively, as collateral for repurchase agreements and FHLB advances. See Note 15 - Repurchase Agreements and Note 17 - Federal Home Loan Bank of Des Moines Advances.

Note 6. Residential Mortgage Loans Held-for-Investment in Securitization Trusts, at Fair Value

The Company purchases subordinated debt and excess servicing rights from securitization trusts sponsored by either third parties or the Company's subsidiaries. The underlying residential mortgage loans held by the trusts, which are consolidated on the Company's condensed consolidated balance sheets, are classified as residential mortgage loans held-for-investment in securitization trusts and carried at fair value as a result of a fair value option election. See Note 3 - Variable Interest Entities for additional information regarding consolidation of the securitization trusts. The following table presents the carrying value of the Company's residential mortgage loans held-for-investment in securitization trusts as of September 30, 2016 and December 31, 2015:

| (in thousands) | September 30, 2016 | December 31, 2015 |
| --- | --- | --- |
| Unpaid principal balance | $ 3,499,285 | $ 3,143,515 |
| Fair value adjustment | 120,752 | 30,212 |
| Carrying value | $ 3,620,037 | $ 3,173,727 |

Note 7. Commercial Real Estate Assets

The Company originates and purchases commercial real estate debt and related instruments generally to be held as long-term investments. These assets are classified as commercial real estate assets on the condensed consolidated balance sheets. Additionally, the Company is the sole certificate holder of a trust entity that holds a commercial real estate loan. The underlying loan held by the trust is consolidated on the Company's condensed consolidated balance sheet and classified as commercial real estate assets. See Note 3 - Variable Interest Entities for additional information regarding consolidation of the trust. Commercial real estate assets are reported at cost, net of any unamortized acquisition premiums or discounts, loan fees and origination costs as applicable, unless the assets are deemed impaired.

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The following tables summarize the Company's commercial real estate assets by asset type, property type and geographic location as of September 30, 2016 and December 31, 2015:

| (in thousands) | September 30, 2016 | | | December 31, 2015 | | |
|---|---|---|---|---|---|---|
| | Mezzanine Loans | First Mortgages | Total | Mezzanine Loans | First Mortgages | Total |
| Unpaid principal balance | $139,334 | $983,463 | $1,122,797 | $153,913 | $513,433 | $667,346 |
| Unamortized (discount) premium | (42) | (190) | (232) | (237) | — | (237) |
| Unamortized net deferred origination fees | (380) | (7,637) | (8,017) | (830) | (5,326) | (6,156) |
| Carrying value | $138,912 | $975,636 | $1,114,548 | $152,846 | $508,107 | $660,953 |
| Unfunded commitments | $1,580 | $93,761 | $95,341 | $1,900 | $50,334 | $52,234 |
| Number of loans | 6 | 22 | 28 | 6 | 12 | 18 |
| Weighted average coupon | 8.4 % | 4.9 % | 5.3 % | 8.1 % | 4.5 % | 5.4 % |
| Weighted average years to maturity [1] | 1.8 | 3.1 | 2.9 | 2.6 | 3.3 | 3.1 |

(1) Based on contractual maturity date. Certain loans are subject to contractual extension options which may be subject to conditions as stipulated in the loan agreement. Actual maturities may differ from contractual maturities stated herein as certain borrowers may have the right to prepay with or without paying a prepayment penalty. The Company may also extend contractual maturities in connection with loan modifications.

| (in thousands) | September 30, 2016 | | December 31, 2015 | |
|---|---|---|---|---|
| Property Type | Carrying Value | % of Commercial Portfolio | Carrying Value | % of Commercial Portfolio |
| Retail | $237,007 | 21.3 % | $185,883 | 28.1 % |
| Hotel | 85,520 | 7.7 % | 80,843 | 12.2 % |
| Industrial | 104,929 | 9.4 % | — | — % |
| Multifamily | 208,265 | 18.7 % | 139,011 | 21.1 % |
| Office | 478,827 | 42.9 % | 255,216 | 38.6 % |
| Total | $1,114,548 | 100.0 % | $660,953 | 100.0 % |

| (in thousands) | September 30, 2016 | | December 31, 2015 | |
|---|---|---|---|---|
| Geographic Location | Carrying Value | % of Commercial Portfolio | Carrying Value | % of Commercial Portfolio |
| West | $180,943 | 16.2 % | $131,488 | 19.9 % |
| Southeast | 104,688 | 9.4 % | 79,118 | 12.0 % |
| Southwest | 266,238 | 23.9 % | 161,721 | 24.4 % |
| Northeast | 491,503 | 44.1 % | 238,913 | 36.2 % |
| Midwest | 71,176 | 6.4 % | 49,713 | 7.5 % |
| Total | $1,114,548 | 100.0 % | $660,953 | 100.0 % |

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At September 30, 2016 and December 31, 2015, the Company pledged commercial real estate assets with a carrying value of $997.2 million and $361.1 million, respectively, as collateral for repurchase agreements and FHLB advances. See Note 15 - Repurchase Agreements and Note 17 - Federal Home Loan Bank of Des Moines Advances.
The following table summarizes activity related to commercial real estate assets for the three and nine months ended September 30, 2016 and 2015.

| (in thousands) | Three Months Ended September 30, 2016 | 2015 | Nine Months Ended September 30, 2016 | 2015 |
|---|---|---|---|---|
| Balance at beginning of period | $926,377 | $45,605 | $660,953 | $— |
| Originations and purchases | 190,100 | 246,644 | 470,547 | 292,200 |
| Repayments | (908) | — | (15,295) | — |
| Net discount accretion (premium amortization) | 64 | 49 | 204 | 98 |
| (Increase) decrease in net deferred origination fees | (2,858) | (1,517) | (6,867) | (1,517) |
| Amortization of net deferred origination fees | 1,773 | 129 | 5,006 | 129 |
| Allowance for loan losses | — | — | — | — |
| Balance at end of period | $1,114,548 | $290,910 | $1,114,548 | $290,910 |

The Company evaluates each loan for impairment at least quarterly by assessing the risk factors of each loan and assigning a risk rating based on a variety of factors. Risk factors include property type, geographic and local market dynamics, physical condition, leasing and tenant profile, projected cash flow, loan structure and exit plan, loan-to-value ratio, project sponsorship, and other factors deemed necessary. Risk ratings are defined as follows:

1 – Lower Risk
2 – Average Risk
3 – Acceptable Risk
4 – Higher Risk: A loan that has exhibited material deterioration in cash flows and/or other credit factors, which, if negative trends continue, could be indicative of future loss.
5 – Impaired/Loss Likely: A loan that has a significantly increased probability of default or principal loss.

The following table presents the number of loans, unpaid principal balance and carrying value (amortized cost) by risk rating for commercial real estate assets as of September 30, 2016 and December 31, 2015:

| (dollars in thousands) | September 30, 2016 | | | December 31, 2015 | | |
|---|---|---|---|---|---|---|
| Risk Rating | Number of Loans | Unpaid Principal Balance | Carrying Value | Number of Loans | Unpaid Principal Balance | Carrying Value |
| 1 – 3 | 28 | $1,122,797 | $1,114,548 | 18 | $667,346 | $660,953 |
| 4 – 5 | — | — | — | — | — | — |
| Total | 28 | $1,122,797 | $1,114,548 | 18 | $667,346 | $660,953 |

The Company has not recorded any allowances for losses as no loans are past-due and it is not deemed probable that the Company will not be able to collect all amounts due pursuant to the contractual terms of the loans.

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Note 8. Servicing Activities
Mortgage Servicing Rights, at Fair Value
One of the Company's wholly owned subsidiaries has approvals from Fannie Mae, Freddie Mac, and Ginnie Mae to own and manage MSR, which represent the right to control the servicing of mortgage loans. The Company and its subsidiaries do not originate or directly service mortgage loans, and instead contract with fully licensed subservicers to handle substantially all servicing functions for the loans underlying the Company's MSR. The following table summarizes activity related to MSR for the three and nine months ended September 30, 2016 and 2015.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| (in thousands) | 2016 | 2015 | 2016 | 2015 |
| Balance at beginning of period | $427,813 | $437,576 | $493,688 | $452,006 |
| Additions from purchases of servicing rights | 98,224 | 67,175 | 204,435 | 75,709 |
| Additions from sales of residential mortgage loans | 242 | 752 | 764 | 1,568 |
| Subtractions from sales of servicing rights | (60,910) | — | (60,910) | — |
| Changes in fair value due to: | | | | |
| Changes in valuation inputs or assumptions used in the valuation model | 3,846 | (49,449) | (139,587) | (63,573) |
| Other changes in fair value [1] | (18,231) | (12,100) | (52,773) | (32,744) |
| Other changes [2] | 4,645 | 3,391 | 10,012 | 14,379 |
| Balance at end of period | $455,629 | $447,345 | $455,629 | $447,345 |

(1) Other changes in fair value primarily represents changes due to the realization of expected cash flows.
(2) Other changes includes purchase price adjustments, contractual prepayment protection, and changes due to the Company's purchase of the underlying collateral.

At September 30, 2016, the Company pledged MSR with a carrying value of $73.5 million as collateral for revolving credit facilities. See Note 18 - Revolving Credit Facilities. The Company did not have any revolving credit facilities in place, and, thus, had not pledged any MSR as collateral, at December 31, 2015.
As of September 30, 2016 and December 31, 2015, the key economic assumptions and sensitivity of the fair value of MSR to immediate 10% and 20% adverse changes in these assumptions were as follows:

| (in thousands) | September 30, 2016 | December 31, 2015 |
|---|---|---|
| Weighted average prepayment speed: | 15.8 % | 11.8 % |
| Impact on fair value of 10% adverse change | $ (25,310) | $ (20,093) |
| Impact on fair value of 20% adverse change | $ (48,388) | $ (38,656) |
| Weighted average delinquency: | 2.1 % | 4.0 % |
| Impact on fair value of 10% adverse change | $ (1,549) | $ (3,826) |
| Impact on fair value of 20% adverse change | $ (4,237) | $ (6,640) |
| Weighted average discount rate: | 9.0 % | 10.1 % |
| Impact on fair value of 10% adverse change | $ (11,937) | $ (16,316) |
| Impact on fair value of 20% adverse change | $ (23,100) | $ (31,522) |

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These assumptions and sensitivities are hypothetical and should be considered with caution. Changes in fair value based on 10% and 20% variations in assumptions generally cannot be extrapolated because the relationship of the change in assumptions to the change in fair value may not be linear. Also, the effect of a variation in a particular assumption on the fair value of MSR is calculated without changing any other assumptions. In reality, changes in one factor may result in changes in another (e.g., increased market interest rates may result in lower prepayments and increased credit losses) that could magnify or counteract the sensitivities. Further, these sensitivities show only the change in the asset balances and do not show any expected change in the fair value of the instruments used to manage the interest rates and prepayment risks associated with these assets.

Risk Mitigation Activities

The primary risk associated with the Company’s MSR is interest rate risk and the resulting impact on prepayments. A significant decline in interest rates could lead to higher-than-expected prepayments that could reduce the value of the MSR. The Company economically hedges the impact of these risks with AFS securities and derivative financial instruments. Refer to Note 11 - Derivative Instruments and Hedging Activities for additional information regarding the derivative financial instruments used to economically hedge MSR.

Mortgage Servicing Income

The following table presents the components of servicing income recorded on the Company’s condensed consolidated statements of comprehensive income (loss) for the three and nine months ended September 30, 2016 and 2015:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| (in thousands) | 2016 | 2015 | 2016 | 2015 |
| Servicing fee income | $37,226 | $31,073 | $104,765 | $91,896 |
| Ancillary fee income | 449 | 535 | 1,423 | 1,650 |
| Float income | 1,033 | 402 | 2,469 | 1,067 |
| Total | $38,708 | $32,010 | $108,657 | $94,613 |

Mortgage Servicing Advances

In connection with the servicing of loans, the Company’s subservicers make certain payments for property taxes and insurance premiums, default and property maintenance payments, as well as advances of principal and interest payments before collecting them from individual borrowers. Servicing advances, including contractual interest, are priority cash flows in the event of a loan principal reduction or foreclosure and ultimate liquidation of the real estate-owned property, thus making their collection reasonably assured. These servicing advances, which are funded by the Company, totaled $46.5 million and $37.5 million and were included in other assets on the condensed consolidated balance sheets as of September 30, 2016 and December 31, 2015, respectively.

Serviced Mortgage Assets

The Company’s total serviced mortgage assets consist of loans owned and classified as residential mortgage loans held-for-sale, loans held in consolidated VIEs classified as residential mortgage loans held-for-investment in securitization trusts, and loans underlying MSR. The following table presents the number of loans and unpaid principal balance of the mortgage assets for which the Company manages the servicing as of September 30, 2016 and December 31, 2015:

| | September 30, 2016 | | December 31, 2015 | |
|---|---|---|---|---|
| (dollars in thousands) | Number of Loans | Unpaid Principal Balance | Number of Loans | Unpaid Principal Balance |
| Residential mortgage loans held-for-sale | 1,439 | $720,609 | 1,415 | $812,661 |
| Residential mortgage loans held-for-investment in securitization trusts | 4,938 | 3,499,285 | 4,329 | 3,117,219 |

| | | | | |
|---|---|---|---|---|
| Mortgage servicing rights | 249,032 | 55,080,859 | 241,228 | 48,566,301 |
| Total serviced mortgage assets | 255,409 | $59,300,753 | 246,972 | $52,496,181 |

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Note 9. Restricted Cash
The Company is required to maintain certain cash balances with counterparties for securities and derivatives trading activity and collateral for the Company's repurchase agreements and FHLB advances in restricted accounts. The Company has also placed cash in a restricted account pursuant to a letter of credit on an office space lease.
The following table presents the Company's restricted cash balances as of September 30, 2016 and December 31, 2015:

| (in thousands) | September 30, 2016 | December 31, 2015 |
|---|---|---|
| Restricted cash balances held by trading counterparties: | | |
| For securities and loan trading activity | $ 20,810 | $ 12,550 |
| For derivatives trading activity | 148,492 | 130,355 |
| As restricted collateral for repurchase agreements and Federal Home Loan Bank advances | 95,223 | 119,310 |
| Total restricted cash balances held by trading counterparties | 264,525 | 262,215 |
| Restricted cash balance pursuant to letter of credit on office lease | 347 | 347 |
| Total | $ 264,872 | $ 262,562 |

Note 10. Accrued Interest Receivable
The following table presents the Company's accrued interest receivable by collateral type as of September 30, 2016 and December 31, 2015:

| (in thousands) | September 30, 2016 | December 31, 2015 |
|---|---|---|
| Available-for-sale securities: | | |
| Agency | | |
| Federal Home Loan Mortgage Corporation | $ 6,421 | $ 6,235 |
| Federal National Mortgage Association | 28,727 | 12,407 |
| Government National Mortgage Association | 3,007 | 4,910 |
| Non-Agency | 2,481 | 2,339 |
| Total available-for-sale securities | 40,636 | 25,891 |
| Residential mortgage loans held-for-sale | 3,377 | 4,173 |
| Residential mortgage loans held-for-investment in securitization trusts | 20,318 | 18,339 |
| Commercial real estate assets | 2,758 | 1,567 |
| Total | $ 67,089 | $ 49,970 |

Note 11. Derivative Instruments and Hedging Activities
The Company enters into a variety of derivative and non-derivative instruments in connection with its risk management activities. The Company's primary objective for executing these derivative and non-derivative instruments is to mitigate the Company's economic exposure to future events that are outside its control. The Company's derivative financial instruments are utilized principally to manage market risk and cash flow volatility associated with interest rate risk (including associated prepayment risk) related to certain assets and liabilities. As part of its risk management activities, the Company may, at times, enter into various forward contracts, including short securities, Agency to-be-announced securities, or TBAs, options, futures, swaps, caps, credit default swaps and total return swaps. In executing on the Company's current risk management strategy, the Company has entered into interest rate swap and swaption agreements, TBAs, short U.S. Treasuries, put and call options for TBAs and U.S. Treasuries, constant maturity swaps, credit default swaps and total return swaps (based on the Markit IOS Index). The Company has also entered into a number of non-derivative instruments to manage interest rate risk, principally Agency

interest-only securities.

