

Edgar Filing: Five Oaks Investment Corp. - Form 10-K

Five Oaks Investment Corp.  
Form 10-K  
March 16, 2018

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

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

For the fiscal year ended December 31, 2017

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: 001-35845

FIVE OAKS INVESTMENT CORP.

(Exact name of registrant as specified in its charter)

Maryland

45-4966519

(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

230 Park Avenue, 19th Floor, New York, New York 10169

(Address of principal executive offices) (Zip Code)

Registrant's Telephone Number, including area code (212) 588-2049

Securities Registered Pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on which registered
---------------------	---

Common stock, \$0.01 par value	New York Stock Exchange
--------------------------------	-------------------------

Series A Cumulative Redeemable Preferred Stock, \$0.01 par value	New York Stock Exchange
--	-------------------------

Securities Registered Pursuant to Section 12(g) of the Act:

None.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes ☐ or No ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes ☐ or No ☒

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ or No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K ☒

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

Large accelerated filer ☐

Accelerated filer ☒

Non-accelerated (Do not check if a smaller reporting company) ☐ Smaller reporting company ☐

Emerging growth company ☒ x

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

The aggregate market value of the registrant's common stock held by non-affiliates was \$87.3 million based on the closing sales price on the New York Stock Exchange on June 30, 2017.

As of March 16, 2018, the registrant had outstanding 23,683,164 shares of common stock, \$0.01 par value.

---

TABLE OF CONTENTS

	Page
<u>PART I</u>	
Item 1. <u>Business</u>	<u>1</u>
Item 1A. <u>Risk Factors</u>	<u>4</u>
Item 1B. <u>Unresolved Staff Comments</u>	<u>33</u>
Item 2. <u>Properties</u>	<u>33</u>
Item 3. <u>Legal Proceedings</u>	<u>33</u>
Item 4. <u>Mine Safety Disclosures</u>	<u>33</u>
<u>PART II</u>	
Item 5. <u>Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	<u>34</u>
Item 6. <u>Selected Financial Data</u>	<u>37</u>
Item 7. <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>38</u>
Item 7A. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>56</u>
Item 8. <u>Financial Statements and Supplementary Data</u>	<u>61</u>
Item 9. <u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	<u>61</u>
Item 9A. <u>Controls and Procedures</u>	<u>61</u>
Item 9B. <u>Other Information</u>	<u>62</u>
<u>PART III</u>	
Item 10. <u>Directors, Executive Officers and Corporate Governance</u>	<u>64</u>
Item 11. <u>Executive Compensation</u>	<u>66</u>
Item 12. <u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	<u>68</u>
Item 13. <u>Certain Relationships and Related Transactions, and Director Independence</u>	<u>70</u>
Item 14. <u>Principal Accounting Fees and Services</u>	<u>72</u>
<u>PART IV</u>	
Item 15. <u>Exhibits, Financial Statements and Schedules</u>	<u>72</u>
Item 16. <u>Form 10-K Summary</u>	<u>72</u>

## Explanatory Note

Unless the context otherwise indicates or requires, as used in this Annual Report on Form 10-K, references to:

- “Agency” means each of Federal National Mortgage Association, or Fannie Mae, Federal Home Loan Mortgage Corporation, or Freddie Mac, and the Government National Mortgage Association, a wholly owned corporate instrumentality of the United States of America within the U.S. Department of Housing and Urban Development, or Ginnie Mae.
- “Agency RMBS” means mortgage-backed securities that are collateralized by residential mortgages, or RMBS, whose principal and interest payments are guaranteed by Ginnie Mae or a U.S. Government-sponsored entity, or GSE, such as Freddie Mac or Fannie Mae. These securities may be either “pass through” securities, where cash flows from the underlying mortgage loan pool are paid to holders of the securities on a pro rata basis, or securities structured from “pass through” securities, as to which cash flows are redirected in various priorities, which we refer to as a collateralized mortgage obligation.
- “ARMs” means adjustable-rate residential mortgage loans.
- “Company,” “we,” “us,” or “our” refers to Five Oaks Investment Corp., together with its wholly owned, subsidiaries, Five Oaks Acquisition Corp., Five Oaks Insurance LLC (prior to its dissolution in July 2016), Oaks Funding LLC, Oaks Funding II LLC and Oaks Holding I LLC unless we specifically state otherwise or the context indicates otherwise.
- “credit enhancement” means techniques to improve the credit ratings of securities, including overcollateralization, creating retained spread, creating subordinated tranches and insurance.
- “FHFA” means the Federal Housing Finance Agency.
- “hybrid ARMs” means residential mortgage loans that have interest rates that are fixed for a specified period of time (typically three, five, seven or ten years) and, thereafter, adjust to an increment over a specified interest rate index.
- “K-Series” means multi-family mortgage loan securitizations sponsored by Freddie Mac.
- “Linked Transaction” means the initial purchase of RMBS securities and contemporaneous financing with a repurchase agreement with the same counterparty from which the securities were purchased.
- “mortgage loans” means loans secured by real estate with a right to receive the payment of principal and interest on the loan (including servicing fees).
- “Multi-Family MBS” means a mortgage-backed securities, or MBS, investment in a securitization backed by multi-family mortgage loans. Such Multi-Family MBS may be sponsored by Fannie Mae, Freddie Mac or Ginnie Mae, or may not be sponsored by Ginnie Mae or a U.S. Government-sponsored entity such as Freddie Mac or Fannie Mae.
- “Non-Agency RMBS” means RMBS that are not issued or guaranteed by Ginnie Mae or a U.S. Government-sponsored entity such as Freddie Mac or Fannie Mae, including investment grade classes (rated AAA through BBB), non-investment grade classes (rated BB or lower) and unrated classes.
- “Oak Circle” means Oak Circle Capital Partners LLC.
- “our Manager” means Oaks Circle prior to January 18, 2018, and thereafter means Hunt Investment Management, LLC.
- “swaption” means an option in which the buyer has the right to enter into an interest rate swap.
- “TBAs” means to-be-announced forward contracts. In a TBA, a buyer will agree to purchase, for future delivery, Agency mortgage investments with certain principal and interest terms and certain types of underlying collateral, but the particular Agency mortgage investments to be delivered are not identified until shortly before the TBA settlement date.
- “VIE” means a variable interest entity that lacks one or more of the characteristics of a voting interest entity. A VIE is defined as an entity in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. We consolidate a VIE when we are the primary beneficiary of such VIE. As primary beneficiary, we have both the power to direct the activities that most significantly impact the economic performance of the VIE and a right to receive benefits or absorb losses of the entity that could be potentially significant to the VIE.

We are required to reconsider our evaluation of whether to consolidate a VIE each reporting period, based upon changes in the facts and circumstances pertaining to the VIE.

- “whole pool” means MBS issued with respect to an underlying pool of mortgage loans in which a buyer holds all of the certificates issued by a pool.

ii

---

## PART I

### ITEM 1. BUSINESS

#### General

We are a real estate specialty finance company focused on investing on a leveraged basis in MBS, mortgages and other real estate related assets. Commencing on January 18, 2018 we are externally managed by our Manager, a subsidiary of Hunt Companies Inc. ("Hunt"), a private, diversified real estate company pursuant to the terms of our management agreement.

