CHIMERA INVESTMENT CORP
Form 10-Q
November 27, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED: SEPTEMBER 30, 2012

OR

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

FOR THE TRANSITION PERIOD FROM _______________ TO _________________

COMMISSION FILE NUMBER: 1-33796

CHIMERA INVESTMENT CORPORATION
(Exact name of Registrant as specified in its Charter)

MARYLAND	26-0630461
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

1211 AVENUE OF THE AMERICAS, SUITE 2902
NEW YORK, NEW YORK
(Address of principal executive offices)

10036
(Zip Code)

(646) 454-3759
(Registrant's telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all documents and reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days:

Yes o No þ

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 (Section 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 o No þ

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

Large accelerated filer þ	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 Exchange Act).

Yes o No þ

APPLICABLE ONLY TO CORPORATE ISSUERS:

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

Class	Outstanding at November 27, 2013
Common Stock, $.01 par value	1,027,527,549

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Part I. FINANCIAL INFORMATION

Item 1. Consolidated Financial Statements:

CHIMERA INVESTMENT CORPORATION
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
(dollars in thousands, except share and per share data)

	September 30, 2012 (Unaudited)	December 31, 2011 (1)
Assets:		
Cash and cash equivalents	$ 458,107	$ 206,299
Non-Agency RMBS, at fair value		
Senior	82	1,020
Senior interest-only	128,868	188,679
Subordinated	509,061	606,895
Subordinated interest-only	16,867	22,019
Agency RMBS, at fair value	1,997,211	3,144,531
Accrued interest receivable	17,767	22,709
Other assets	13,319	1,403
Subtotal	3,141,282	4,193,555
Assets of Consolidated VIEs:		
Non-Agency RMBS transferred to consolidated variable interest entities ("VIEs"), at fair value	3,235,572	3,270,332
Securitized loans held for investment, net of allowance for loan losses of $11.3 million and $13.9 million, respectively	1,136,923	256,632
Accrued interest receivable	25,215	26,616
Subtotal	4,397,710	3,553,580
Total assets	$ 7,538,992	$ 7,747,135
Liabilities:		
Repurchase agreements, Agency RMBS ($1.7 billion and $2.8 billion pledged as collateral, respectively)	$ 1,658,906	$ 2,672,989
Accrued interest payable	2,434	3,294
Dividends payable	92,416	112,937
Accounts payable and other liabilities	1,289	1,687
Investment management fees and expenses payable to affiliate	11,531	12,958
Interest rate swaps, at fair value	59,073	44,467
Subtotal	1,825,649	2,848,332
Non-Recourse Liabilities of Consolidated VIEs		
Securitized debt, collateralized by Non-Agency RMBS ($3.2 billion and $3.3 billion pledged as collateral, respectively)	1,252,752	1,630,276
Securitized debt, collateralized by loans held for investment ($1.2 billion and $238.0 million pledged as collateral, respectively)	1,033,925	212,778
Accrued interest payable	8,477	8,130
Subtotal	2,295,154	1,851,184
Total liabilities	$ 4,120,803	$ 4,699,516
Commitments and Contingencies (See Note 15)		

Stockholders' Equity:						
Preferred Stock: par value $0.01 per share; 100,000,000 shares authorized, 0 shares issued and outstanding, respectively			-		-	
Common stock: par value $0.01 per share; 1,500,000,000 shares authorized, 1,027,505,028 and 1,027,467,089 shares issued and outstanding, respectively		10,268			10,267	
Additional paid-in-capital		3,604,097			3,603,739	
Accumulated other comprehensive income (loss)		852,357			433,453	
Retained earnings (accumulated deficit)		(1,048,533	)		(999,840	)
Total stockholders' equity	$	3,418,189		$	3,047,619	
Total liabilities and stockholders' equity	$	7,538,992		$	7,747,135	

(1) Derived from the audited consolidated financial statements.

See accompanying notes to consolidated financial statements.

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CHIMERA INVESTMENT CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
(dollars in thousands, except share and per share data)
(unaudited)

	For the Quarter Ended		For the Nine Months Ended	
	September 30, 2012	September 30, 2011	September 30, 2012	September 30, 2011
Net Interest Income:				
Interest income	$ 36,576	$ 68,776	$ 139,926	$ 197,718
Interest expense	(2,281)	(3,149)	(7,080)	(9,160)
Interest income, Assets of consolidated VIEs	108,120	116,805	315,962	339,765
Interest expense, Non-recourse liabilities of consolidated VIEs	(32,075)	(29,643)	(85,604)	(95,002)
Net interest income (expense)	110,340	152,789	363,204	433,321
Other-than-temporary impairments:				
Total other-than-temporary impairment losses	(2,713)	(78,950)	(47,264)	(161,924)
Portion of loss recognized in other comprehensive income (loss)	(7,301)	(71,610)	(76,801)	(83,989)
Net other-than-temporary credit impairment losses	(10,014)	(150,560)	(124,065)	(245,913)
Other gains (losses):				
Net unrealized gains (losses) on interest rate swaps	(4,427)	(25,312)	(14,607)	(34,981)
Net realized gains (losses) on interest rate swaps	(5,298)	(4,500)	(14,890)	(11,644)
Net gains (losses) on interest rate swaps	(9,725)	(29,812)	(29,497)	(46,625)
Net unrealized gains (losses) on interest-only RMBS	(15,393)	(17,600)	22	(1,611)
Net realized gains (losses) on sales of investments	69,155	58	85,165	1,787
Total other gains (losses)	44,037	(47,354)	55,690	(46,449)
Net investment income (loss)	144,363	(45,125)	294,829	140,959
Other expenses:				
Management fees	13,051	13,252	38,863	39,154
Expense recoveries from Manager	(1,910)	-	(1,910)	-
Net Management fees	11,141	13,252	36,953	39,154
Provision for loan losses, net	496	-	(396)	1,442
General and administrative expenses	4,658	1,830	9,188	5,137

Total other expenses	16,295	15,082	45,745	45,733
Income (loss) before income taxes	128,068	(60,207)	249,084	95,226
Income taxes	-	(171)	2	645
Net income (loss)	$ 128,068	$ (60,036)	$ 249,082	$ 94,581
Net income (loss) per share available to common shareholders:				
Basic	$ 0.12	$ (0.06)	$ 0.24	$ 0.09
Diluted	$ 0.12	$ (0.06)	$ 0.24	$ 0.09
Weighted average number of common shares outstanding:				
Basic	1,026,841,087	1,026,404,030	1,026,804,427	1,026,308,073
Diluted	1,027,505,030	1,027,195,404	1,027,499,973	1,027,130,136
Dividends declared per share of common stock	$ 0.09	$ 0.13	$ 0.29	$ 0.40
Comprehensive income (loss):				
Net income (loss)	$ 128,068	$ (60,036)	249,082	$ 94,581
Other comprehensive income (loss):				
Unrealized gains (losses) on available-for-sale securities, net	260,891	(41,863)	380,004	(258,253)
Reclassification adjustment for net losses included in net income (loss) for other-than-temporary credit impairment losses	10,014	150,560	124,065	245,913
Reclassification adjustment for net realized losses (gains) included in net income (loss)	(69,155)	(58)	(85,165)	(1,787)
Other comprehensive income (loss)	201,750	108,639	418,904	(14,127)
Comprehensive income (loss)	$ 329,818	$ 48,603	$ 667,986	$ 80,454

See accompanying notes to consolidated financial statements.

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CHIMERA INVESTMENT CORPORATION
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY (DEFICIT)
(dollars in thousands, except per share data)
(unaudited)

	Common Stock Par Value	Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings (Accumulated Deficit)	Total
Balance, December 31, 2010	$10,261	$3,601,890	$ 680,123	$ (613,688)	$3,678,586
Net income	-	-	-	94,581	94,581
Unrealized gains (losses) on available-for-sale securities, net	-	-	(258,253)	-	(258,253)
Reclassification adjustment for net losses included in net income (loss) for other-than-temporary credit impairment losses	-	-	245,913	-	245,913
Reclassification adjustment for net realized losses (gains) included in net income (loss)	-	-	(1,787)	-	(1,787)
Proceeds from direct purchase and dividend reinvestment	3	783	-	-	786
Proceeds from common stock offerings	-	7	-	-	7
Proceeds from restricted stock grants	-	360	-	-	360
Common dividends declared, $0.40 per share	-	-	-	(410,544)	(410,544)
Balance, September 30, 2011	$10,264	$3,603,040	$ 665,996	$ (929,651)	$3,349,649
Balance, December 31, 2011	$10,267	$3,603,739	$ 433,453	$ (999,840)	$3,047,619
Net income	-	-	-	249,082	249,082
Unrealized gains (losses) on available-for-sale securities, net	-	-	380,004	-	380,004
Reclassification adjustment for net losses included in net income (loss) for other-than-temporary credit impairment losses	-	-	124,065	-	124,065
Reclassification adjustment for net realized losses (gains) included in net income (loss)	-	-	(85,165)	-	(85,165)
Proceeds from direct purchase and dividend reinvestment	1	116	-	-	117
Proceeds from restricted stock grants	-	242	-	-	242
Common dividends declared, $0.29 per share	-	-	-	(297,775)	(297,775)
Balance, September 30, 2012	$10,268	$3,604,097	$ 852,357	$ (1,048,533)	$3,418,189

See accompanying notes to consolidated financial statements.

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CHIMERA INVESTMENT CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(dollars in thousands)

	For the Nine Months Ended	
	September 30, 2012	September 30, 2011
Cash Flows From Operating Activities:		
Net income (loss)	$ 249,082	$ 94,581
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
(Accretion) amortization of investment discounts/premiums, net	(44,745)	(43,420)
Amortization of deferred financing costs	6,480	1,294
Accretion (amortization) of securitized debt discounts/premiums, net	3,469	9,452
Net unrealized losses (gains) on interest rate swaps	14,607	34,981
Net unrealized losses (gains) on interest-only RMBS	(22)	1,611
Net realized losses (gains) on sales of investments	(85,165)	(1,787)
Net other-than-temporary credit impairment losses	124,065	245,913
Provision for loan losses, net	(396)	1,442
Equity-based compensation expense	242	360
Changes in operating assets:		
Decrease (increase) in accrued interest receivable, net	5,459	(6,591)
Decrease (increase) in other assets	952	790
Changes in operating liabilities:		
Increase (decrease) in accounts payable and other liabilities	(398)	1,190
Increase (decrease) in investment management fees and expenses payable to affiliate	(1,427)	995
Increase (decrease) in accrued interest payable, net	(513)	(103)
Net cash provided by (used in) operating activities	271,690	340,708
Cash Flows From Investing Activities:		
RMBS portfolio:		
Purchases	(119,429)	(3,664,513)
Sales	943,350	670,863
Principal payments	549,478	408,030
Non-Agency RMBS transferred to consolidated VIEs:		
Principal payments	394,641	541,348
Securitized loans held for investment:		
Purchases	(1,185,664)	-
Principal payments	297,923	65,347
Net cash provided by (used in) investing activities	880,299	(1,978,925)
Cash Flows From Financing Activities:		
Proceeds from repurchase agreements	5,114,759	12,863,367
Payments on repurchase agreements	(6,128,842)	(10,500,974)
Net proceeds from common stock offerings	-	7
Payment of deferred financing costs	(8,073)	-
Proceeds from securitized debt borrowings, collateralized by loans held for investment	1,113,154	-
	(292,568)	(61,054)

Payments on securitized debt borrowings, collateralized by loans held for investment				
Proceeds from securitized debt borrowings, collateralized by Non-Agency RMBS		-		311,012
Payments on securitized debt borrowings, collateralized by Non-Agency RMBS		(380,432)		(520,730)
Net proceeds from direct purchase and dividend reinvestment		117		786
Common dividends paid		(318,296)		(451,546)
Net cash provided by (used in) financing activities		(900,181)		1,640,868
Net increase (decrease) in cash and cash equivalents		251,808		2,651
Cash and cash equivalents at beginning of period		206,299		7,173
Cash and cash equivalents at end of period	$	458,107	$	9,824

Supplemental disclosure of cash flow information:				
Interest received	$	417,513	$	485,314
Interest paid	$	89,717	$	93,952
Taxes paid	$	-	$	3
Management fees and expenses paid to affiliate	$	40,290	$	38,640
Non-cash investing activities:				
Net change in unrealized gain (loss) on available-for sale securities	$	418,904	$	(14,127)
Non-cash financing activities:				
Common dividends declared, not yet paid	$	92,416	$	133,443

See accompanying notes to consolidated financial statements.

CHIMERA INVESTMENT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Organization

Chimera Investment Corporation (the “Company”) was organized in Maryland on June 1, 2007. The Company commenced operations on November 21, 2007 when it completed its initial public offering. The Company elected to be taxed as a real estate investment trust (“REIT”) under the Internal Revenue Code of 1986, as amended, and regulations promulgated thereunder (the "Code"). The Company formed the following wholly-owned qualified REIT subsidiaries: Chimera Securities Holdings, LLC in July 2008; Chimera Asset Holding LLC and Chimera Holding LLC in June 2009; and Chimera Special Holding LLC in January 2010 which is a wholly-owned subsidiary of Chimera Asset Holding LLC. In July 2010, the Company formed CIM Trading Company LLC, a wholly-owned taxable REIT subsidiary (“TRS”).

Annaly Capital Management, Inc. (“Annaly”) owns approximately 4.38% of the Company’s common shares. The Company is managed by Fixed Income Discount Advisory Company (“FIDAC”), an investment advisor registered with the Securities and Exchange Commission (“SEC”). FIDAC is a wholly-owned subsidiary of Annaly.