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The following summarizes the Company's significant asset and liability classes, the risk exposure for these classes, and the Company's risk management activities used to mitigate certain of these risks. The discussion includes both derivative and non-derivative instruments used as part of these risk management activities. Any of the Company's derivative and non-derivative instruments may be entered into in conjunction with one another in order to mitigate risks associated with the Company's investment portfolio. As a result, the following discussions of each type of instrument should be read as a collective representation of the Company's risk mitigation efforts and should not be considered independent of one another. While the Company uses derivative and non-derivative instruments to achieve the Company's risk management activities, it is possible that these instruments will not effectively mitigate all or a substantial portion of the Company's market rate risk. In addition, the Company might elect, at times, not to enter into certain hedging arrangements in order to maintain compliance with REIT requirements.

Balance Sheet Presentation

In accordance with ASC 815, Derivatives and Hedging, or ASC 815, the Company records derivative financial instruments on its condensed consolidated balance sheets as assets or liabilities at fair value. Changes in fair value are accounted for depending on the use of the derivative instruments and whether they qualify for hedge accounting treatment. Due to the volatility of the credit markets and difficulty in effectively matching pricing or cash flows, the Company has elected to treat all current derivative contracts as trading instruments.

The following tables present the gross fair value and notional amounts of the Company's derivative financial instruments treated as trading instruments as of September 30, 2016 and December 31, 2015.

| (in thousands) | September 30, 2016 | | | |
|---|---|---|---|---|
| | Derivative Assets | | Derivative Liabilities | |
| Trading instruments | Fair Value | Notional | Fair Value | Notional |
| Inverse interest-only securities | $142,597 | $784,823 | $— | $— |
| Interest rate swap agreements | 36,306 | 10,338,367 | (27,048) | 6,607,063 |
| Credit default swaps | — | — | (52) | 25,000 |
| Swaptions, net | 95 | 600,000 | (3,001) | 330,000 |
| TBAs | 17,527 | 1,040,000 | (4,340) | 1,629,000 |
| Put and call options for TBAs, net | 2,178 | 3,950,000 | (4,685) | 519,000 |
| Markit IOS total return swaps | — | — | (752) | 96,248 |
| Forward purchase commitments | 310 | 46,134 | (40) | 15,269 |
| Total | $199,013 | $16,759,324 | $(39,918) | $9,221,580 |

| (in thousands) | December 31, 2015 | | | |
|---|---|---|---|---|
| | Derivative Assets | | Derivative Liabilities | |
| Trading instruments | Fair Value | Notional | Fair Value | Notional |
| Inverse interest-only securities | $159,582 | $932,037 | $— | $— |
| Interest rate swap agreements | 91,757 | 14,268,806 | — | — |
| Credit default swaps | — | — | (703) | 125,000 |
| Swaptions, net | 17,374 | 4,700,000 | (4,831) | 500,000 |
| TBAs | 1,074 | 847,000 | (1,324) | 550,000 |
| Markit IOS total return swaps | 1,645 | 889,418 | — | — |
| Forward purchase commitments | 77 | 98,736 | (427) | 187,384 |
| Total | $271,509 | $21,735,997 | $(7,285) | $1,362,384 |

Comprehensive Income (Loss) Statement Presentation

The Company has not applied hedge accounting to its current derivative portfolio held to mitigate the interest rate risk and credit risk associated with its portfolio. As a result, the Company is subject to volatility in its earnings due to movement in the unrealized gains and losses associated with its interest rate swaps and its other derivative instruments.

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The following table summarizes the location and amount of gains and losses on derivative instruments reported in the condensed consolidated statements of comprehensive income (loss):

| Trading Instruments | Location of Gain (Loss) Recognized in Income on Derivatives | Amount of Gain (Loss) Recognized in Income on Derivatives | | | |
|---|---|---|---|---|---|
| (in thousands) | | Three Months Ended September 30, | | Nine Months Ended September 30, | |
| | | 2016 | 2015 | 2016 | 2015 |
| Interest rate risk management | | | | | |
| TBAs [1] | Loss on other derivative instruments | $(522) | $(2,982) | $26,369 | $(25,677) |
| Short U.S. Treasuries [1] | Loss on other derivative instruments | — | — | — | 125 |
| Put and call options for TBAs [1] | Loss on other derivative instruments | (6,226) | (1,358) | (51,259) | 6,848 |
| Put and call options for U.S. Treasuries [1] | Loss on other derivative instruments | — | — | — | (837) |
| Constant maturity swaps [1] | Loss on other derivative instruments | — | — | — | 6,164 |
| Interest rate swap agreements - Receivers [1] | Gain (loss) on interest rate swap and swaption agreements | (18,381) | 86,672 | 131,465 | 86,528 |
| Interest rate swap agreements - Payers [1] | Gain (loss) on interest rate swap and swaption agreements | 22,973 | (70,546) | (89,043) | (102,392) |
| Swaptions [1] | Gain (loss) on interest rate swap and swaption agreements | (24,394) | (66,809) | (18,397) | (65,563) |
| Markit IOS total return swaps [1] | Loss on other derivative instruments | (6,550) | (5,966) | (41,541) | (23,492) |
| Interest rate swap agreements - Payers [2] | Gain (loss) on interest rate swap and swaption agreements | 25,386 | (120,973) | (156,633) | (171,720) |
| Credit risk management | | | | | |
| Credit default swaps - Receive protection [3] | Loss on other derivative instruments | (18) | (75) | 364 | (199) |
| Non-risk management | | | | | |
| Inverse interest-only securities | Loss on other derivative instruments | 1,288 | 9,926 | 22,003 | 34,096 |
| Forward purchase commitments | (Loss) gain on residential mortgage loans held-for-sale | 107 | 2,834 | 2,455 | (1,327) |
| Total | | $(6,337) | $(169,277) | $(174,217) | $(257,446) |

(1) Includes derivative instruments held to mitigate interest rate risk associated with the Company’s investment portfolio.
(2) Includes derivative instruments held to mitigate interest rate risk associated with the Company’s repurchase agreements and FHLB advances.
(3) Includes derivative instruments held to mitigate credit risk associated with the Company’s non-Agency RMBS and residential mortgage loans held-for-sale.

For the three and nine months ended September 30, 2016, the Company recognized $4.3 million and $18.1 million, respectively, of expenses for the accrual and/or settlement of the net interest expense associated with its interest rate swaps. The expenses result from paying either a fixed interest rate or LIBOR interest on an average $14.5 billion and $14.8 billion notional, respectively, and receiving either LIBOR interest or a fixed interest rate. For the three and nine

months ended September 30, 2015, the Company recognized $19.4 million and $73.1 million, respectively, of expenses for the accrual and/or settlement of the net interest expense associated with its interest rate swaps. The expenses result from paying either a fixed interest rate or LIBOR interest on an average $15.4 billion and $16.8 billion notional, respectively, and receiving either LIBOR interest or a fixed interest rate.

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The following tables present information with respect to the volume of activity in the Company's derivative instruments during the three and nine months ended September 30, 2016 and 2015:

| | Three Months Ended September 30, 2016 | | | | | |
|---|---|---|---|---|---|---|
| (in thousands) | Beginning of Period Notional Amount | Additions | Settlement, Termination, Expiration or Exercise | End of Period Notional Amount | Average Notional Amount | Realized Gain (Loss), net [1] |
| Inverse interest-only securities | $834,866 | $— | $(50,043) | $784,823 | $813,045 | $— |
| Interest rate swap agreements | 13,697,000 | 4,451,430 | (1,203,000) | 16,945,430 | 14,497,913 | (39,369) |
| Credit default swaps | 25,000 | — | — | 25,000 | 25,000 | — |
| Swaptions, net | 1,800,000 | (1,537,000) | 7,000 | 270,000 | 219,315 | (55,692) |
| TBAs, net | (337,000) | (5,622,000) | 5,370,000 | (589,000) | (1,051,989) | (18,819) |
| Put and call options for TBAs, net | 8,897,000 | 2,269,000 | (6,697,000) | 4,469,000 | 5,607,728 | (26,955) |
| Markit IOS total return swaps | 588,037 | 99,911 | (591,700) | 96,248 | 113,334 | (13,897) |
| Forward purchase commitments | 636,467 | 315,787 | (890,851) | 61,403 | 418,333 | 577 |
| Total | $26,141,370 | $(22,872) | $(4,055,594) | $22,062,904 | $20,642,679 | $(154,155) |

| | Three Months Ended September 30, 2015 | | | | | |
|---|---|---|---|---|---|---|
| (in thousands) | Beginning of Period Notional Amount | Additions | Settlement, Termination, Expiration or Exercise | End of Period Notional Amount | Average Notional Amount | Realized Gain (Loss), net [1] |
| Inverse interest-only securities | $1,049,743 | $— | $(63,842) | $985,901 | $1,020,199 | $— |
| Interest rate swap agreements | 16,225,523 | 5,280,000 | (7,480,000) | 14,025,523 | 15,371,175 | (24,948) |
| Credit default swaps | 125,000 | — | — | 125,000 | 125,000 | — |
| Swaptions, net | 9,410,000 | — | 600,000 | 10,010,000 | 9,481,739 | (36,960) |
| TBAs, net | (1,024,000) | (468,000) | 2,274,000 | 782,000 | (343,272) | (13,615) |
| Short U.S. Treasuries | — | — | — | — | — | — |
| Put and call options for TBAs, net | — | 1,000,000 | — | 1,000,000 | 163,043 | — |
| Put and call options for U.S. Treasuries, net | — | — | — | — | — | — |
| Constant maturity swaps | — | — | — | — | — | — |
| Markit IOS total return swaps | 988,409 | 176,807 | (277,252) | 887,964 | 828,323 | (2,368) |
| Forward purchase commitments | 626,660 | 941,480 | (1,066,948) | 501,192 | 576,251 | (392) |
| Total | $27,401,335 | $6,930,287 | $(6,014,042) | $28,317,580 | $27,222,458 | $(78,283) |

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| | Nine Months Ended September 30, 2016 | | | | | |
|---|---|---|---|---|---|---|
| (in thousands) | Beginning of Period Notional Amount | Additions | Settlement, Termination, Expiration or Exercise | End of Period Notional Amount | Average Notional Amount | Realized Gain (Loss), net (1) |
| Inverse interest-only securities | $932,037 | $— | $(147,214) | $784,823 | $860,920 | $— |
| Interest rate swap agreements | 14,268,806 | 16,553,456 | (13,876,832) | 16,945,430 | 14,751,923 | (33,067) |
| Credit default swaps | 125,000 | 10,000 | (110,000) | 25,000 | 87,883 | 412 |
| Swaptions, net | 5,200,000 | 1,063,000 | (5,993,000) | 270,000 | 3,192,617 | (86,481) |
| TBAs, net | 297,000 | (1,186,000) | 300,000 | (589,000) | (239,493) | 12,932 |
| Put and call options for TBAs, net | — | 13,166,000 | (8,697,000) | 4,469,000 | 3,091,679 | (28,303) |
| Markit IOS total return swaps | 889,418 | 99,911 | (893,081) | 96,248 | 598,163 | (13,374) |
| Forward purchase commitments | 286,120 | 1,548,027 | (1,772,744) | 61,403 | 357,448 | 1,835 |
| Total | $21,998,381 | $31,254,394 | $(31,189,871) | $22,062,904 | $22,701,140 | $(146,046) |

| | Nine Months Ended September 30, 2015 | | | | | |
|---|---|---|---|---|---|---|
| (in thousands) | Beginning of Period Notional Amount | Additions | Settlement, Termination, Expiration or Exercise | End of Period Notional Amount | Average Notional Amount | Realized Gain (Loss), net (1) |
| Inverse interest-only securities | $1,168,226 | $12,563 | $(194,888) | $985,901 | $1,081,376 | $64 |
| Interest rate swap agreements | 18,584,000 | 22,393,227 | (26,951,704) | 14,025,523 | 16,753,347 | (92,816) |
| Credit default swaps | 125,000 | — | — | 125,000 | 125,000 | — |
| Swaptions, net | 12,410,000 | 7,050,000 | (9,450,000) | 10,010,000 | 10,862,930 | (32,168) |
| TBAs, net | (1,325,000) | (11,330,000) | 13,437,000 | 782,000 | (729,916) | (38,461) |
| Short U.S. Treasuries | — | (50,000) | 50,000 | — | — | 125 |
| Put and call options for TBAs, net | 2,000,000 | 1,250,000 | (2,250,000) | 1,000,000 | (183,150) | 7,796 |
| Put and call options for U.S. Treasuries, net | — | 500,000 | (500,000) | — | 916 | (837) |
| Constant maturity swaps | 14,000,000 | 6,000,000 | (20,000,000) | — | 3,018,315 | 7,694 |
| Markit IOS total return swaps | 598,459 | 1,601,350 | (1,311,845) | 887,964 | 968,223 | (11,296) |
| Forward purchase commitments | 554,838 | 3,048,411 | (3,102,057) | 501,192 | 634,356 | (766) |
| Total | $48,115,523 | $30,475,551 | $(50,273,494) | $28,317,580 | $32,531,397 | $(160,665) |

(1) Excludes net interest paid or received in full settlement of the net interest spread liability.

Cash flow activity related to derivative instruments is reflected within the operating activities and investing activities sections of the condensed consolidated statements of cash flows. Derivative fair value adjustments are reflected within the unrealized (gain) loss on interest rate swaps and swaptions, unrealized loss (gain) on other derivative instruments, and gain on residential mortgage loans held-for-sale line items within the operating activities section of the condensed consolidated statements of cash flows. Realized gains and losses on interest rate swap and swaption agreements are reflected within the loss on termination and option expiration of interest rate swaps and swaptions line item within the operating activities section of the condensed consolidated statements of cash flows. The remaining cash flow activity related to derivative instruments is reflected within the (purchases) short sales of other derivative instruments, proceeds from sales (payments for termination) of other derivative instruments, net and increase (decrease) in due to

counterparties, net line items within the investing activities section of the condensed consolidated statements of cash flows.



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Interest Rate Sensitive Assets/Liabilities
The Company's RMBS investment securities and MSR are generally subject to change in value when mortgage rates decline or increase, depending on the type of investment. Rising mortgage rates generally result in a slowing of refinancing activity, which slows prepayments and results in a decline in the value of the Company's fixed-rate Agency pools and an increase in the value of the Company's MSR. To mitigate the impact of this risk, the Company maintains a portfolio of fixed-rate interest-only securities, which increase in value when interest rates increase, as well as TBA positions, short U.S. Treasuries, put and call options for TBAs and U.S. Treasuries, constant maturity swaps, interest rate swap and swaption agreements and Markit IOS total return swaps to further mitigate its exposure to higher interest rates, decreased prepayment speeds and widening mortgage spreads.
As of September 30, 2016 and December 31, 2015, the Company had outstanding fair value of $50.1 million and $42.9 million, respectively, of interest-only securities in place to economically hedge its investment securities. These interest-only securities are included in AFS securities, at fair value, in the condensed consolidated balance sheets.
The Company is exposed to interest rate risk on residential mortgage loans from the time it commits to purchase a mortgage loan until it acquires the loan from the originator and subsequently sells the loan to a third party. Changes in interest rates impact the market price for the mortgage loans. For example, as market interest rates decline, the value of residential mortgage loans held-for-sale increases, and vice versa. To mitigate the impact of this risk, the Company may enter into derivative contracts to hedge the interest rate risk related to its commitments to purchase residential mortgage loans and residential mortgage loans held-for-sale, such as interest rate swaps, swaptions, TBA positions, short U.S. Treasuries, put and call options for TBAs and U.S. Treasuries and constant maturity swaps.
TBAs. At times, the Company may use TBAs for risk management purposes or as a means of deploying capital until targeted investments are available and to take advantage of temporary displacements in the marketplace. Additionally, the Company may use TBAs independently, or in conjunction with other derivative and non-derivative instruments, in order to mitigate risks associated with the Company's investment portfolio. TBAs are forward contracts for the purchase (long notional positions) or sale (short notional positions) of Agency RMBS. The issuer, coupon and stated maturity of the Agency RMBS are predetermined as well as the trade price, face amount and future settle date (published each month by the Securities Industry and Financial Markets Association). However, the specific Agency RMBS to be delivered upon settlement is not known at the time of the TBA transaction. As a result, and because physical delivery of the Agency RMBS upon settlement cannot be assured, the Company accounts for TBAs as derivative instruments.
As of September 30, 2016, $1.0 billion of the Company's long notional TBA positions and $1.6 billion of the Company's short notional TBA positions were held in order to economically hedge portfolio risk. As of December 31, 2015, $847.0 million of the Company's long notional TBA positions and $550.0 million of the Company's short notional TBA positions were held in order to economically hedge portfolio risk. The Company discloses these positions on a gross basis according to the unrealized gain or loss position of each TBA contract regardless of long or short notional position. The following tables present the notional amount, cost basis, market value and carrying value (which approximates fair value) of the Company's TBA positions as of September 30, 2016 and December 31, 2015:

| | As of September 30, 2016 | | | | |
|---|---|---|---|---|---|
| | | | | Net Carrying Value [4] | |
| (in thousands) | Notional Amount [1] | Cost Basis [2] | Market Value [3] | Derivative Assets | Derivative Liabilities |
| Purchase contracts | $1,040,000 | $1,060,175 | $1,077,702 | $17,527 | $— |
| Sale contracts | (1,629,000 ) | (1,693,953 ) | (1,698,293 ) | — | (4,340 ) |
| TBAs, net | $(589,000 ) | $(633,778 ) | $(620,591 ) | $17,527 | $(4,340 ) |

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| | As of December 31, 2015 | | | | |
|---|---|---|---|---|---|
| | | | | Net Carrying Value (4) | |
| (in thousands) | Notional Amount (1) | Cost Basis (2) | Market Value (3) | Derivative Assets | Derivative Liabilities |
| Purchase contracts | $847,000 | $858,572 | $859,646 | $1,074 | $— |
| Sale contracts | (550,000 ) | (568,813 ) | (570,137 ) | — | (1,324 ) |
| TBAs, net | $297,000 | $289,759 | $289,509 | $1,074 | $(1,324 ) |

(1) Notional amount represents the face amount of the underlying Agency RMBS.
(2) Cost basis represents the forward price to be paid (received) for the underlying Agency RMBS.
(3) Market value represents the current market value of the TBA (or of the underlying Agency RMBS) as of period-end.
(4) Net carrying value represents the difference between the market value of the TBA as of period-end and its cost basis, and is reported in derivative assets / (liabilities), at fair value, in the condensed consolidated balance sheets.