We are a Maryland corporation formed in March 2012 and commenced operations in May 2012; we completed our initial public offering, or our IPO, in March 2013. We have elected and qualified to be taxed as a real estate investment trust ("REIT") for U.S. federal income tax purposes under the Internal Revenue Code of 1986, as amended ("Code"). Our common stock is traded on the New York Stock Exchange, Inc., or the NYSE, under the symbol "OAKS" and our Series A Preferred Stock is traded on the NYSE under the symbol "OAKS-PRA". For information regarding our subsidiaries and their operations as well as for the geographical concentrations of the mortgage loans underlying certain of our assets, see "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Notes to our consolidated financial statements.

#### The Hunt Transaction

On January 18, 2018, we announced a new strategic direction, and the entry into a new external management agreement with Hunt Investment Management, LLC, an affiliate of the Hunt Companies, Inc. ("Hunt") and the concurrent mutual termination of our management agreement with Oak Circle. Management by Hunt is expected to provide Five Oaks with a new strategic direction through the reallocation of capital into new investment opportunities focused in the commercial real estate mortgage space and direct access to Hunt's significant pipeline of transitional floating-rate multi-family and commercial real estate loans. Hunt and its affiliates have extensive experience in the origination, servicing, risk management and financing of this asset class and the floating-rate nature of the loans should reduce or eliminate the need for complex interest-rate hedging. The new management agreement is expected to better align our interests with those of our new manager through an incentive fee arrangement and agreed upon limitations on manager expense reimbursements from us, as further described below. Pursuant to the terms of the termination agreement between Five Oaks and Oak Circle, the termination of the prior management agreement did not trigger, and Oak Circle was not paid, a termination fee by us. Hunt separately agreed to pay Oak Circle a negotiated payment in connection with the termination agreement.

In connection with the transaction, an affiliate of Hunt purchased 1,539,406 shares of our common stock in a private placement, at a purchase price of \$4.77 per share resulting in an aggregate capital raise of \$7,342,967. In addition, such Hunt affiliate also purchased 710,495 Five Oaks shares from our largest shareholder, XL Investments Ltd. ("XL Investments"), for the same price per share. The purchase price per share represents a 56.9% premium over the Five Oaks common share price as of the closing on January 17, 2018. In connection with the acquisition of shares from XL Investments, XL Investments agreed to terminate all of its currently held Five Oaks warrants. After completion of these share purchases, Hunt and its affiliates own approximately 9.5% of Five Oaks outstanding common shares. Also in connection with the transaction, and as further described in Sections 10 hereof and in our Current Report on Form 8-K filed with the Securities and Exchange Commission on January 18, 2018, David Carroll resigned as a director, Chairman and CEO of the Company and the Five Oaks board appointed James C. ("Chris") Hunt as a director and Chairman of the board and named James P. Flynn as CEO of Five Oaks and Michael P. Larsen President of Five Oaks.

## Our Investment Strategy

Since the middle of 2016, we have sought to simplify and streamline our business model in response to a number of developments in the residential and multi-family mortgage markets. Due to progressively less attractive market conditions for the aggregation and securitization of prime jumbo mortgage loans, we ceased this activity in the second half of 2016, and reduced our expenses through personnel and other overhead reductions. Similarly, we have substantially exited the business of owning Non-Agency RMBS based on a significant decline in the number of repurchase agreement financing counterparties willing to finance securitized credit combined with a reduction in the yields available on such assets. The capital released from this portfolio re-balancing has primarily been invested in Agency RMBS, with a particular focus on shorter duration Agency securities backed by hybrid ARMs. Additionally, we have continued to maintain exposure to multi-family MBS, principally through owning subordinated and first-loss tranches in Freddie Mac K-series securitizations. We have sought to do so while reducing our reliance on short-term repurchase agreement financing, including through the use of re-securitization, or re-REMIC, financings.

In parallel with the shift to a more Agency-focused, and thus more liquid, asset portfolio and an ongoing focus on further expense reductions, we have continually sought to explore opportunities to reallocate our capital into complimentary business sectors we believe have positive fundamentals and do not rely on short-term financing. The entry into the new management agreement with Hunt Investment Management, LLC, is expected to provide us with a new strategic direction through the reallocation of capital into new investment opportunities in the commercial real estate space, and in particular direct access to Hunt's significant pipeline of specified transitional floating-rate multi-family and commercial real estate loans. Hunt and its affiliates have extensive experience in the origination, servicing, risk management and financing of this asset class and the floating-rate nature of the loans should reduce or eliminate the need for complex interest-rate hedging. Subject to our ability to put in place term repurchase facilities and/or collateralized loan obligations of the type Hunt has historically used to finance this asset class, we intend to transition our portfolio towards loan assets that are positively correlated with rising interest rates and that have exhibited strong historical credit performance.

In furtherance of our objective to provide attractive cash flow returns over time to our investors, our investment strategy targets the following assets:

- Transitional multi-family and other commercial real estate loans, which are floating-rate loans secured by multi-family and other commercial real estate properties that are not guaranteed by a U.S. Government sponsored entity, or securitizations backed by such loans;
- Securitizations backed by multi-family mortgage loans, or Multi-Family MBS;
- Agency RMBS, which are residential mortgage-backed securities, for which a U.S. Government agency such as Ginnie Mae or a federally chartered corporation such as Fannie Mae or Freddie Mac, guarantees payments of principal and interest on the securities;
- To a limited extent, Non-Agency RMBS, which are RMBS that are not issued or guaranteed by a U.S. Government-sponsored entity; and
- Other mortgage-related investments, including mortgage servicing rights, or MSRs, CMBS, or other loans or securities backed by real estate.

Our primary sources of income are net interest income from our investment portfolio and non-interest income from our mortgage loan-related activities. Net interest income represents the interest income we earn on investments less the expenses of funding these investments.

## Our Portfolio

### Our Available-for-Sale Portfolio

As of December 31, 2017, our portfolio was comprised of 99.6% Agency RMBS and 0.4% Multi-Family MBS on a United States generally accepted accounting principles, or GAAP, basis, or 97.6% Agency RMBS, 2.1% Multi-Family MBS including our net investment in Multi-Family securitization trusts and 0.3% Non-Agency RMBS including our net investment in residential mortgage loan securitization trusts on a non-GAAP basis. As further described below, as of December 31, 2017, we have determined that we were the primary beneficiary of two Multi-Family MBS securitization trusts and one residential mortgage loan securitization trust, based in each case on our ownership of all or substantially all of the most subordinated, or first-loss, tranches in each transaction. Although our consolidated balance sheet at December 31, 2017 includes the gross assets and liabilities of the three trusts, the assets of each trust are restricted and can only be used to fulfill the obligations of the individual entity. Furthermore, we are only exposed to the risk of loss on our net investment in the trusts. We therefore have also presented certain information that includes our net investments in the Multi-Family MBS and residential mortgage loan securitization trusts. This information constitutes non-GAAP financial measures within the meaning of Item 10(e) of Regulation S-K, as promulgated by the U.S. Securities and Exchange Commission, or the SEC. We believe that this non-GAAP information enhances the ability of investors to analyze our MBS portfolio and the performance of our MBS in the same way that we assess our portfolio and such assets.