2. Summary of the Significant Accounting Policies

Restatement

The Company restated its previously issued (i) Consolidated Statement of Financial Condition included in its Annual Report on Form 10-K as of December 31, 2010 and (ii) Consolidated Statements of Operations and Comprehensive Income, Consolidated Statements of Changes in Stockholders’ Equity, and Consolidated Statements of Cash Flows for the years ended December 31, 2010 and 2009, including the cumulative effect of the Restatement on Retained Earnings (Accumulated Deficit) as of the earliest period presented (the “Restatement”) as part of its Form 10-K for the year ended December 31, 2011. The Restatement also impacted each of the quarters for the periods beginning with the Company’s inception in November 2007 through the quarter ended September 30, 2011. The historical interim periods included in this Form 10-Q reflect the Restatement.

Immaterial Restatement

The Company corrected amounts previously reported in Total other-than-temporary impairments (“OTTI”) losses and the Portion of loss recognized in other comprehensive income (loss) in the Consolidated Statements of Operations and Comprehensive Income as the previous presentation was reported on a cumulative basis. The current presentation reflects only that portion of Total other-than-temporary impairments loss and the Portion of loss recognized in other comprehensive income (loss) that is incremental for the reporting period by giving consideration to both the credit and portions of OTTI reported in Other comprehensive income (loss) and recognized in prior periods. For the three and nine month periods ended September 30, 2011, the previously reported Total other-than-temporary impairments losses of $151.3 million and $293.9 million was reduced by $72.4 million and $132.0 million, respectively. This change was fully offset by an adjustment to the previously reported Portion of loss recognized in other comprehensive income (loss) of $728 thousand and $48.0 million, respectively. The corrections had no impact on any previously reported Net other-than-temporary credit impairment losses, Net income (loss), Other comprehensive income (loss), Net income (loss) per share available to common shareholders or Consolidated Statements of Cash Flows.

(a) Basis of Presentation and Consolidation

The accompanying consolidated financial statements and related notes of the Company have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP"). In the opinion of management, all adjustments considered necessary for a fair presentation of the Company's financial position, results of operations and cash flows have been included. The accompanying unaudited consolidated interim financial statements should be read in conjunction with the consolidated financial statements and the related management's discussion and analysis of financial condition and results of operations filed with our Annual Report on Form 10-K for the fiscal year ended December 31, 2011.

The consolidated financial statements include, on a consolidated basis, the Company's accounts, the accounts of its wholly-owned subsidiaries, and variable interest entities ("VIEs") in which the Company is the primary beneficiary. All significant intercompany balances and transactions have been eliminated in consolidation.

VIEs are defined as entities in which equity investors (i) do not have the characteristics of a controlling financial interest, and/or (ii) do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. The entity that consolidates a VIE is known as its primary beneficiary, and is generally the entity with (i) the power to direct the activities that most significantly impact the VIE's economic performance, and (ii) the right to receive benefits from the VIE or the obligation to absorb losses of the VIE that could be significant to the VIE. For VIEs that do not have substantial on going activities, the power to direct the activities that most significantly impact the VIEs' economic performance may be determined by an entity's involvement with the design and structure of the VIE.

The Company uses securitization trusts considered to be VIEs in its securitization and re-securitization transactions. Prior to January 1, 2010, these VIEs met the definition of Qualified Special Purpose Entities ("QSPE") and, as such, were not subject to consolidation by the Company. Effective January 1, 2010, all such VIEs were considered for consolidation based on the criteria in ASC 810, Consolidation, resulting in the consolidation of certain VIEs that were not previously consolidated. Non-Agency RMBS transferred to consolidated VIEs are composed entirely of senior certificates.

(b) Statement of Financial Condition Presentation

The Company's consolidated statements of financial condition separately present: (i) the Company's direct assets and liabilities, and (ii) the assets and liabilities of consolidated securitization vehicles. Assets of each consolidated VIE can only be used to satisfy the obligations of that VIE, and the liabilities of consolidated VIEs are non-recourse to the Company.

The Company has aggregated all the assets and liabilities of the consolidated securitization vehicles due to the determination that these entities are substantively similar and therefore a further disaggregated presentation would not be more meaningful. The notes to the consolidated financial statements describe the Company's direct assets and liabilities and the assets and liabilities of consolidated securitization vehicles. See Note 8 for additional information related to the Company's investments in consolidated securitization vehicles.

(c) Cash and Cash Equivalents

Cash and cash equivalents include cash on hand and cash deposited overnight in money market funds, which are not bank deposits and are not insured or guaranteed by the Federal Deposit Insurance Corporation. There were no restrictions on cash and cash equivalents at September 30, 2012 and December 31, 2011.

(d) Agency and Non-Agency Residential Mortgage-Backed Securities

The Company invests in residential mortgage-backed securities ("RMBS") representing interests in obligations backed by pools of mortgage loans. The Company delineates between (1) Agency RMBS and (2) Non-Agency RMBS as follows: Agency RMBS are mortgage pass-through certificates, collateralized mortgage obligations ("CMOs"), and other RMBS representing interests in or obligations backed by pools of mortgage loans issued or guaranteed by agencies of the U.S. Government, such as Ginnie Mae, or federally chartered corporations such as Freddie Mac or Fannie Mae where principal and interest repayments are guaranteed by the respective agency of the U.S. Government or federally chartered corporation. Non-Agency RMBS are not issued or guaranteed by a U.S. Government Agency or other institution and are subject to credit risk. Repayment of principal and interest on Non-Agency RMBS is subject to the performance of the mortgage loans or RMBS collateralizing the obligation.

The Company classifies its RMBS as available-for-sale, records investments at estimated fair value as described in Note 5 of these consolidated financial statements, and includes unrealized gains and losses considered to be temporary on all RMBS, excluding interest-only strips, in other comprehensive income (loss) in the Consolidated Statements of Operations and Comprehensive Income. Interest-only strips are recorded at estimated fair value and all unrealized gains and losses are included in earnings in the Consolidated Statements of Operations and Comprehensive Income. From time to time, as part of the overall management of its portfolio, the Company may sell any of its RMBS investments and recognize a realized gain or loss as a component of earnings in the Consolidated Statements of Operations and Comprehensive Income utilizing the average cost method.

The Company's accounting policy for interest income and impairment related to its RMBS is as follows:

Interest Income Recognition

The recognition of interest income on RMBS securities varies depending on the characteristics of the security as follows:

Agency RMBS and Non-Agency RMBS of High Credit Quality

ASC 310-20, Nonrefundable Fees and Other Costs ("ASC 310-20") is applied to the recognition of interest income for the following securities:

- Agency RMBS
- Non-Agency RMBS that meet all of the following conditions at the acquisition date (referred to hereafter as "Non-Agency RMBS of High Credit Quality"):

1. Rated AA or higher by a nationally recognized credit rating agency. The Company uses the lowest rating available.
2. The Company expects to collect all of the security's contractual cash flows.
3. The security cannot be contractually prepaid such that the Company would not recover substantially all of its recorded investment.

Under ASC 310-20, interest income, including premiums and discounts associated with the acquisition of these securities, is recognized over the life of such securities using the interest method based on the contractual cash flows of the security. In applying the interest method, the Company considers estimates of future principal prepayments in the calculation of the constant effective yield. Differences that arise between previously anticipated prepayments and actual prepayments received, as well as changes in future prepayment assumptions, result in a recalculation of the effective yield on the security on a quarterly basis. This recalculation results in the recognition of an adjustment to the carrying amount of the security based on the revised prepayment assumptions and a corresponding increase or decrease in reported interest income.

Non-Agency RMBS Not of High Credit Quality

Non-Agency RMBS that are purchased at a discount and that are not of high credit quality at the time of purchase are accounted for under ASC 310-30, Loans and Debt Securities Acquired with Deteriorated Credit Quality ("ASC 310-30") or ASC 325-40, Beneficial Interests in Securitized Financial Assets ("ASC 325-40") (referred to hereafter as "Non-Agency RMBS Not of High Credit Quality").

Non-Agency RMBS are accounted for under ASC 310-30 if the following conditions are met as of the acquisition date:

1. There is evidence of deterioration in credit quality of the security from its inception.
2. It is probable that the Company will be unable to collect all contractual cash flows of the security.

Non-Agency RMBS that are not within the scope of ASC 310-30 are accounted for under ASC 325-40 if at the acquisition date:

1. The security is not of high credit quality (defined as rated below AA or is unrated), or
2. The security can contractually be prepaid or otherwise settled in such a way that the Company would not recover substantially all of its recorded investment.

Interest income on Non-Agency RMBS Not of High Credit Quality is recognized using the interest method based on management's estimates of cash flows expected to be collected. The effective interest rate on these securities is based on management's estimate for each security of the projected cash flows, which are estimated based on observation of current market information and include assumptions related to fluctuations in prepayment speeds and the timing and amount of credit losses. Quarterly, the Company reviews and, if appropriate, makes adjustments to its cash flow projections based on inputs and analyses received from external sources, internal models, and the Company's judgments about prepayment rates, the timing and amount of credit losses, and other factors. Changes in the amount and/or timing of cash flows from those originally projected, or from those estimated at the last evaluation date, are considered to be either positive changes or adverse changes. For securities accounted for under ASC 325-40, any positive or adverse change in cash flows that does not result in the recognition of an other-than-temporary impairment results in a prospective increase or decrease in the effective interest rate used to recognize interest income. For securities accounted for under ASC 310-30, only significant positive changes are reflected prospectively in the effective interest rate used to recognize interest income. Adverse changes in cash flows expected to be collected are generally treated consistently for RMBS accounted for under ASC 325-40 and ASC 310-30, and generally result in recognition of an other-than-temporary impairment with no change in the effective interest rate used to recognize interest income.

Impairment

Considerations Applicable to all RMBS

When the fair value of an available-for-sale RMBS is less than its amortized cost the security is considered impaired. On at least a quarterly basis the Company evaluates its securities for OTTI. If the Company intends to sell an impaired security, or it is more-likely-than-not that the Company will be required to sell an impaired security before its anticipated recovery, then the Company must recognize an OTTI through a charge to earnings equal to the entire difference between the investment's amortized cost and its fair value at the measurement date. If the Company does not intend to sell an impaired security and it is not more-likely-than-not that it would be required to sell an impaired security before recovery, the Company must further evaluate the security for impairment due to credit losses. The credit component of OTTI is recognized in earnings and the remaining or non-credit component is recorded as a component of OCI. Following the recognition of an OTTI through earnings, a new amortized cost basis is established for the security and subsequent recoveries in fair value may not be adjusted through earnings.

When evaluating whether the Company intends to sell an impaired security or will more-likely-than-not be required to sell an impaired security before recovery, the Company makes judgments that consider among other things, its liquidity, leverage, contractual obligations, and targeted investment strategy to determine its intent and ability to hold the investments that are deemed impaired. The determination as to whether an OTTI exists is subjective as such determinations are based on factual information available at the time of assessment as well as the Company's estimates of future conditions. As a result, the determination of OTTI, its timing and amount, is based on estimates that may change materially over time.

The Company's estimate of the amount and timing of cash flows for its RMBS is based on its review of the underlying securities or mortgage loans securing the RMBS. The Company considers historical information available and expected future performance of the underlying securities or mortgage loans, including timing of expected future cash flows, prepayment rates, default rates, loss severities, delinquency rates, percentage of non-performing loans, extent of credit support available, Fair Isaac Corporation ("FICO") scores at loan origination, year of origination, loan-to-value ratios, geographic concentrations, as well as reports by credit rating agencies, such as Moody's Investors Service, Inc., Standard & Poor's Rating Services or Fitch Ratings, Inc., general market assessments and dialogue with market participants. As a result, substantial judgment is used in the Company's analysis to determine the expected cash flows for its RMBS.

Considerations Applicable to Non-Agency RMBS of High Credit Quality

The impairment assessment for Non-Agency RMBS of High Credit Quality involves comparing the present value of the remaining cash flows expected to be collected to the amortized cost of the security at the assessment date. The discount rate used to calculate the present value of the expected future cash flows is based on the security's effective interest rate as calculated under ASC 310-20 (i.e., the discount rate implicit in the security as of the last measurement date). If the present value of the remaining cash flows expected to be collected is less than the amortized cost basis, an OTTI is recognized in earnings for the difference. This amount is considered to be the credit loss component; the remaining difference between amortized cost and the fair value of the security is considered to be the portion of loss recognized in other comprehensive income (loss).

Following the recognition of an OTTI through earnings for the credit loss component, a new amortized cost basis is established for the security and subsequent recoveries in fair value may not be adjusted through earnings.

Considerations Applicable to Non-Agency RMBS Not of High Credit Quality

Non-Agency RMBS within the scope of ASC 325-40 or ASC 310-30 are considered other-than-temporarily impaired when the following two conditions exist: (1) the fair value is less than the amortized cost basis, and (2) there has been an adverse change in cash flows expected to be collected from the last measurement date (i.e., adverse changes in either the amount or timing of cash flows from those previously expected).

The other-than-temporary impairment is separated into a credit loss component that is recognized in earnings and the portion of loss recognized in other comprehensive income (loss). The credit component is comprised of the impact of the fair value decline due to changes in assumptions related to default (collection) risk and prepayments. The portion of loss recognized in other comprehensive income (loss) comprises the change in fair value of the security due to all other factors, including changes in benchmark interest rates and market liquidity. In determining the OTTI related to credit losses for securities, the Company compares the present value of the remaining cash flows adjusted for prepayments expected to be collected at the current financial reporting date to the present value of the remaining cash flows expected to be collected at the original purchase date (or the last date those estimates were revised for accounting purposes). The discount rate used to calculate the present value of expected future cash flows is the effective interest rate used for income recognition purposes as determined under ASC 325-40 or ASC 310-30.

Following the recognition of an OTTI through earnings for the credit component, a new amortized cost basis is established for the security and subsequent recoveries in fair value may not be adjusted through earnings. However, to the extent that there are subsequent increases in cash flows expected to be collected, the OTTI previously recorded through earnings may be accreted into interest income following the guidance in ASC 325-40 or ASC 310-30.