Put and Call Options for TBAs. The Company may use put and call options for TBAs independently, or in conjunction with other derivative and non-derivative instruments, in order to mitigate risks associated with the Company's investment portfolio. As of September 30, 2016, the Company had purchased put options for TBAs with a notional amount of $6.9 billion, short sold call options for TBAs with a notional amount of $2.4 billion and paid upfront premiums of approximately $20.5 million. The last of the options expires in December 2016. The put and call options had a net fair market value of $2.2 million included in derivative assets, at fair value, and $4.7 million included in derivative liabilities, at fair value, on the condensed consolidated balance sheet as of September 30, 2016. The Company did not hold any put and call options for TBAs as of December 31, 2015.
Interest Rate Swap Agreements. The Company may use interest rate swaps independently, or in conjunction with other derivative and non-derivative instruments, in order to mitigate risks associated with the Company's investment portfolio. As of September 30, 2016 and December 31, 2015, the Company held the following interest rate swaps in order to mitigate mortgage interest rate exposure (or duration) risk associated with the Company's investment portfolio whereby the Company receives interest at a three-month LIBOR rate:
(notional in thousands)
September 30, 2016

| Swaps Maturities | Notional Amounts | Weighted Average Fixed Pay Rate | Weighted Average Receive Rate | Weighted Average Maturity (Years) |
|---|---|---|---|---|
| 2018 | $4,669,049 | 1.273 % | 0.853 % | 1.85 |
| 2020 and Thereafter | 1,341,512 | 2.094 % | 0.812 % | 4.88 |
| Total | $6,010,561 | 1.456 % | 0.843 % | 2.53 |

(notional in thousands)
December 31, 2015

| Swaps Maturities | Notional Amounts | Weighted Average Fixed Pay Rate | Weighted Average Receive Rate | Weighted Average Maturity (Years) |
|---|---|---|---|---|

| | | | | | | |
|---|---|---|---|---|---|---|
| 2018 | $2,040,000 | 1.563 | % | 0.487 | % | 2.94 |
| 2020 and Thereafter | 1,210,000 | 2.164 | % | 0.531 | % | 5.08 |
| Total | $3,250,000 | 1.787 | % | 0.503 | % | 3.74 |

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Additionally, as of September 30, 2016 and December 31, 2015, the Company held the following interest rate swaps in order to mitigate mortgage interest rate exposure (or duration) risk associated with the Company's investment portfolio whereby the Company pays interest at a three-month LIBOR rate:
(notional in thousands)
September 30, 2016

| Swaps Maturities | Notional Amounts | Weighted Average Pay Rate | | Weighted Average Fixed Receive Rate | | Weighted Average Maturity (Years) |
|---|---|---|---|---|---|---|
| 2018 | $1,207,294 | 0.729 | % | 1.214 | % | 2.07 |
| 2019 | 500,000 | 0.702 | % | 1.042 | % | 2.31 |
| 2020 and Thereafter | 2,120,512 | 0.783 | % | 2.037 | % | 6.07 |
| Total | $3,827,806 | 0.755 | % | 1.647 | % | 4.32 |

(notional in thousands)
December 31, 2015

| Swaps Maturities | Notional Amounts | Weighted Average Pay Rate | | Weighted Average Fixed Receive Rate | | Weighted Average Maturity (Years) |
|---|---|---|---|---|---|---|
| 2018 | $575,000 | 0.329 | % | 1.440 | % | 2.89 |
| 2020 and Thereafter | 2,589,000 | 0.453 | % | 2.301 | % | 7.00 |
| Total | $3,164,000 | 0.431 | % | 2.145 | % | 6.26 |

The Company monitors its borrowings under repurchase agreements and FHLB advances, which are generally floating rate debt, in relation to the rate profile of its investment securities. When it is cost effective to do so, the Company may enter into interest rate swap arrangements to align the interest rate composition of its borrowings under repurchase agreements and FHLB advances with that of its investment securities and debt portfolios. This particularly applies to borrowing agreements with maturities or interest rate resets of less than six months. Typically, the interest receivable terms (i.e., LIBOR) of the interest rate swaps match the terms of the underlying debt, resulting in an effective conversion of the rate of the related repurchase agreement or FHLB advance from floating to fixed.
As of September 30, 2016 and December 31, 2015, the Company had the following outstanding interest rate swaps that were utilized as economic hedges of interest rate exposure (or duration) associated with the Company's short-term repurchase agreements and FHLB advances:
(notional in thousands)
September 30, 2016

| Swaps Maturities | Notional Amount (1) | Weighted Average Fixed Pay Rate (2) | | Weighted Average Receive Rate (2) | | Weighted Average Maturity (Years) (2) |
|---|---|---|---|---|---|---|
| 2016 | $1,000,000 | 0.435 | % | 0.857 | % | 0.23 |
| 2017 | 2,375,000 | 0.765 | % | 0.787 | % | 0.84 |
| 2018 | 1,300,000 | 1.002 | % | 0.674 | % | 1.85 |
| 2019 | 350,000 | 1.283 | % | 0.731 | % | 2.69 |

| | | | | | | |
|---|---|---|---|---|---|---|
| 2020 and Thereafter | 2,082,063 | 1.733 | % | 0.731 | % | 6.74 |
| Total | $7,107,063 | 0.858 | % | 0.765 | % | 1.48 |

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(notional in thousands)
December 31, 2015

| Swaps Maturities | Notional Amount [1] | Weighted Average Fixed Pay Rate [2] | Weighted Average Receive Rate [2] | Weighted Average Maturity (Years) [2] |
|---|---|---|---|---|
| 2016 | $1,700,000 | 0.462 % | 0.481 % | 0.73 |
| 2017 | 2,375,000 | 0.765 % | 0.510 % | 1.59 |
| 2018 | 800,000 | 0.944 % | 0.384 % | 2.14 |
| 2019 | 350,000 | 1.283 % | 0.340 % | 3.44 |
| 2020 and Thereafter | 2,629,806 | 1.821 % | 0.371 % | 8.04 |
| Total | $7,854,806 | 1.094 % | 0.437 % | 3.71 |

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(1) Notional amount includes $577.1 million in forward starting interest rate swaps as of September 30, 2016. The Company did not have any forward starting interest rate swaps as of December 31, 2015.

(2) Weighted averages exclude forward starting interest rate swaps. As of September 30, 2016, the weighted average fixed pay rate on interest rate swaps starting in March 2017 was 1.8%. The Company did not have any forward starting interest rate swaps as of December 31, 2015.

Interest Rate Swaptions. The Company may use interest rate swaptions (agreements to enter into interest rate swaps in the future for which the Company would either pay or receive a fixed rate) independently, or in conjunction with other derivative and non-derivative instruments, in order to mitigate risks associated with the Company's investment portfolio. As of September 30, 2016 and December 31, 2015, the Company had the following outstanding interest rate swaptions that were utilized as macro-economic hedges:

| (notional and dollars in thousands) | September 30, 2016 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Option | | | | Underlying Swap | | | |
| Swaption | Expiration | Cost | Fair Value | Average Months to Expiration | Notional Amount | Average Pay Rate | Average Receive Rate | Average Term (Years) |
| Purchase contracts: | | | | | | | | |
| Payer | ≥ 6 Months | $43,015 | $145 | 8.84 | $1,800,000 | 3.27 % | 3M Libor | 5.6 |
| Total Payer | | $43,015 | $145 | 8.84 | $1,800,000 | 3.27 % | 3M Libor | 5.6 |
| | | | | | | | | |
| Receiver | < 6 Months | $— | $3,061 | 4.93 | $1,500,000 | 3M Libor | 1.34 % | 3.0 |
| Total Receiver | | $— | $3,061 | 4.93 | $1,500,000 | 3M Libor | 1.34 % | 3.0 |
| | | | | | | | | |
| Sale contracts: | | | | | | | | |
| Payer | < 6 Months | $— | $(5,882) | 4.45 | $(2,230,000) | 1.14 % | 3M Libor | 4.6 |
| Payer | ≥ 6 Months | (81,248) | (230) | 8.99 | (800,000) | 3.44 % | | 10.0 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Total Payer | $(81,248) | $(6,112) | 4.49 | $(3,030,000) | 1.74 % | 3M Libor 3M Libor | 6.0 |

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| (notional and dollars in thousands) | December 31, 2015 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Option | | | | Underlying Swap | | | |
| Swaption | Expiration | Cost | Fair Value | Average Months to Expiration | Notional Amount | Average Fixed Pay Rate | Average Receive Rate | Average Term (Years) |
| Purchase contracts: | | | | | | | | |
| Payer | < 6 Months | $375 | $174 | 0.75 | $2,000,000 | 2.23 % | 3M Libor | 6.3 |
| Payer | ≥ 6 Months | 126,273 | 19,150 | 39.17 | 4,500,000 | 3.69 % | 3M Libor | 5.8 |
| Total Payer | | $126,648 | $19,324 | 38.51 | $6,500,000 | 3.24 % | 3M Libor | 5.9 |
| Sale contracts: | | | | | | | | |
| Payer | ≥ 6 Months | $(81,248) | $(6,738) | 18.01 | $(800,000) | 3.44 % | 3M Libor | 10.0 |
| Total Payer | | $(81,248) | $(6,738) | 18.01 | $(800,000) | 3.44 % | 3M Libor | 10.0 |
| Receiver | < 6 Months | $(100) | $(43) | 0.73 | $(500,000) | 3M Libor | 1.75 % | 10.0 |
| Total Receiver | | $(100) | $(43) | 0.73 | $(500,000) | 3M Libor | 1.75 % | 10.0 |

Markit IOS Total Return Swaps. The Company may use total return swaps (agreements whereby the Company receives or makes payments based on the total return of an underlying instrument or index, such as the Markit IOS Index, in exchange for fixed or floating rate interest payments) independently, or in conjunction with other derivative and non-derivative instruments, in order to mitigate risks associated with the Company's investment portfolio. The Company enters into total return swaps to help mitigate the potential impact of larger increases or decreases in interest rates on the performance of our investment portfolio (referred to as "convexity risk"). Total return swaps based on the Markit IOS Index are intended to synthetically replicate the performance of interest-only securities. The Company had the following total return swap agreements in place at September 30, 2016 and December 31, 2015:

| (notional and dollars in thousands) | | | | |
|---|---|---|---|---|
| September 30, 2016 | | | | |
| Maturity Date | Current Notional Amount | Fair Value | Upfront Payable | Unrealized Gain (Loss) |
| January 12, 2043 | $(47,910) | $(363) | $(320) | $(683) |
| January 12, 2044 | (48,338) | (389) | (366) | (755) |
| Total | $(96,248) | $(752) | $(686) | $(1,438) |

(notional and dollars in thousands)
December 31, 2015

| Maturity Date | Current Notional Amount | Fair Value | Upfront Payable | Unrealized Gain (Loss) |
|---|---|---|---|---|
| January 12, 2043 | $(369,639) | $456 | $(866 ) | $ (410 ) |
| January 12, 2044 | (325,003 ) | 350 | (1,679 ) | (1,329 ) |
| January 12, 2045 | (194,776 ) | 839 | 1,162 | 2,001 |
| Total | $(889,418) | $1,645 | $(1,383) | $ 262 |

Credit Risk

The Company's exposure to credit losses on its Agency RMBS portfolio is limited due to implicit or explicit backing from the GSEs. The payment of principal and interest on the Freddie Mac and Fannie Mae mortgage-backed securities are guaranteed by those respective agencies, and the payment of principal and interest on the Ginnie Mae mortgage-backed securities are backed by the full faith and credit of the U.S. Government.

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Credit Default Swaps. For non-Agency investment securities, residential mortgage loans and commercial real estate assets, the Company may enter into credit default swaps to hedge credit risk. In future periods, the Company could enhance its credit risk protection, enter into further paired derivative positions, including both long and short credit default swaps, and/or seek opportunistic trades in the event of a market disruption (see discussion under "Non-Risk Management Activities" below). The Company also has processes and controls in place to monitor, analyze, manage and mitigate its credit risk with respect to non-Agency RMBS, residential mortgage loans and commercial real estate assets.
As of September 30, 2016 and December 31, 2015, the Company held credit default swaps through which the Company received credit protection for a fixed premium. The maximum payouts for these credit default swaps are limited to the current notional amounts of each swap contract. Maximum payouts for credit default swaps do not represent the expected future cash requirements, as the Company's credit default swaps are typically liquidated or expire and are not exercised by the holder of the credit default swaps.
The following tables present credit default swaps through which the Company is receiving protection held as of September 30, 2016 and December 31, 2015:
(notional and dollars in thousands)
September 30, 2016

| Protection | Maturity Date | Average Implied Credit Spread | Current Notional Amount | Fair Value | Upfront (Payable) Receivable | Unrealized Gain (Loss) |
|---|---|---|---|---|---|---|
| Receive | December 20, 2016 | 496.00 | $(25,000) | $(52) | $(4,062) | $(4,114) |
| | Total | 496.00 | $(25,000) | $(52) | $(4,062) | $(4,114) |

(notional and dollars in thousands)
December 31, 2015

| Protection | Maturity Date | Average Implied Credit Spread | Current Notional Amount | Fair Value | Upfront (Payable) Receivable | Unrealized Gain (Loss) |
|---|---|---|---|---|---|---|
| Receive | June 20, 2016 | 105.50 | $(100,000) | $(502) | $(260) | $(762) |
| | December 20, 2016 | 496.00 | (25,000) | (201) | (4,062) | (4,263) |
| | Total | 183.60 | $(125,000) | $(703) | $(4,322) | $(5,025) |

Derivative financial instruments contain an element of credit risk if counterparties are unable to meet the terms of the agreements. Credit risk associated with derivative financial instruments is measured as the net replacement cost should the counterparties that owe the Company under such contracts completely fail to perform under the terms of these contracts, assuming there are no recoveries of underlying collateral, as measured by the market value of the derivative financial instruments. As of September 30, 2016, the fair value of derivative financial instruments as an asset and liability position was $199.0 million and $39.9 million, respectively.
The Company attempts to mitigate its credit risk exposure on derivative financial instruments by limiting its counterparties to banks and financial institutions that meet established credit guidelines. The Company also seeks to spread its credit risk exposure across multiple counterparties in order to reduce its exposure to any single counterparty. Additionally, the Company reduces credit risk on the majority of its derivative instruments by entering into agreements that permit the closeout and netting of transactions with the same counterparty or clearing agency, in the case of centrally cleared interest rate swaps, upon the occurrence of certain events. To further mitigate the risk of counterparty default, the Company maintains collateral agreements with certain of its counterparties and clearing agencies, which require both parties to maintain cash deposits in the event the fair values of the derivative financial

instruments exceed established thresholds. As of September 30, 2016, the Company had received cash deposits from counterparties of $12.1 million and placed cash deposits of $161.8 million in accounts maintained by counterparties, of which the amounts are netted on a counterparty basis and classified within restricted cash, due from counterparties, or due to counterparties on the Company's condensed consolidated balance sheets.

