CHIMERA INVESTMENT CORP
Form 10-Q
November 03, 2016
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q
[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE QUARTERLY PERIOD ENDED: September 30, 2016
OR
[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE TRANSITION PERIOD FROM _______________ TO _________________
COMMISSION FILE NUMBER: 1-33796
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.) |

520 Madison Avenue
32nd Floor
NEW YORK, NEW YORK
(Address of principal executive offices)
10022
(Zip Code)
(212) 626-2300
(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 þ No
Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (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 þ No
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 Non-accelerated filer Smaller reporting company
Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes No 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 October 31, 2016 |
|---|---|
| Common Stock, $.01 par value | 187,729,838 |

CHIMERA INVESTMENT CORPORATION
FORM 10-Q
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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)
(Unaudited)

| | September 30, 2016 | December 31, 2015 |
|---|---|---|
| Assets: | | |
| Cash and cash equivalents | $156,608 | $114,062 |
| Non-Agency RMBS, at fair value | 3,437,235 | 3,675,841 |
| Agency MBS, at fair value | 4,362,550 | 6,514,824 |
| Securitized loans held for investment, at fair value | 8,909,037 | 4,768,416 |
| Accrued interest receivable | 84,328 | 66,247 |
| Other assets | 216,790 | 189,796 |
| Derivatives, at fair value, net | 2,153 | 15,460 |
| Total assets (1) | $17,168,701 | $15,344,646 |
| Liabilities: | | |
| Repurchase agreements, MBS ($7.3 billion and $8.8 billion pledged as collateral, respectively) | $5,817,519 | $7,439,339 |
| Securitized debt, collateralized by Non-Agency RMBS ($1.9 billion and $2.1 billion pledged as collateral, respectively) | 380,715 | 529,415 |
| Securitized debt at fair value, collateralized by loans held for investment ($8.9 billion and $4.8 billion pledged as collateral, respectively) | 7,191,462 | 3,720,496 |
| Payable for investments purchased | 578,499 | 560,641 |
| Accrued interest payable | 49,743 | 37,432 |
| Dividends payable | 90,645 | 90,097 |
| Accounts payable and other liabilities | 15,309 | 11,404 |
| Derivatives, at fair value | 8,009 | 9,634 |
| Total liabilities (1) | $14,131,901 | $12,398,458 |
| | | |
| 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; 300,000,000 shares authorized, 187,729,765 and 187,711,868 shares issued and outstanding, respectively | 1,877 | 1,877 |
| Additional paid-in-capital | 3,367,943 | 3,366,568 |
| Accumulated other comprehensive income | 897,703 | 773,791 |
| Accumulated deficit | (1,230,723) | (1,196,048) |
| Total stockholders' equity | $3,036,800 | $2,946,188 |
| Total liabilities and stockholders' equity | $17,168,701 | $15,344,646 |

(1) The Company's consolidated statements of financial condition include assets of consolidated variable interest entities (“VIEs”) that can only be used to settle obligations and liabilities of the VIE for which creditors do not have recourse to the primary beneficiary (Chimera Investment Corporation). As of September 30, 2016 and December 31, 2015, total assets of consolidated VIEs were $10,996,318 and $7,031,278, respectively, and total liabilities of consolidated VIEs were $7,599,439 and $4,262,017, respectively. See Note 8 for further discussion.

See accompanying notes to consolidated financial statements.

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, 2016 | September 30, 2015 | September 30, 2016 | September 30, 2015 |
| Net Interest Income: | | | | |
| Interest income (1) | $250,953 | $ 211,876 | $673,246 | $ 670,825 |
| Interest expense (2) | 94,911 | 67,910 | 241,120 | 194,410 |
| Net interest income | 156,042 | 143,966 | 432,126 | 476,415 |
| Other-than-temporary impairments: | | | | |
| Total other-than-temporary impairment losses | (993) | (3,129) | (8,555) | (6,389) |
| Portion of loss recognized in other comprehensive income | (10,581) | (14,703) | (34,652) | (46,359) |
| Net other-than-temporary credit impairment losses | (11,574) | (17,832) | (43,207) | (52,748) |
| Other investment gains (losses): | | | | |
| Net unrealized gains (losses) on derivatives | 27,628 | (71,540) | (51,382) | 20,543 |
| Realized gains (losses) on terminations of interest rate swaps | — | — | (60,616) | (99,703) |
| Net realized gains (losses) on derivatives | (14,268) | (21,160) | (58,934) | (80,023) |
| Net gains (losses) on derivatives | 13,360 | (92,700) | (170,932) | (159,183) |
| Net unrealized gains (losses) on financial instruments at fair value | 32,999 | (40,955) | 80,217 | (88,640) |
| Net realized gains (losses) on sales of investments | 3,079 | 3,539 | 7,035 | 42,789 |
| Gains (losses) on Extinguishment of Debt | (45) | (19,915) | (1,811) | (14,836) |
| Total other gains (losses) | 49,393 | (150,031) | (85,491) | (219,870) |
| Other income: | | | | |
| Other income | — | — | 95,000 | — |
| Total other income | — | — | 95,000 | — |
| Other expenses: | | | | |
| Management fees | — | 4,088 | — | 24,610 |
| Expense recoveries from Manager | — | (1,140) | — | (6,905) |
| Net management fees | — | 2,948 | — | 17,705 |
| Compensation and benefits | 6,911 | 3,955 | 19,087 | 4,482 |
| General and administrative expenses | 4,332 | 8,534 | 13,073 | 22,028 |
| Servicing Fees of consolidated VIEs | 9,788 | 6,499 | 23,139 | 19,276 |
| Deal Expenses | — | 2,426 | 13,022 | 5,337 |
| Total other expenses | 21,031 | 24,362 | 68,321 | 68,828 |
| Income (loss) before income taxes | 172,830 | (48,259) | 330,107 | 134,969 |
| Income taxes | 13 | — | 65 | — |
| Net income (loss) | $172,817 | $ (48,259) | $330,042 | $ 134,969 |
| | | | | |
| Net income (loss) per share available to common shareholders: | | | | |
| Basic | $0.92 | $ (0.24) | $1.76 | $ 0.67 |
| Diluted | $0.92 | $ (0.24) | $1.76 | $ 0.66 |
| | | | | |
| Weighted average number of common shares outstanding: | | | | |
| Basic | 187,729,765 | 197,787,858 | 187,727,662 | 202,891,610 |
| Diluted | 187,919,792 | 197,875,408 | 187,917,694 | 202,979,160 |