The determination of whether an OTTI exists and, if so, the extent of the credit component is subject to significant judgment and management's estimates of both historical information available at the time of assessment, the current market environment, as well as the Company's estimates of the future performance and projected amount and timing of cash flows expected to be collected on the security. As a result, the timing and amount of OTTI constitutes an accounting estimate that may change materially over time.

(e) Interest-Only RMBS

The Company invests in interest-only ("IO") Agency and Non-Agency RMBS. IO RMBS represent the Company's right to receive a specified proportion of the contractual interest flows of the collateral. The Company has accounted for IO RMBS at fair value with changes in fair value recognized in the Company's Consolidated Statements of Operations and Comprehensive Income. The Company has elected the fair value option to account for IO RMBS to simplify the reporting of changes in fair value. The IO RMBS are included in RMBS, at fair value, on the accompanying Consolidated Statements of Financial Condition. Coupon income on IO RMBS is accrued based on the outstanding notional balance and the security's contractual terms, and amortization is computed in accordance with ASC 325-40. Changes in fair value are presented in Net unrealized gains (losses) on interest-only RMBS on the Consolidated Statement of Operations and Comprehensive Income. Interest income reported on IO securities was $5.0 million and $6.2 million for the quarters ended September 30, 2012 and September 30, 2011, respectively. Interest income reported on IO securities was $18.8 million and $20.5 million for the nine months ended September 30, 2012 and September 30, 2011, respectively.

(f) Securitized Loans Held for Investment and Related Allowance for Loan Losses

The Company's securitized residential mortgage loans are comprised of fixed-rate and variable-rate loans. Mortgage loans are designated as held for investment, and are carried at their principal balance outstanding, plus any premiums, less discounts and allowances for loan losses. Interest income on loans held for investment is recognized over the expected life of the loans using the interest method. Income recognition is suspended for loans when, based on information from the servicer, a full recovery of income and principal becomes doubtful. Income recognition is resumed when the loan becomes contractually current and performance is demonstrated to be resumed. The Company estimates the fair value of securitized loans for disclosure purposes only as described in Note 5 of these consolidated financial statements.

(g) Allowance for Loan Losses – Securitized Loans Held for Investment

The securitized loan portfolio is comprised primarily of non-conforming, single family, owner occupied, jumbo, prime loans that are not guaranteed as to repayment of principal or interest. Securitized loans are serviced and modified by a third-party servicer. The Company is not involved in the loan modification process, except as it relates to the CSMC 2012-CIM1 and CSMC 2012-CIM2 securitization vehicles consolidated by the Company that are collateralized by residential mortgage loans. As it relates solely to CSMC 2012-CIM1 and CSMC 2012-CIM2, the Company has the ability to approve certain loan modifications and determine the course of action to be taken as it relates to loans in technical default, including whether or not to proceed with foreclosure.

The Company has established an allowance for loan losses related to securitized loans that is composed of a general and specific reserve. The general reserve relates to loans that have not been individually evaluated for impairment and is accounted for under ASC 450, Contingencies. The general reserve is based on historical loss rates for pools of loans with similar credit characteristics, adjusted for current trends and conditions.

Certain loans are individually evaluated for impairment, including securitized loans modified by the servicer and loans more than 60 days delinquent under ASC 310, Receivables. Loan modifications made by the servicer are evaluated to determine if they constitute troubled debt restructurings (“TDRs”). A restructuring of a loan constitutes a TDR if the servicer, for economic or legal reasons related to the borrower's financial difficulties, grants a concession to the borrower that it would not otherwise consider. Impairment of modified loans considered to be TDRs is measured based on the present value of expected cash flows discounted at the loan’s effective interest rate at inception. If the present value of expected cash flows is less than the recorded investment in the loan, an allowance for loan losses is recognized with a corresponding charge to provision for loan losses. Impairment of all other loans individually evaluated is measured as the difference between the unpaid principal balance and the estimated fair value of the collateral, less estimated costs to sell. The Company charges off the corresponding loan allowance and related principal balance when the servicer reports a realized loss. A complete discussion of securitized loans held for investment is included in Note 4 to these financial statements.

(h) Repurchase Agreements

The Company finances the acquisition of a significant portion of its Agency mortgage-backed securities with repurchase agreements. The Company examines each of the specified criteria in ASC 860, Transfers and Servicing (“ASC 860”), at the inception of each transaction and has determined that each of the Company’s repurchase agreements meet the specified criteria in this guidance to be accounted for as secured borrowings. None of the Company’s repurchase agreements are accounted for as components of linked transactions. As a result, the Company separately accounts for the financial assets posted as collateral and related repurchase agreements in the accompanying consolidated financial statements.

(i) Securitized Debt, Non-Agency RMBS Transferred to Consolidated VIEs, and Securitized Debt, Loans Held for Investment

The Company has issued securitized debt to finance a portion of its residential mortgage loan and RMBS portfolios. Certain transactions involving residential mortgage loans are accounted for as secured borrowings, and are recorded as “Securitized loans held for investment” and the corresponding debt as “Securitized debt, loans held for investment” in the Consolidated Statements of Financial Condition. These securitizations are collateralized by residential adjustable or fixed rate mortgage loans that have been placed in a trust and pay interest and principal to the debt holders of that securitization. Re-securitization transactions classified as “Securitized debt, Non-Agency RMBS transferred to consolidated VIEs” reflect the transfer to a trust of fixed or adjustable rate RMBS which are classified as “Non-Agency RMBS transferred to consolidated VIEs” that pay interest and principal to the debt holders of that re-securitization. Re-securitization transactions completed by the Company that did not qualify as sales are accounted for as secured borrowings pursuant to ASC 860. For the nine months ended September 30, 2012, the Company did not have any continuing involvement, other than as a passive investor, with any loans or securities previously sold, except as it relates to the loans in the CSMC 2012-CIM1 and CSMC 2012-CIM2 securitizations as further described above. The holders of securitized debt have no recourse to the Company and the Company does not receive any interest or principal paid on such debt. As of September 30, 2012 and December 31, 2011 the Company recorded $2.3 billion and $1.9 billion in principal on securitized debt and accrued interest payable, respectively. The associated securitized debt is carried at amortized cost. The Company estimates the fair value of its securitized debt for disclosure purposes as described in Note 5 to these consolidated financial statements.

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(j) Fair Value Disclosure

A complete discussion of the methodology utilized by the Company to estimate the fair value of its financial instruments is included in Note 5 to these consolidated financial statements.

(k) Derivative Financial Instruments

The Company's policies permit it to enter into derivative contracts, including interest rate swaps and interest rate caps, as a means of managing its interest rate risk. The Company intends to use interest rate derivative instruments to manage interest rate risk rather than to enhance returns. Interest rate swaps are recorded as either assets or liabilities in the Consolidated Statements of Financial Condition and measured at fair value. Net payments on interest rate swaps are included in the Consolidated Statements of Cash Flows as a component of net income (loss). Unrealized gains (losses) on interest rate swaps are removed from net income (loss) to arrive at cash flows from operating activities. The Company estimates the fair value of interest rate swaps as described in Note 5 of these consolidated financial statements.

The Company elects to net by counterparty the fair value of interest rate swap contracts. These contracts contain legally enforceable provisions that allow for netting or setting off of all individual swaps receivable and payable with each counterparty and, therefore, the fair value of those swap contracts are reported net by counterparty. The credit support annex provisions of the Company's interest rate swap contracts allow the parties to mitigate their credit risk by requiring the party which is in a net payable position to post collateral. As the Company elects to net by counterparty the fair value of interest rate swap contracts, it also nets by counterparty any collateral exchanged as part of the interest rate swap contracts.

(l) Sales, Securitizations, and Re-Securitizations

The Company periodically enters into transactions in which it sells financial assets, such as RMBS, and mortgage loans. Gains and losses on sales of assets are computed on the average cost method whereby the Company records a gain or loss on the difference between the average value of the asset and the proceeds from the sale. In addition, the Company from time to time securitizes or re-securitizes assets and sells tranches in the newly securitized assets. These transactions may be recorded as either sales and the assets contributed to the securitization are removed from the Consolidated Statements of Financial Condition and a gain or loss is recognized, or as secured borrowings whereby the assets contributed to the securitization are not derecognized but rather the debt issued by the securitization are recorded to reflect the term financing of the assets. In these securitizations and re-securitizations, the Company may retain senior or subordinated interests in the securitized and/or re-securitized assets.

(m) Income Taxes

The Company has elected to be taxed as a REIT and intends to comply with provision of the Code, with respect thereto. Accordingly, the Company will not be subject to federal, state or local income tax to the extent that qualifying distributions are made to stockholders and as long as certain asset, income and stock ownership tests are met. If the Company failed to qualify as a REIT and did not qualify for certain statutory relief provisions, the Company would be subject to federal, state and local income taxes and may be precluded from qualifying as a REIT for the subsequent four taxable years following the year in which the REIT qualification was lost. The Company and CIM Trading made a joint election to treat CIM Trading as a TRS. As such, CIM Trading is taxable as a domestic C corporation and subject to federal, state, and local income taxes based upon its taxable income.

The provisions of ASC 740, Income Taxes ("ASC 740"), clarify the accounting for uncertainty in income taxes recognized in financial statements and prescribe a recognition threshold and measurement attribute for tax positions taken or expected to be taken on a tax return. The Company does not have any unrecognized tax benefits that would affect its financial position. The Company has not taken any tax positions that would require disclosure under ASC 740. No accruals for penalties and interest were necessary as of September 30, 2012 or December 31, 2011.

(n) Net Income per Share

The Company calculates basic net income per share by dividing net income for the period by the basic weighted-average shares of its common stock outstanding for that period. Diluted net income per share takes into account the effect of dilutive instruments, such as unvested restricted stock, but uses the average share price for the period in determining the number of incremental shares that are to be added to the diluted weighted average number of shares outstanding.

(o) Stock-Based Compensation

The Company accounts for stock-based compensation awards granted to the employees of FIDAC and FIDAC's affiliates in accordance with ASC 505-50, Equity-Based Payments to Non-Employees ("ASC 505-50"). Pursuant to ASC 505-50 the Company measures the fair value of the equity instrument using the stock prices and other measurement assumptions as of the earlier of either the date at which a performance commitment by the recipient is reached or the date at which the recipient's performance is complete. Compensation expense related to the grants of stock is recognized over the vesting period of such grants based on the fair value of the stock on each quarterly vesting date, at which the recipient's performance is complete.

The Company accounts for stock-based compensation awards granted to the Company's independent directors in accordance with ASC 718, Compensation – Stock Compensation ("ASC 718"). Compensation expense for equity based awards granted to the Company's independent directors is recognized pro-rata over the vesting period of such awards, based upon the fair value of such awards at the grant date.

(p) Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although the Company's estimates contemplate current conditions and how it expects them to change in the future, it is reasonably possible that actual conditions could be materially different than anticipated in those estimates, which could have a material adverse impact on the Company's results of operations and its financial condition. Management has made significant estimates in accounting for income recognition and OTTI on Agency and Non-Agency RMBS and IO RMBS (Note 3), valuation of Agency and Non-Agency RMBS (Notes 3 and 5), and interest rate swaps (Notes 5 and 9). Actual results could differ materially from those estimates.

(q) Recent Accounting Pronouncements

Presentation

Balance Sheet (Topic 210)

On December 23, 2011, the FASB released Accounting Standards Update ("ASU") 2011-11, Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities. Under this update, the Company will be required to disclose both gross information and net information about both instruments and transactions eligible for offset in the statement of financial position and transactions subject to an agreement similar to a master netting arrangement. The scope would include derivatives, sale and repurchase agreements and reverse sale and repurchase agreements and securities borrowing and securities lending arrangements. This disclosure is intended to enable financial statement users to understand the effect of such arrangements on the Company's financial position. This update is effective for the Company for financial statements presented beginning in the first quarter of 2013. This update will result in additional disclosure but will have no impact on total assets, liabilities, stockholders' equity, or Net income (loss).

Comprehensive Income (Topic 220)

In June 2011, the FASB released ASU 2011-05, Comprehensive Income: Presentation of Comprehensive Income, which attempts to improve the comparability, consistency, and transparency of financial reporting and increase the prominence of items reported in Other Comprehensive Income ("OCI"). ASU 2011-05 requires that all non-owner changes in stockholders' equity be presented either in a single continuous statement of net income and comprehensive income or two separate consecutive statements. Either presentation requires the presentation on the face of the financial statements any reclassification adjustments for items that are reclassified from OCI to net income in the statements. There is no change in what must be reported in OCI or when an item of OCI must be reclassified to net income. This update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. The Company adopted the provisions of ASU 2011-05 effective January 1, 2012. Adoption of ASU 2011-05 did not have a significant impact on the Company’s consolidated financial statements.

On December 23, 2011, the FASB issued ASU 2011-12, Comprehensive Income: Deferral of Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income In ASU No. 2011-05, which defers those changes in ASU 2011-05 that relate to the presentation of reclassification adjustments out of accumulated OCI. This was done to allow the FASB time to re-deliberate the presentation, on the face of the financial statements, of the effects of reclassifications out of accumulated OCI on the components of net income and OCI. No other requirements under ASU 2011-05 are affected by ASU 2011-12. FASB tentatively decided not to require presentation of reclassification adjustments out of accumulated other comprehensive income on the face of the financial statements and to propose new disclosures instead.

In February 2013, the FASB issued ASU 2013-02 Comprehensive Income: Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income. This update addresses the disclosure issue left open at the deferral under ASU 2011-12. This update requires the provision of information about the amounts reclassified out of accumulated OCI by component. In addition, it requires presentation, either on the face of the statement where net income is presented or in the Notes, significant amounts reclassified out of accumulated OCI by the respective line items of net income but only if the amount reclassified is required under GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required under GAAP to be reclassified in their entirety to net income, a cross-reference must be provided to other disclosures required under GAAP that provide additional detail about those amounts. This update is effective for the Company for financial statements presented beginning in the first quarter of 2013. Adoption of ASU 2013-02 is not expected to have a significant impact on the consolidated financial statements.