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Non-Risk Management Activities
The Company has entered into certain financial instruments that are considered derivative contracts under ASC 815 that are not for purposes of hedging. These contracts are currently limited to forward purchase commitments and inverse interest-only RMBS.
Commitments to Purchase Residential Mortgage Loans Held-for-Sale. Prior to a mortgage loan purchase, the Company may enter into forward purchase commitments with counterparties whereby the Company commits to purchasing the loans at a particular interest rate, provided the borrower elects to close the loan. These commitments to purchase mortgage loans have been defined as derivatives and are, therefore, recorded on the Company's condensed consolidated balance sheets as assets or liabilities and measured at fair value. Subsequent changes in fair value are recorded on the Company's condensed consolidated balance sheets as adjustments to the carrying value of these assets or liabilities with a corresponding adjustment recognized in current period earnings. As of September 30, 2016 and December 31, 2015, the Company had outstanding commitments to purchase $61.4 million and $286.1 million of mortgage loans, subject to fallout if the loans do not close, with a fair value asset of $310,294 and a fair value liability of $40,111 at September 30, 2016, and a fair value asset of $77,227 and a fair value liability of $427,468 at December 31, 2015, respectively.
Inverse Interest-Only Securities. As of September 30, 2016 and December 31, 2015, inverse interest-only securities with a carrying value of $142.6 million and $159.6 million, including accrued interest receivable of $1.4 million and $1.7 million, respectively, are accounted for as derivative financial instruments in the condensed consolidated financial statements. The following table presents the amortized cost and carrying value (which approximates fair value) of inverse interest-only securities as of September 30, 2016 and December 31, 2015:

| (in thousands) | September 30, 2016 | December 31, 2015 |
|---|---|---|
| Face Value | $ 784,823 | $ 932,037 |
| Unamortized premium | — | — |
| Unamortized discount | | |
| Designated credit reserve | — | — |
| Net, unamortized | (668,282 ) | (792,178 ) |
| Amortized Cost | 116,541 | 139,859 |
| Gross unrealized gains | 25,420 | 19,655 |
| Gross unrealized losses | (729 ) | (1,608 ) |
| Carrying Value | $ 141,232 | $ 157,906 |

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## Note 12. Other Assets

Other assets as of September 30, 2016 and December 31, 2015 are summarized in the following table:

| (in thousands) | September 30, 2016 | December 31, 2015 |
|---|---|---|
| Property and equipment at cost | $ 6,469 | $ 5,997 |
| Accumulated depreciation [(1)] | (4,264) | (3,303) |
| Net property and equipment | 2,205 | 2,694 |
| Prepaid expenses | 1,142 | 1,572 |
| Income taxes receivable | 1,619 | 5,286 |
| Deferred tax assets, net | 75,075 | 44,318 |
| Servicing advances | 46,464 | 37,499 |
| Federal Home Loan Bank stock | 167,856 | 156,650 |
| Equity investments | 3,000 | 3,000 |
| Other receivables | 29,035 | 20,556 |
| Total other assets | $ 326,396 | $ 271,575 |

(1) Depreciation expense for the three and nine months ended September 30, 2016 was $0.3 million and $1.0 million, respectively.

## Note 13. Other Liabilities

Other liabilities as of September 30, 2016 and December 31, 2015 are summarized in the following table:

| (in thousands) | September 30, 2016 | December 31, 2015 |
|---|---|---|
| Accrued expenses | $ 27,063 | $ 37,052 |
| Accrued interest payable | 29,807 | 18,723 |
| Income taxes payable | — | 70 |
| Other | 23,453 | 16,387 |
| Total other liabilities | $ 80,323 | $ 72,232 |

## Note 14. Fair Value

### Fair Value Measurements

ASC 820, Fair Value Measurements and Disclosures, or ASC 820, defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820 clarifies that fair value should be based on the assumptions market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. The fair value hierarchy gives the highest priority to quoted prices available in active markets (i.e., observable inputs) and the lowest priority to data lacking transparency (i.e., unobservable inputs). Additionally, ASC 820 requires an entity to consider all aspects of nonperformance risk, including the entity’s own credit standing, when measuring fair value of a liability.

ASC 820 establishes a three-level hierarchy to be used when measuring and disclosing fair value. An instrument’s categorization within the fair value hierarchy is based on the lowest level of significant input to its valuation. Following is a description of the three levels:

Level 1 Inputs are quoted prices in active markets for identical assets or liabilities as of the measurement date under current market conditions. Additionally, the entity must have the ability to access the active market and the quoted prices cannot be adjusted by the entity.

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| | |
|---|---|
| Level 2 | Inputs include quoted prices in active markets for similar assets or liabilities; quoted prices in inactive markets for identical or similar assets or liabilities; or inputs that are observable or can be corroborated by observable market data by correlation or other means for substantially the full-term of the assets or liabilities. |
| Level 3 | Unobservable inputs are supported by little or no market activity. The unobservable inputs represent the assumptions that market participants would use to price the assets and liabilities, including risk. Generally, Level 3 assets and liabilities are valued using pricing models, discounted cash flow methodologies, or similar techniques that require significant judgment or estimation. |

Following are descriptions of the valuation methodologies used to measure material assets and liabilities at fair value and details of the valuation models, key inputs to those models and significant assumptions utilized.
Available-for-sale securities. The Company holds a portfolio of AFS securities that are carried at fair value in the condensed consolidated balance sheets and primarily comprised of Agency and non-Agency RMBS. The Company determines the fair value of its Agency RMBS based upon prices obtained from third-party pricing providers or broker quotes received using bid price, which are deemed indicative of market activity. The third-party pricing providers and brokers use pricing models that generally incorporate such factors as coupons, primary and secondary mortgage rates, rate reset period, issuer, prepayment speeds, credit enhancements and expected life of the security. In determining the fair value of its non-Agency RMBS, management judgment may be used to arrive at fair value that considers prices obtained from third-party pricing providers, broker quotes received and other applicable market data. If observable market prices are not available or insufficient to determine fair value due principally to illiquidity in the marketplace, then fair value is based upon internally developed models that are primarily based on observable market-based inputs but also include unobservable market data inputs (including prepayment speeds, delinquency levels, and credit losses). The Company classified 100% of its RMBS AFS securities reported at fair value as Level 2 at September 30, 2016. AFS securities account for 74.1% of all assets reported at fair value at September 30, 2016.
Residential mortgage loans held-for-sale. The Company holds residential mortgage loans held-for-sale that are carried at fair value in the condensed consolidated balance sheets as a result of a fair value option election. The Company determines fair value of its residential mortgage loans based on prices obtained from third-party pricing providers and other applicable market data. If observable market prices are not available or insufficient to determine fair value due principally to illiquidity in the marketplace, then fair value is based upon cash flow models that are primarily based on observable market-based inputs but also include unobservable market data inputs (including prepayment speeds, delinquency levels and credit losses). The Company classified 90.7% and 9.3% of its residential mortgage loans held-for-sale as Level 2 and Level 3 fair value assets, respectively, at September 30, 2016.
Residential mortgage loans held-for-investment in securitization trusts. The Company recognizes on its condensed consolidated balance sheets residential mortgage loans held-for-investment in securitization trusts that are carried at fair value as a result of a fair value option election. An entity is allowed to measure both the financial assets and financial liabilities of a qualifying CFE it consolidates using the fair value of either the CFE’s financial assets or financial liabilities, whichever is more observable. As the Company’s securitization trusts are considered qualifying CFEs, the Company determines the fair value of these residential mortgage loans based on the fair value of its collateralized borrowings in securitization trusts and its retained interests from the Company’s on-balance sheet securitizations (eliminated in consolidation in accordance with U.S. GAAP), as the fair value of these instruments is more observable. The Company classified 100% of its residential mortgage loans held-for-investment in securitization trusts as Level 2 fair value assets at September 30, 2016.
Mortgage servicing rights. The Company holds a portfolio of MSR that are carried at fair value on the condensed consolidated balance sheets. The Company determines fair value of its MSR based on prices obtained from third-party pricing providers. Although MSR transactions are observable in the marketplace, the valuation is based upon cash flow models that include unobservable market data inputs (including prepayment speeds, delinquency levels and discount rates). As a result, the Company classified 100% of its MSR as Level 3 fair value assets at September 30,

2016.

Derivative instruments. The Company may enter into a variety of derivative financial instruments as part of its hedging strategies. The Company principally executes over-the-counter, or OTC, derivative contracts, such as interest rate swaps, swaptions, put and call options for TBAs and U.S. Treasuries, credit default swaps, constant maturity swaps and Markit IOS total return swaps. The Company utilizes third-party pricing providers to value its financial derivative instruments. The Company classified 100% of the interest rate swaps, swaptions, put and call options for TBAs and U.S. Treasuries, credit default swaps, constant maturity swaps and total returns swaps reported at fair value as Level 2 at September 30, 2016.

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The Company may also enter into certain other derivative financial instruments, such as TBAs, short U.S. Treasuries and inverse interest-only securities. These instruments are similar in form to the Company's AFS securities and the Company utilizes a pricing service to value TBAs and broker quotes to value short U.S. Treasuries and inverse interest-only securities. The Company classified 100% of its inverse interest-only securities at fair value as Level 2 at September 30, 2016. The Company reported 100% of its TBAs as Level 1 as of September 30, 2016. The Company did not hold any short U.S. Treasuries at September 30, 2016.

The Company may also enter into forward purchase commitments on residential mortgage loans whereby the Company commits to purchasing the loans at a particular interest rate. The fair value of these derivatives is determined based on prices currently offered in the marketplace for new commitments. Fallout assumptions if the borrower elects not to close the loan are applied to the pricing. As of September 30, 2016, the Company had outstanding commitments to purchase $61.4 million of mortgage loans, subject to fallout if the loans do not close, with a fair value asset of $310,294 and a fair value liability of $40,111. The Company classified 100% of the forward purchase commitments reported at fair value as Level 2 at September 30, 2016.

The Company's risk management committee governs trading activity relating to derivative instruments. The Company's policy is to minimize credit exposure related to financial derivatives used for hedging by limiting the hedge counterparties to major banks, financial institutions, exchanges, and private investors who meet established capital and credit guidelines as well as by limiting the amount of exposure to any individual counterparty.

The Company has netting arrangements in place with all derivative counterparties pursuant to standard documentation developed by ISDA, or central clearing exchange agreements, in the case of centrally cleared interest rate swaps. Additionally, both the Company and the counterparty or clearing agency are required to post cash collateral based upon the net underlying market value of the Company's open positions with the counterparty. Posting of cash collateral typically occurs daily, subject to certain dollar thresholds. Due to the existence of netting arrangements, as well as frequent cash collateral posting at low posting thresholds, credit exposure to the Company and/or to the counterparty or clearing agency is considered materially mitigated. Based on the Company's assessment, there is no requirement for any additional adjustment to derivative valuations specifically for credit.

Collateralized borrowings in securitization trusts. The Company recognizes on its condensed consolidated balance sheets collateralized borrowings that are carried at fair value as a result of a fair value option election. In determining the fair value of its collateralized borrowings, management judgment may be used to arrive at fair value that considers prices obtained from third-party pricing providers, broker quotes received and other applicable market data. If observable market prices are not available or insufficient to determine fair value due principally to illiquidity in the marketplace, then fair value is based upon internally developed models that are primarily based on observable market-based inputs but also include unobservable market data inputs (including prepayment speeds, delinquency levels, and credit losses). The Company classified 100% of its collateralized borrowings in securitization trusts as Level 2 fair value liabilities at September 30, 2016.

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The following tables display the Company’s assets and liabilities measured at fair value on a recurring basis. The Company often economically hedges the fair value change of its assets or liabilities with derivatives and other financial instruments. The tables below display the hedges separately from the hedged items, and therefore do not directly display the impact of the Company’s risk management activities.

| | Recurring Fair Value Measurements At September 30, 2016 | | | |
|---|---|---|---|---|
| (in thousands) | Level 1 | Level 2 | Level 3 | Total |
| Assets | | | | |
| Available-for-sale securities | $— | $14,284,625 | $— | $14,284,625 |
| Residential mortgage loans held-for-sale | — | 655,751 | 67,423 | 723,174 |
| Residential mortgage loans held-for-investment in securitization trusts | — | 3,620,037 | — | 3,620,037 |
| Mortgage servicing rights | — | — | 455,629 | 455,629 |
| Derivative assets | 17,527 | 181,486 | — | 199,013 |
| Total assets | $17,527 | $18,741,899 | $523,052 | $19,282,478 |
| Liabilities | | | | |
| Collateralized borrowings in securitization trusts | $— | $3,375,906 | $— | $3,375,906 |
| Derivative liabilities | 4,340 | 35,578 | — | 39,918 |
| Total liabilities | $4,340 | $3,411,484 | $— | $3,415,824 |

| | Recurring Fair Value Measurements At December 31, 2015 | | | |
|---|---|---|---|---|
| (in thousands) | Level 1 | Level 2 | Level 3 | Total |
| Assets | | | | |
| Available-for-sale securities | $— | $7,825,320 | $— | $7,825,320 |
| Residential mortgage loans held-for-sale | — | 764,319 | 47,112 | 811,431 |
| Residential mortgage loans held-for-investment in securitization trusts | — | 3,173,727 | — | 3,173,727 |
| Mortgage servicing rights | — | — | 493,688 | 493,688 |
| Derivative assets | 1,074 | 270,435 | — | 271,509 |
| Total assets | $1,074 | $12,033,801 | $540,800 | $12,575,675 |
| Liabilities | | | | |
| Collateralized borrowings in securitization trusts | $— | $2,000,110 | $— | $2,000,110 |
| Derivative liabilities | 1,324 | 5,961 | — | 7,285 |
| Total liabilities | $1,324 | $2,006,071 | $— | $2,007,395 |

The Company may be required to measure certain assets or liabilities at fair value from time to time. These periodic fair value measures typically result from application of certain impairment measures under U.S. GAAP. These items would constitute nonrecurring fair value measures under ASC 820. As of September 30, 2016, the Company did not have any assets or liabilities measured at fair value on a nonrecurring basis in the periods presented.

The valuation of Level 3 instruments requires significant judgment by the third-party pricing providers and/or management. The third-party pricing providers and/or management rely on inputs such as market price quotations from market makers (either market or indicative levels), original transaction price, recent transactions in the same or similar instruments, and changes in financial ratios or cash flows to determine fair value. Level 3 instruments may also be discounted to reflect illiquidity and/or non-transferability, with the amount of such discount estimated by the third-party pricing provider in the absence of market information. Assumptions used by the third-party pricing provider due to lack of observable inputs may significantly impact the resulting fair value and therefore the Company's condensed consolidated financial statements. The Company's valuation committee reviews all valuations that are based on pricing information received from a third-party pricing provider. As part of this review, prices are compared against other pricing or input data points in the marketplace, along with internal valuation expertise, to ensure the pricing is reasonable. In addition, the Company performs back-testing of pricing information to validate price information and identify any pricing trends of a third-party price provider.

In determining fair value, third-party pricing providers use various valuation approaches, including market and income approaches. Inputs that are used in determining fair value of an instrument may include pricing information, credit data, volatility statistics, and other factors. In addition, inputs can be either observable or unobservable.

The availability of observable inputs can vary by instrument and is affected by a wide variety of factors, including the type of instrument, whether the instrument is new and not yet established in the marketplace and other characteristics particular to the instrument. The third-party pricing provider uses prices and inputs that are current as of the measurement date, including during periods of market dislocations. In periods of market dislocation, the availability of prices and inputs may be reduced for many instruments. This condition could cause an instrument to be reclassified to or from various levels within the fair value hierarchy.

Securities for which market quotations are readily available are valued at the bid price (in the case of long positions) or the ask price (in the case of short positions) at the close of trading on the date as of which value is determined. Exchange-traded securities for which no bid or ask price is available are valued at the last traded price. OTC derivative contracts, including interest rate swaps and swaption agreements, put and call options for TBAs and U.S. Treasuries, constant maturity swaps, credit default swaps and Markit IOS total return swaps, are valued by the Company using observable inputs, specifically quotations received from third-party pricing providers, and are therefore classified within Level 2.