| | | | | |
|---|---|---|---|---|
| Dividends declared per share of common stock | $0.48 | $ 0.48 | $1.94 | $ 1.44 |
| | | | | |
| Comprehensive income (loss): | | | | |
| Net income (loss) | $172,817 | $ (48,259) | $330,042 | $ 134,969 |
| Other comprehensive income: | | | | |
| Unrealized gains (losses) on available-for-sale securities, net | (18,364) | 16,512 | 94,059 | (121,142) |
| Reclassification adjustment for net losses included in net income for other-than-temporary credit impairment losses | 11,574 | 17,832 | 43,207 | 52,748 |
| Reclassification adjustment for net realized losses (gains) included in net income | (2,680) | (3,903) | (13,354) | (43,038) |
| Other comprehensive income (loss) | (9,470) | 30,441 | 123,912 | (111,432) |
| Comprehensive income (loss) | $163,347 | $ (17,818) | $453,954 | $ 23,537 |

(1) Includes interest income of consolidated VIEs of $195,488 and $142,053 for the quarters ended September 30, 2016 and 2015, respectively and interest income of consolidated VIEs of $488,353 and $439,571 for the nine months ended September 30, 2016 and 2015, respectively. See Note 8 to consolidated financial statements for further discussion.
(2) Includes interest expense of consolidated VIEs of $70,715 and $50,837 for the quarters ended September 30, 2016 and 2015, respectively and interest expense of consolidated VIEs of $168,738 and $148,017 for the nine months ended September 30, 2016 and 2015, respectively. See Note 8 to consolidated financial statements for further discussion.

See accompanying notes to consolidated financial statements.

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

| | Common Stock Par Value | Additional Paid-in Capital | Accumulated Other Comprehensive Income | Accumulated Deficit | Total |
|---|---|---|---|---|---|
| Balance, December 31, 2014 | $ 2,055 | $ 3,614,411 | $ 1,046,680 | $ (1,055,456) | $ 3,607,690 |
| Net income (loss) | — | — | — | 134,969 | 134,969 |
| Cumulative effect of accounting change (1) | — | — | — | (12,137) | (12,137) |
| Other comprehensive income (loss) | — | — | (111,432) | — | (111,432) |
| Stock based compensation | 2 | 944 | — | — | 946 |
| Repurchase of common stock | (114) | (212,498) | — | — | (212,612) |
| Common dividends declared | — | — | — | (288,707) | (288,707) |
| Balance, September 30, 2015 | $ 1,943 | $ 3,402,857 | $ 935,248 | $ (1,221,331) | $ 3,118,717 |
| | | | | | |
| Balance, December 31, 2015 | $ 1,877 | $ 3,366,568 | $ 773,791 | $ (1,196,048) | $ 2,946,188 |
| Net income (loss) | — | — | — | 330,042 | 330,042 |
| Other comprehensive income (loss) | — | — | 123,912 | — | 123,912 |
| Stock based compensation | — | 1,375 | — | — | 1,375 |
| Common dividends declared | — | — | — | (364,717) | $ (364,717) |
| Balance, September 30, 2016 | $ 1,877 | $ 3,367,943 | $ 897,703 | $ (1,230,723) | $ 3,036,800 |

(1) Adoption of ASU No. 2014-13, Measuring the Financial Assets and the Financial Liabilities of a Consolidated Collateralized Financing Entity.

See accompanying notes to consolidated financial statements.