Broad Transactions

Fair Value Measurements and Disclosures (Topic 820)

In May 2011, the FASB released ASU 2011-04, Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS, further converging U.S. GAAP and IFRS by providing common fair value measurement and disclosure requirements. FASB made changes to the fair value measurement guidance, which include: 1) prohibiting the inclusion of block discounts in all fair value measurements, not just Level 1 measurements, 2) adding guidance on when to include other premiums and discounts in fair value measurements, 3) clarifying that the concepts of “highest and best use” and “valuation premise” apply only when measuring the fair value of non-financial assets and 4) adding an exception that allows the measurement of a group of financial assets and liabilities with offsetting risks (e.g., a portfolio of derivative contracts) at their net exposure to a particular risk if certain criteria are met. ASU 2011-04 also requires additional disclosure related to items categorized as Level 3 in the fair value hierarchy, including a description of the processes for valuing these assets, providing quantitative information about the significant unobservable inputs used to measure fair value and, in certain cases, explaining the sensitivity of the fair value measurements to changes in unobservable inputs. The Company adopted this standard in the first quarter 2012. Adoption of ASU 2011-04 increased the footnote disclosure but had no impact on the Company’s consolidated financial statements.

Transfers and Servicing (Topic 860)

In April 2011, the FASB issued ASU 2011-03, Transfers and Servicing: Reconsideration of Effective Control for Repurchase Agreements. In a typical repurchase agreement transaction, an entity transfers financial assets to the counterparty in exchange for cash with an agreement for the counterparty to return the same or equivalent financial assets for a fixed price in the future. Prior to this update, one of the factors in determining whether sale treatment could be used was whether the transferor maintained effective control of the transferred assets and, in order to do so, the transferor must have the ability to repurchase such assets. In connection with the issuance of ASU 2011-03, the FASB concluded that the assessment of effective control should focus on a transferor’s contractual rights and obligations with respect to transferred financial assets, rather than whether the transferor has the practical ability to perform in accordance with those rights or obligations. ASU 2011-03 removes the transferor's ability criterion from consideration of effective control. The Company adopted this standard in the first quarter 2012. As the Company records repurchase agreements as secured borrowings and not sales, this update has no significant effect on the Company's consolidated financial statements.

Financial Services – Investment Companies (Topic 946)

In June 2013, the FASB finalized ASU 2013-08 amending the scope, measurement and disclosure requirements under Topic 946 – Financial Services-Investment Companies. The Board decided not to address issues related to the applicability of investment company accounting for real estate entities and the measurement of real estate investments at this time. Further, as stated in ASC 946-10-15-3, the guidance in Topic 946 does not apply to real estate investment trusts, and thus has no effect on the Company's consolidated financial statements.

3. Residential Mortgage-Backed Securities

The Company classifies its Non-Agency RMBS as senior, senior interest-only, subordinated, subordinated interest-only, and Non-Agency RMBS transferred to consolidated VIEs. The Company also invests in Agency RMBS. Senior interests in Non-Agency RMBS are considered to be entitled to the first principal repayments in their pro-rata ownership interests at the reporting date. The total fair value of the Non-Agency RMBS that are held by the re-securitization trusts consolidated pursuant to ASC 810 was $3.2 billion and $3.3 billion at September 30, 2012 and December 31, 2011, respectively. See Note 8 of these consolidated financial statements for further discussion of consolidated VIEs.

The following tables present the principal or notional value, total premium, total discount, amortized cost, fair value, gross unrealized gains, gross unrealized losses, and net unrealized gain (loss) related to the Company's available-for-sale RMBS portfolio as of September 30, 2012 and December 31, 2011, by asset class.

September 30, 2012
(dollars in thousands)

	Principal or Notional Value	Total Premium	Total Discount	Amortized Cost	Fair Value	Gross Unrealized Gains	Gross Unrealized Losses	Net Unrealized Gain/(Loss)
Non-Agency RMBS								
Senior	$135	$-	$(56)	$79	$82	$3	$-	$3
Senior interest-only	3,120,432	139,827	-	139,827	128,868	8,353	(19,312)	(10,959)
Subordinated	1,074,560	-	(597,306)	477,254	509,061	50,307	(18,500)	31,807
Subordinated interest-only	264,052	17,397	-	17,397	16,867	1,714	(2,244)	(530)
RMBS transferred to consolidated variable interest entities ("VIEs")	4,795,819	9,356	(2,194,898)	2,512,765	3,235,572	723,073	(266)	722,807
Agency RMBS	1,934,283	57,604	-	1,893,633	1,997,211	103,961	(383)	103,578
	$11,189,281	$224,184	$(2,792,260)	$5,040,955	$5,887,661	$887,411	$(40,705)	$846,706

December 31, 2011
(dollars in thousands)

	Principal or Notional Value	Total Premium	Total Discount	Amortized Cost	Fair Value	Gross Unrealized Gains	Gross Unrealized Losses	Net Unrealized Gain/(Loss)
Non-Agency RMBS								
Senior	$1,115	$-	$(56)	$1,059	$1,020	$2	$(41)	$(39)
Senior interest-only	3,734,452	199,288	-	199,288	188,679	11,308	(21,917)	(10,609)
Subordinated	1,378,891	-	(724,739)	654,152	606,895	30,997	(78,254)	(47,257)
Subordinated interest-only	277,560	21,910	-	21,910	22,019	1,663	(1,554)	109
RMBS transferred to consolidated variable interest entities ("VIEs")	5,265,128	19,869	(2,382,995)	2,902,002	3,270,332	420,505	(52,175)	368,330
Agency RMBS	3,018,347	90,403	(159)	3,027,285	3,144,531	117,601	(355)	117,246
	$13,675,493	$331,470	$(3,107,949)	$6,805,696	$7,233,476	$582,076	$(154,296)	$427,780

The table below presents changes in Accretable Yield, or the excess of the security's cash flows expected to be collected over the Company's investment, solely as it pertains to the Company's Non-Agency RMBS portfolio accounted for according to the provisions of ASC 310-30.

	For the Quarter Ended		For the Nine Months Ended	
	September 30, 2012	September 30, 2011	September 30, 2012	September 30, 2011
	(dollars in thousands)		(dollars in thousands)	
Balance at beginning of period	$ 2,234,791	$ 2,585,488	$ 2,342,462	$ 2,521,723
Purchases	-	-	86,847	91,680
Accretion	(89,256)	(102,517)	(276,696)	(293,727)
Reclassification (to) from non-accretable difference	(1,809)	(151,278)	12,776	59,397
Sales	-	-	(21,663)	(47,380)
Balance at end of period	$ 2,143,726	$ 2,331,693	$ 2,143,726	$ 2,331,693

The table below presents the outstanding principal balance and related carrying amount at the beginning and ending of the quarterly periods ended September 30, 2012 and December 31, 2011 as it pertains to the Company's Non-Agency RMBS portfolio accounted for according to the provisions of ASC 310-30.

	For the Quarter Ended September 30, 2012	For the Quarter Ended December 31, 2011
	(dollars in thousands)	
Outstanding principal balance:		
Beginning of period	$ 4,878,479	$ 5,264,486
End of period	$ 4,690,083	$ 5,245,184
Amortized cost:		
Beginning of period	$ 2,420,502	$ 2,761,672
End of period	$ 2,333,309	$ 2,649,303

The following tables present the gross unrealized losses and estimated fair value of the Company's RMBS by length of time that such securities have been in a continuous unrealized loss position at September 30, 2012 and December 31, 2011. All securities in an unrealized loss position have been evaluated by the Company for OTTI as discussed in Note 2(d).

September 30, 2012 (dollars in thousands)

	Unrealized Loss Position for Less than 12 Months			Unrealized Loss Position for 12 Months or More			Total		
	Estimated Fair Value	Unrealized Losses	Number of Securities	Estimated Fair Value	Unrealized Losses	Number of Securities	Estimated Fair Value	Unrealized Losses	Number of Securities
Non-Agency RMBS									
Senior	$ -	$ -	-	$ -	$ -	-	$ -	$ -	-
Senior interest-only	18,928	(3,048)	10	50,449	(16,264)	20	69,377	(19,312)	30
Subordinated	-	-	1	192,675	(18,500)	17	192,675	(18,500)	18
Subordinated interest-only	9,870	(2,244)	1	-	-	-	9,870	(2,244)	1
RMBS transferred to consolidated VIEs	-	-	-	36,527	(266)	2	36,527	(266)	2
Agency RMBS	3,848	(164)	3	935	(219)	1	4,783	(383)	4
Total	$ 32,646	$ (5,456)	15	$ 280,586	$ (35,249)	40	$ 313,232	$ (40,705)	55

December 31, 2011 (dollars in thousands)

Total

	Unrealized Loss Position for Less than 12 Months			Unrealized Loss Position for 12 Months or More					
	Estimated Fair Value	Unrealized Losses	Number of Securities	Estimated Fair Value	Unrealized Losses	Number of Securities	Estimated Fair Value	Unrealized Losses	Number of Securities
Non-Agency RMBS									
Senior	$ -	$ -	-	$ 127	$ (41)	1	$ 127	$ (41)	1
Senior interest-only	99,351	(18,756)	26	17,647	(3,161)	12	116,998	(21,917)	38
Subordinated	321,416	(52,824)	33	111,167	(25,430)	17	432,583	(78,254)	50
Subordinated interest-only	16,300	(1,554)	2	-	-	-	16,300	(1,554)	2
RMBS transferred to consolidated VIEs	-	-	-	594,369	(52,175)	18	594,369	(52,175)	18
Agency RMBS	3,888	(355)	2	-	-	-	3,888	(355)	2
Total	$ 440,955	$ (73,489)	63	$ 723,310	$ (80,807)	48	$ 1,164,265	$ (154,296)	111

At September 30, 2012, the Company did not intend to sell any of its RMBS that were in an unrealized loss position, and it was not more likely than not that the Company would be required to sell these RMBS before recovery of their amortized cost basis, which may be at their maturity. With respect to RMBS held by consolidated VIEs, the ability of any entity to cause the sale by the VIE prior to the maturity of these RMBS is either expressly prohibited, not probable, or is limited to specified events of default, none of which have occurred to date.

Gross unrealized losses on the Company’s Agency RMBS were $383 thousand and $355 thousand at September 30, 2012 and December 31, 2011, respectively. Given the credit quality inherent in Agency RMBS, the Company does not consider any of the current impairments on its Agency RMBS to be credit related. In evaluating whether it is more likely than not that it will be required to sell any impaired security before its anticipated recovery, which may be at their maturity, the Company considers the significance of each investment, the amount of impairment, the projected future performance of such impaired securities, as well as the Company’s current and anticipated leverage capacity and liquidity position. Based on these analyses, the Company determined that at September 30, 2012 and December 31, 2011 unrealized losses on its Agency RMBS were temporary.

Gross unrealized losses on the Company’s Non-Agency RMBS (including Non-Agency RMBS held by consolidated VIEs) were $40.3 million and $153.9 million at September 30, 2012 and December 31, 2011, respectively. Based upon the most recent evaluation, the Company does not consider these unrealized losses to be indicative of OTTI and does not believe that these unrealized losses are credit related, but rather are due to other factors. The Company has reviewed its Non-Agency RMBS that are in an unrealized loss position to identify those securities with losses that are other-than-temporary based on an assessment of changes in cash flows expected to be collected for such RMBS, which considers recent bond performance and expected future performance of the underlying collateral.

A summary of the OTTI included in earnings for the quarters and nine months ended September 30, 2012 and September 30, 2011 is presented below.

	For the Quarter Ended September 30, 2012	September 30, 2011
	(dollars in thousands)	
Total other-than-temporary impairment losses	$ (2,713)	$ (78,950)
Portion of loss recognized in other comprehensive income (loss)	(7,301)	(71,610)
Net other-than-temporary credit impairment losses	$ (10,014)	$ (150,560)

	For the Nine Months Ended September 30, 2012	September 30, 2011
	(dollars in thousands)	
Total other-than-temporary impairment losses	$ (47,264)	$ (161,924)
Portion of loss recognized in other comprehensive income (loss)	(76,801)	(83,989)
Net other-than-temporary credit impairment losses	$ (124,065)	$ (245,913)

The following table presents a roll forward of the credit loss component of OTTI on the Company's Non-Agency RMBS for which a portion of loss was previously recognized in other comprehensive income. The table delineates between those securities that are recognizing OTTI for the first time as opposed to those that have previously recognized OTTI.

	For the Quarter Ended September 30, 2012	September 30, 2011
	(dollars in thousands)	
Cumulative credit loss beginning balance	$ 540,659	$ 242,649
Additions:		
Other-than-temporary impairments not previously recognized	7,275	107,553
Reductions for securities sold during the period	(33,817)	(36)
Increases related to other-than-temporary impairments on securities with previously recognized other-than-temporary impairments	2,739	43,007
Reductions for increases in cash flows expected to be collected that are recognized over the remaining life of the security	(8,160)	(44,817)
Cumulative credit loss ending balance	$ 508,696	$ 348,356

	For the Nine Months Ended September 30, 2012	September 30, 2011
	(dollars in thousands)	
Cumulative credit loss beginning balance	$ 452,060	$ 237,746
Additions:		
Other-than-temporary impairments not previously recognized	97,203	185,375
Reductions for securities sold during the period	(34,107)	(1,298)
Increases related to other-than-temporary impairments on securities with previously recognized other-than-temporary impairments	26,862	60,538
Reductions for increases in cash flows expected to be collected over the remaining life of the securities	(33,322)	(134,005)
Cumulative credit impairment loss ending balance	$ 508,696	$ 348,356

Cash flows generated to determine net other-than-temporary credit impairment losses recognized in earnings are estimated using significant unobservable inputs. The significant inputs used to measure the component of OTTI recognized in earnings for the Company's Non-Agency RMBS are summarized as follows:

	For the Quarter Ended	
	September 30, 2012	September 30, 2011
Loss Severity		
Weighted Average	56%	63%
Range	41% - 80%	42% - 71%
60+ days delinquent		
Weighted Average	23%	30%
Range	0% - 41%	0% - 68%
Credit Enhancement (1)		
Weighted Average	13%	17%
Range	0% - 73%	0% - 89%
3 Month CPR		
Weighted Average	16%	16%
Range	0% - 20%	3% - 63%
12 Month CPR		
Weighted Average	17%	17%
Range	12% - 42%	6% - 38%

(1) Calculated as the combined credit enhancement to the Re-REMIC and underlying from each of their respective capital structures.