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The following table presents the reconciliation for all of the Company's Level 3 assets measured at fair value on a recurring basis:

| | Level 3 Recurring Fair Value Measurements | | | |
|---|---|---|---|---|
| | Three Months Ended September 30, 2016 | | Nine Months Ended September 30, 2016 | |
| (in thousands) | Residential Mortgage Loans Held-For-Sale | Mortgage Servicing Rights | Residential Mortgage Loans Held-For-Sale | Mortgage Servicing Rights |
| Beginning of period level 3 fair value | $66,369 | $427,813 | $47,112 | $493,688 |
| Gains (losses) included in net income (loss): | | | | |
| Realized gains (losses) | (725) | (37,297) | 3,615 | (71,839) |
| Unrealized gains (losses) | (309) [(1)] | 3,846 [(3)] | (313) [(1)] | (139,587) [(3)] |
| Total gains (losses) included in net income (loss) | (1,034) | (33,451) | 3,302 | (211,426) |
| Other comprehensive income (loss) | — | — | — | — |
| Purchases | 56,121 | 98,466 | 181,679 | 205,199 |
| Sales | (26,954) | (41,844) | (82,204) | (41,844) |
| Settlements | (27,079) | 4,645 | (82,466) | 10,012 |
| Gross transfers into level 3 | — | — | — | — |
| Gross transfers out of level 3 | — | — | — | — |
| End of period level 3 fair value | $67,423 | $455,629 | $67,423 | $455,629 |
| Change in unrealized gains or losses for the period included in earnings for assets held at the end of the reporting period | $68 [(2)] | $(7,254) [(4)] | $180 [(2)] | $(150,687) [(4)] |

(1) The change in unrealized gains or losses on residential mortgage loans held-for-sale was recorded in (loss) gain on residential mortgage loans held-for-sale on the condensed consolidated statements of comprehensive income (loss).

(2) The change in unrealized gains or losses on residential mortgage loans held-for-sale that were held at the end of the reporting period was recorded in (loss) gain on residential mortgage loans held-for-sale on the condensed consolidated statements of comprehensive income (loss).

(3) The change in unrealized gains or losses on MSR was recorded in loss on servicing asset on the condensed consolidated statements of comprehensive income (loss).

(4) The change in unrealized gains or losses on MSR that were held at the end of the reporting period was recorded in loss on servicing asset on the condensed consolidated statements of comprehensive income (loss).

The Company did not incur transfers between Level 1, Level 2 or Level 3 during the nine months ended September 30, 2016. Transfers between Levels are deemed to take place on the first day of the reporting period in which the transfer has taken place.

The Company used a third-party pricing provider in the fair value measurement of its Level 3 residential mortgage loans held-for-sale. The significant unobservable inputs used by the third-party pricing provider included expected default, severity and discount rate. Significant increases (decreases) in any of the inputs in isolation may result in significantly lower (higher) fair value measurement.

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The Company also used a third-party pricing provider in the fair value measurement of its Level 3 MSR. The table below presents information about the significant unobservable inputs used by the third-party pricing provider in the fair value measurement of the Company's MSR classified as Level 3 fair value assets at September 30, 2016:

As of September 30, 2016

| Valuation Technique | Unobservable Input [1] | Range | Weighted Average |
|---|---|---|---|
| Discounted cash flow | Constant prepayment speed | 13.6 - 18.5 % | 15.8% |
| | Delinquency | 2.0 - 2.2 % | 2.1% |
| | Discount rate | 8.2 - 9.8 % | 9.0% |

(1) Significant increases (decreases) in any of the inputs in isolation may result in significantly lower (higher) fair value measurement. A change in the assumption used for discount rates may be accompanied by a directionally similar change in the assumption used for the probability of delinquency and a directionally opposite change in the assumption used for prepayment rates.

Fair Value Option for Financial Assets and Financial Liabilities

On July 1, 2015, the Company elected the fair value option for Agency interest-only securities and GSE credit risk transfer securities acquired on or after such date. The fair value option was elected to simplify the reporting of changes in fair value. Agency interest-only securities and GSE credit risk transfer securities are carried within AFS securities on the condensed consolidated balance sheets. The Company's policy is to separately record interest income, net of premium amortization or including discount accretion, on these fair value elected securities. Fair value adjustments are reported in gain on investment securities on the condensed consolidated statements of comprehensive income (loss).

The Company elected the fair value option for the residential mortgage loans it has acquired. The fair value option was elected to mitigate earnings volatility by better matching the accounting for the assets with the related hedges. The mortgage loans are carried within residential mortgage loans held-for-sale on the condensed consolidated balance sheets. The Company's policy is to separately record interest income on these fair value elected loans. Upfront fees and costs related to the fair value elected loans are not deferred or capitalized. Fair value adjustments are reported in (loss) gain on residential mortgage loans held-for-sale on the condensed consolidated statements of comprehensive income (loss). The fair value option is irrevocable once the loan is acquired.

The Company also elected the fair value option for both the residential mortgage loans held-for-investment in securitization trusts and the collateralized borrowings in securitization trusts carried on the condensed consolidated balance sheets. The fair value option was elected to better reflect the economics of the Company's retained interests. The Company's policy is to separately record interest income on the fair value elected loans and interest expense on the fair value elected borrowings. Upfront fees and costs are not deferred or capitalized. Fair value adjustments are reported in other income (loss) on the condensed consolidated statements of comprehensive income (loss).

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The following tables summarize the fair value option elections and information regarding the line items and amounts recognized in the condensed consolidated statements of comprehensive income (loss) for each fair value option-elected item.

| | Three Months Ended September 30, 2016 | | | | | |
|---|---|---|---|---|---|---|
| (in thousands) | Interest income (expense) | Gain on investment securities | (Loss) gain on residential mortgage loans held-for-sale | Other income (loss) | Total included in net income (loss) | Change in fair value due to credit risk |
| Assets | | | | | | |
| Available-for-sale securities | $(249) | $ 12 | $ — | $— | $(237) | N/A |
| Residential mortgage loans held-for-sale | 7,627 [1] | — | (419) | — | 7,208 | $145 [2] |
| Residential mortgage loans held-for-investment in securitization trusts | 33,495 [1] | — | — | 24,628 | 58,123 | — [3] |
| Liabilities | | | | | | |
| Collateralized borrowings in securitization trusts | (26,422) | — | — | (20,360) | (46,782) | — [3] |
| Total | $14,451 | $ 12 | $ (419) | $4,268 | $18,312 | $145 |

| | Three Months Ended September 30, 2015 | | | | | |
|---|---|---|---|---|---|---|
| (in thousands) | Interest income (expense) | Gain on investment securities | (Loss) gain on residential mortgage loans held-for-sale | Other income (loss) | Total included in net income (loss) | Change in fair value due to credit risk |
| Assets | | | | | | |
| Available-for-sale securities | $89 | $ (47) | $ — | $— | $42 | N/A |
| Residential mortgage loans held-for-sale | 9,479 [1] | — | 12,814 | — | 22,293 | $721 [2] |
| Residential mortgage loans held-for-investment in securitization trusts | 24,841 [1] | — | — | 16,006 | 40,847 | — [3] |
| Liabilities | | | | | | |
| Collateralized borrowings in securitization trusts | (15,562) | — | — | (14,922) | (30,484) | — [3] |
| Total | $18,847 | $ (47) | $ 12,814 | $1,084 | $32,698 | $721 |

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| (in thousands) | Nine Months Ended September 30, 2016 | | | | | |
|---|---|---|---|---|---|---|
| | Interest income (expense) | Gain on investment securities | (Loss) gain on residential mortgage loans held-for-sale | Other income (loss) | Total included in net income (loss) | Change in fair value due to credit risk |
| Assets | | | | | | |
| Available-for-sale securities | $(132) | $(1,262) | $— | $— | $(1,394) | N/A |
| Residential mortgage loans held-for-sale | 19,789 [(1)] | — | 17,028 | — | 36,817 | $209 [(2)] |
| Residential mortgage loans held-for-investment in securitization trusts | 100,765 [(1)] | — | — | 63,737 | 164,502 | — [(3)] |
| Liabilities | | | | | | |
| Collateralized borrowings in securitization trusts | (70,965) | — | — | (68,910) | (139,875) | — [(3)] |
| Total | $49,457 | $(1,262) | $ 17,028 | $(5,173) | $60,050 | $209 |

| (in thousands) | Nine Months Ended September 30, 2015 | | | | | |
|---|---|---|---|---|---|---|
| | Interest income (expense) | Gain on investment securities | (Loss) gain on residential mortgage loans held-for-sale | Other income (loss) | Total included in net income (loss) | Change in fair value due to credit risk |
| Assets | | | | | | |
| Available-for-sale securities | $89 | $ (47) | $— | $— | $42 | N/A |
| Residential mortgage loans held-for-sale | 21,268 [(1)] | — | 18,861 | — | 40,129 | $751 [(2)] |
| Residential mortgage loans held-for-investment in securitization trusts | 64,908 [(1)] | — | — | (33,088) | 31,820 | — [(3)] |
| Liabilities | | | | | | |
| Collateralized borrowings in securitization trusts | (39,401) | — | — | 13,647 | (25,754) | — [(3)] |
| Total | $46,864 | $ (47) | $ 18,861 | $(19,441) | $46,237 | $751 |

(1) Interest income on residential mortgage loans held-for-sale and residential mortgage loans held-for-investment in securitization trusts is measured by multiplying the unpaid principal balance on the loans by the coupon rate and the number of days of interest due.

(2) The change in fair value due to credit risk on residential mortgage loans held-for-sale was quantified by holding yield constant in the cash flow model in order to isolate credit risk component.

(3) The change in fair value on residential mortgage loans held-for-investment in securitization trusts and collateralized borrowings in securitization trusts was due entirely to changes in market interest rates.

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The table below provides the fair value and the unpaid principal balance for the Company’s fair value option-elected loans and collateralized borrowings.

| (in thousands) | September 30, 2016 | | December 31, 2015 | |
|---|---|---|---|---|
| | Unpaid Principal Balance | Fair Value (1) | Unpaid Principal Balance | Fair Value (1) |
| Residential mortgage loans held-for-sale | | | | |
| Total loans | $720,609 | $723,174 | $812,661 | $811,431 |
| Nonaccrual loans | $51,156 | $45,843 | $30,438 | $25,771 |
| Loans 90+ days past due | $45,759 | $40,936 | $26,702 | $22,470 |
| Residential mortgage loans held-for-investment in securitization trusts | | | | |
| Total loans | $3,499,285 | $3,620,037 | $3,143,515 | $3,173,727 |
| Nonaccrual loans | $860 | $887 | $860 | $868 |
| Loans 90+ days past due | $860 | $887 | $860 | $868 |
| Collateralized borrowings in securitization trusts | | | | |
| Total borrowings | $3,277,103 | $3,375,906 | $1,987,628 | $2,000,110 |

(1) Excludes accrued interest receivable.

Fair Value of Financial Instruments

In accordance with ASC 820, the Company is required to disclose the fair value of financial instruments, both assets and liabilities recognized and not recognized in the condensed consolidated balance sheets, for which fair value can be estimated.

The following describes the Company’s methods for estimating the fair value for financial instruments. Descriptions are not provided for those items that have zero balances as of the current balance sheet date.

- AFS securities, residential mortgage loans held-for-sale, residential mortgage loans held-for-investment in securitization trusts, MSR, derivative assets and liabilities, and collateralized borrowings in securitization trusts are recurring fair value measurements; carrying value equals fair value. See discussion of valuation methods and assumptions within the Fair Value Measurements section of this Note 14.
- Commercial real estate assets are carried at cost, net of any unamortized acquisition premiums or discounts, loan fees and origination costs as applicable, unless deemed impaired. The Company estimates the fair value of its commercial real estate assets by assessing any changes in market interest rates, shifts in credit profiles and actual operating results for mezzanine commercial real estate loans and commercial real estate first mortgages, taking into consideration such factors as underlying property type, property competitive position within its market, market and submarket fundamentals, tenant mix, nature of business plan, sponsorship, extent of leverage and other loan terms. The Company categorizes the fair value measurement of these assets as Level 3.
- Cash and cash equivalents and restricted cash have a carrying value which approximates fair value because of the short maturities of these instruments. The Company categorizes the fair value measurement of these assets as Level 1.
- As a condition to membership in the FHLB, the Company is required to purchase and hold a certain amount of FHLB stock, which is considered a non-marketable, long-term investment, and is carried at cost. Because this stock can only be redeemed or sold at its par value, and only to the FHLB, carrying value, or cost, approximates fair value. The Company categorizes the fair value measurement of these assets as Level 3.
- Equity investments include cost method investments for which fair value is not estimated. Carrying value, or cost, approximates fair value. The Company categorizes the fair value measurement of these assets as Level 3.

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The carrying value of repurchase agreements, FHLB advances and revolving credit facilities that mature in less than one year generally approximates fair value due to the short maturities. As of September 30, 2016, the Company held $222.6 million of repurchase agreements and $3.3 billion of FHLB advances that are considered long-term. The Company's long-term repurchase agreements and FHLB advances have floating rates based on an index plus a spread and, for members of the FHLB, the credit spread is typically consistent with those demanded in the market. Accordingly, the interest rates on these borrowings are at market and thus carrying value approximates fair value. The Company categorizes the fair value measurement of these liabilities as Level 2.

The following table presents the carrying values and estimated fair values of assets and liabilities that are required to be recorded or disclosed at fair value at September 30, 2016 and December 31, 2015.

| | September 30, 2016 | | December 31, 2015 | |
|---|---|---|---|---|
| (in thousands) | Carrying Value | Fair Value | Carrying Value | Fair Value |
| Assets | | | | |
| Available-for-sale securities | $14,284,625 | $14,284,625 | $7,825,320 | $7,825,320 |
| Residential mortgage loans held-for-sale | $723,174 | $723,174 | $811,431 | $811,431 |
| Residential mortgage loans held-for-investment in securitization trusts | $3,620,037 | $3,620,037 | $3,173,727 | $3,173,727 |
| Commercial real estate assets | $1,114,548 | $1,113,756 | $660,953 | $660,953 |
| Mortgage servicing rights | $455,629 | $455,629 | $493,688 | $493,688 |
| Cash and cash equivalents | $688,418 | $688,418 | $737,831 | $737,831 |
| Restricted cash | $264,872 | $264,872 | $262,562 | $262,562 |
| Derivative assets | $199,013 | $199,013 | $271,509 | $271,509 |
| Federal Home Loan Bank stock | $167,856 | $167,856 | $156,650 | $156,650 |
| Equity investments | $3,000 | $3,000 | $3,000 | $3,000 |
| Liabilities | | | | |
| Repurchase agreements | $10,637,373 | $10,637,373 | $5,008,274 | $5,008,274 |
| Collateralized borrowings in securitization trusts | $3,375,906 | $3,375,906 | $2,000,110 | $2,000,110 |
| Federal Home Loan Bank advances | $4,000,000 | $4,000,000 | $3,785,000 | $3,785,000 |
| Revolving credit facilities | $30,000 | $30,000 | $— | $— |
| Derivative liabilities | $39,918 | $39,918 | $7,285 | $7,285 |

Note 15. Repurchase Agreements

As of September 30, 2016 and December 31, 2015, the Company had outstanding $10.6 billion and $5.0 billion, respectively, of repurchase agreements. Excluding the effect of the Company's interest rate swaps, the repurchase agreements had a weighted average borrowing rate of 1.06% and 1.10% and weighted average remaining maturities of 69 and 35 days as of September 30, 2016 and December 31, 2015, respectively.