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

| | For the Nine Month Ended | |
|---|---|---|
| | September 30, 2016 | September 30, 2015 |
| Cash Flows From Operating Activities: | | |
| Net income | $330,042 | $134,969 |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: | | |
| (Accretion) amortization of investment discounts/premiums, net | 4,084 | (3,425) |
| Accretion (amortization) of deferred financing costs and securitized debt discounts/premiums, net | (5,769) | 11,554 |
| Amortization of swaption premium | 5,130 | — |
| Net unrealized losses (gains) on derivatives | 51,382 | (20,543) |
| Proceeds (payments) for derivative sales and settlements | — | (12,327) |
| Margin (paid) received on derivatives | (41,283) | 30,911 |
| Net unrealized losses (gains) on financial instruments at fair value | (80,217) | 88,640 |
| Net realized losses (gains) on sales of investments | (7,035) | (42,789) |
| Net other-than-temporary credit impairment losses | 43,207 | 52,748 |
| (Gain) loss on extinguishment of debt | 1,811 | 14,836 |
| Equity-based compensation expense | 1,375 | 946 |
| Changes in operating assets: | | |
| Decrease (increase) in accrued interest receivable, net | (18,081) | 1,325 |
| Decrease (increase) in other assets | (36,969) | (13,540) |
| Changes in operating liabilities: | | |
| Increase (decrease) in accounts payable and other liabilities | 3,905 | 9,047 |
| Increase (decrease) in investment management fees and expenses payable to affiliate | — | (6,365) |
| Increase (decrease) in accrued interest payable, net | 12,311 | 7,954 |
| Net cash provided by (used in) operating activities | $263,893 | $253,941 |
| Cash Flows From Investing Activities: | | |
| Agency MBS portfolio: | | |
| Purchases | $(810,630) | $(3,452,119) |
| Sales | 2,555,228 | 4,780,881 |
| Principal payments | 471,657 | 888,591 |
| Non-Agency RMBS portfolio: | | |
| Purchases | (160,805) | (792,408) |
| Sales | 95,399 | 109,999 |
| Principal payments | 402,971 | 280,867 |
| Securitized loans held for investment: | | |
| Purchases | (4,745,083) | (281,811) |
| Principal payments | 696,281 | 533,628 |
| Acquisition of investments in consolidated VIEs | — | (109,872) |
| Net cash provided by (used in) investing activities | $(1,494,982) | $1,957,756 |
| Cash Flows From Financing Activities: | | |
| Proceeds from repurchase agreements | $27,792,856 | $32,627,948 |
| Payments on repurchase agreements | (29,414,676) | (33,932,508) |
| Proceeds from securitized debt borrowings, collateralized by loans held for investment | 4,180,227 | 1,064,789 |
| Payments on securitized debt borrowings, collateralized by loans held for investment | (773,875) | (1,456,021) |

| | | |
|---|---|---|
| Payments on securitized debt borrowings, collateralized by Non-Agency RMBS | (146,729) | (138,009) |
| Payments on repurchase of common stock | — | (212,612) |
| Common dividends paid | (364,168) | (289,807) |
| Net cash provided by (used in) financing activities | $1,273,635 | $(2,336,220) |
| Net increase (decrease) in cash and cash equivalents | 42,546 | (124,523) |
| Cash and cash equivalents at beginning of period | 114,062 | 164,620 |
| Cash and cash equivalents at end of period | $156,608 | $40,097 |
| | | |
| Supplemental disclosure of cash flow information: | | |
| Interest received | $659,249 | $668,725 |
| Interest paid | $234,577 | $198,010 |
| Management fees and expenses paid | $— | $30,975 |
| Non-cash investing activities: | | |
| Receivable for investments sold | $— | $57,680 |
| Payable for investments purchased | $578,499 | $715,512 |
| Net change in unrealized gain (loss) on available-for sale securities | $123,912 | $(111,432) |

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| | | |
|---|---|---|
| Acquisition of investments in consolidated VIEs: | | |
| Securitized loans held for investment, at fair value | $— | $295,225 |
| Securitized debt at fair value | $— | $185,353 |
| | | |
| Non-cash financing activities: | | |
| Common dividends declared, not yet paid | $90,645 | $91,383 |

See accompanying notes to consolidated financial statements.

CHIMERA INVESTMENT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

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 conducts its operations through various subsidiaries including subsidiaries it treats as taxable REIT subsidiaries (“TRS”). In general, a TRS may hold assets and engage in activities that the Company cannot hold or engage in directly and generally may engage in any real estate or non-real estate related business. The Company currently has eight wholly owned direct subsidiaries: Chimera RMBS Whole Pool LLC, and Chimera RMBS LLC formed in June 2009; Chimera Special Holdings LLC, formed in January 2010; CIM Trading Company LLC (“CIM Trading”), a TRS formed in July 2010; Chimera Funding TRS LLC (“CIM Funding TRS”), a TRS formed in October 2013, Chimera CMBS Whole Pool LLC formed in March 2015; Chimera Insurance Company, LLC formed in July 2015 and Chimera RR Holdings LLC formed in April 2016.