### Multi-Family MBS

While multi-family securitizations are generally considered to be commercial mortgage-backed securities, the demographic, geographic and credit risk analyses necessary to evaluate such securities share many similarities with the investment analyses that we have previously undertaken for Non-Agency RMBS. Multi-Family MBS securitizations, including those sponsored by Freddie Mac and known as the K series, have historically exhibited positive credit characteristics.

### Transitional Multi-Family and Commercial Real Estate Loans

In general, transitional loans are floating-rate bridge loans with a short to medium term maturity of one to five years, secured by a first lien on multi-family or other commercial real estate properties. The purpose of the loan is generally some form of renovation or upgrade to the property that is intended to increase the net operating income of the property, and thus its value, prior to a take-out through a longer term loan. As of December 31, 2017, we did not own any such loans, but following completion of the Hunt transaction, and subject to securing the necessary financing facilities, we intend to invest in such loans going forward.

### MSRs

In June 2013, we established FOAC as our TRS to increase the range of our investments in mortgage-related assets. Previously FOAC aggregated mortgage loans primarily for sale into securitization transactions, with the expectation that we would purchase the subordinated tranches issued by the related securitization trusts, and that these would represent high quality credit investments. Starting in 2016, we ceased the aggregation and securitization of residential mortgage loans, and as of December 31, 2017, we had no such loans remaining on our balance sheet. Residential mortgage loans for which FOAC owns the MSRs are directly serviced by one or more licensed sub-servicers since



FOAC does not directly service any residential mortgage loans.

### Financing Strategy

We use leverage to seek to increase potential returns to our stockholders by borrowing against existing assets through short-term repurchase agreements, and in the future we intend to utilize longer-term secured financings, in each case, using the proceeds to acquire additional assets including floating-rate transitional loans. Financing of Agency RMBS, Multi-Family MBS and Non-Agency RMBS is generally available through, among other vehicles, short-term repurchase agreements. Haircuts or the discount attributed to the value of securities sold under repurchase agreements, range between 5% and 40% across all our borrowing facilities, with an average of 5.2%, as of December 31, 2017, depending on the specific security used as collateral for such repurchase agreements.

Neither our organizational documents nor our investment guidelines place any limit on the maximum amount of leverage that we may use, and we are not required to maintain any particular debt-to-equity leverage ratio. We may continue to change our financing strategy and leverage without the consent of our stockholders. Depending on the different cost of borrowing funds at different maturities, we vary the maturities of our borrowed funds to attempt to produce lower borrowing costs and reduce interest rate risk. Generally, we seek to enter into collateralized borrowings only with institutions that are rated investment grade by at least one nationally-recognized statistical rating organization. Going forward, as we seek to continue expanding the range of available financing sources, we have borrowed and may continue to borrow from institutions that, although not rated investment grade by at least one nationally recognized statistical rating organization, in the assessment of our management team represent an acceptable counterparty credit risk in providing collateralized financing for our portfolio.

The goal of our leverage strategy is to ensure that, at all times, our investment portfolio's leverage ratio is appropriate for the level of risk inherent in the investment portfolio and that each asset class has individual leverage targets that are appropriate for its potential price volatility.

### Hedging Strategy

As part of our risk management strategy, our Manager actively manages the financing, interest rate, credit, prepayment and convexity risks associated with holding a portfolio of Agency and Non-Agency RMBS, Multi-Family MBS and other mortgage-related investments. We rely on our Manager to manage these risks on our behalf, and, subject to maintaining our qualification as a REIT, our Manager may incorporate various hedging, asset/liability risk management and credit risk mitigation techniques in order to facilitate our risk management.

**Interest Rate Risk.** We hedge some of our exposure to potential interest rate mismatches between the interest we earn on our longer term investments and the borrowing costs on our shorter term borrowings. Because a majority of our leverage will continue to be in the form of repurchase agreements, our financing costs will fluctuate based on short-term interest rate indices, such as the London Interbank Offered Rate, or LIBOR. Subject to maintaining our qualification as a REIT, the hedging techniques utilized may include interest rate swap agreements, interest rate swaptions, interest rate caps or floor contracts, futures or forward contracts and other derivative securities. Management by Hunt is expected to provide us with a new strategic direction through the reallocation of capital into new investment

opportunities focused in the commercial real estate mortgage space including transitional floating-rate multi-family and commercial real estate loans which should reduce or eliminate the need for complex interest-rate hedging.

**Prepayment Risk.** Because residential borrowers are able to prepay their mortgage loans at par at any time, we face the risk that we will experience a return of principal on our investments earlier than anticipated, and we may have to re-invest that principal at potentially lower yields. In order to manage our prepayment and interest rate risks, we monitor, among other things, our “duration gap” and our convexity exposure. Duration is the relative expected percentage change in market value of our assets that would be caused by a parallel change in short and long-term interest rates. Convexity exposure relates to the way the duration of a mortgage security changes when the interest rate and prepayment environment changes.

**Credit Risk.** We intend to accept mortgage credit exposure at levels our Manager deems prudent as an integral part of our diversified investment strategy. Therefore, we retain the risk of potential credit losses on the loans underlying the Multi-Family MBS and Non-Agency RMBS we hold, and going forward we will also be exposed to potential credit losses on the transitional multi-family and commercial mortgage loans we intend to invest in. We will seek to manage this risk through prudent asset selection, pre-acquisition due diligence, post-acquisition performance monitoring, sale of assets which we identify as experiencing negative credit trends, the use of various types of credit enhancements, and by using non-recourse financing. Nevertheless, actual credit losses could adversely affect our operating results.

#### Our Manager

With effect from January 18, 2018, we are now externally managed and advised by Hunt Investment Management, LLC (“HIM”), pursuant to a management agreement between us and HIM, and the simultaneous termination of our previous management agreement with Oak Circle. HIM is a subsidiary of Hunt Companies, Inc. (“Hunt”) a private, diversified real estate company. As our Manager, HIM implements our business strategy, performs investment advisory services and activities with respect to our assets and is responsible for performing all of our day-to-day operations. HIM is an investment adviser registered with the SEC.

Pursuant to the terms of the new management agreement, we are required to pay our Manager an annual base management fee of 1.50% of Stockholders’ Equity (as defined in the management agreement, payable quarterly (0.375% per quarter) in arrears. Starting in the first full calendar quarter following January 18, 2019, we are also required to pay our Manager a quarterly incentive fee equal to 20% of the excess of Core Earnings (as defined in the management agreement) over a hurdle rate of 8% per annum. We are also required to reimburse our Manager for costs associated with an allocable share of the costs of non-investment management personnel who spend all or a portion of their time managing our affairs. In order to assist in our ongoing efforts to reduce expenses, our Manager has agreed to cap such reimbursement at 1.5% of the average Stockholders’ Equity for the applicable fiscal year. We also reimburse our Manager for other costs and expenses associated with our operations.