At September 30, 2016 and December 31, 2015, the repurchase agreement balances were as follows:

| (in thousands) | September 30, 2016 | December 31, 2015 |
|---|---|---|
| Short-term | $ 10,414,745 | $ 5,008,274 |
| Long-term | 222,628 | — |
| Total | $ 10,637,373 | $ 5,008,274 |

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At September 30, 2016 and December 31, 2015, the repurchase agreements had the following characteristics and remaining maturities:

| | September 30, 2016<br>Collateral Type | | | | | |
|---|---|---|---|---|---|---|
| (in thousands) | Agency RMBS | Non-Agency RMBS [1] | Agency Derivatives | Residential Mortgage Loans Held-for-Sale | Commercial Real Estate Assets | Total Amount Outstanding |
| Within 30 days | $3,341,276 | $588,934 | $15,385 | $ — | $21,933 | $3,967,528 |
| 30 to 59 days | 2,595,970 | 207,856 | 65,018 | — | 27,820 | 2,896,664 |
| 60 to 89 days | 1,185,026 | — | — | — | — | 1,185,026 |
| 90 to 119 days | 622,725 | 373,474 | 16,373 | — | — | 1,012,572 |
| 120 to 364 days | 1,116,541 | 218,431 | 17,983 | — | — | 1,352,955 |
| One year and over | — | — | — | — | 222,628 | 222,628 |
| Total | $8,861,538 | $1,388,695 | $114,759 | $ — | $272,381 | $10,637,373 |
| Weighted average borrowing rate | 0.79 % | 2.41 % | 1.60 % | — % | 2.93 % | 1.06 % |

| | December 31, 2015<br>Collateral Type | | | | | |
|---|---|---|---|---|---|---|
| (in thousands) | Agency RMBS | Non-Agency RMBS [1] | Agency Derivatives | Residential Mortgage Loans Held-for-Sale | Commercial Real Estate Assets | Total Amount Outstanding |
| Within 30 days | $1,719,292 | $852,436 | $58,286 | $ — | $59,349 | $2,689,363 |
| 30 to 59 days | 1,407,353 | 271,819 | 60,065 | — | — | 1,739,237 |
| 60 to 89 days | 143,051 | 15,691 | 2,707 | — | — | 161,449 |
| 90 to 119 days | 68,014 | 106,007 | 1,465 | — | — | 175,486 |
| 120 to 364 days | — | 234,229 | — | 8,510 | — | 242,739 |
| Total | $3,337,710 | $1,480,182 | $122,523 | $ 8,510 | $59,349 | $5,008,274 |
| Weighted average borrowing rate | 0.65 % | 2.03 % | 1.18 % | 2.87 % | 2.62 % | 1.10 % |

(1) Includes repurchase agreements collateralized by retained interests from the Company’s on-balance sheet securitizations, which are eliminated in consolidation in accordance with U.S. GAAP.

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The following table summarizes assets at carrying values that are pledged or restricted as collateral for the future payment obligations of repurchase agreements:

| (in thousands) | September 30, 2016 | December 31, 2015 |
|---|---|---|
| Available-for-sale securities, at fair value | $ 11,115,563 | $ 5,354,104 |
| Residential mortgage loans held-for-sale, at fair value | — | 9,543 |
| Commercial real estate assets | 399,594 | 108,958 |
| Net economic interests in consolidated securitization trusts [1] | 218,971 | 274,949 |
| Cash and cash equivalents | 12,094 | 15,000 |
| Restricted cash | 95,223 | 119,310 |
| Due from counterparties | 29,477 | 10,211 |
| Derivative assets, at fair value | 140,868 | 157,879 |
| Total | $ 12,011,790 | $ 6,049,954 |

(1) Includes the retained interests from the Company's on-balance sheet securitizations, which are eliminated in consolidation in accordance with U.S. GAAP.

Although the transactions under repurchase agreements represent committed borrowings until maturity, the respective lender retains the right to mark the underlying collateral to fair value. A reduction in the value of pledged assets would require the Company to provide additional collateral or fund margin calls.
The following table summarizes certain characteristics of the Company's repurchase agreements and counterparty concentration at September 30, 2016 and December 31, 2015:

| | September 30, 2016 | | | | December 31, 2015 | | | |
|---|---|---|---|---|---|---|---|---|
| (dollars in thousands) | Amount Outstanding | Net Counterparty Exposure [1] | Percent of Equity | Weighted Average Days to Maturity | Amount Outstanding | Net Counterparty Exposure [1] | Percent of Equity | Weighted Average Days to Maturity |
| Royal Bank of Canada | $ 1,202,327 | $ 260,862 | 7 % | 76.4 | $ 799,527 | $ 217,677 | 6 % | 31.5 |
| All other counterparties [2] | 9,435,046 | 1,115,813 | 32 % | 68.1 | 4,208,747 | 818,108 | 23 % | 36.2 |
| Total | $ 10,637,373 | $ 1,376,675 | | | $ 5,008,274 | $ 1,035,785 | | |

(1) Represents the net carrying value of the securities, residential mortgage loans held-for-sale and commercial real estate assets sold under agreements to repurchase, including accrued interest plus any cash or assets on deposit to secure the repurchase obligation, less the amount of the repurchase liability, including accrued interest. However, at both September 30, 2016 and December 31, 2015, the Company did not have any such payables.
(2) Represents amounts outstanding with 21 and 20 counterparties at September 30, 2016 and December 31, 2015, respectively.

The Company does not anticipate any defaults by its repurchase agreement counterparties. There can be no assurance, however, that any such default or defaults will not occur.

Note 16. Collateralized Borrowings in Securitization Trusts, at Fair Value
The Company purchases subordinated debt and excess servicing rights from securitization trusts sponsored by either third parties or the Company's subsidiaries. The debt associated with the underlying residential mortgage loans held by the trusts, which are consolidated on the Company's condensed consolidated balance sheets, is classified as collateralized borrowings in securitization trusts and carried at fair value as a result of a fair value option election. See

Note 3 - Variable Interest Entities for additional information regarding consolidation of the securitization trusts. As of September 30, 2016 and December 31, 2015, collateralized borrowings in securitization trusts had a carrying value of $3.4 billion and $2.0 billion with a weighted average interest rate of 3.4% and 3.6%, respectively. The stated maturity dates for all collateralized borrowings were more than five years from both September 30, 2016 and December 31, 2015.



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Note 17. Federal Home Loan Bank of Des Moines Advances

The Company's wholly owned subsidiary, TH Insurance Holdings Company LLC, or TH Insurance, is a member of the FHLB. As a member of the FHLB, TH Insurance has access to a variety of products and services offered by the FHLB, including secured advances. As of September 30, 2016 and December 31, 2015, TH Insurance had $4.0 billion and $3.8 billion in outstanding secured advances with a weighted average borrowing rate of 0.67% and 0.58%, respectively, and had no additional uncommitted capacity to borrow as of September 30, 2016. As of December 31, 2015, TH Insurance had an additional $215.0 million of available uncommitted capacity for borrowings. To the extent TH Insurance has uncommitted capacity, it may be adjusted at the sole discretion of the FHLB.

The ability to borrow from the FHLB is subject to the Company's continued creditworthiness, pledging of sufficient eligible collateral to secure advances, and compliance with certain agreements with the FHLB. Each advance requires approval by the FHLB and is secured by collateral in accordance with the FHLB's credit and collateral guidelines, as may be revised from time to time by the FHLB. Eligible collateral may include conventional 1-4 family residential mortgage loans, commercial real estate loans, Agency RMBS and certain non-Agency RMBS with a rating of A and above.

On January 11, 2016, the Federal Housing Finance Agency, or FHFA, released a final rule regarding membership in the Federal Home Loan Bank system. Among other effects, the final rule excludes captive insurers from membership eligibility, including the Company's subsidiary member, TH Insurance. Since TH Insurance was admitted as a member in 2013, it is eligible for a five-year membership grace period, during which new advances or renewals that mature beyond the grace period will be prohibited; however, any existing advances that mature beyond this grace period will be permitted to remain in place subject to their terms insofar as the Company maintains good standing with the FHLB. If any new advances or renewals occur, TH Insurance's outstanding advances will be limited to 40% of its total assets.

At September 30, 2016 and December 31, 2015, FHLB advances had the following remaining maturities:

| (in thousands) | September 30, 2016 | December 31, 2015 |
|---|---|---|
| ≤ 1 year | $ 651,238 | $ — |
| > 1 and ≤ 3 years | 815,024 | 651,238 |
| > 3 and ≤ 5 years | — | 815,024 |
| > 5 and ≤ 10 years | — | — |
| > 10 years | 2,533,738 | 2,318,738 |
| Total | $ 4,000,000 | $ 3,785,000 |

The following table summarizes assets at carrying values that are pledged or restricted as collateral for the future payment obligations of FHLB advances:

| (in thousands) | September 30, 2016 | December 31, 2015 |
|---|---|---|
| Available-for-sale securities, at fair value | $ 3,156,325 | $ 2,412,970 |
| Residential mortgage loans held-for-sale, at fair value | 632,698 | 735,911 |
| Commercial real estate assets | 597,603 | 252,172 |
| Net economic interests in consolidated securitization trusts [1] | 4,124 | 863,363 |
| Total | $ 4,390,750 | $ 4,264,416 |

(1) Includes the retained interests from the Company's on-balance sheet securitizations, which are eliminated in consolidation in accordance with U.S. GAAP.

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The FHLB retains the right to mark the underlying collateral for FHLB advances to fair value. A reduction in the value of pledged assets would require the Company to provide additional collateral. In addition, as a condition to membership in the FHLB, the Company is required to purchase and hold a certain amount of FHLB stock, which is based, in part, upon the outstanding principal balance of advances from the FHLB. At September 30, 2016 and December 31, 2015, the Company had stock in the FHLB totaling $167.9 million and $156.7 million, respectively, which is included in other assets on the condensed consolidated balance sheets. FHLB stock is considered a non-marketable, long-term investment, is carried at cost and is subject to recoverability testing under applicable accounting standards. This stock can only be redeemed or sold at its par value, and only to the FHLB. Accordingly, when evaluating FHLB stock for impairment, the Company considers the ultimate recoverability of the par value rather than recognizing temporary declines in value. As of September 30, 2016 and December 31, 2015, the Company had not recognized an impairment charge related to its FHLB stock.

Note 18. Revolving Credit Facilities
To finance MSR, the Company enters into revolving credit facilities collateralized by the value of the MSR pledged. As of September 30, 2016, the Company had outstanding short-term borrowings under revolving credit facilities of $30.0 million with a weighted average borrowing rate of 4.27% and remaining maturities of 336 days. The Company did not have any revolving credit facilities in place at December 31, 2015.
Although the transactions under revolving credit facilities represent committed borrowings until maturity, the respective lender retains the right to mark the underlying collateral to fair value. A reduction in the value of pledged assets below a designated threshold would require the Company to provide additional collateral or fund margin calls. As of September 30, 2016, MSR with a carrying value of $73.5 million was pledged as collateral for the Company's future payment obligations under its revolving credit facilities. The Company does not anticipate any defaults by its revolving credit facility counterparties. There can be no assurance, however, that any such default or defaults will not occur.

Note 19. Stockholders' Equity
Distributions to Stockholders
The following table presents cash dividends declared by the Company on its common stock during the three months ended September 30, 2016, and the four immediately preceding quarters:

| Declaration Date | Record Date | Payment Date | Cash Dividend Per Share |
|---|---|---|---|
| September 15, 2016 | September 30, 2016 | October 20, 2016 | $ 0.23 |
| June 16, 2016 | June 30, 2016 | July 20, 2016 | $ 0.23 |
| March 15, 2016 | March 31, 2016 | April 21, 2016 | $ 0.23 |
| December 16, 2015 | December 30, 2015 | January 20, 2016 | $ 0.26 |
| September 16, 2015 | September 30, 2015 | October 22, 2015 | $ 0.26 |

Accumulated Other Comprehensive Income
Accumulated other comprehensive income at September 30, 2016 and December 31, 2015 was as follows:

| (in thousands) | September 30, 2016 | December 31, 2015 |
|---|---|---|
| Available-for-sale securities | | |
| Unrealized gains | $ 551,343 | $ 405,177 |
| Unrealized losses | (12,900) | (46,116) |
| Accumulated other comprehensive income | $ 538,443 | $ 359,061 |

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Reclassifications out of Accumulated Other Comprehensive Income
The following table summarizes reclassifications out of accumulated other comprehensive income for the three and nine months ended September 30, 2016 and 2015:

| (in thousands) | Affected Line Item in the Condensed Consolidated Statements of Comprehensive Income (Loss) | Amount Reclassified out of Accumulated Other Comprehensive Income | | | |
|---|---|---|---|---|---|
| | | Three Months Ended September 30, | | Nine Months Ended September 30, | |
| | | 2016 | 2015 | 2016 | 2015 |
| Other-than-temporary impairments on AFS securities | Total other-than-temporary impairment losses | $1,015 | $238 | $1,822 | $535 |
| Realized gains on sales of certain AFS securities, net of tax | Gain on investment securities | (30,396) | (53,447) | (54,652) | (228,518) |
| Total | | $(29,381) | $(53,209) | $(52,830) | $(227,983) |

Dividend Reinvestment and Direct Stock Purchase Plan
The Company sponsors a dividend reinvestment and direct stock purchase plan through which stockholders may purchase additional shares of the Company's common stock by reinvesting some or all of the cash dividends received on shares of the Company's common stock. Stockholders may also make optional cash purchases of shares of the Company's common stock subject to certain limitations detailed in the plan prospectus. An aggregate of 7.5 million shares of the Company's common stock were originally reserved for issuance under the plan. As of September 30, 2016, 327,056 shares have been issued under the plan for total proceeds of approximately $3.3 million, of which 14,621 and 43,764 shares were issued for total proceeds of $0.1 million and $0.4 million during the three and nine months ended September 30, 2016, respectively. During the three and nine months ended September 30, 2015, 17,904 and 54,088 shares were issued for total proceeds of $0.2 million and $0.6 million, respectively.
Share Repurchase Program
As of December 31, 2015, the Company's share repurchase program allowed the Company to repurchase up to 25,000,000 shares of its common stock. During the nine months ended September 30, 2016, the Company's board of directors authorized an increase of 50,000,000 shares, for up to a total of 75,000,000 shares authorized under the program. Shares may be repurchased from time to time through privately negotiated transactions or open market transactions, pursuant to a trading plan in accordance with Rules 10b5-1 and 10b-18 under the Securities Exchange Act of 1934, as amended, or the Exchange Act, or by any combination of such methods. The manner, price, number and timing of share repurchases are subject to a variety of factors, including market conditions and applicable SEC rules. The share repurchase program does not require the purchase of any minimum number of shares, and, subject to SEC rules, purchases may be commenced or suspended at any time without prior notice. The share repurchase program does not have an expiration date. As of September 30, 2016, a total of 24,135,000 shares had been repurchased by the Company under the program for an aggregate cost of $200.4 million; of these, 8,020,000 shares were repurchased for a total cost of $61.3 million during the nine months ended September 30, 2016. No shares were repurchased during the three months ended September 30, 2016. During the three and nine months ended September 30, 2015, 1,391,887 shares were repurchased for a total cost of $12.5 million.
At-the-Market Offering
On May 25, 2012, the Company entered into an equity distribution agreement under which the Company may sell up to an aggregate of 20,000,000 shares of its common stock from time to time in any method permitted by law deemed to be an "at the market" offering as defined in Rule 415 under the Securities Act of 1933, as amended, or the Securities

Act. On May 22, 2015, the Company entered into an amendment to the equity distribution agreement providing that any subsequent offers or sales of the Company's common stock under the equity distribution agreement shall be made pursuant to a new prospectus supplement, which was filed on the same date. As of September 30, 2016, 7,585,869 shares of common stock have been sold under the equity distribution agreement for total accumulated net proceeds of approximately $77.6 million; however, no shares were sold during the three and nine months ended September 30, 2016 and 2015.

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Note 20. Equity Incentive Plan

On May 14, 2015, the Company's stockholders approved the Company's Second Restated 2009 Equity Incentive Plan, which replaced the previous Restated 2009 Equity Incentive Plan, both of which are referred to collectively as the Plan. This stockholder approval effectuated, among other changes, an increase in the number of shares of common stock available for issuance under the Plan by 10,000,000 shares, to a total of 13,000,000 shares.

During the nine months ended September 30, 2016 and 2015, the Company granted 81,739 and 55,229 shares of common stock, respectively, to its independent directors pursuant to the Plan. The estimated fair value of these awards was $8.43 and $10.41 per share on grant date, based on the closing price of the Company's common stock on the NYSE on such date. The grants vested immediately.

Additionally, during the nine months ended September 30, 2016 and 2015, the Company granted 1,937,522 and 1,115,574 shares of restricted common stock, respectively, to key employees of PRCM Advisers pursuant to the terms of the Plan and the associated award agreements. The estimated fair value of these awards was $7.52 and $10.49 per share on grant date, based on the closing market price of the Company's common stock on the NYSE on such date. However, as the cost of these awards is measured at fair value at each reporting date based on the price of the Company's stock as of period end in accordance with ASC 505, Equity, or ASC 505, the fair value of these awards as of September 30, 2016 was $8.53 per share based on the closing market price of the Company's common stock on the NYSE on such date. The shares underlying the grants vest in three equal annual installments commencing on the first anniversary of the grant date, as long as such grantee complies with the terms and conditions of his or her applicable restricted stock award agreement. During the nine months ended September 30, 2016, in connection with the restructuring described in Note 21 - Restructuring Charges, certain agreements were forfeited and re-granted with accelerated vesting terms, in accordance with ASC 718, Compensation - Stock Compensation.