The following tables present a summary of unrealized gains and losses at September 30, 2012 and December 31, 2011. Interest-only RMBS included in the tables below represent the right to receive a specified proportion of the contractual interest cash flows of the underlying principal balance of specific securities. At September 30, 2012, interest-only RMBS had a net unrealized loss of $5.7 million and had an amortized cost of $172.0 million. At December 31, 2011, interest-only RMBS had a net unrealized loss of $5.7 million and had an amortized cost of $237.8 million. The fair value of IOs at September 30, 2012 and December 31, 2011 was $166.3 million, and $232.2 million, respectively.

	September 30, 2012 (dollars in thousands)					
	Gross Unrealized Gain Included in Accumulated Other Comprehensive Income	Gross Unrealized Gain Included in Accumulated Deficit	Total Gross Unrealized Gain	Gross Unrealized Loss Included in Accumulated Other Comprehensive Income	Gross Unrealized Loss Included in Accumulated Deficit	Total Gross Unrealized Loss
Non-Agency RMBS						
Senior	$ 3	$ -	$ 3	$ -	$ -	$ -
Senior interest-only	-	8,353	8,353	-	(19,312)	(19,312)

Subordinated	50,307	-	50,307	(18,500)	-	(18,500)
Subordinated interest-only	-	1,714	1,714	(0)	(2,244)	(2,244)
RMBS transferred to consolidated VIEs	716,876	6,197	723,073	(266)	-	(266)
Agency RMBS	103,938	23	103,961	(0)	(383)	(383)
Total	$ 871,124	$ 16,287	$ 887,411	$ (18,766)	$ (21,939)	$ (40,705)

December 31, 2011
(dollars in thousands)

	Gross Unrealized Gain Included in Accumulated Other Comprehensive Income	Gross Unrealized Gain Included in Accumulated Deficit	Total Gross Unrealized Gain	Gross Unrealized Loss Included in Accumulated Other Comprehensive Income	Gross Unrealized Loss Included in Accumulated Deficit	Total Gross Unrealized Loss
Non-Agency RMBS						
Senior	$ 2	$ -	$ 2	$ (41)	$ -	$ (41)
Senior interest-only	-	11,308	11,308	-	(21,917)	(21,917)
Subordinated	30,997	-	30,997	(78,254)	-	(78,254)
Subordinated interest-only	-	1,663	1,663	-	(1,554)	(1,554)
RMBS transferred to consolidated VIEs	415,688	4,817	420,505	(52,175)	-	(52,175)
Agency RMBS	117,236	365	117,601	-	(355)	(355)
Total	$ 563,923	$ 18,153	$ 582,076	$ (130,470)	$ (23,826)	$ (154,296)

Changes in prepayments, actual cash flows, and cash flows expected to be collected, among other items, are affected by the collateral characteristics of each asset class. The portfolio is most heavily weighted to contain Non-Agency RMBS with credit risk. The Company chooses assets for the portfolio after carefully evaluating each investment's risk profile.

The following tables provide a summary of the Company's RMBS portfolio at September 30, 2012 and December 31, 2011.

	September 30, 2012					December 31, 2011				
	Principal or Notional Value at Period-End (dollars in thousands)	Weighted Average Amortized Cost Basis	Weighted Average Fair Value	Weighted Average Coupon	Weighted Average Yield at Period-End (1)	Principal or Notional Value at Period-End (dollars in thousands)	Weighted Average Amortized Cost Basis	Weighted Average Fair Value	Weighted Average Coupon	Weighted Average Yield at Period-End (1)
Non-Agency Mortgage-Backed Securities										
Senior	$ 135	$ 58.37	$ 60.88	0.00 %	11.26 %	$ 1,115	$ 95.13	$ 91.55	1.02 %	2.95 %
Senior, interest only	$ 3,120,432	$ 4.48	$ 4.13	1.74 %	8.81 %	$ 3,734,452	$ 5.34	$ 5.05	1.96 %	13.28 %
Subordinated	$ 1,074,560	$ 44.41	$ 47.37	3.17 %	10.83 %	$ 1,378,891	$ 47.44	$ 44.01	3.44 %	9.57 %
Subordinated, interest only	$ 264,052	$ 6.59	$ 6.39	2.45 %	5.96 %	$ 277,560	$ 7.89	$ 7.93	2.94 %	9.93 %
RMBS transferred to consolidated variable interest entities	$ 4,795,819	$ 53.48	$ 68.87	4.96 %	15.44 %	$ 5,265,128	$ 55.14	$ 62.11	5.32 %	14.56 %
Agency Mortgage-Backed Securities	$ 1,934,283	$ 103.14	$ 108.78	4.65 %	3.61 %	$ 3,018,347	$ 103.07	$ 107.06	4.66 %	3.83 %

(1) Bond Equivalent Yield at period end.

The following table presents the weighted average credit rating, based on the lowest rating available, of the Company's Non-Agency RMBS portfolio at September 30, 2012 and December 31, 2011.

	September 30, 2012	December 31, 2011
AAA	0.00 %	0.53 %
AA	0.46 %	0.14 %
A	0.03 %	0.45 %
BBB	0.00 %	1.54 %
BB	0.36 %	0.00 %
B	1.44 %	0.43 %
Below B or not rated	97.71 %	96.91 %
Total	100.00 %	100.00 %

Actual maturities of RMBS are generally shorter than the stated contractual maturities. Actual maturities of the Company's RMBS are affected by the contractual lives of the underlying mortgages, periodic payments of principal and prepayments of principal. The following tables provide a summary of the fair value and amortized cost of the Company's RMBS at September 30, 2012 and December 31, 2011 according to their estimated weighted-average life classifications. The weighted-average lives of the RMBS in the tables below are based on lifetime expected prepayment rates using an industry prepayment model for the Agency RMBS portfolio and the Company's prepayment assumptions for the Non-Agency RMBS. The prepayment model considers current yield, forward yield, steepness of the interest rate curve, current mortgage rates, mortgage rates of the outstanding loan, loan age, margin, and volatility.

September 30, 2012
(dollars in thousands)

	Weighted Average Life				
	Less than one year	Greater than one year and less than five years	Greater than five years and less than ten years	Greater than ten years	Total
Fair value					
Non-Agency RMBS					
Senior	$ -	$ -	$ 82	$ -	$ 82
Senior interest-only	570	63,876	53,324	11,098	128,868
Subordinated	521	67,397	305,436	135,707	509,061
Subordinated interest-only	-	-	-	16,867	16,867
RMBS transferred to consolidated VIEs	15,028	320,800	2,143,280	756,464	3,235,572
Agency RMBS	224	1,996,987	-	-	1,997,211
Total fair value	$ 16,343	$ 2,449,060	$ 2,502,122	$ 920,136	$ 5,887,661
Amortized cost					
Non-Agency RMBS					
Senior	$ -	$ -	$ 79	$ -	$ 79
Senior interest-only	798	77,297	53,085	8,647	139,827
Subordinated	357	64,832	293,471	118,594	477,254
Subordinated interest-only	-	-	-	17,397	17,397
RMBS transferred to consolidated VIEs	14,228	247,324	1,650,825	600,388	2,512,765
Agency RMBS	202	1,893,431	-	-	1,893,633
Total amortized cost	$ 15,585	$ 2,282,884	$ 1,997,460	$ 745,026	$ 5,040,955

December 31, 2011
(dollars in thousands)

	Weighted Average Life				
	Less than one year	Greater than one year and less than	Greater than five years and less than ten years	Greater than ten years	Total

		five years			
Fair value					
Non-Agency RMBS					
Senior	$ 892	$ -	$ 128	$ -	$ 1,020
Senior interest-only	-	85,633	69,204	33,842	188,679
Subordinated	6,530	101,984	259,549	238,832	606,895
Subordinated interest-only	-	-	1,812	20,207	22,019
RMBS transferred to consolidated VIEs	25,375	338,616	2,119,030	787,311	3,270,332
Agency RMBS	17,932	1,735,106	824,645	566,848	3,144,531
Total fair value	$ 50,729	$ 2,261,339	$ 3,274,368	$ 1,647,040	$ 7,233,476
Amortized cost					
Non-Agency RMBS					
Senior	$ 891	$ -	$ 168	$ -	$ 1,059
Senior interest-only	-	95,974	69,953	33,361	199,288
Subordinated	5,616	98,657	300,489	249,390	654,152
Subordinated interest-only	-	-	1,946	19,964	21,910
RMBS transferred to consolidated VIEs	32,806	296,144	1,827,000	746,052	2,902,002
Agency RMBS	17,610	1,663,917	798,632	547,126	3,027,285
Total amortized cost	$ 56,923	$ 2,154,692	$ 2,998,188	$ 1,595,893	$ 6,805,696

The Non-Agency RMBS portfolio is subject to credit risk. The Company seeks to mitigate credit risk through its asset selection process. The Non-Agency RMBS portfolio is primarily collateralized by what the Company classifies as Alt-A first lien mortgages. The Company categorizes collateral as Alt-A regardless of whether the loans were originally described as “prime” if the behavior of the collateral when the Company purchased the security more typically resembles Alt-A. The Company defines Alt-A collateral characteristics to be evidenced by the 60+ day delinquency bucket of the pool being greater than 5% and the weighted average FICO scores at the time of origination as greater than 650. At September 30, 2012, 99.6% of the Non-Agency RMBS collateral was Alt-A. At December 31, 2011, 97.4% of the Non-Agency RMBS collateral was Alt-A.

The Non-Agency RMBS in the Portfolio have the following collateral characteristics at September 30, 2012 and December 31, 2011.

	September 30, 2012		December 31, 2011	
Weighted average maturity (years)		24.8		25.7
Weighted average amortized loan to value (1)		71.6 %		71.5 %
Weighted average FICO (2)		717.3		718.4
Weighted average loan balance (in thousands)	$	453.1	$	469.0
Weighted average percentage owner occupied		85.1 %		85.3 %
Weighted average percentage single family residence		65.5 %		65.6 %
Weighted average current credit enhancement		3.1 %		4.5 %
Weighted average geographic concentration of top five states	CA	37.1 %	CA	38.1 %
	FL	8.6 %	FL	8.5 %
	NY	6.3 %	NY	6.1 %
	VA	2.6 %	NJ	2.7 %
	NJ	2.5 %	VA	2.4 %

(1) Value represents appraised value of the collateral at the time of loan origination.
(2) FICO as determined at the time of loan origination.

The table below presents the origination year of the underlying loans related to the Company's portfolio of Non-Agency RMBS at September 30, 2012 and December 31, 2011.

Origination Year	September 30, 2012		December 31, 2011	
2001	0.2	%	0.2	%
2003	0.4	%	0.9	%
2004	0.5	%	1.3	%
2005	13.8	%	13.8	%
2006	32.2	%	31.8	%
2007	49.9	%	48.7	%
2008	3.0	%	3.3	%
Total	100.0	%	100.0	%

During the quarter ended September 30, 2012, the Company sold RMBS with a carrying value of $795.1 million for realized gains of $69.2 million. During the quarter ended September 30, 2011, the Company sold RMBS with a carrying value of $2.3 million for realized gains of $58 thousand. During the nine months ended September 30, 2012, the Company sold RMBS with a carrying value of $858.2 million for realized gains of $85.2 million. During the nine months ended September 30, 2011, the Company sold RMBS with a carrying value of $669.1 million for realized gains of $1.8 million.

4. Securitized Loans Held for Investment

The Company is considered to be the primary beneficiary of VIEs formed for the purpose of securitizing whole mortgage loans. Refer to Note 8 for additional details regarding the Company's involvement with VIEs.

The following table provides a summary of the changes in the carrying value of securitized loans held for investment at September 30, 2012 and December 31, 2011:

	September 30, 2012	December 31, 2011
	(dollars in thousands)	
Balance, beginning of period	$ 256,632	$ 349,112
Purchases	1,185,664	-
Principal paydowns	(297,923)	(85,526)
Net periodic amortization (accretion)	(7,846)	(1,663)
Change to loan loss provision	396	(5,291)
Balance, end of period	$ 1,136,923	$ 256,632

The following table represents the Company's securitized residential mortgage loans classified as held for investment at September 30, 2012 and December 31, 2011:

	September 30, 2012	December 31, 2011
	(dollars in thousands)	
Securitized loans, at amortized cost	$ 1,148,187	$ 270,570
Less: allowance for loan losses	11,264	13,938
Securitized loans held for investment	$ 1,136,923	$ 256,632

The securitized loan portfolio is collateralized by prime, jumbo, first lien residential mortgages of which 9.8% were originated during 2012, 59.8% were originated during 2011, 13.2% during 2010, and the remaining 17.2% of the loans were originated prior to 2010. A summary of key characteristics of these loans follows.