On January 18, 2018, we and Oak Circle, entered into a Termination Agreement (“Termination Agreement”) pursuant to which we and Oak Circle agreed to mutually and immediately terminate that certain management agreement, dated May 16, 2012, by and between us and Oak Circle. Under the terms of the Termination Agreement, the termination of the management agreement with Oak Circle did not trigger, and Oak Circle was not paid, a termination fee by us. Hunt separately agreed to pay Oak Circle a negotiated payment in connection with the termination agreement.

#### Competition

We operate in a highly competitive market for available financing facilities and investment opportunities. Our profitability depends, in large part, on our ability to acquire RMBS, Multi-Family MBS, transitional multi-family and commercial real estate loans and other mortgage related investments at favorable prices. In acquiring these assets, we

will compete with a variety of institutional investors, including other REITs, specialty finance companies, public and private funds, hedge funds, commercial and investment banks, commercial finance and insurance companies and other financial institutions. We believe that direct access to Hunt's established pipeline of transitional floating-rate loans may provide us with a competitive advantage in sourcing attractive assets for our balance sheet. Nevertheless, many of our competitors are substantially larger and have considerably greater financial, technical, marketing and other resources than we do. Some competitors have a lower cost of funds and access to funding sources (including the FHLB system) that are not available to us, such as funding from the U.S. Government. Many of our competitors are not subject to the operating constraints associated with REIT tax compliance or maintenance of an exclusion from the Investment Company Act of 1940, as amended. In addition, some of our competitors may have higher risk tolerances or different risk assessments, which could allow them to consider a wider variety of investments and establish more relationships than us.

#### Taxation

We elected to be taxed as a REIT commencing with our short taxable year ended December 31, 2012, and comply with the provisions of the Internal Revenue Code of 1986, as amended, or the Internal Revenue Code, with respect thereto. Accordingly, we are generally not subject to U.S. federal income tax on our REIT taxable income that we currently distribute to our stockholders so long as we maintain our qualification as a REIT. Our continued qualification as a REIT depends on our ability to meet, on a continuing basis, various complex requirements under the Internal Revenue Code relating to, among other things, the source of our gross income, the composition and values of our assets, our distribution levels and the concentration of ownership of our capital stock. Even if we maintain our qualification as a REIT, we may be subject to some U.S. federal, state and local taxes on our income.

Taxable income generated by our TRS is subject to regular corporate income tax. For the fiscal year 2017, our TRS did not generate any taxable income.

#### Qualification as a REIT

Continued qualification as a REIT requires that we satisfy a variety of tests relating to our income, assets, distributions and ownership. The significant tests are summarized below.

**Income Tests.** In order to maintain our REIT qualification, we must satisfy two gross income requirements on an annual basis. First, at least 75% of our gross income for each taxable year, excluding gross income from sales of inventory or dealer property in "prohibited transactions" (as defined herein), discharge of indebtedness and certain hedging transactions, generally must be derived from investments relating to real property or mortgages on real property, including interest income derived from mortgage loans secured by real property (including certain types of mortgage-backed securities), rents from real property, dividends received from other REITs, and gains from the sale of designated real estate assets, as well as specified income from temporary investments. Second, at least 95% of our gross income in each taxable year, excluding gross income from "prohibited transactions", discharge of indebtedness and certain hedging transactions, must be derived from some combination of income that qualifies under the 75% gross income test described above, as well as other dividends, interest, and gain from

the sale or disposition of stock or securities, which need not have any relation to real property. Income and gain from certain hedging transactions will be excluded from both the numerator and the denominator for purposes of both the 75% and 95% gross income tests.

**Asset Tests.** At the close of each calendar quarter, we must also satisfy five tests relating to the nature of our assets. First, at least 75% of the value of our total assets must be represented by some combination of designated real estate assets, cash, cash items, U.S. Government securities and, under some circumstances, stock or debt instruments purchased with new capital. Second, the value of any one issuer's securities that we own may not exceed 5% of the value of our total assets. Third, we may not own more than 10% of any one issuer's outstanding securities, as measured by either value (the "10% of value asset test") or voting power. The 5% and 10% asset tests do not apply to securities that qualify under the 75% asset test or to securities of a TRS and qualified REIT subsidiaries, and the 10% of value asset test does not apply to "straight debt" having specified characteristics and to certain other securities. Fourth, the aggregate value of all securities of TRSs that we hold may not exceed 25% (20% for taxable years beginning after December 31, 2017) of the value of our total assets. Fifth, not more than 25% of the value of our total assets may be represented by debt instruments of publicly offered REITs to the extent those debt instruments would not be real estate assets but for the inclusion of debt instruments of publicly offered REITs in the meaning of real estate assets.

**Distribution Requirements.** In order to maintain our REIT qualification, we are required to distribute dividends, other than capital gain dividends, to our stockholders in an amount at least equal to: (1) the sum of (a) 90% of our REIT taxable income computed without regard to our net capital gains and the deduction for dividends paid, and (b) 90% of our net income, if any, (after tax) from foreclosure property; minus (2) the sum of specified items of non-cash income that exceeds a certain percentage of our income.

**Ownership.** In order to maintain our REIT status, we must not be deemed to be closely held and must have more than 100 shareholders. The closely held prohibition requires that not more than 50% of the value of our outstanding shares be owned by five or fewer "individuals" (as defined for this purpose to include certain trusts and foundations) during the last half of our taxable year. The "more than 100 shareholders" rule requires that we have at least 100 shareholders for at least 335 days of a taxable year. Failure to satisfy either of these rules would cause us to fail to maintain our qualification for taxation as a REIT unless certain relief provisions are available.

#### Corporate Offices and Personnel

We were formed as a Maryland corporation in 2012. With effect from January 18, 2018, our corporate headquarters are located at 230 Park Avenue, 19th Floor, New York, NY 10169 and our telephone number is (212) 588 2049. As of December 31, 2017 and March 16, 2018, we had three executive officers, all of whom were provided by our Manager. We have no employees.

#### Access to our Periodic SEC Reports and Other Corporate Information

Our internet website address is [www.fiveoaksinvestment.com](http://www.fiveoaksinvestment.com). We make available free of charge, through our website, our annual report on Form 10-K, our quarterly reports on Form 10-Q, current reports on Form 8-K and any amendments thereto that we file pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, or the Exchange Act, as soon as reasonably practicable after such material is electronically filed with or furnished to the SEC. Our Code of Business Conduct and Ethics and Policy Against Insider Trading and our Corporate Governance Guidelines along with the charters of our Audit, Compensation and Nominating and Corporate Governance Committees are also available on our website. Information on our website is neither part of nor incorporated into this Annual Report on Form 10-K.

The public may read and copy any materials we file with the SEC at the SEC's Public Reference Room at 100 F Street, NE., Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC at <http://www.sec.gov>.

#### Cautionary Note Regarding Forward-Looking Statements

When used in this Annual Report on Form 10-K, in future filings with the SEC or in press releases or other written or oral communications, statements which are not historical in nature, including those containing words such as “believe”, “expect”, “anticipate”, “estimate”, “plan”, “continue”, “intend”, “should”, “would”, “could”, “goal”, “objective”, “will”, “may”, expressions, are intended to identify “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended, or the Securities Act, and Section 21E of the Exchange Act and, as such, may involve known and unknown risks, uncertainties and assumptions. You can also identify forward-looking statements by discussions of strategy, plans or intentions.