The following table summarizes the activity related to restricted common stock for the nine months ended September 30, 2016 and 2015:

| | Nine Months Ended September 30, | | | |
|---|---|---|---|---|
| | 2016 | | 2015 | |
| (in thousands) | Shares | Weighted Average Grant Date Fair Market Value | Shares | Weighted Average Grant Date Fair Market Value |
| Outstanding at Beginning of Period | 2,290,609 | $ 10.36 | 2,002,406 | $ 10.32 |
| Granted | 2,019,261 | 7.56 | 1,170,803 | 10.48 |
| Vested | (1,209,116) | (10.10 ) | (730,832 ) | (10.45 ) |
| Forfeited | (301,217 ) | (8.50 ) | (61,159 ) | (10.17 ) |
| Outstanding at End of Period | 2,799,537 | $ 8.65 | 2,381,218 | $ 10.36 |

For the three and nine months ended September 30, 2016, the Company recognized compensation costs and restructuring charges related to restricted common stock of $3.5 million and $11.2 million, respectively. For the three and nine months ended September 30, 2015, the Company recognized compensation costs related to restricted common stock of $1.7 million and $7.4 million, respectively.

Note 21. Restructuring Charges

On July 28, 2016, the Company announced that its board of directors had approved a plan to discontinue the Company's mortgage loan conduit and securitization business. The wind down process is expected to be substantially completed by the end of 2016.

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In connection with the closure, the Company incurred the following charges, included within restructuring charges on the Company’s condensed consolidated statements of comprehensive income (loss), for the three and nine months ended September 30, 2016:

| (in thousands) | Three Months Ended September 30, 2016 | Nine Months Ended September 30, 2016 |
|---|---|---|
| Termination benefits | $ 652 | $ 652 |
| Contract terminations | 519 | 519 |
| Other associated costs | 18 | 18 |
| Total | $ 1,189 | $ 1,189 |

The Company expects to incur an estimated $1.6 million in additional restructuring costs, which will be expensed in the period in which they occur. The additional expenses, which are expected to be substantially incurred by the end of 2016, relate to termination benefits and contract terminations.

## Note 22. Income Taxes

For the three and nine months ended September 30, 2016 and 2015, the Company qualified to be taxed as a REIT under the Code for U.S. federal income tax purposes. As long as the Company qualifies as a REIT, the Company generally will not be subject to U.S. federal income taxes on its taxable income to the extent it annually distributes its net taxable income to stockholders, and does not engage in prohibited transactions. The Company intends to distribute 100% of its REIT taxable income and comply with all requirements to continue to qualify as a REIT. The majority of states also recognize the Company’s REIT status. The Company’s TRSs file separate tax returns and are fully taxed as standalone U.S. C-corporations. It is assumed that the Company will retain its REIT status and will incur no REIT level taxation as it intends to comply with the REIT regulations and annual distribution requirements.
During the three and nine months ended September 30, 2016, the Company’s TRSs recognized a benefit from income taxes of $16.8 million and $26.1 million, respectively, which was primarily due to losses incurred on MSR and derivative instruments held in the Company’s TRSs. During the three and nine months ended September 30, 2015, the Company’s TRSs recognized a benefit from income taxes of $7.7 million and $25.3 million, respectively, which was primarily due to losses incurred on MSR and derivative instruments held in the Company’s TRSs.
Based on the Company’s evaluation, it has been concluded that there are no significant uncertain tax positions requiring recognition in the Company’s condensed consolidated financial statements of a contingent tax liability for uncertain tax positions.

## Note 23. Earnings Per Share

The following table presents a reconciliation of the earnings (loss) and shares used in calculating basic and diluted earnings (loss) per share for the three and nine months ended September 30, 2016 and 2015:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| (in thousands, except share data) | 2016 | 2015 | 2016 | 2015 |
| Numerator: | | | | |
| Net income (loss) | $117,786 | $ (34,790 ) | $11,875 | $ 281,504 |
| Denominator: | | | | |
| Weighted average common shares outstanding | 344,744,917 | 364,979,716 | 345,091,765 | 364,844,032 |
| Weighted average restricted stock shares | 2,882,309 | 2,386,257 | 3,126,469 | 2,141,699 |
| Basic and diluted weighted average shares outstanding | 347,627,226 | 367,365,973 | 348,218,234 | 366,985,731 |

| | | | | |
|---|---|---|---|---|
| Basic and Diluted Earnings (Loss) Per Share | $0.34 | $(0.09) | $0.03 | $0.77 |

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Note 24. Related Party Transactions

The following summary provides disclosure of the material transactions with affiliates of the Company.

In accordance with its Management Agreement with PRCM Advisers, the Company incurred $11.4 million and $35.3 million as a management fee to PRCM Advisers for the three and nine months ended September 30, 2016, respectively, and $12.6 million and $38.0 million as a management fee to PRCM Advisers for the three and nine months ended September 30, 2015, respectively, which represents approximately 1.5% of stockholders' equity on an annualized basis as defined by the Management Agreement. For purposes of calculating the management fee, stockholders' equity is adjusted to exclude any common stock repurchases as well as any unrealized gains, losses or other items that do not affect realized net income (loss), among other adjustments, in accordance with the Management Agreement. In addition, the Company reimbursed PRCM Advisers for direct and allocated costs incurred by PRCM Advisers on behalf of the Company. These direct and allocated costs totaled approximately $6.3 million and $19.1 million for the three and nine months ended September 30, 2016, respectively, and $5.9 million and $16.0 million for the three and nine months ended September 30, 2015, respectively.

The Company has direct relationships with the majority of its third-party vendors. The Company will continue to have certain costs allocated to it by PRCM Advisers for compensation, data services, proprietary technology and certain office lease payments, but most direct expenses with third-party vendors are paid directly by the Company.

The Company recognized $3.5 million and $11.2 million of compensation expense and restructuring charges during the three and nine months ended September 30, 2016, respectively, and $1.7 million and $7.4 million of compensation expense during the three and nine months ended September 30, 2015, respectively, related to restricted common stock issued to employees of PRCM Advisers and the Company's independent directors pursuant to the Plan. See Note 20 - Equity Incentive Plan for additional information.

Note 25. Subsequent Events

Events subsequent to September 30, 2016, were evaluated through the date these financial statements were issued and no additional events were identified requiring further disclosure in these condensed consolidated financial statements.

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

The following discussion and analysis should be read in conjunction with our unaudited condensed consolidated financial statements and accompanying notes included elsewhere in this Quarterly Report on Form 10-Q as well as our Annual Report on Form 10-K for the year ended December 31, 2015.

### General

We are a Maryland corporation focused on investing in, financing and managing residential mortgage-backed securities, or RMBS, residential mortgage loans, mortgage servicing rights, or MSR, commercial real estate and other financial assets, which we collectively refer to as our target assets. We operate as a real estate investment trust, or REIT, as defined under the Internal Revenue Code of 1986, as amended, or the Code.

We are externally managed by PRCM Advisers LLC, or PRCM Advisers, which is a wholly owned subsidiary of Pine River Capital Management L.P., or Pine River, a global multi-strategy asset management firm providing comprehensive portfolio management, transparency and liquidity to institutional and high net worth investors.

Our objective is to provide attractive risk-adjusted total return to our stockholders over the long term, primarily through dividends and secondarily through capital appreciation. We selectively acquire and manage an investment portfolio of our target assets, which is constructed to generate attractive returns through market cycles. We focus on asset selection and implement a relative value investment approach across various sectors within the mortgage market. Our target assets include the following:

- Agency RMBS (which includes inverse interest-only Agency securities classified as "Agency Derivatives" for purposes of U.S. generally accepted accounting principles, or U.S. GAAP), meaning RMBS whose principal and interest payments are guaranteed by the Government National Mortgage Association (or Ginnie Mae), the Federal National Mortgage Association (or Fannie Mae), or the Federal Home Loan Mortgage Corporation (or Freddie Mac), or collectively, the government sponsored entities, or GSEs;
- Non-Agency RMBS, meaning RMBS that are not issued or guaranteed by Ginnie Mae, Fannie Mae or Freddie Mac;
- Residential mortgage loans;
- MSR;
- Commercial real estate assets; and
- Other financial assets comprising approximately 5% to 10% of the portfolio.

We generally view our target assets in three strategies that are based on our core competencies of understanding and managing prepayment and credit risk. Our rates strategy includes assets that are sensitive to changes in interest rates and prepayment speeds, specifically Agency RMBS and MSR. Our credit strategy includes assets with inherent credit risk including non-Agency RMBS, prime nonconforming residential mortgage loans and net economic interests in consolidated securitization trusts. Our commercial strategy includes as target assets first mortgage loans, mezzanine loans, b-notes and preferred equity.

As opportunities in the residential and commercial mortgage marketplace change, we continue to evolve our business model. From a capital allocation perspective, we expect to continue to increase our allocation towards MSR and commercial real estate assets, and decrease our exposure to RMBS and residential mortgage loans over time. During the nine months ended September 30, 2016, however, we increased our allocation towards Agency RMBS due to attractive market prices. Within our non-Agency RMBS portfolio, we have historically had a substantial emphasis on "legacy" securities, which include securities issued prior to 2009. Over the course of the past two years, however, we have sold a number of these securities that we believe had reached maximum value, some of which were replaced with "new issue" non-Agency RMBS. We believe these "new issue" securities, which include some GSE credit risk transfer securities, have enabled us to find attractive returns and further diversify our non-Agency RMBS portfolio.

In July 2016, we announced a plan to discontinue our mortgage loan conduit and securitization business, whereby we acquire prime nonconforming residential mortgage loans from select mortgage loan originators and secondary market institutions with the intent to securitize the loans through the issuance of non-Agency mortgage-backed securities and/or exit through a whole loan sale. We expect the wind down process to be substantially completed by the end of

2016, though we currently intend to retain certain subordinated securities from our prior securitization transactions. In addition, we hold a small legacy portfolio of credit sensitive residential mortgage loans, or CSL, which are loans where the borrower has previously experienced payment delinquencies and is more likely to be underwater (i.e., the amount owed on a mortgage loan exceeds the current market value of the home). As a result, there is a higher probability of default on CSL than on newly originated residential mortgage loans. We do not originate residential mortgage loans or provide direct financing to lenders.

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Within our MSR business, we purchase the right to control the servicing of mortgage loans from high-quality originators. Additionally, as an owner of MSR on loans from securitizations guaranteed by Ginnie Mae, we are obligated to purchase these loans from time to time in order to complete modifications on the mortgage loans or to convey foreclosed properties to the U.S. Department of Housing and Urban Development, or HUD. We also have the option to buy out delinquent mortgages in order to better control loss mitigation activities. We held a small portfolio of these Ginnie Mae buyout residential mortgage loans as of September 30, 2016. We do not directly service the mortgage loans we acquire, nor the mortgage loans underlying the MSR we acquire; rather, we contract with fully licensed third-party subservicers to handle substantially all servicing functions.

We believe our investment model allows management to allocate capital across various sectors within the mortgage market, with a focus on asset selection and the implementation of a relative value investment approach. Our capital allocation decisions factor in the opportunities in the marketplace, the cost of financing and the cost of hedging interest rate, prepayment, credit and other portfolio risks. As a result, capital allocation reflects management's opportunistic approach to investing in the marketplace. The following table provides our capital allocation among the target assets in each of our investment strategies as of September 30, 2016 and the four immediately preceding period ends:

| | As of | | | | |
|---|---|---|---|---|---|
| | September 30, 2016 | June 30, 2016 | March 31, 2016 | December 31, 2015 | September 30, 2015 |
| Rates strategy | 54% | 56% | 56% | 49% | 53% |
| Credit strategy | 31% | 31% | 33% | 43% | 43% |
| Commercial strategy | 15% | 13% | 11% | 8% | 4% |

As our capital allocation shifts, our annualized yields and cost of financing shift. As previously discussed, our investment decisions are not driven solely by annualized yields, but rather a multitude of macroeconomic drivers, including market environments and their respective impacts (e.g., uncertainty of prepayment speeds, extension risk and credit events).

For the three months ended September 30, 2016, our net yield realized on the portfolio was lower than previous periods. Yields and net interest spreads on RMBS and MSR are generally lower than recent quarters, while net yields on net economic interests in consolidated securitization trusts have increased due to sales of higher-rated retained interests from on-balance sheet securitizations. Net yields on residential mortgage loans held-for-sale and commercial real estate assets have been relatively consistent. Our cost of financing has decreased slightly as a result of lower swap spread. The following table provides the average annualized yield on our target assets, including Agency and non-Agency RMBS, residential mortgage loans held-for-sale, residential mortgage loans held-for-investment, net of collateralized borrowings, in securitization trusts, commercial real estate assets and MSR for the three months ended September 30, 2016, and the four immediately preceding quarters:

| | Three Months Ended | | | | |
|---|---|---|---|---|---|
| | September 30, 2016 | June 30, 2016 | March 31, 2016 | December 31, 2015 | September 30, 2015 |
| Average annualized portfolio yield [1] | 3.50% | 3.77% | 4.58% | 4.56% | 4.14% |
| Cost of financing [2] | 1.08% | 1.18% | 1.21% | 1.30% | 1.31% |
| Net portfolio yield | 2.42% | 2.59% | 3.37% | 3.26% | 2.83% |

(1) Average annualized yield incorporates future prepayment, credit loss and other assumptions, all of which are estimates and subject to change.

(2) Cost of financing includes swap interest rate spread.

We seek to deploy moderate leverage as part of our investment strategy. We generally finance our RMBS, residential mortgage loans held-for-sale and commercial real estate assets through short- and long-term borrowings structured as repurchase agreements and through short- and long-term advances from the Federal Home Loan Bank of Des Moines, or the FHLB. We also finance our MSR through revolving credit facilities. Our Agency RMBS, given their liquidity and high credit quality, are eligible for higher levels of leverage, while non-Agency RMBS, residential mortgage loans held-for-sale, commercial real estate assets and MSR, with less liquidity and more exposure to credit risk, utilize lower levels of leverage. We believe the debt-to-equity ratio funding our Agency RMBS, non-Agency RMBS, residential mortgage loans held-for-sale, commercial real estate assets and MSR is the most meaningful leverage measure as collateralized borrowings on residential mortgage loans held-for-investment in securitization trusts represents term financing with no stated maturity. As a result, our debt-to-equity ratio is determined by our portfolio mix as well as many additional factors, including the liquidity of our portfolio, the sustainability and price of our financing, diversification of our counterparties and their available capacity to finance our assets, and anticipated regulatory developments. Over the past several quarters, we have generally maintained a debt-to-equity ratio range of 3.0 to 5.0 times to finance our RMBS portfolio, residential mortgage loans held-for-sale, commercial real estate assets and MSR, on a fully deployed capital basis. Our debt-to-equity ratio is directly correlated to the make-up of our portfolio; specifically, the higher percentage of Agency RMBS we hold, the higher our debt-to-equity ratio is, while the higher percentage of non-Agency RMBS, mortgage loans, commercial real estate assets and MSR we hold, the lower our debt-to-equity ratio is. We may alter the percentage allocation of our portfolio among our target assets depending on the relative value of the assets that are available to purchase from time to time, including at times when we are deploying proceeds from common stock offerings we conduct. See the section titled "Management's Discussion and Analysis of Financial Condition and Results of Operations - Financial Condition - Repurchase Agreements" for further discussion.

We recognize that investing in our target assets is competitive and we compete with other entities for attractive investment opportunities. We rely on our management team and our dedicated team of investment professionals provided by our external manager to identify investment opportunities. In addition, we have benefited and expect to continue to benefit from our external manager's analytical and portfolio management expertise and infrastructure. We believe that our significant focus in the mortgage market, the extensive mortgage market expertise of our investment team, our strong analytics and our disciplined relative value investment approach give us a competitive advantage versus our peers.