Until August 5, 2015, the Company was externally managed by Fixed Income Discount Advisory Company (“FIDAC” or “Manager”), under the terms of a management agreement (“Management Agreement”). On August 5, 2015, the Company announced it had internalized its management and would continue to be led by its key professionals. In connection with the internalization, the Company and FIDAC terminated the Management Agreement.

2. Summary of the Significant Accounting Policies

(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. Certain prior period amounts have been reclassified to conform to the current period's presentation.

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 intercompany balances and transactions have been eliminated in consolidation.

The Company uses securitization trusts considered to be VIEs in its securitization and re-securitization transactions. VIEs are defined as entities in which equity investors (i) do not have the characteristics of a controlling financial interest, 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 VIEs’ 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 trusts are structured as pass through entities that receive principal and interest on the underlying collateral and distribute those payments to the security 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 holder of the security it has retained. There have been no recent changes to the nature of risks associated with the Company's involvement with VIEs.

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 provides the Company with the obligation to absorb losses or the right to receive benefits from the VIE that could be significant to the VIE. In addition, the Company has the power to direct the activities of the VIEs that most significantly impact the VIEs' economic performance ("power") such as rights to direct servicer activity or the Company was determined to have power in connection with its involvement with the purpose and design of the VIE.

The Company's interest in the assets held by these securitization vehicles, which are consolidated on the Company's Statements 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 Statements of Financial Condition, are non-recourse to the Company, and can generally only be satisfied from each securitization vehicle's respective asset pool.

The securitization entities are comprised of senior classes of residential mortgage backed securities ("RMBS") and residential mortgage loans. See Notes 3, 4 and 8 for further discussion of the characteristics of the securities and loans in the Company's portfolio.

(b) Statements of Financial Condition Presentation

The Company's Consolidated Statements of Financial Condition include both the Company's direct assets and liabilities and 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 is not obligated to provide, nor does it intend to provide, any financial support to these consolidated securitization vehicles. The notes to the consolidated financial statements describe the Company's assets and liabilities including 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, 2016 and December 31, 2015.

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

The Company invests in mortgage backed securities ("MBS") representing interests in obligations backed by pools of mortgage loans. The Company delineates between Agency MBS and Non-Agency MBS as follows: (1) Agency MBS are mortgage pass-through certificates, collateralized mortgage obligations ("CMOs"), and other MBS 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; and (2) Non-Agency MBS 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 MBS is subject to the performance of the mortgage loans or MBS collateralizing the obligation.

The Company also invests in Interest Only Agency MBS strips and Interest Only Non-Agency RMBS strips ("IO MBS strips"). IO MBS strips represent the Company's right to receive a specified proportion of the contractual interest flows of the collateral. Interest income on IO MBS strips is accrued based on the outstanding notional balance and the security's contractual terms, and amortization of any premium is calculated in accordance with the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 325-40, Beneficial Interests in Securitized Financial Assets ("ASC 325-40"). The Company accounts for IO MBS strips at fair value with changes in fair value recognized in the Company's Consolidated Statements of Operations and Comprehensive Income.

The Company classifies the majority of its MBS as available-for-sale and records investments at estimated fair value as described in Note 5 of these consolidated financial statements. The Company includes unrealized gains and losses considered to be temporary on all MBS in Other comprehensive income ("OCI") in the Consolidated Statements of Operations and Comprehensive Income. For IO MBS strips and certain other MBS investments, the Company carries these investments at fair value with changes in fair value 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 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 MBS is as follows:

Interest Income Recognition

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

Agency MBS and Non-Agency RMBS of High Credit Quality

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

- Agency MBS
- 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 using the lowest rating available;
2. The Company expects to collect all of the security's contractual cash flows; and
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 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 purchased at a discount and 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 (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; and
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 rate 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. On a quarterly basis, 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 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 (“OTTI”) 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 Non-Agency RMBS accounted for under ASC 325-40 and ASC 310-30, and generally result in recognition of an OTTI with no change in the effective interest rate used to recognize interest income.

Impairment

Considerations Applicable to all MBS

When the fair value of an available-for-sale MBS is less than its amortized cost, the security is considered impaired. On 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 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 recovery in fair value may not be adjusted through current earnings. Subsequent recoveries are amortized into income over the remaining life of the security as an adjustment to yield.

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 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 and 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 MBS is based on its review of the underlying securities or mortgage loans securing the MBS. 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, 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 MBS.

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.

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 OTTI is separated into a credit loss component that is recognized in earnings and the portion of loss recognized in other comprehensive income. 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 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.

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.

Investments for which the Company has elected the fair value option are not evaluated for OTTI as all changes in fair value are reflected in earnings.

(e) Securitized Loans Held for Investment

Prime residential mortgage loans:

A portion of the securitized loan portfolio is comprised of non-conforming, single family, owner occupied, jumbo prime loans that are not guaranteed as to repayment of principal or interest. These securitized loans are serviced and may be modified, in the event of a default, by a third-party servicer. The Company generally has the ability to approve certain loan modifications and determine the course of action to be taken as it relates to certain loans in default, including whether or not to proceed with foreclosure. These mortgage loans are designated as held for investment. Interest income on loans held for investment is recognized over the expected life of the loans using the interest method with changes in yield reflected in earnings on a prospective basis. The securitized loan portfolio comprised of non-conforming, single family, owner occupied, jumbo, prime loans is carried at fair value with changes in fair value recorded in earnings.