Forward-looking statements are based on our beliefs, assumptions and expectations of our future performance, taking into account all information currently available to us. These beliefs, assumptions and expectations are subject to risks and uncertainties and can change as a result of many possible events or factors, not all of which are known to us. If a change occurs, our business, financial condition, liquidity and results of operations may vary materially from those expressed in our forward-looking statements. The following factors are examples of those that could cause actual results to vary from our forward-looking statements: changes in interest rates and the market value of our securities; changes in credit spreads; the impact of the downgrade of the long-term credit ratings of the U.S., Fannie Mae, Freddie Mac, and Ginnie Mae; market volatility; changes in the prepayment rates on the mortgage loans underlying our investment securities; increased rates of default and/or decreased recovery rates on our assets; our ability to borrow to finance our assets; changes in government regulations affecting our business; our ability to maintain our qualification as a REIT for federal tax purposes; our ability to maintain our exemption from registration under the Investment Company Act; and risks associated with investing in real estate assets, including changes in business conditions and the general economy. These and other risks, uncertainties and factors, including the risk factors described in Item 1A - “Risk Factors” and Item 7A - “Quantitative and Qualitative Disclosures About Market Risk”, of this Annual Report on Form 10-K, could cause our actual results to differ materially from those projected in any forward-looking statements we make. All subsequent written and oral forward-looking statements that we make, or that are attributable to us, are expressly qualified in their entirety by this cautionary notice. Any forward-looking statement speaks only as of the date on which it is made. Except as required by law, we are not obligated to, and do not intend to, update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

#### ITEM 1A. RISK FACTORS

Set forth below are the risks that we believe are material to stockholders. You should carefully consider the following risk factors identified in or incorporated by reference into any other documents filed by us with the SEC in evaluating our company and our business. If any of the following risks occur, our business, financial condition, results of operations and our ability to make distributions to our stockholders could be adversely affected. In that case, the trading price of our stock could decline. The risk factors described below are not the only risks that may affect us. Additional risks and uncertainties not presently known to us also may adversely affect our business, financial condition, results of operations and our ability to make distributions to our stockholders.

## Risks Related to Our Investment Strategies and Our Businesses

We may not be able to operate our businesses successfully or generate sufficient revenue to make or sustain distributions to our stockholders.

We cannot assure you that we will be able to operate our businesses successfully or implement our operating policies and strategies. Our Manager may not be able to successfully execute our investment, financing and hedging strategies as described in this Annual Report on Form 10-K (including the expected new strategic direction through the reallocation of capital into new investment opportunities focused in the commercial real estate mortgage space), which could result in a loss of some or all of your investment. The results of our operations depend on several factors, including our Manager's ability to execute on our investment, financing and hedging strategies (including the aforementioned expected new strategic direction), the availability of opportunities for the acquisition of target assets, the level and volatility of interest rates, the availability of adequate short and long-term financing, conditions in the financial markets and economic conditions. Our revenues will depend, in large part, on our Manager's ability to execute on our investment, financing and hedging strategies, and our ability to acquire assets at favorable spreads over our borrowing costs. If our Manager is unable to execute on our investment, financing and hedging strategies, or we are unable to acquire assets that generate favorable spreads, our results of operations may be adversely affected, which could adversely affect our ability to make or sustain distributions to our stockholders.

If we fail to develop, enhance and implement strategies to adapt to changing conditions in the mortgage industry and capital markets, our business, financial condition, results of operations and our ability to make distributions to our stockholders may be adversely affected.

The manner in which we compete and the products for which we compete are affected by changing conditions, which can take the form of trends or sudden changes in our industry, regulatory environment, changes in the role of GSEs, changes in the role of credit rating agencies or their rating criteria or process, or the U.S. economy more generally. If we do not effectively respond to these changes, or if our strategies to respond to these changes are not successful, our business, financial condition, results of operations and our ability to make distributions to our stockholders may be adversely affected.

We may not realize gains or income from our assets.

We seek to generate current income and capital appreciation for our stockholders. However, the assets that we acquire may not appreciate in value and, in fact, may decline in value, and the securities that we acquire may experience defaults of interest and/or principal payments. Accordingly, we may not be able to realize gains or income from our assets. Any gains that we do realize may not be sufficient to offset other losses that we experience.

We may continue to change our target assets, investment or financing strategies and other operational policies without stockholder consent, which may adversely affect our business, financial condition, results of operations and our ability to make distributions to our stockholders.

We may continue to change any of our strategies, policies or procedures with respect to investments, acquisitions, growth, operations, indebtedness, capitalization, distributions, financing strategy and leverage at any time without the consent of our stockholders, which could result in an investment portfolio with a different, and possibly greater, risk profile. A change in our target assets, investment strategy or guidelines, financing strategy or other operational policies may increase our exposure to interest rate risk, default risk and real estate market fluctuations. Furthermore, a change in our asset allocation could result in our making investments in asset categories different from those described in this Annual Report on Form 10-K. In addition, our charter provides that our board of directors may revoke or

otherwise terminate our REIT election, without approval of our stockholders, if it determines that it is no longer in our best interests to maintain our REIT qualification. These changes could adversely affect our business, financial condition, results of operations and our ability to make distributions to our stockholders.

Our portfolio of assets may be concentrated in terms of credit risk.

Although as a general policy we seek to acquire and hold a diverse portfolio of assets, we are not required to observe specific diversification criteria, except as may be set forth in the investment guidelines adopted by our board of directors. Therefore, our asset portfolio may at times be concentrated in certain property types that are subject to higher risk of foreclosure or secured by properties concentrated in a limited number of geographic locations. To the extent that our portfolio is concentrated in any one region or type of security, downturns relating generally to such region or type of security may result in defaults on a number of our assets within a short time period, which could have a material adverse effect on our business, financial condition, results of operations and our ability to make distributions to our stockholders. Our portfolio may contain other concentrations of risk, and we may fail to identify, detect or hedge against those risks, resulting in large or unexpected losses. Lack of diversification can increase the correlation of non-performance and foreclosure risks among our investments.

To the extent we invest in Non-Agency RMBS, they may be secured by properties in a small number of geographic areas and may be disproportionately affected by economic or housing downturns, natural disasters, terrorist events, adverse climate changes or other adverse events specific to those markets.

A significant number of the mortgages underlying our Non-Agency RMBS are concentrated in certain geographic areas. For example, we have significantly higher exposure in California and Washington, (See Part II, Item 7A “Quantitative and Qualitative Disclosures About Market Risk” in this Annual Report on Form 10-K). Certain markets within these states (particularly California) experienced significant decreases in residential home values during the financial crisis of 2007-2008 and the years thereafter. Any event that adversely affects the economy or real estate market in any of these states could have a disproportionately adverse effect on our Non-Agency RMBS. In general, any material decline in the economy or significant problems in a particular real estate market would likely cause a decline in the value of residential properties securing the mortgages in that market, thereby increasing the risk of delinquency, default and foreclosure of re-performing loans and the loans underlying our Non-Agency RMBS. This could, in turn, have a material adverse effect on our credit loss experience on our Non-Agency RMBS in the affected market if higher-than-expected rates of default and/or higher-than-expected loss severities on our re-performing loan investments or the mortgages underlying our Non-Agency RMBS were to occur.