We have elected to be treated as a REIT for U.S. federal income tax purposes. To qualify as a REIT we are required to meet certain investment and operating tests and annual distribution requirements. We generally will not be subject to U.S. federal income taxes on our taxable income to the extent that we annually distribute all of our net taxable income to stockholders, do not participate in prohibited transactions and maintain our intended qualification as a REIT. However, certain activities that we may perform may cause us to earn income which will not be qualifying income for REIT purposes. We have designated certain of our subsidiaries as taxable REIT subsidiaries, or TRSs, as defined in the Code, to engage in such activities, and we may form additional TRSs in the future. We also operate our business in a manner that will permit us to maintain our exemption from registration under the Investment Company Act of 1940, as amended, or the 1940 Act. While we do not currently originate or service residential mortgage loans, certain of our subsidiaries have obtained the requisite licenses and approvals to purchase and sell residential mortgage loans in the secondary market and to own and manage MSR. Additionally, certain of our subsidiaries are licensed to originate commercial real estate loans.

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains, or incorporates by reference, not only historical information, but also forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, or the Securities Act, and Section 21E of the Securities Exchange Act of 1934, or the Exchange Act, and that are subject to the safe harbors created by such sections. Forward-looking statements involve numerous risks and uncertainties. Our

actual results may differ from our beliefs, expectations, estimates, and projections and, consequently, you should not rely on these forward-looking statements as predictions of future events. Forward-looking statements are not historical in nature and can be identified by words such as "anticipate," "estimate," "will," "should," "expect," "target," "believe," "inten "plan," "goals," "future," "likely," "may" and similar expressions or their negative forms, or by references to strategy, plans, or intentions. These forward-looking statements are subject to risks and uncertainties, including, among other things, those described in our Annual Report on Form 10-K for the year ended December 31, 2015, under the caption "Risk Factors." Other risks, uncertainties and factors that could cause actual results to differ materially from those projected are described below and may be described from time to time in reports we file with the Securities and Exchange Commission, or SEC, including our Quarterly Reports on Form 10-Q and Current Reports on Form 8-K. Forward-looking statements speak only as of the date they are made, and we undertake no obligation to update or revise any such forward-looking statements, whether as a result of new information, future events, or otherwise.

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Important factors, among others, that may affect our actual results include:

- changes in interest rates and the market value of our target assets;
- changes in prepayment rates of mortgages underlying our target assets;
- the occurrence, extent and timing of credit losses within our portfolio;
- our exposure to adjustable-rate and negative amortization mortgage loans underlying our target assets;
- the state of the credit markets and other general economic conditions, particularly as they affect the price of earning assets and the credit status of borrowers;
- the concentration of the credit risks to which we are exposed;
- legislative and regulatory actions affecting our business;
- the availability and cost of our target assets;
- the availability and cost of financing for our target assets, including repurchase agreement financing, lines of credit, revolving credit facilities and financing through the FHLB;
- declines in home prices;
- increases in payment delinquencies and defaults on the mortgages comprising and underlying our target assets;
- changes in liquidity in the market for real estate securities, the re-pricing of credit risk in the capital markets, inaccurate ratings of securities by rating agencies, rating agency downgrades of securities, and increases in the supply of real estate securities available-for-sale;
- changes in the values of securities we own and the impact of adjustments reflecting those changes on our condensed consolidated statements of comprehensive income (loss) and balance sheets, including our stockholders' equity;
- our ability to generate cash flow from our target assets;
- changes in our investment, financing and hedging strategies and the new risks to which those changes may expose us;
- changes in the competitive landscape within our industry, including changes that may affect our ability to attract and retain personnel;
- our decision to discontinue our mortgage loan conduit and securitization business, and our ability to sell our remaining mortgage loans;
- our exposure to legal and regulatory claims, penalties or enforcement activities, including those arising from our involvement in securitization transactions and ownership and management of MSR;
- our exposure to counterparties involved in our mortgage loan conduit and MSR businesses and our ability to enforce representations and warranties made by them;
- our ability to acquire MSR and successfully operate our seller-servicer subsidiary and oversee the activities of our subservicers;
- the state of commercial real estate markets, including the demand for commercial loans;
- our ability to acquire commercial real estate assets, and to originate commercial loans;
- our ability to successfully diversify our business into new asset classes, and manage the new risks to which they may expose us;
- our ability to manage various operational and regulatory risks associated with our business;
- interruptions in or impairments to our communications and information technology systems;
- our ability to maintain appropriate internal controls over financial reporting;
- our ability to establish, adjust and maintain appropriate hedges for the risks in our portfolio;
- our ability to maintain our REIT qualification for U.S. federal income tax purposes; and
- limitations imposed on our business due to our REIT status and our status as exempt from registration under the 1940 Act.

This Quarterly Report on Form 10-Q may contain statistics and other data that, in some cases, have been obtained or compiled from information made available by mortgage loan servicers and other third-party service providers.

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Factors Affecting our Operating Results

Our net interest income includes income from our RMBS portfolio, including the amortization of purchase premiums and accretion of purchase discounts, and income from our residential mortgage loans and commercial real estate assets. Net interest income, as well as our servicing income, net of subservicing expenses, will fluctuate primarily as a result of changes in market interest rates, our financing costs, and prepayment speeds on our assets. Interest rates, financing costs and prepayment rates vary according to the type of investment, conditions in the financial markets, competition and other factors, none of which can be predicted with any certainty. Our operating results will also be affected by default rates and credit losses with respect to the mortgage loans underlying our non-Agency RMBS and in our residential mortgage loan and commercial real estate portfolios.

Fair Value Measurement

A significant portion of our assets and liabilities are reported at fair value and, therefore, our condensed consolidated balance sheets and statements of comprehensive income (loss) are significantly affected by fluctuations in market prices. At September 30, 2016, approximately 88.5% of total assets, or $19.3 billion, and approximately 18.6% of total liabilities, or $3.4 billion, consisted of financial instruments recorded at fair value. See Note 14 - Fair Value to the condensed consolidated financial statements, included in this Quarterly Report on Form 10-Q, for descriptions of valuation methodologies used to measure material assets and liabilities at fair value and details of the valuation models, key inputs to those models and significant assumptions utilized. Although we execute various hedging strategies to mitigate our exposure to changes in fair value, we cannot fully eliminate our exposure to volatility caused by fluctuations in market prices. Although markets for asset-backed securities, including RMBS, have modestly stabilized since the severe dislocations experienced as a result of the financial crisis, these markets continue to experience volatility and, as a result, our assets and liabilities will be subject to valuation adjustment as well as changes in the inputs we use to measure fair value.

Any temporary change in the fair value of our available-for-sale, or AFS, securities, excluding Agency interest-only mortgage-backed securities and GSE credit risk transfer securities, is recorded as a component of accumulated other comprehensive income and does not impact our earnings. Our reported earnings (loss) for U.S. GAAP purposes, or GAAP net income (loss), is affected, however, by fluctuations in market prices on the remainder of our financial assets and liabilities recorded at fair value. For the three and nine months ended September 30, 2016, our unrealized fair value gains on interest rate swap and swaption agreements, which are accounted for as derivative trading instruments under U.S. GAAP, positively affected our financial results. The change in fair value of interest rate swaps was a result of changes to LIBOR, the swap curve and corresponding counterparty borrowing rates during the three and nine months ended September 30, 2016. Our financial results for the three months ended September 30, 2016 were negatively affected by unrealized fair value losses on Agency interest-only mortgage-backed securities and GSE credit risk transfer securities and residential mortgage loans held-for-sale, and positively affected by unrealized fair value gains on net economic interests in consolidated securitization trusts and MSR. Our financial results for the nine months ended September 30, 2016 were positively affected by unrealized fair value gains on Agency interest-only mortgage-backed securities and GSE credit risk transfer securities and residential mortgage loans held-for-sale, and negatively affected by unrealized fair value losses on net economic interests in consolidated securitization trusts and MSR.

For the three and nine months ended September 30, 2015, our unrealized fair value losses on interest rate swap and swaption agreements negatively affected our financial results. The change in fair value of the interest rate swaps was a result of changes to LIBOR, the swap curve and corresponding counterparty borrowing rates during the three and nine months ended September 30, 2015. Our financial results for the three and nine months ended September 30, 2015 were negatively affected by unrealized fair value losses on Agency interest-only mortgage-backed securities and GSE credit risk transfer securities and MSR. For the three months ended September 30, 2015, our financial results were positively affected by unrealized fair value gains on residential mortgage loans held-for-sale and net economic interests in consolidated securitization trusts. Our financial results for the nine months ended September 30, 2015

were negatively affected by unrealized fair value losses on residential mortgage loans held-for-sale and net economic interests in consolidated securitization trusts.
In addition, our financial results for the three and nine months ended September 30, 2016 and 2015 were affected by the unrealized gains and losses of certain other derivative instruments that were accounted for as trading derivative instruments (i.e., credit default swaps, TBAs, short U.S. Treasuries, put and call options for TBAs and U.S. Treasuries, constant maturity swaps, Markit IOS total return swaps, inverse interest-only securities and forward residential mortgage loan purchase commitments).

We have numerous internal controls in place to help ensure the appropriateness of fair value measurements. Significant fair value measures are subject to detailed analytics and management review and approval. Our entire investment portfolio reported at fair value is priced by third-party brokers and/or by independent pricing providers. We generally receive three or more broker and vendor quotes on pass-through Agency RMBS, and generally receive multiple broker or vendor quotes on all other RMBS instruments, including interest-only Agency RMBS, inverse interest-only Agency RMBS, and non-Agency RMBS. We also typically receive two vendor quotes for the residential mortgage loans and MSR in our investment portfolio. For Agency RMBS, the third-party pricing providers and brokers use pricing models that commonly incorporate such factors as coupons, primary and secondary mortgage rates, rate reset period, issuer, prepayment speeds, credit enhancements and expected life of the security. For non-Agency RMBS, the third-party pricing providers and brokers utilize both observable and unobservable inputs such as pool specific characteristics (i.e., loan age, loan size, credit quality of borrowers, vintage, servicer quality), floating rate indices, prepayment and default assumptions, and recent trading of the same or similar securities. For residential mortgage loans and MSR, vendors use pricing models that generally incorporate observable inputs such as principal balance, note rate, geographical location, loan-to-value (LTV) ratios, FICO, appraised value and other loan characteristics, along with observed market yields, securitization economics and trading levels. Additionally for MSR, pricing providers will customarily incorporate loan servicing cost, servicing fee, ancillary income, and earnings rate on escrow as observable inputs. Unobservable or model-driven inputs include forecast cumulative defaults, default curve, forecast loss severity and forecast voluntary prepayment.

We evaluate the prices we receive from both brokers and independent pricing providers by comparing those prices to actual purchase and sale transactions, our internally modeled prices calculated based on market observable rates and credit spreads, and to each other both in current and prior periods. We review and may challenge broker quotes and valuations from third-party pricing providers to ensure that such quotes and valuations are indicative of fair value as a result of this analysis. We then estimate the fair value of each security based upon the median of the final broker quotes received, and we estimate the fair value of residential mortgage loans and MSR based upon the average of prices received from independent providers, subject to internally-established hierarchy and override procedures.

We utilize “bid side” pricing for our RMBS assets and, as a result, certain assets, especially the most recent purchases, may realize a markdown due to the “bid-offer” spread. To the extent that this occurs, any economic effect of this would be reflected in accumulated other comprehensive income.

Considerable judgment is used in forming conclusions and estimating inputs to our Level 3 fair value measurements. Level 3 inputs such as interest rate movements, prepayments speeds, credit losses and discount rates are inherently difficult to estimate. Changes to these inputs can have a significant effect on fair value measurements. Accordingly, there is no assurance that our estimates of fair value are indicative of the amounts that would be realized on the ultimate sale or exchange of these assets.

## Market Conditions and Outlook

The key macroeconomic factors that impact our business are U.S. residential and commercial property prices, national employment rates and the interest rate environment. Home prices increased modestly through the third quarter of 2016 and are expected to gradually appreciate over the next several years. Credit standards remain tight, despite a modest easing in recent months, and have limited borrowers’ ability to refinance their mortgages notwithstanding low interest rates and government programs that promote refinancing. Employment market conditions remain relatively solid as jobless claims, unemployment and payroll data are showing stability, although underemployment levels remain stubbornly high and new job creation has been disappointing. Other than LTV ratios and cash reserves, we believe employment is the most powerful determinant of homeowners’ ongoing likelihood to pay their mortgages. Home price performance and employment are particularly important to our non-Agency portfolio.

The interest rate environment remained volatile in the third quarter of 2016 as a result of domestic economic data and international events. Interest rates decreased at the beginning of the third quarter following Britain’s vote to exit the European Union, and did not experience much improvement throughout the remainder of the quarter. This had the

effect of driving down inflation expectations and dimming the outlook for global growth. The low interest rate environment is expected to persist in the near term, as the Federal Reserve has suggested it will take a measured and conservative approach to future interest rate decisions. Additionally, it appears the Federal Reserve will continue to reinvest its mortgage-backed security principal repayments for the foreseeable future.

The U.S. economy continues to navigate headwinds that include: global economic lethargy, specifically in China; geopolitical unrest across various regions worldwide; the ongoing European debt crisis; quantitative easing by the European Central Bank; and persistently high underemployment.

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Regulatory and legislative actions taken in response to the financial and foreclosure crises continue to impact the market. Regulatory actions that could affect the value and availability of our target assets, either positively or negatively, include: attempts by the U.S. government or the GSEs to establish long-term simplifying changes to the refinancing process to allow more borrowers to refinance into lower interest rate mortgage loans; any new programs or standards established after the expiration of both the Home Affordable Modification Program, or HAMP, and the Home Affordable Refinance Program 2.0, or HARP 2.0, at the end of 2016; the strict “ability-to-repay” and “qualified mortgage” regulations promulgated by the Consumer Financial Protection Bureau, or the CFPB; the compliance with, enforcement of and potential liability associated with the new TILA-RESPA Integrated Disclosure, or TRID, rules recently implemented by the CFPB; and the application of the risk retention requirements of Section 15G of the Exchange Act. Additionally, the implementation of bank capital and liquidity rules could affect both the financing and liquidity of our target assets.

There have also been a number of legislative proposals aimed at eventually winding down or phasing out the GSEs. It remains uncertain as to whether any such proposal will ultimately become legislation, as recent efforts appear to have little momentum in Congress. We will continue to monitor these and other regulatory and policy activities closely.

In January 2016, the FHFA released a final rule regarding membership in the Federal Home Loan Bank system. Among other effects, the final rule excludes captive insurers from membership eligibility, including our subsidiary member, TH Insurance Holdings Company LLC, or TH Insurance. Since TH Insurance was admitted as a member in 2013, it is eligible for a five-year membership grace period, during which new advances or renewals that mature beyond the grace period will be prohibited; however, any existing advances that mature beyond this grace period will be permitted to remain in place subject to their terms insofar as we maintain good standing with the FHLB. If any new advances or renewals occur, TH Insurance’s outstanding advances will be limited to 40% of its total assets. Notwithstanding the FHFA’s ruling, we continue to believe our mission aligns well with that of the Federal Home Loan Bank system.

We believe our blended Agency and non-Agency RMBS portfolio and our investing expertise, as well as our operational capabilities to invest in net economic interests in consolidated securitization trusts, MSR and commercial real estate assets, will allow us to better navigate the dynamic mortgage market while future regulatory and policy activities take shape. Having a diversified portfolio allows us to mitigate a variety of risks, including interest rate and RMBS spread volatility. As such, we have diversified into several target assets that capitalize on our prepayment and credit expertise.

We expect that the majority of our assets will remain in whole-pool Agency RMBS in light of the long-term attractiveness of the asset class and in order to continue to satisfy the requirements of our exemption from registration under the 1940 Act. Interest-only Agency securities and MSR also provide a complementary investment and risk-management strategy to our principal and interest Agency RMBS investments. Risk-adjusted returns in our Agency RMBS portfolio may decline if we are required to pay higher purchase premiums due to lower interest rates or additional liquidity in the market. Additionally, the Federal Reserve’s prior quantitative easing programs and continued reinvestment of its mortgage-backed security principal repayments and other policy changes may impact the returns of our Agency RMBS portfolio.

The following table provides the carrying value of our RMBS portfolio by product type:

| (dollars in thousands) | September 30, 2016 | | December 31, 2015 | |
|---|---|---|---|---|
| Agency | | | | |
| Fixed Rate | $12,404,228 | 86.0% | $5,864,294 | 73.4% |
| Hybrid ARM | 32,588 | 0.2 % | 108,596 | 1.4 % |
| Total Agency | 12,436,816 | 86.2% | 5,972,890 | 74.8% |
| Agency Derivatives | 141,232 | 1.0 % | 157,906 | 2.0 % |
| Non-Agency | | | | |
| Senior | 1,192,975 | 8.3 % | 1,313,695 | |