The Company estimates the fair value of securitized loans as described in Note 5 of these consolidated financial statements.

Seasoned subprime residential mortgage loans:

A portion of the securitized loan portfolio is comprised of seasoned subprime residential mortgage loans that are not guaranteed as to repayment of principal or interest. These securitized loans are serviced and may be modified, in the event of default, by a third-party servicer. The Company generally has the ability to approve certain loan modifications and determine the course of action to be taken as it relates to certain loans in default, including whether or not to proceed with foreclosure. These mortgage loans are designated as held for investment. Interest income on loans held for investment is recognized over the expected life of the loans using the interest method with changes in yield reflected in earnings on a prospective basis. The securitized loan portfolio comprised primarily of seasoned subprime residential mortgage loans is carried at fair value with changes in fair value recorded in earnings.

The Company estimates the fair value of securitized loans as described in Note 5 of these consolidated financial statements.

All residential mortgage loans:

Interest is accrued on all securitized loans held for investment when due. Interest which is not received at the due date is written off when it becomes delinquent. Nonrefundable fees and costs related to acquiring the Company’s securitized residential mortgage loans are recognized as expenses in the Statement of operations and comprehensive income. Income recognition is suspended for loans when, based on information from the servicer, a full recovery of interest or principal becomes doubtful.

Real estate owned (“REO”) represents properties which the Company has received the legal title of the property to satisfy the outstanding loan. REO is re-categorized from loan to REO when the Company takes legal title of the property. REO assets are measured and reported at the estimated fair value less the estimated cost to sell at the end of each reporting period. At the time the asset is re-categorized, any difference between the previously recorded loan balance and the carrying value of the REO at the time the Company takes legal title of the property, is recognized as a loss. All REO assets of the Company are held-for-sale and it is the Company's intention to sell the property in the shortest time possible to maximize their return and recovery on the previously recorded loan. The carrying value of REO assets at September 30, 2016 and December 31, 2015 was $12 million and $18 million, respectively, and were recorded in Other Assets on the Company's consolidated statements of financial condition.

(f) Repurchase Agreements

The Company finances the acquisition of a significant portion of its mortgage-backed securities with repurchase agreements. The Company has evaluated each agreement and has determined that each of the repurchase agreements be accounted for as secured borrowings.

(g) Securitized Debt, collateralized by Non-Agency RMBS and Securitized Debt, collateralized by loans held for investment

Certain re-securitization transactions classified as Securitized Debt, collateralized by Non-Agency RMBS, reflect the transfer to a trust of fixed or adjustable rate MBS which are classified as Non-Agency RMBS 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. The associated securitized debt is carried at amortized cost, net of any unamortized premiums or discounts.

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, collateralized by 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. The Securitized debt, collateralized by loans held for investment, is carried at fair value.

The Company recognizes interest expense on securitized debt over the expected life of the debt using the interest method with changes in yield reflected in earnings on a prospective basis.

The Company estimates the fair value of its securitized debt as described in Note 5 to these consolidated financial statements.

(h) Fair Value

Interest-Only MBS:

The Company accounts for the IO MBS strips at fair value with changes in fair value reported in earnings. The IO MBS strips are included in MBS, at fair value, on the accompanying Consolidated Statements of Financial Condition.

Included in Non-Agency RMBS, at fair value on the Consolidated Statements of Financial Condition are IO MBS strips carried at fair value with changes in fair value reflected in earnings of $305 million and $245 million as of September 30, 2016 and December 31, 2015. Included in Agency MBS, at fair value on the Consolidated Statements of Financial Condition are IO MBS strips carried at fair value with changes in fair value reflected in earnings of $157 million and $273 million as of September 30, 2016 and December 31, 2015. Interest income reported on all IO MBS securities was $10 million and $13 million for the quarters ended September 30, 2016 and 2015, respectively. Interest income reported on all IO MBS securities was $32 million and $38 million for the nine months ended September 30, 2016 and 2015, respectively.

Non-Agency RMBS:

The Company has elected the fair value option for certain interests in Non-Agency RMBS which we refer to as the overcollateralization classes. The cash flows for these holdings are generally subordinate to all other interests of the trusts and generally only pay out funds when certain ratios are met and excess cash holdings, as determined by the trustee, are available for distribution to the overcollateralization class. Many of the investments in this group have no current cash flows and may not ever pay cash flows, depending on the loss experience of the collateral group supporting the investment. Estimating future cash flows for this group of Non-Agency RMBS investments is highly subjective and uncertain; therefore, the Company has elected to carry these holdings at fair value with changes in fair value reflected in earnings.