	September 30, 2012			December 31, 2011		
Number of loans		1,384			392	
Weighted average maturity (years)		28.2			25.8	
Weighted average loan to value (1)		71.7	%		75.5	%
Weighted average FICO (2)		767			752	
Weighted average loan balance (in thousands)		$ 820.1			$ 684.0	
Weighted average percentage owner occupied		94.0	%		91.1	%
Weighted average percentage single family residence		65.9	%		58.1	%
Weighted average geographic concentration of top five states	CA	39.6	%	CA	36.0	%
	NY	7.7	%	FL	6.1	%
	WA	6.6	%	AZ	5.8	%
	VA	4.7	%	NJ	5.4	%
	MD	4.2	%	IL	5.3	%

(1) Value represents appraised value of the collateral at the time of loan origination.
(2) FICO as determined at the time of loan origination.

The following table summarizes the changes in the allowance for loan losses for the securitized mortgage loan portfolio for the nine months ended September 30, 2012 and year ended December 31, 2011:

	For the Nine Months Ended September 30, 2012	For the Year Ended December 31, 2011
	(dollars in thousands)	
Balance, beginning of period	$ 13,938	$ 11,006
Provision for loan losses	(396)	5,291
Charge-offs	(2,278)	(2,359)
Balance, end of period	$ 11,264	$ 13,938

The Company has established an allowance for loan losses related to securitized loans that is composed of a general and specific reserve. The balance in the allowance for loan losses related to the general reserve at September 30, 2012 and December 31, 2011 was $4.7 million and $6.3 million, respectively. The balance in the allowance for loan losses related to the specific reserve at September 30, 2012 and December 31, 2011 was $6.6 million and $7.6 million, respectively.

The Company's overall provision for loan losses is described in Note 2(g). The Company's general reserve is based on historical loss rates for pools of loans with similar credit characteristics, adjusted for current trends and market conditions, including current trends in delinquencies and severities. The Company has established a specific reserve that reflects consideration of loans more than 60 days delinquent, loans in foreclosure, borrowers that have declared bankruptcy, and real estate owned. The loan loss provision related to these loans is measured as the difference between the unpaid principal balance and the estimated fair value of the property securing the mortgage, less estimated costs to sell. The specific reserve also reflects consideration of concessions granted to borrowers by the servicer in the form of modifications (i.e., reductions). Loan loss provisions related to these modifications are based on the contractual principal and interest payments, post-modification, discounted at the loan's original effective interest rate.

The total unpaid principal balance of impaired loans for which the Company established a specific reserve was $28.3 million and $32.9 million at September 30, 2012 and December 31, 2011, respectively. The Company's recorded investment in impaired loans for which there is a related allowance for credit losses at September 30, 2012 and December 31, 2011 was $21.2 million and $14.3 million, respectively. The total unpaid principal balance of non-impaired loans for which the Company established a general reserve was $1.1 billion and $235.2 million at September 30, 2012 and December 31, 2011, respectively. The Company's recorded investment in loans that are not impaired for which there is a related general reserve for credit losses at September 30, 2012 and December 31, 2011 was $1.1 billion and $228.9 million, respectively.

The following table summarizes the outstanding principal balance of loans 30 days delinquent and greater as reported by the servicer at September 30, 2012 and December 31, 2011.

	30 Days Delinquent	60 Days Delinquent	90+ Days Delinquent	Bankruptcy	Foreclosure	REO	Total
			(dollars in thousands)				
September 30, 2012	$ 2,372	$ 2,008	$ 3,999	$ 0	$ 4,030	$ 1,768	$ 14,177
December 31, 2011	$ 1,342	$ 1,828	$ 2,338	$ 1,659	$ 3,626	$ 5,201	$ 15,994

With the exception of its ability to approve loan modifications solely as it relates to CSMC 2012-CIM1 and CSMC 2012-CIM2 as further described in Note 2(g), the Company does not service or modify loans held for investment. The trustee and servicer of the respective securitization are responsible for servicing and modifying these loans. The Company is required to make certain assumptions in accounting for loans held for investment due to the limitation of information available to the Company. The following table presents the loans that were modified by the servicer during the nine months ended September 30, 2012 and September 30, 2011.

	Number of Loans Modified During Period	Unpaid Principal Balance of Modified Loans (Pre-modification)	Unpaid Principal Balance of Modified Loans (Post-modification)	Amortized Cost of Modified Loans	Amortized Cost of Modified Loans For Which There is an Allowance for Loan Losses	Amortized Cost of Modified Loans For Which There is No Allowance for Loan Losses
			(dollars in thousands)			
Nine Months Ended						
September 30, 2012	7	$ 3,943	$ 4,053	$ 4,025	$ 4,025	$ 0
September 30, 2011	6	$ 4,447	$ 4,821	$ 4,876	$ 4,876	$ 0

Loans are modified by the servicer as a method of loss mitigation. Based on the information available, during the quarter and nine months ended September 30, 2012, the Company determined that all loans modified by the servicer were considered troubled debt restructurings, as defined under GAAP. A troubled debt restructuring is generally any modification of a loan to a borrower that is experiencing financial difficulties, where a lender agrees to terms that are more favorable to the borrower than are otherwise available in the current market. All loan modifications during the quarters and nine months ended September 30, 2012 and September 30, 2011 included a reduction of the stated interest rates. Loans modified by the servicer have been individually assessed for impairment and measurement of impairment is based on the excess of the recorded investment in the loan over the present value of the expected cash flows, post modification, discounted at the loan's effective interest rate at inception. In the absence of additional loan modifications by the servicer in future periods that are considered to be TDR's, the $4.5 million specific reserve related to TDR's as of September 30, 2012 will be recognized in net income in future periods by way of a decrease in the provision for loan losses.

As of September 30, 2012, one loan with an outstanding principal balance of approximately $1.6 million that was modified in the past twelve months was delinquent on its scheduled payments. This loan was individually evaluated for impairment and the related allowance for loan loss is based on the excess of the recorded investment in the loan over the present value of the expected cash flows, post modification, discounted at the loan's effective interest rate at inception.

5. Fair Value Measurements

The Company follows fair value guidance in accordance with GAAP to account for its financial instruments. The Company categorizes its financial instruments, based on the priority of the inputs to the valuation technique, into a three-level fair value hierarchy. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). If the inputs used to measure the financial instruments fall within different levels of the hierarchy, the categorization is based on the lowest level input that is significant to the fair value measurement of the instrument. Financial assets and liabilities recorded at fair value on the consolidated statements of financial condition or disclosed in the related notes are categorized based on the inputs to the valuation techniques as follows:

Level 1 – inputs to the valuation methodology are quoted prices (unadjusted) for identical assets and liabilities in active markets.

Level 2 – inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3 – inputs to the valuation methodology are unobservable and significant to fair value.

Fair value measurements categorized within Level 3 are sensitive to changes in the assumptions or methodology used to determine fair value and such changes could result in a significant increase or decrease in the fair value. For the Company's investments in Non-Agency RMBS categorized within Level 3 of the fair value hierarchy, the significant unobservable inputs include the discount rates, assumptions relating to prepayments, default rates and loss severities. Significant increases (decreases) in any of the discount rates, default rates or loss severities in isolation would result in a significantly lower (higher) fair value measurement. The impact of changes in prepayment speeds would have differing impacts on fair value, depending on the seniority of the investment. Generally, a change in the default assumption is accompanied by directionally similar changes in the assumptions used for the loss severity and the prepayment speed.

Any changes to the valuation methodology are reviewed by management to ensure the changes are appropriate. As markets and products evolve and the pricing for certain products becomes more transparent, the Company will continue to refine its valuation methodologies. The methodology utilized by the Company for the periods presented is unchanged. The methods used to produce a fair value calculation may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Company believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies, or assumptions, to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date. The Company uses inputs that are current as of the measurement date, which may include periods of market dislocation, during which price transparency may be reduced.

During times of market dislocation, as has been experienced for some time and continues to exist, the observability of prices and inputs can be difficult for certain Non-Agency RMBS. If third party pricing services are unable to provide a price for an asset, or if the price provided by them is deemed unreliable by the Company, then the asset will be valued at its fair value as determined by the Company without validation to third-party pricing. In addition, validating third party pricing for the Company’s investments may be more subjective as fewer participants may be willing to provide this service to the Company. Illiquid investments typically experience greater price volatility as an active market does not exist. Observability of prices and inputs can vary significantly from period to period and may cause instruments to change classifications within the three level hierarchy.

A description of the methodologies utilized by the Company to estimate the fair value of its financial instruments by instrument class follows:

Short-term Instruments

The carrying value of cash and cash equivalents, accrued interest receivable, dividends payable, and accrued interest payable are considered to be a reasonable estimate of fair value due to the short term nature of these financial instruments.

Agency and Non-Agency RMBS

Generally, the Company determines the fair value of its investment securities utilizing an internal pricing model that incorporates such factors as coupon, prepayment speeds, weighted average life, collateral composition, borrower characteristics, expected interest rates, life caps, periodic caps, reset dates, collateral seasoning, expected losses, expected default severity, credit enhancement, and other pertinent factors. Management reviews the fair values generated by the model to determine whether prices are reflective of the current market. Management indirectly corroborates its estimates of the fair value using pricing models by comparing its results to independent prices provided by dealers in the securities and/or third party pricing services. Certain very liquid asset classes, such as Agency fixed-rate pass-throughs may be priced using independent sources such as quoted prices for To-Be-Announced (“TBA”) securities.

The Agency RMBS market is considered to be an active market such that participants transact with sufficient frequency and volume to provide transparent pricing information on an ongoing basis. The liquidity of the Agency RMBS market and the similarity of the Company’s securities to those actively traded enable the Company to observe quoted prices in the market and utilize those prices as a basis for formulating fair value measurements. Consequently, the Company has classified Agency RMBS as Level 2 inputs in the fair value hierarchy.

The Company’s fair value estimation process for Non-Agency RMBS utilizes inputs other than quoted prices that are observed in the market. The Company’s estimate of prepayment, default and severity curves all involve Management judgment and assumptions that are deemed to be significant to the fair value measurement process, which renders the resulting Non-Agency fair value estimates Level 3 inputs in the fair value hierarchy.

Interest Rate Swaps

The Company utilizes dealer quotes to determine the fair values of its interest rate swaps. The Company compares the dealer quotations received to its own estimate of fair value to evaluate for reasonableness. The dealer quotes incorporate common market pricing methods, including a spread measurement to the Treasury yield curve or interest rate swap curve as well as underlying characteristics of the particular contract. Interest rate swaps are modeled by the Company by incorporating such factors as the term to maturity, Treasury curve, LIBOR rates, and the payment rates on the fixed portion of the interest rate swaps. The Company has classified Interest Rate Swaps as Level 2 inputs in the fair value hierarchy.

During the fourth quarter of 2011, the Company changed its discount rate assumption used to determine the fair value of interest rate swaps from LIBOR to the overnight index swap rate in response to changes in market valuation practices for interest rate swaps that are collateralized.

The Company's financial assets and liabilities carried at fair value on a recurring basis, including the level in the fair value hierarchy, at September 30, 2012 and December 31, 2011 is presented below.

	September 30, 2012		
	Level 1	Level 2	Level 3
		(dollars in thousands)	
Assets:			
Non-Agency RMBS			
Senior	$ -	$ -	$ 82
Senior interest-only	-	-	128,868
Subordinated	-	-	509,061
Subordinated interest-only	-	-	16,867
RMBS transferred to consolidated VIEs	-	-	3,235,572
Agency mortgage-backed securities	-	1,997,211	-
Liabilities:			
Interest rate swaps	-	59,073	-
Total	$ -	$ 2,056,284	$ 3,890,450

	December 31, 2011		
	Level 1	Level 2	Level 3
		(dollars in thousands)	
Assets:			
Non-Agency RMBS			
Senior	$ -	$ -	$ 1,020
Senior interest-only	-	-	188,679
Subordinated	-	-	606,895
Subordinated interest-only	-	-	22,019
RMBS transferred to consolidated VIEs	-	-	3,270,332
Agency mortgage-backed securities	-	3,144,531	-

Liabilities:						
Interest rate swaps		-		44,467		-
Total	$	-	$	3,188,998	$	4,088,945

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The table below provides a summary of the changes in the fair value of securities classified as Level 3.

Fair Value Reconciliation, Level 3
(dollars in thousands)

	For the Nine Months Ended September 30, 2012	For the Year Ended December 31, 2011
Non-Agency RMBS		
Beginning balance Level 3 assets	$ 4,088,945	$ 5,529,109
Transfers in to Level 3 assets	-	-
Transfers out of Level 3 assets	-	-
Purchases	116,627	446,207
Principal payments	(404,294)	(695,277)
Sales	(328,261)	(631,642)
Accretion of purchase discounts	69,532	81,224
Gains (losses) included in net income		
Other than temporary credit impairment losses	(124,065)	(357,105)
Realized gains (losses) on sales	48,434	445
Net unrealized gains (losses) on interest-only RMBS	393	(14,717)
Gains (losses) included in other comprehensive income		
Total unrealized gains (losses) for the period	423,139	(269,299)
Ending balance Level 3 assets	$ 3,890,450	$ 4,088,945

There were no transfers to or from Level 3 during the quarter ended September 30, 2012 and the year ended December 31, 2011.