The occurrence of a natural disaster (such as an earthquake, tornado, hurricane or a flood), terrorist attack or a significant adverse climate change may cause a sudden decrease in the value of real estate in the area or areas affected and would likely reduce the value of the properties securing the mortgages collateralizing our Non-Agency RMBS. Because certain natural disasters are not typically covered by the standard hazard insurance policies maintained by borrowers, the affected borrowers may have to pay for any repairs themselves. Borrowers may decide not to repair their property or may stop paying their mortgages under those circumstances. This would likely cause defaults and credit loss severities to increase.

Changes in governmental laws and regulations, fiscal policies, property taxes and zoning ordinances can also have a negative impact on property values, which could result in borrowers' deciding to stop paying their mortgages. This circumstance could cause credit loss severities to increase, thereby adversely impacting our results of operations.

Lack of diversification in the number of assets we acquire would increase our dependence on relatively few individual assets.

Our management objectives and policies do not place a limit on the size of the amount of capital used to support, or the exposure to (by any other measure), any individual asset or any group of assets with similar characteristics or risks. In addition, because we are a small company, we may be unable to sufficiently deploy capital into a number of assets or asset groups. As a result, our portfolio may be concentrated in a small number of assets or may be otherwise undiversified, increasing the risk of loss and the magnitude of potential losses to us and our stockholders if one or more of these assets perform poorly.

Our investments may include subordinated tranches of MBS, which are subordinate in right of payment to more senior securities.

Our investments may include subordinated tranches of MBS, which are subordinated classes of securities in a structure of securities collateralized by a pool of mortgage loans and, accordingly, are the first or among the first to bear the loss upon a restructuring or liquidation of the underlying collateral and the last to receive payment of interest and principal. Additionally, estimated fair values of these subordinated interests tend to be more sensitive to changes in economic conditions than more senior securities. As a result, such subordinated interests generally are not actively traded and may not provide holders thereof with liquid investments.

We invest in Multi-Family MBS that are subordinate to more senior securities issued by the applicable securitization, which entails certain risks.

We purchase principal-only Multi-Family MBS that represent the first loss tranche of a multi-family mortgage loan securitization. These first loss principal only securities are subject to the first risk of loss if any losses are realized on the underlying mortgage loans in the securitization. We also purchase interest only securities issued by multi-family mortgage loan securitizations. However, these interest only Multi-Family MBS typically only receive payments of interest to the extent that there are funds available in the securitization to make the payments. Multi-Family MBS generally entitle the holders thereof to receive payments that depend primarily on the cash flow from a specified pool of multi-family mortgage loans. Consequently, first loss principal only Multi-Family MBS, will be adversely affected by payment defaults, delinquencies and losses on the underlying multi-family mortgage loans, each of which could have a material adverse effect on our cash flows and results of operations.

Transitional loans involve greater risk than conventional mortgage loans.

The typical borrower in a transitional loan has usually identified an undervalued asset that has been under-managed and/or is located in a recovering market. If the market in which the assets is located fails to improve according to the borrower's projections, or if the borrower fails to improve the quality of the asset's management and/or value of the asset, the borrower may not receive a sufficient return on the asset to satisfy the transitional loan, and we bear the risk that we may not recover some or all of our investment.

In addition, borrowers usually use the proceeds of a conventional mortgage to repay a transitional loan. Transitional loans therefore are subject to the risk of a borrower's inability to obtain permanent financing to repay the transitional loan. Risks of cost overruns and renovations of properties in transition may result in significant losses. The renovation, refurbishment or expansion of a property by a borrower involves risks of cost overruns and



non-completion. Estimates of the costs of improvements to bring an acquired property up to the standards established for the market position intended for the property may prove inaccurate. Other risks may include rehabilitation costs exceeding original estimates, possibly making a project uneconomical, environmental risks, delays in legal and other approvals (e.g., for condominiums) and rehabilitation and subsequent leasing of the property not being completed on schedule. If such renovation is not completed in a timely manner, or if it costs more than expected, the borrower may experience a prolonged impairment of net operating income and may not be able to make payments on our investment on a timely basis or at all. In the event of any default under transitional loans that may be held by us, we bear the risk of loss of principal and non-payment of interest and fees to the extent of any deficiency between the value of the mortgage collateral and the principal amount and unpaid interest on the transitional loan. To the extent we suffer such losses with respect to these transitional loans, it could adversely affect our results of operations and financial condition.

Investments in non-investment grade MBS may be illiquid, may have a higher risk of default, increased risk of loss and may not produce current returns.

We invest in MBS that are non-investment grade or unrated, which means that major rating agencies rate them below the top four investment-grade rating categories (i.e., “AAA” through “BBB”) or do not provide any rating for such MBS. Non-investment grade MBS securities tend to be less liquid, may have a higher risk of default and may be more difficult to value than investment grade bonds. Recessions or poor economic or pricing conditions in the markets associated with MBS may cause defaults or losses on loans underlying such securities. Non-investment grade securities are considered speculative, and their capacity to pay principal and interest in accordance with the terms of their issue is not certain and they should be expected to have a higher risk of default and loss than investment grade rated assets.

Non-Agency MBS and Multi-Family MBS have more price sensitivity than Agency MBS which can cause greater fluctuations in our book value. In addition, we finance our Non-Agency MBS and Multi-Family MBS with a limited number of repurchase agreement lenders. A withdrawal by one or more of these lenders could force us to sell our Non-Agency MBS and Multi-Family MBS at potentially distressed prices, which could impact our profitability. It could also cause other lenders to withdraw financing for our Agency MBS.

Non-Agency MBS and Multi-Family MBS historically have been more price sensitive than Agency MBS which limits the number of lenders willing to provide repurchase agreement financing for these securities. In a period of price volatility, we may be subject to margin calls, which could adversely impact our liquidity. These margin calls could result from price changes in Non-Agency MBS or Multi-Family MBS or from higher margin requirements by the lender in order to provide additional collateral as a result of the price volatility. In addition, lenders may no longer offer financing of Non-Agency MBS or Multi-Family MBS which could force us to sell some or all of these investments if we could not find replacement financing. In either instance we may be required to sell assets, which could negatively impact our profitability. In an extreme situation, if we lost significant amounts of financing or if we received a significant amount of margin calls on our Non-Agency MBS or Multi-Family MBS, other lenders may also seek to reduce their financing of our Agency MBS. In such a case we would likely have to sell additional investments to maintain our liquidity.

We invest in Multi-Family MBS and commercial real estate loans, which are secured by income producing properties. Such loans are typically made to single-asset entities, and the repayment of the loan is dependent principally on the net operating income from performance and value of the underlying property. The volatility of income performance results and property values may adversely affect our Multi-Family MBS.