Changes in fair value are presented in Net unrealized gains (losses) on financial instruments at fair value on the Consolidated Statement of Operations and Comprehensive Income. The fair value of the Non-Agency RMBS carried at fair value with changes in fair value reflected in earnings is $21 million and $20 million as of September 30, 2016 and December 31, 2015, respectively.

Securitized Loans Held for Investment:

The Company’s securitized loans held for investment are carried at fair value with changes in fair value reflected in earnings. The Company carries securitized loans held for investment at fair value as it may resecuritize these loans in the future. Additionally, the fair value option allows both the loans and related financing to be consistently reported at fair value and to achieve operational and valuation simplifications.

Changes in fair value of securitized loans held for investment are presented in Net unrealized gains (losses) on financial instruments at fair value on the Consolidated Statement of Operations and Comprehensive Income.

Securitized Debt, Collateralized by Loans Held for Investment:

The Company’s securitized debt, collateralized by loans held for investment, is carried at fair value with changes in fair value reflected in earnings. The Company has elected the fair value option for these financings as it may call or restructure these debt financings in the future. Additionally, the fair value option allows both the loans and related financing to be consistently reported at fair value and to achieve operational and valuation simplifications.

Changes in fair value of securitized debt, collateralized by loans held for investment are presented in Net unrealized gains (losses) on financial instruments at fair value on the Consolidated Statement of Operations and Comprehensive Income.

(i) Derivative Financial Instruments

The Company’s investment policies permit it to enter into derivative contracts, including interest rate swaps, swaptions, mortgage options, futures, and interest rate caps to manage its interest rate risk and, from time to time, enhance investment returns. The Company’s derivatives are recorded as either assets or liabilities in the Consolidated Statements of Financial Condition and measured at fair value. These derivative financial instrument contracts are not designated as hedges for GAAP; therefore, all changes in fair value are recognized in earnings. The Company estimates the fair value of its derivative instruments as described in Note 5 of these consolidated financial statements. Net payments on derivative instruments are included in the Consolidated Statements of Cash Flows as a component of net income. Unrealized gains (losses) on derivatives are removed from net income to arrive at cash flows from operating activities.

The Company elects to net the fair value of its derivative contracts by counterparty when appropriate. These contracts contain legally enforceable provisions that allow for netting or setting off of all individual derivative receivables and payables with each counterparty and therefore, the fair value of those derivative contracts are reported net by counterparty. The credit support annex provisions of the Company’s derivative 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 derivative contracts, it also nets by counterparty any cash collateral exchanged as part of the derivative. Refer to Note 9 Derivative Instruments for further details.

(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) Sales, Securitizations, and Re-Securitizations

The Company periodically enters into transactions in which it sells financial assets, such as MBS and mortgage loans. Gains and losses on sales of assets are calculated using the average cost method whereby the Company records a gain or loss on the difference between the average amortized cost 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, whereby 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 entity 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 or re-securitized assets. In transfers that are considered secured borrowings, no gain or loss is recognized. Any difference in the proceeds received and the carrying value of the transferred asset is recorded as a premium or discount and amortized into earnings as an adjustment to yield.

(l) Income Taxes

The Company has elected to be taxed as a REIT and intends to comply with the provision of the Code, with respect thereto. Accordingly, the Company will generally not be subject to federal, state or local income taxes to the extent that qualifying distributions are made to stockholders and as long as certain asset, income, distribution 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, CIM Trading and CIM Funding TRS made joint elections to treat CIM Trading and CIM Funding TRS as TRS's. As such, CIM Trading and CIM Funding TRS are taxable as domestic C corporations and subject to federal, state, and local income taxes based upon their respective taxable income.

A tax position is recognized only when, based on management's judgment regarding the application of income tax laws, it is more likely than not that the tax position will be sustained upon examination. The Company does not have any unrecognized tax positions that would affect its financial statements or require disclosure. No accruals for penalties and interest were necessary as of September 30, 2016 or 2015.

(m) 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.

(n) Stock-Based Compensation

The Company measures the fair value of the equity instrument granted to non-employees 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. Stock 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 vesting date at which the recipient's performance is complete.

Compensation expense for equity based awards granted to the Company's independent directors and stock based compensation awards granted to employees of the Company subject only to service condition is recognized on a straight-line basis over the vesting period of such awards, based upon the fair value of such awards at the grant date adjusted, as applicable, for estimated forfeitures.  For awards subject to graded vesting, the total amount of expense is at least equal to the measured expense of each vested tranche.  Awards subject to only a service condition are valued according to the market price for the Company's common stock at the date of grant. For awards based on the performance of the Company's stock price, the Company generally engages an independent appraisal company to determine the value of the shares at the date of grant, taking into account the underlying contingency risks associated with the performance criteria. The values of these grants are expensed ratably over their respective vesting periods (irrespective of achievement of the performance criteria) adjusted, as applicable, for forfeitures.

(o) 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 MBS (Note 3), valuation of Agency MBS and Non-Agency RMBS (Notes 3 and 5), residential mortgage loans (Note 4), securitized debt (Note 7) and derivative instruments (Notes 5 and 9). Actual results could differ materially from those estimates.