A summary of the significant inputs used to estimate the fair value of Non-Agency RMBS as of September 30, 2012 and December 31, 2011 follows:

	September 30, 2012				December 31, 2011			
		Significant Inputs				Significant Inputs		
	Weighted Average Discount Rate	Prepayment Speed (CPR)	Cumulative Default Rate	Loss Severity	Weighted Average Discount Rate	Prepayment Speed (CPR)	Cumulative Default Rate	Loss Severity
		Range			Range			
Non-Agency RMBS								
Senior	10.0 %	12% - 12 %	0% - 4 %	50% - 54 %	4.3 %	1% - 12 %	0% - 19 %	50% - 85 %

Senior interest-only	14.1 %	1% - 20 %	0% - 26 %	50% - 85 %	14.9 %	1% - 22 %	0% - 24 %	50% - 85 %
Subordinated	23.7 %	1% - 18 %	0% - 26 %	50% - 85 %	28.5 %	1% - 20 %	0% - 23 %	50% - 85 %
Subordinated interest-only	13.1 %	4% - 10 %	0% - 18 %	50% - 71 %	13.5 %	3% - 9 %	0% - 21 %	50% - 80 %
RMBS transferred to consolidated VIEs	6.7 %	1% - 14 %	0% - 36 %	50% - 85 %	9.1 %	1% - 13 %	0% - 35 %	50% - 85 %

All of the significant inputs listed have some degree of market observability, based on the Company's knowledge of the market, information available to market participants, and use of common market data sources. Collateral default and loss severity projections are in the form of "curves" that are updated quarterly to reflect the Company's collateral cash flow projections. Methods used to develop these projections conform to industry conventions. The Company uses assumptions it considers its best estimate of future cash flows for each respective security.

The discount rates applied to the expected cash flows to determine fair value are derived from a range of observable prices on securities backed by similar collateral. As the market becomes more or less liquid, the availability of these observable inputs will change.

The prepayment speed specifies the percentage of the collateral balance that is expected to pay off at each point in the future. The prepayment speed is based on factors such as collateral FICO score, loan-to-value ratio, debt-to-income ratio, and vintage on a loan level basis and is scaled up or down to reflect recent collateral-specific prepayment experience as obtained from remittance reports and market data services.

Default vectors are determined from the current "pipeline" of loans that are more than 30 days delinquent, in foreclosure, bankruptcy, or are real estate owned ("REO"). These delinquent loans determine the first 30 months of the default curve. Beyond month 30, the default curve transitions to a value that is reflective of a portion of the current delinquency pipeline.

The curve generated to reflect the Company's expected loss severity is based on collateral-specific experience with consideration given to other mitigating collateral characteristics. Characteristics such as seasoning are taken into consideration because severities tend to initially increase on newly originated securities, before beginning to decline as the collateral ages and eventually stabilizes. Collateral characteristics such as loan size, loan-to-value, and geographic location of collateral also effect loss severity.

Securitized Loans Held for Investment

The Company carries securitized loans held for investment at principal value, plus unamortized premiums, less unaccreted discounts and allowance for loan losses. The Company estimates the fair value of its securitized loans held for investment by considering the loan characteristics, including the credit characteristics of the borrower, purpose of the loan, use of the collateral securing the loan, and management's expectations of general economic conditions in the sector and greater economy.

Repurchase Agreements

Repurchase agreements are collateralized financing transactions utilized by the Company to acquire investment securities. Due to the short term nature of these financial instruments, the Company estimates and records the fair value of these repurchase agreements using the contractual obligation plus accrued interest payable at maturity.

Securitized Debt, Non-Agency RMBS Transferred to Consolidated VIEs and Securitized Debt, Loans Held for Investment

The Company records securitized debt for certificates or notes financed without recourse to the Company in securitization or re-securitization transactions treated as secured borrowings pursuant to ASC 860. The Company carries securitized debt at the principal balance outstanding plus unamortized premiums, less unaccreted discounts recorded in connection with the financing of the loans or RMBS with third parties. The premiums or discounts associated with the financing of the notes or certificates are amortized over the contractual life of the instrument using the interest method. The Company estimates the fair value of securitized debt by estimating the future cash flows associated with the underlying assets collateralizing the secured debt outstanding. The Company models the fair value of each underlying asset by considering, among other items, the structure of the underlying security, coupon, servicer, actual and expected defaults, actual and expected default severities, reset indices, and prepayment speeds in conjunction with market research for similar collateral performance and management's expectations of general economic conditions in the sector and other economic factors.

The following table presents the carrying value and fair value, as described above, of the Company's financial instruments at September 30, 2012 and December 31, 2011.

		September 30, 2012		December 31, 2011	
	Level in Fair Value Hierarchy	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Non-Agency RMBS	3	$ 3,890,450	$ 3,890,450	$ 4,088,945	$ 4,088,945
Agency RMBS	2	1,997,211	1,997,211	3,144,531	3,144,531
Securitized loans held for investment	3	1,136,923	1,153,764	256,632	237,977
Repurchase agreements	2	(1,658,906)	(1,662,651)	(2,672,989)	(2,677,402)
Securitized debt, collateralized by Non-Agency RMBS	3	(1,252,752)	(1,319,372)	(1,630,276)	(1,546,237)
Securitized debt, collateralized by	3	(1,033,925)	(1,046,118)	(212,778)	(222,921)

loans held for investment					
Interest rate swaps	2	(59,073)	(59,073)	(44,467)	(44,467)

6. Repurchase Agreements

The Company had outstanding $1.7 billion and $2.7 billion of repurchase agreements with weighted average borrowing rates of 0.48% and 0.35% and weighted average remaining maturities of 64 days and 48 days as of September 30, 2012 and December 31, 2011, respectively. At September 30, 2012 and December 31, 2011, Agency RMBS pledged as collateral under these repurchase agreements had an estimated fair value of $1.7 billion and $2.8 billion, respectively. The average daily balances of the Company's repurchase agreements for the nine months ended September 30, 2012 and year ended December 31, 2011 were $2.3 billion and $3.8 billion, respectively. The interest rates of these repurchase agreements are generally indexed to the one-month or the three-month LIBOR rate and re-price accordingly.

At September 30, 2012 and December 31, 2011, the repurchase agreements collateralized by Agency RMBS had the following remaining maturities.

	September 30, 2012	December 31, 2011
	(dollars in thousands)	
Overnight	$ 35,430	$ -
1-29 days	1,130,037	1,368,945
30 to 59 days	144,595	836,007
60 to 89 days	-	-
90 to 119 days	35,475	171,836
Greater than or equal to 120 days	313,369	296,201
Total	$ 1,658,906	$ 2,672,989

At September 30, 2012 and December 31, 2011, the Company did not have an amount at risk under its repurchase agreements greater than 10% of its equity with any counterparty.

7. Securitized Debt

All of the Company's securitized debt is collateralized by residential mortgage loans or Non-Agency RMBS. For financial reporting purposes, the Company's securitized debt is accounted for as secured borrowings. Thus, the residential mortgage loans or RMBS held as collateral are recorded in the assets of the Company as securitized loans held for investment or Non-Agency RMBS transferred to consolidated VIEs and the securitized debt is recorded as a non-recourse liability in the accompanying Consolidated Statements of Financial Condition.

At September 30, 2012 the Company's securitized debt collateralized by residential mortgage loans had a principal balance of $1.0 billion. The debt matures between the years 2023 and 2042. At September 30, 2012 the debt carried a weighted average cost of financing equal to 3.63%. At December 31, 2011, the Company's securitized debt collateralized by residential mortgage loans had a principal balance of $222.9 million. At December 31, 2011, the debt carried a weighted average cost of financing equal to 5.48%.

At September 30, 2012 the Company's securitized debt collateralized by Non-Agency RMBS had a principal balance of $1.3 billion. The debt matures between the years 2035 and 2047. At September 30, 2012 the debt carried a weighted average cost of financing equal to 4.96%. At December 31, 2011, the Company's securitized debt collateralized by Non-Agency RMBS had a principal balance of $1.7 billion. At December 31, 2011, the debt carried a weighted average cost of financing equal to 5.09%.

The carrying value of securitized debt is based on its amortized cost, net of premiums or discounts related to sales of senior certificates to third parties. The following table presents the estimated principal repayment schedule of the securitized debt at September 30, 2012 and December 31, 2011, based on expected cash flows of the residential mortgage loans or RMBS, as adjusted for projected losses on the underlying collateral of the debt. All of the securitized debt recorded in the Company's Consolidated Statements of Financial Condition is non-recourse to the Company.

	September 30, 2012	December 31, 2011
	(dollars in thousands)	
Within One Year	$ 640,029	$ 488,886

One to Three Years	737,935	598,921
Three to Five Years	388,354	276,965
Greater Than or Equal to Five Years	454,842	404,386
Total	$ 2,221,160	$ 1,769,158

Maturities of the Company's securitized debt are dependent upon cash flows received from the underlying loans. The estimate of their repayment is based on scheduled principal payments on the underlying loans. This estimate will differ from actual amounts to the extent prepayments and/or loan losses are experienced. See Notes 3 and 4 for a more detailed discussion of the securities and loans collateralizing the securitized debt.

8. Consolidated Securitization Vehicles and Other Variable Interest Entities

Since its inception, the Company has created VIEs for the purpose of securitizing whole mortgage loans or re-securitizing RMBS and obtaining permanent, non-recourse term financing. The Company evaluated its interest in each VIE to determine if it is the primary beneficiary.

Determining the primary beneficiary of a VIE requires significant judgment. The Company determined that for the securitizations it consolidates, its ownership of substantially all subordinate interests provided the Company with the obligation to absorb losses and/or the right to receive benefits from the VIE that could be significant to the VIE. In addition, the Company is considered to have the power to direct the activities of the VIEs that most significantly impact the VIEs' economic performance ("power") or the Company was determined to have power in connection with its involvement with the purpose and design of the VIE. Two trusts formed prior to January 1, 2010 that were evaluated by the Company did not meet the requirements for consolidation due to the Company's inability to control certain activities of the VIEs.

As of September 30, 2012, the Company's consolidated statement of financial condition includes nine consolidated VIE's with $4.4 billion of assets and $2.3 billion of liabilities.

The Company's interest in the assets held by these securitization vehicles, which are consolidated on the Company's statement of financial condition, is restricted by the structural provisions of these entities, and a recovery of the Company's investment in the vehicles will be limited by each entity's distribution provisions. The liabilities of the securitization vehicles, which are also consolidated on the Company's statement of financial condition, are non-recourse to the Company, and can generally only be satisfied from each securitization vehicle's respective asset pool.

The Company is not obligated to provide, nor has it provided, any financial support to these consolidated securitization vehicles.

VIEs for Which the Company is the Primary Beneficiary

The retained beneficial interests in VIEs for which the Company is the primary beneficiary are typically the subordinated tranches of these re-securitizations and in some cases the Company may hold interests in additional tranches. The result of consolidation at September 30, 2012 is the inclusion of $3.2 billion of Non-Agency RMBS at fair value representing the underlying securities of the trusts, the inclusion of $1.1 billion of securitized loans held for investment, the recognition of $1.3 billion of securitized debt associated with Non-Agency RMBS transferred to consolidated VIEs and $1.0 billion of securitized debt associated with loans held for investment. In addition, at September 30, 2012 the Company recognized $25.2 million and $8.5 million of accrued interest receivable and accrued interest payable, respectively, of the securitizations.

The trusts are structured as pass through entities that receive principal and interest on the underlying collateral and distribute those payments to the certificate holders. The assets held by the securitization entities are restricted in that they can only be used to fulfill the obligations of the securitization entity. The Company's risks associated with its involvement with these VIEs are limited to its risks and rights as a certificate holder of the bonds it has retained. There have been no recent changes to the nature of risks associated with the Company's involvement with VIEs.

The securitization entities are comprised of senior classes of RMBS and jumbo, prime, residential mortgage loans. See Notes 3 and 4 for a discussion of the characteristics of the securities and loans in the Company's portfolio.

The table below reflects the assets and liabilities recorded in the consolidated statements of financial condition related to the consolidated VIEs as of September 30, 2012 and December 31, 2011.

	September 30, 2012	December 31, 2011
	(dollars in thousands)	
Assets		

Non-Agency RMBS transferred to consolidated VIEs	$	3,235,572	$	3,270,332
Securitized loans held for investment		1,136,923		256,632
Accrued interest receivable		25,215		26,616
Liabilities				
Securitized debt, collateralized by Non-Agency RMBS	$	1,252,752	$	1,630,276
Securitized debt, collateralized by loans held for investment		1,033,925		212,778
Accrued interest payable		8,477		8,130

Income and expense and OTTI amounts related to consolidated VIEs recorded in the Consolidated Statements of Operations and Comprehensive Income is presented in the table below.

	For the Quarter Ended	
	September 30, 2012	September 30, 2011
	(dollars in thousands)	
Interest income, Assets of consolidated VIEs	$ 108,120	$ 116,805
Interest expense, Non-recourse liabilities of VIEs	(32,075)	(29,643)
Net interest income	$ 76,045	$ 87,162
Total other-than-temporary impairment losses	(241)	(36,082)
Portion of loss recognized in other comprehensive income (loss)	(3,032)	(100,701)
Net other-than-temporary credit impairment losses	$ (3,273)	$ (136,783)

	For the Nine Months Ended:	
	September 30, 2012	September 30, 2011
	(dollars in thousands)	
Interest income, Assets of consolidated VIEs	$ 315,962	$ 339,765
Interest expense, Non-recourse liabilities of VIEs	(85,604)	(95,002)
Net interest income	$ 230,358	$ 244,763
Total other-than-temporary impairment losses	$ (7,510)	$ (62,970)
Portion of loss recognized in other comprehensive income (loss)	(76,164)	(112,985)
Net other-than-temporary credit impairment losses	$ (83,674)	$ (175,955)

The amounts recorded on the consolidated statements of cash flows related to consolidated VIEs is presented in the table below for the periods presented.