Our Multi-Family MBS are secured by multi-family properties and our commercial real estate loans are secured by the underlying commercial property and, in each case are subject to risks of delinquency, foreclosure and loss. Multi-Family MBS and commercial real estate loans generally have a higher principal balance and the ability of a borrower to repay a loan secured by an income-producing property typically is dependent upon the successful operation of the property rather than upon the existence of independent income or assets of the borrower. If the net operating income of the property is reduced, the borrower's ability to repay the loan may be impaired. Net operating income of an income-producing property can be affected by, among other things: tenant mix, success of tenant businesses, property management decisions, property location and condition, competition from comparable types of properties, changes in laws that increase operating expenses or limit rents that may be charged, any need to address environmental contamination at the property, changes in national, regional or local economic conditions and/or specific industry segments, declines in regional or local real estate values and declines in regional or local rental or occupancy rates, increases in interest rates, real estate tax rates and other operating expenses, changes in governmental rules, regulations and fiscal policies, including environmental and/or tax legislation, and acts of God, terrorism, social unrest and civil disturbances.

Multi-family and commercial real estate property values and net operating income derived there from are subject to volatility and may be affected adversely by a number of factors, including, but not limited to, national, regional and local economic conditions; changes in tax laws; local real estate conditions; changes or continued weakness in specific industry segments; perceptions by prospective tenants, retailers and shoppers of the safety, convenience, services and attractiveness of the property; the willingness and ability of the property's owner to provide capable management and adequate maintenance; construction quality, age and design; demographic factors; retroactive changes to building or similar codes; and increases in operating expenses (such as energy costs).

Declines in the borrowers' net operating income and/or declines in property values of collateral securing Multi-Family MBS or commercial real estate loans could result in defaults on such loans, declines in our book value from reduced earnings and/or reductions to the market value of the investment.

Our target assets may include commercial real estate loans which are funded with interest reserves and borrowers may be unable to replenish such interest reserves once they run out.

We may invest in transitional commercial real estate and if we do so, we expect that we may require borrowers to post reserves to cover interest and operating expenses until the property cash flows are projected to increase sufficiently to cover debt service costs. We may also require the borrower to replenish reserves if they become depleted due to underperformance or if the borrower wishes to exercise extension options under the loan. Revenues on the properties underlying any commercial real estate loan investments may decrease in an economic downturn which would make it more difficult for borrowers to meet their payment obligations to us. Some borrowers may have difficulty servicing our debt and may not have sufficient capital to replenish reserves, which could have a significant impact on our operating results and cash flows.

We may not have control over certain of our loans and investments.

Our ability to manage our portfolio of loans and investments may be limited by the form in which they are made. In certain situations, we may:

- acquire investments subject to rights of senior classes, special servicers or collateral managers under intercreditor, servicing agreements or securitization documents;
- pledge our investments as collateral for financing arrangements;
- acquire only a minority and/or non-controlling participation in an underlying investment;
- co-invest with others through partnership, joint ventures or other entities, thereby acquiring non-controlling interests;
- or
- rely on independent third party management or servicing with respect to the management of an asset.

Therefore, we may not be able to exercise control over all aspects of our loans or investments. Such financial assets may involve risks not present in investments where senior creditors, junior creditors, servicers or third-party controlling investors are not involved. Our rights to control the process following a borrower default may be subject to the rights of senior or junior creditors or servicers whose interests may not be aligned with ours. A partner or co-venturer may have financial difficulties resulting in a negative impact on such asset, may have economic or business interests or goals that are inconsistent with ours, or may be in a position to take action contrary to our investment objectives.

Current market conditions for our target assets have been and may continue to be significantly influenced by U.S. Government and U.S. Federal Reserve intervention and attractive opportunities for investment in our target assets may not continue, which could have a material adverse effect on our business, financial condition, results of operations and our ability to make distributions to our stockholders.

Following the 2007-2008 financial crisis the U.S. Government and U.S. Federal Reserve, or the Fed, took unprecedented actions to stabilize the market for mortgage-related investments along with the broader economy. Such intervention has previously included maintenance of a near-zero target of the federal funds rate by the U.S. Federal Reserve, or the Fed; U.S. Government programs, such as the Home Affordable Modification Program, or HAMP, and the Home Affordable Refinance Program, or HARP; and quantitative easing, or QE, which was an open-ended program designed to expand the Fed's holdings of long-term securities by purchasing Agency RMBS and long-term Treasury bonds. Beginning in early 2014, the Fed gradually reduced its purchases of both Agency RMBS and Treasury bonds, and in October 2014 ended its purchase program under its third round of quantitative easing, or QE3 (although it is still reinvesting a portion of the principal and interest it receives on the Agency RMBS and U.S. Treasuries held in its portfolio).

It is unclear what effect, if any, the absence of the Fed's monthly purchases, other than its reinvestment of certain principal and interest payments it receives for Agency RMBS in its portfolio, will have on the value of the Agency RMBS in which we invest. However, it is possible that the market for such securities, the price of such securities and, as a result, our book value and/or net interest margin could be negatively affected.

Further, the mortgage industry has and continues to undergo fundamental changes, such as the conservatorship and possible future changes in the nature of participation in the mortgage market by Fannie Mae and Freddie Mac. While we believe that prices and yields for many of our target assets have been more favorable than in the past, and the yield curve environment for a leveraged Agency portfolio is currently very favorable, and that there are attractive opportunities for investment across our target asset classes, there is no way of knowing what impact government intervention or any future actions by the Fed will have on the prices and liquidity of Agency RMBS or other assets in which we may invest. The prices and yields of our target assets may be adversely affected, and could be subject to significant volatility upon changes, or perceived future changes, to such policies. Further, such prices and yields may not reflect the underlying value

of our target assets and may be significantly inflated due to these policies and the uncertainty of future changes to the mortgage industry. If current market conditions do not continue, and we are unable to structure or reposition our investment portfolio accordingly, there could be a material adverse effect on our business, financial condition, results of operations and our ability to make distributions to our stockholders.

Mortgage loan modification and refinancing programs and future legislative action may adversely affect the supply of, value of, and our returns on, our target assets.

In addition, in recent years, the U.S. Government, through the U.S. Federal Reserve, the Federal Housing Administration, or FHA, and the Federal Deposit Insurance Corporation, has implemented a number of federal programs designed to assist homeowners or reduce the number of properties going into foreclosure or going into non-performing status, including the Home Affordable Modification Program, or HAMP, which provides homeowners with assistance in avoiding residential mortgage loan foreclosures, the Hope for Homeowners Program, or H4H Program, which allows certain distressed borrowers to refinance their mortgages into FHA-insured loans in order to avoid residential mortgage loan foreclosures, and the Home Affordable Refinance Program, or HARP, which allows Fannie Mae and Freddie Mac borrowers who are current on their mortgage payments to refinance and reduce their monthly mortgage payments at loan-to-value ratios up to 125% (and, in some cases, above 125%) without new mortgage insurance. HAMP, the H4H Program, HARP and other loss mitigation programs may involve, among other things, the modification of mortgage loans to reduce the principal amount of the loans (through forbearance and/or forgiveness) and/or the rate of interest payable on the loans, or the extension of payment terms of the loans.