(p) Recent Accounting Pronouncements

Statement of Cash Flows - Classification of Certain Cash Receipts and Cash Payments – (Topic 230)

In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows - Classification of Certain Cash Receipts and Cash Payments. This update provides guidance on eight specific cash flow issues. The guidance is intended to reduce diversity in practice on those issues across all industries. The guidance in the ASU is effective for the Company as of January 1, 2018. Early adoption is allowed. The guidance is to be applied retrospectively, unless it is impracticable to do so for an issue, then the amendments related to that issue would be applied prospectively. The Company is currently evaluating what impact this update will have on the consolidated financial statements.

Financial Instruments - Credit Losses – (Topic 326)

In June 2016, the FASB issued ASU No. 2016-13, Measurement of Credit Losses on Financial Instruments. This update replaces the current model for recognizing credit losses from an incurred credit loss model to a current expected credit loss (CECL) model for instruments measured at amortized cost and requires entities to record allowances for available-for-sale (AFS) debt securities when the fair value of an AFS debt security is below the amortized cost of the asset rather than reduce the carrying amount, as we do under the current OTTI model. This update also simplifies the accounting model for purchased credit-impaired debt securities and loans. The changes in the allowances created in accordance with this update will be recorded in earnings. The update also expands the disclosure requirements regarding the Company's assumptions, models, and methods for estimating the expected credit losses. In addition, the Company will disclose the amortized cost balance for each class of financial asset by credit quality indicator, disaggregated by the year of origination. The guidance in the ASU is effective for the Company as of January 1, 2020. Early adoption is allowed, beginning January 1, 2019. The standard requires entities to record a cumulative-effect adjustment to the statement of financial position as of the beginning of the first reporting period in which the guidance is effective. The Company is currently evaluating what impact this update will have on the consolidated financial statements.

Share Based Payments – (Topic 718)

In March 2016, the FASB issued ASU No. 2016-09, Improvements to Employee Share-Based Payment Accounting. Under this update companies will no longer record excess tax benefits and certain tax deficiencies associated with an award of equity instruments in additional paid-in capital. Instead, they will record all excess tax benefits and tax deficiencies as income tax expense or benefit in the income statement when the awards vest or are settled, and additional paid-in capital pools will be eliminated. The updated guidance will also allow the Company to repurchase more shares than it can today for tax withholding purposes without triggering liability accounting and to make a policy election to account for forfeitures as they occur. The guidance in the ASU is effective for the Company as of January 1, 2017. Early adoption is allowed. The guidance is to be applied using a modified retrospective transition method with a cumulative-effect adjustment recorded in retained earnings. The Company is currently evaluating what impact this update will have on the consolidated financial statements.

Contingent Put and Call Options in Debt Instruments – (Topic 815)

In March 2016, the FASB issued ASU No. 2016-06, Contingent Put and Call Options in Debt Instruments Accounting.  This update clarifies that when a call or put option in a debt instrument can accelerate the repayment of principal on the debt instrument, a reporting entity does not need to assess whether the contingent event that triggers the ability to exercise the call or put option is related to interest rates or credit risk in determining whether the option should be accounted for separately as a derivative. The guidance in the ASU is effective for the Company as of January 1, 2017. Early adoption is permitted.  The new guidance applies to existing debt instruments (or hybrid financial instruments that are determined to have a debt host) using a modified retrospective method as of the beginning of the period of adoption. The adoption of this guidance is not expected to have a material effect on the Company’s financial statements as all of its debt instruments with contingent Put and Call options are eliminated on consolidation.

Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships – (Topic 815)

In March 2016, the FASB issued ASU No. 2016-05, Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships. The amendments in this update clarify that a change in the counterparty to a derivative instrument that has been designated as the hedging instrument under Topic 815 does not, in and of itself, require de-designation of that hedging relationship provided that all other hedge accounting criteria continue to be met. The guidance in the ASU is effective for the Company as of January 1, 2017. Early adoption is allowed.  The new guidance may be applied prospectively or on a modified retrospective basis. The Company currently does not use hedge accounting for GAAP reporting purposes, therefore this guidance is not expected to have a material effect on the Company’s financial statements.

Financial Instruments—Overall (Subtopic 825-10)

In January 2016, the FASB issued ASU No. 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities. This update changes how the Company will present changes in the fair value of financial liabilities measured under the fair value option that are attributable to our own credit. Under the updated guidance, the Company will record changes in instrument-specific credit risk for financial liabilities measured under the fair value option in other comprehensive income. The update also requires fair value measurement for equity investments that do not result in consolidation and are not accounted for under the equity method to be measured at fair value with any changes in fair value recognized in net income. The update also eliminates the requirement to disclose the methods and significant assumptions used to estimate the fair value of financial instruments measured at amortized cost. In addition, the Company will have to use the exit price notion when measuring the fair value of financial instruments measured at amortized cost for disclosure purposes. The guidance in the ASU is effective for the Company as of January 1, 2018. Early adoption for certain provisions of the update is allowed. Any adjustment as a result of the adoption of this standard will be recorded as a cumulative-effect adjustment to beginning retained earnings as of the first period in which the guidance is adopted. The Company is currently evaluating what impact this update will have on the consolidated financial statements.