	For the Quarter Ended	
	September 30, 2012	September 30, 2011
	(dollars in thousands)	
Amortization of deferred financing costs	1,215	386
Accretion (amortization) of securitized debt discounts/premiums, net	4,352	2,949
Principal payments, Non-Agency RMBS transferred to consolidated VIE's	130,869	156,180
Principal payments, Securitized loans held for investment	183,775	16,945
Proceeds from securitized debt borrowings, collateralized by loans held for investment	11,628	-
Payments on securitized debt borrowings, collateralized by loans held for investment	(182,073)	(15,895)
	(122,494)	(153,979)

Payments on securitized debt borrowings, collateralized by Non-Agency RMBS				
Decrease (increase) in accrued interest receivable		927		(1,689)
Increase (decrease) in accrued interest payable		(1,080)		(861)
Net cash provided by/(used in) consolidated VIEs	$	27,119	$	4,036

	For the Nine Months Ended:			
	September 30, 2012		September 30, 2011	
	(dollars in thousands)			
Amortization of deferred financing costs	$	6,480	$	1,294
Accretion (amortization) of securitized debt discounts/premiums, net		3,469		9,452
Payment of deferred financing costs		(8,073)		-
Principal payments, Non-Agency RMBS transferred to consolidated VIE's		394,641		541,348
Principal payments, Securitized loans held for investment		297,923		65,347
Proceeds from securitized debt borrowings, collateralized by loans held for investment		1,113,154		-
Payments on securitized debt borrowings, collateralized by loans held for investment		(292,568)		(61,054)
Proceeds from securitized debt borrowings, collateralized by Non-Agency RMBS		-		311,012
Payments on securitized debt borrowings, collateralized by Non-Agency RMBS		(380,432)		(520,730)
Decrease (increase) in accrued interest receivable		1,401		(3,592)
Increase (decrease) in accrued interest payable		347		(1,241)
Net cash provided by/(used in) consolidated VIEs	$	1,136,342	$	341,836

VIEs for Which the Company is Not the Primary Beneficiary

The Company has interests in the following VIEs in addition to the RMBS described in Note 3.

The Company’s involvement with VIEs for which it is not considered the primary beneficiary generally is in the form of owning securities issued by the trusts, similar to its investments in other RMBS that do not provide the Company with a controlling financial interest. The Company’s maximum exposure to loss does not include other-than-temporary impairments or other write-downs that the Company previously recognized through earnings.

The table below represents the carrying amounts and classification of assets recorded on the Company's consolidated financial statements related to its variable interests in non-consolidated VIEs, as well as its maximum exposure to loss as a result of its involvement with these VIEs, which is represented by the fair value of the Company's investments in the trusts.

	September 30, 2012		December 31, 2011	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(dollars in thousands)			
Assets				
Non-Agency RMBS				
Senior	$79	$82	$168	$127
Senior interest-only	-	179	128	266
Subordinated	894	2,709	4,651	4,858
Agency RMBS	1,356	1,148	1,890	2,273
Total	$2,329	$4,118	$6,837	$7,524

9. Interest Rate Swaps

In connection with the Company's interest rate risk management strategy, the Company economically hedges a portion of its interest rate risk by entering into derivative financial instrument contracts in the form of interest rate swaps. The Company's swaps are used to lock in a fixed rate related to a portion of its current and anticipated payments on its repurchase agreements. The Company typically agrees to pay a fixed rate of interest ("pay rate") in exchange for the right to receive a floating rate of interest ("receive rate") over a specified period of time. These derivative financial instrument contracts are not designated as hedges under ASC 815, Derivatives and Hedging. The use of interest rate swaps creates exposure to credit risk relating to potential losses that could be recognized if the counterparties to these instruments fail to perform their obligations under the contracts. In the event of a default by the counterparty, the Company could have difficulty obtaining its RMBS pledged as collateral for swaps. The Company periodically monitors the credit of its counterparties to determine if it is exposed to counterparty credit risk. See Note 13 for further discussion.

The table below summarizes the location and fair value of interest rate swaps reported in the Consolidated Statements of Financial Condition as of September 30, 2012 and December 31, 2011.

	Location on Consolidated Statement of Financial Condition	Notional Amount	Net Estimated Fair Value/Carrying Value	Value of Agency RMBS Pledged as Collateral
(dollars in thousands)				
September 30, 2012	Liabilities	$ 1,355,000	$ (59,073)	$ 62,734
December 31, 2011	Liabilities	$ 950,000	$ (44,467)	$ 46,647

The effect of the Company's interest rate swaps on the Consolidated Statements of Operations and Comprehensive Income is presented below.

Location on Consolidated Statements of Operations and

	Comprehensive Income Net Unrealized Gains (Losses) on Interest Rate Swaps	Net Realized Gains (Losses) on Interest Rate Swaps
	(dollars in thousands)	
For the Quarter Ended:		
September 30, 2012	$ (4,427)	$ (5,298)
September 30, 2011	$ (25,312)	$ (4,500)
For the Nine Months Ended:		
September 30, 2012	$ (14,607)	$ (14,890)
September 30, 2011	$ (34,981)	$ (11,644)

The weighted average pay rate on the Company's interest rate swaps at September 30, 2012 was 1.81% and the weighted average receive rate was 0.22%. The weighted average pay rate on the Company's interest rate swaps at December 31, 2011 was 2.08% and the weighted average receive rate was 0.29%.

The following table summarizes the notional amounts and unrealized gains (losses) of interest rate swap contracts on a gross basis, amounts offset in accordance with netting arrangements and net amounts as presented in the Consolidated Statements of Financial Condition as of September 30, 2012 and December 31, 2011.

	September 30, 2012			
	Interest Rate Swaps - Asset		Interest Rate Swaps - Liability	
	Notional	Unrealized Gains	Notional	Unrealized Losses
	(dollars in thousands)			
Gross Amounts	$ -	$ -	$ 1,355,000	$ 59,073
Amounts Offset	-	-	-	-
Netted Amounts	$ -	$ -	$ 1,355,000	$ 59,073

	December 31, 2011			
	Interest Rate Swaps - Asset		Interest Rate Swaps - Liability	
	Notional	Unrealized Gains	Notional	Unrealized Losses
	(dollars in thousands)			
Gross Amounts	$ -	$ -	$ 950,000	$ 44,467
Amounts Offset	-	-	-	-
Netted Amounts	$ -	$ -	$ 950,000	$ 44,467

All of the Company's derivative contracts are subject to International Swaps and Derivatives Association Master Agreements ("ISDA") which contain provisions that grant counterparties certain rights with respect to the applicable ISDA upon the occurrence of (i) negative performance that results in a decline in net assets in excess of specified thresholds or dollar amounts over set periods of time, (ii) the Company's failure to maintain its REIT status, (iii) the Company's failure to comply with limits on the amount of leverage, and (iv) the Company's stock being delisted from the New York Stock Exchange (NYSE). Upon the occurrence of items (i) through (iv), the counterparty to the applicable ISDA has a right to terminate the ISDA in accordance with its provisions. The aggregate fair value of all derivative instruments with credit-risk-related contingent features that are in a net liability position at September 30, 2012 is approximately $59.1 million including accrued interest, which represents the maximum amount the Company would be required to pay upon termination, which is fully collateralized.

10. Common Stock

On January 28, 2011 the Company entered into an equity distribution agreement with FIDAC and UBS Securities LLC ("UBS"). Through this agreement, the Company may sell through UBS, as its sales agent, up to 125,000,000 shares of its common stock in ordinary brokers' transactions at market prices or other transactions as agreed between the Company and UBS. The Company did not sell any shares of its common stock under the equity distribution agreement during the quarter and nine months ended September 30, 2012 or September 30, 2011. As a result of the Company's delay in filing its SEC reports by the filing date required by the SEC (including the grace period permitted by Rule 12b-25 under the Securities Exchange Act of 1934, as amended), the Company will not be able to issue shares of its common stock under the equity distribution agreement until filings with the SEC have been timely made for a full year.

On September 24, 2009, the Company implemented a Dividend Reinvestment and Share Purchase Plan ("DRSPP"). The DRSPP provides holders of record of its common stock an opportunity to automatically reinvest all or a portion of their cash distributions received on common stock in additional shares of the Company's common stock as well as to make optional cash payments to purchase shares of its common stock. Persons who are not already stockholders may also purchase the Company's common stock under the plan through optional cash payments. The DRSPP is administered by the Administrator, Computershare. The DRSPP was suspended during the quarter ended March 31, 2012 when the Company was no longer current in its filings with the SEC. During the nine months ended September 30, 2012 the Company raised $117 thousand by issuing 39,000 shares through the DRSPP. During the nine months ended September 30, 2011 the Company raised $786 thousand by issuing 214,000 shares through the DRSPP. As a result of the Company's delay in filing its SEC reports by the filing date required by the SEC (including the grace period permitted by Rule 12b-25 under the Securities Exchange Act of 1934, as amended), the Company will not be able to issue shares under the DRSPP until filings with the SEC have been timely made for a full year.

During the quarter ended September 30, 2012 the Company declared dividends to common shareholders totaling $92.4 million, or $0.09 per share. During the quarter ended September 30, 2011, the Company declared dividends to common shareholders totaling $133.4 million, or $0.13 per share.

During the nine months ended September 30, 2012 the Company declared dividends to common shareholders totaling $297.8 million, or $0.29 per share. During the nine months ended September 30, 2011, the Company declared dividends to common shareholders totaling $410.5 million, or $0.40 per share.

Earnings per share for the quarters and nine months ended September 30, 2012 and September 30, 2011, respectively, is computed as follows:

	For the Quarter Ended September 30, 2012 (dollars in thousands)	September 30, 2011
Numerator:		
Net income	$ 128,068	$ (60,036)
Effect of dilutive securities:	-	-
Dilutive net income available to stockholders	$ 128,068	$ (60,036)
Denominator:		
Weighted average basic shares	1,026,841,087	1,026,404,030
Effect of dilutive securities	663,943	791,374
Weighted average dilutive shares	1,027,505,030	1,027,195,404
Net income per average share attributable to common stockholders - Basic	$ 0.12	$ (0.06)
Net income per average share attributable to common stockholders - Diluted	$ 0.12	$ (0.06)

	For the Nine Months Ended: September 30, 2012 (dollars in thousands)	September 30, 2011
Numerator:		
Net income	$ 249,082	$ 94,581
Effect of dilutive securities:	-	-
Dilutive net income available to stockholders	$ 249,082	$ 94,581
Denominator:		
Weighted average basic shares	1,026,804,427	1,026,308,073
Effect of dilutive securities	695,546	822,063
Weighted average dilutive shares	1,027,499,973	1,027,130,136

Net income per average share attributable to common stockholders - Basic	$	0.24	$	0.09
Net income per average share attributable to common stockholders - Diluted	$	0.24	$	0.09

11. Long Term Incentive Plan

The Company has adopted a long term stock incentive plan to provide incentives to its independent directors and employees of FIDAC and its affiliates, to reward their efforts, to attract, reward and retain personnel and other service providers, and to align their interest with the common share investors. The incentive plan authorizes the Compensation Committee of the board of directors to grant awards, including incentive stock options, non-qualified stock options, restricted shares and other types of incentive awards. The specific award granted to an individual is based upon, in part, the individual's position within FIDAC, the individual's position within the Company, his or her contribution to the Company's performance, as well as the recommendations of FIDAC. The incentive plan authorizes the granting of options or other awards for an aggregate of the greater of 8.0% of the outstanding shares of the Company's common stock up to a ceiling of 40,000,000 shares.

On January 2, 2008, the Company granted restricted stock awards in the amount of 1,301,000 shares to FIDAC's employees and the Company's independent directors. The awards to the independent directors vested on the date of grant and the awards to FIDAC's employees vest quarterly over a period of 10 years. Of these shares, as of September 30, 2012, 637,000 shares have vested and 46,000 shares were forfeited. As of September 30, 2012 there was $11.8 million of total unrecognized compensation costs related to non-vested share-based compensation arrangements granted under the long term incentive plan, based on the closing price of the shares on the grant date. As of September 30, 2012 there was $1.8 million of total unrecognized compensation costs related to non-vested share-based compensation arrangements granted under the long term incentive plan, based on the closing price of the shares at the quarter end. That cost is expected to be recognized over a weighted-average period of 5.3 years.

The total fair value of shares vested, less those forfeited, during the quarters ended September 30, 2012 and September 30, 2011 was $74 thousand and $111 thousand, respectively, based on the closing price of the stock on the vesting date. The total fair value of shares vested, less those forfeited, during the nine months ended September 30, 2012 and September 30, 2011 was $244 thousand and $361 thousand, respectively. For the quarters ended September 30, 2012 and September 30, 2011, compensation expense associated with the amortization of the fair value of the restricted stock was approximately $75 thousand and $112 thousand, respectively. For the nine months ended September 30, 2012 and September 30, 2011, compensation expense associated with the amortization of the fair value of the restricted stock was approximately $242 thousand and $360 thousand, respectively.

The Company's independent directors receive a fixed dollar amount of the Company's common stock in return for services provided to the Company. Equity based awards granted to the independent directors vest during the year of service. For the quarters ended September 30, 2012 and September 30, 2011, the Company recognized $75 thousand and $68 thousand, respectively, of stock based compensation to independent directors. For the nine months ended September 30, 2012 and September 30, 2011, the Company recognized $225 thousand and $203 thousand, respectively, of stock based compensation to independent directors.

The following table presents information with respect to the Company's restricted stock awards during the quarters and nine months ended September 30, 2012 and September 30, 2011:

	For the Quarter Ended			
	September 30, 2012		September 30, 2011	
	Number of Shares	Weighted Average Grant Date Fair Value	Number of Shares	Weighted Average Grant Date Fair Value
Unvested shares outstanding - beginning of period	695,200	17.72	821,600	17.72
Granted	-	-	-	-
Vested	(31,383)	17.72	(31,374)	17.72
Forfeited	(217)	17.72	(226)	17.72
Unvested shares outstanding - end of period	663,600	17.72	790,000	17.72

	For the Nine Months Ended			
	September 30, 2012		September 30, 2011	
	Number of Shares	Weighted Average Grant Date Fair Value	Number of Shares	Weighted Average Grant Date Fair Value
Unvested shares outstanding - beginning of period	758,400	17.72	884,800	17.72
Granted	-	-	-	-
Vested	(94,202)	17.72	(93,074)	17.72
Forfeited	(598)	17.72	(1,726	