Presentation of Financial Statements—Going Concern (Subtopic 205-40)

In August 2014, the FASB issued ASU No. 2014-15, Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. This update provides guidance on determining when and how to disclose going-concern uncertainties in the financial statements. The new standard requires the Company to perform interim and annual assessments of its ability to continue as a going concern within one year of the date the financial statements are issued. The Company must provide certain disclosures if conditions or events raise substantial doubt about its ability to continue as a going concern. The ASU applies to all entities and is effective for the Company for the year ended December 31, 2016. Early adoption is permitted. The Company does not expect this update to have any impact as we do not expect to have the conditions or events which would raise substantial doubt about the Company's ability to continue as a going concern.

3. Mortgage-Backed Securities

The Company classifies its Non-Agency RMBS as senior, senior IO, subordinated, or subordinated IO. The Company also invests in residential and commercial Agency MBS. Senior interests in Non-Agency RMBS are considered to be entitled to the first principal repayments in their pro-rata ownership interests at the acquisition date.

September 30, 2016
(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 | $3,308,463 | $237 | $(1,457,711) | $1,850,990 | $2,585,386 | $734,998 | $(602) | $734,396 |
| Senior, interest-only | 5,733,457 | 303,539 | — | 303,539 | 291,526 | 28,598 | (40,611) | $(12,013) |
| Subordinated | 668,946 | 16,416 | (218,239) | 467,125 | 546,825 | 79,895 | (195) | $79,700 |
| Subordinated, interest-only | 269,868 | 14,183 | — | 14,183 | 13,498 | 41 | (726) | $(685) |
| Agency MBS | | | | | | | | |
| Residential | 2,672,093 | 138,970 | — | 2,811,063 | 2,861,468 | 51,842 | (1,437) | $50,405 |
| Commercial | 1,273,235 | 36,001 | (2,717) | 1,306,518 | 1,343,994 | 39,496 | (2,020) | $37,476 |
| Interest-only | 3,474,731 | 163,542 | — | 163,542 | 157,088 | 2,274 | (8,728) | $(6,454) |
| Total | $17,400,793 | $672,888 | $(1,678,667) | $6,916,960 | $7,799,785 | $937,144 | $(54,319) | $882,825 |

December 31, 2015
(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 | $3,651,869 | $309 | $(1,553,317) | $2,098,860 | $2,826,121 | $736,040 | $(8,779) | $727,261 |
| Senior, interest-only | 5,426,029 | 268,515 | — | 268,515 | 234,171 | 18,113 | (52,457) | (34,344) |
| Subordinated | 762,466 | 23,635 | (258,128) | 527,975 | 604,295 | 83,896 | (7,577) | 76,319 |
| Subordinated, interest-only | 284,931 | 15,226 | — | 15,226 | 11,254 | 62 | (4,035) | (3,973) |
| Agency MBS | | | | | | | | |
| Residential | 5,045,418 | 255,837 | — | 5,301,255 | 5,267,848 | 18,593 | (52,001) | (33,408) |
| Commercial | 952,091 | 24,815 | (3,170) | 973,736 | 973,787 | 8,052 | (8,001) | 51 |
| Interest-only | 6,722,472 | 280,073 | — | 280,073 | 273,189 | 2,756 | (9,640) | (6,884) |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Total | $22,845,276 | $868,410 | $(1,814,615) | $9,465,640 | $10,190,665 | $867,512 | $(142,490) | $725,022 |

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, 2016 | September 30, 2015 | September 30, 2016 | September 30, 2015 |
| | (dollars in thousands) | | (dollars in thousands) | |
| Balance at beginning of period | $1,714,592 | $1,698,323 | $1,742,744 | $1,534,497 |
| Purchases | 18,316 | 133,227 | 60,915 | 241,852 |
| Yield income earned | (69,850) | (72,557) | (141,256) | (213,267) |
| Reclassification (to) from non-accretable difference | (29,490) | 19,205 | (2,031) | 238,012 |
| Sales and deconsolidation | (12,907) | (418) | (39,711) | (23,314) |
| Balance at end of period | $1,620,661 | $1,777,780 | $1,620,661 | $1,777,780 |

The table below presents the outstanding principal balance and related amortized cost at September 30, 2016 and December 31, 2015 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, 2016 | For the Year Ended December 31, 2015 |
|---|---|---|
| | (dollars in thousands) | |
| Outstanding principal balance: | | |
| Beginning of period | $3,343,812 | $3,325,335 |
| End of period | $3,228,137 | $3,550,698 |
| Amortized cost: | | |
| Beginning of period | $1,806,344 | $1,741,780 |
| End of period | $1,743,116 | $1,958,726 |

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, 2016 and December 31, 2015. All securities in an unrealized loss position have been evaluated by the Company for OTTI as discussed in Note 2(d).

September 30, 2016