Especially with Non-Agency RMBS, a significant number of loan modifications with respect to a given security, including, but not limited to, those related to principal forgiveness and coupon reduction, could result in increased prepayment rates and thereby negatively impact the realized yields and cash flows on such securities. These loan modification programs, future legislative or regulatory actions, including possible amendments to the bankruptcy laws that result in the modification of outstanding residential mortgage loans, as well as changes in the requirements necessary to qualify for refinancing mortgage loans with Fannie Mae, Freddie Mac or Ginnie Mae may adversely affect the value of, and the returns on, Agency RMBS and other mortgage-related investments that we may purchase.

Other governmental actions may affect our business by hindering the pace of foreclosures. Over the past few years, there has been a backlog of foreclosures in certain jurisdictions, due to a combination of volume constraints and legal actions, including those brought by the U.S. Department of Justice, or DOJ, HUD, State Attorneys General, the office of the Comptroller of the Currency, and the Federal Reserve Board against mortgage servicers alleging wrongful foreclosure practices. Legal claims brought or threatened by the DOJ, HUD, the Consumer Financial Protection Bureau, or the CFPB, and State Attorneys General against residential mortgage servicers have produced large settlements. A portion of the funds from these settlements are directed to homeowners seeking to avoid foreclosure through mortgage modifications, and servicers are required to adopt specified measures to reduce mortgage obligations in certain situations. It is expected that the settlements will help many homeowners avoid foreclosures that would otherwise have occurred in the near-term. It is also possible that other residential mortgage servicers will agree to similar settlements. These developments will reduce the number of homes in the process of foreclosure and decrease the supply of properties and assets that meet our investment criteria.

Actions of the U.S. Government, including the U.S. Congress, U.S. Federal Reserve, U.S. Treasury Department and other governmental and regulatory bodies, to stabilize or reform the financial markets, or market responses to those actions, may not achieve the intended effect and may adversely affect our business, financial condition, results of operations and our ability to make distributions to our stockholders.

In response to the financial issues affecting the banking system and financial markets and going concern threats to commercial banks, investment banks and other financial institutions, Congress, the Obama Administration and various

regulatory agencies took numerous actions intended to stabilize and restructure the financial system. Members of the Trump Administration have announced an intent to vary a number of these actions. To the extent the markets do not respond favorably to any such actions by the U.S. Government or such actions do not function as intended, there may be broad adverse market implications, and our business may be adversely affected.

In July 2010, the U.S. Congress enacted the Dodd Frank Wall Street Reform and Consumer Protection Act, or the Dodd-Frank Act, in part to impose significant investment restrictions and capital requirements on banking entities and other organizations that are significant to U.S. financial markets. In part, it requires the retention of a portion of the credit risk inherent in the pool of securitized assets and by imposing additional registration and disclosure requirements. Although certain of the new requirements and restrictions exempt Agency RMBS, other government issued or guaranteed securities, or other securities, the Dodd-Frank Act imposes significant regulatory restrictions on the origination and securitization of residential mortgage loans, which will affect Non-Agency RMBS.

Furthermore, the revised regulation of over-the-counter derivatives and the inclusion of swaps as an investment that can cause a pooled investment vehicle to be a commodity pool would require us to register with and be regulated by the U.S. Commodity Futures Trading Commission, or the CFTC, as a commodity pool operator, or CPO, unless an exemption or other relief is available. Our Manager relies on relief from registration as a CPO based on a no-action letter issued on December 7, 2012 (the “No Action Letter”) by the CFTC staff that is applicable to CPOs of mortgage REITs, subject to complying with certain criteria. Further, advisors to commodity pools, which could potentially include our Manager, are required to register as commodity trading advisors, or CTAs, unless exemptive, no-action or similar relief is available. We believe such relief is available to our Manager on the basis of the No-Action Letter and existing regulations of the CFTC. If in the future our Manager does not meet the conditions set forth in the No-Action Letter for relief from registration as a CPO, the relief provided by the No-Action letter from registration as a CPO becomes unavailable for any other reason, or our belief regarding the availability of relief from registration as a CTA proves incorrect, and we or our Manager are unable to rely upon or obtain other exemptions from registration as a CPO or CTA, we may be required to reduce or eliminate our use of interest rate swaps or vary the manner in which we deploy interest rate swaps in our business, the interest-rate risk associated with our investments may increase, our investment performance may be adversely affected or the cost associated with employing other kinds of hedges against interest rate fluctuations could be higher. Alternatively, our Manager may be required to register as a CPO. If our Manager is required to and does register as a CPO, we nevertheless expect it to remain exempt from registration as a CTA with the CFTC because its advisory activities would relate only to its activities as CPO of the company. The Commodity Exchange Act and CFTC regulations impose various requirements on CPOs and CTAs, including record keeping, reporting, operational and marketing requirements, disclosure obligations and prohibitions on fraudulent activities. Complying with these requirements could increase our expenses and negatively impact our business, financial condition, results of operations and our ability to make distributions to our stockholders. It may also be difficult to comply with the reporting and disclosure requirements with respect to the kinds of products that we offer.

While the full impact of the Dodd-Frank Act cannot be assessed until all implementing regulations are released, the Dodd-Frank Act’s extensive requirements have had a significant effect on the financial markets, and may affect the availability or terms of financing from our lender counterparties, the availability or terms of swaps and swaptions into which we enter, and the availability or terms of mortgage-backed securities, both of which may have an adverse effect on our business, financial condition, results of operations and our ability to make distributions to our stockholders.

Even if certain of the new statutes and regulations imposed by the Dodd-Frank Act are not directly applicable to us, they may still increase our costs of entering into transactions with the parties to whom the requirements are directly applicable. Moreover, new exchange-trading and trade reporting requirements may lead to reductions in the liquidity of derivative transactions, causing higher pricing or reduced availability of derivatives, or the reduction of arbitrage opportunities for us, which could adversely affect the performance of certain of our hedging strategies. Importantly, many key aspects of the changes imposed by the Dodd-Frank Act will be established by various regulatory bodies and other groups over the next several years. As a result, we do not know how significantly the Dodd-Frank Act will affect us. It is possible that the Dodd-Frank Act could, among other things, increase our costs of operating as a public company, impose restrictions on our ability to securitize assets and reduce our investment returns on securitized assets.

Certain actions by the U.S. Federal Reserve could cause a flattening of the yield curve, which could adversely affect our business, financial condition, results of operations and our ability to make distributions to our stockholders.

On December 13, 2017, based on its outlook for economic activity, the labor market and inflation and weighing the uncertainties associated with this outlook, the Federal Reserve raised its target range for the federal funds rate to 1-¼ to 1-½ percent and on January 31, 2018, maintained the target range at 1-¼ to 1-½ percent. The Federal Reserve also indicated that it would likely contemplate additional rate increases in 2018 and beyond in a manner consistent with policy normalization, while indicating that such additional increases would likely be gradual and data dependent. Additionally, the Federal Reserve initiated its balance sheet normalization program in October 2017 that was announced in June 2017. This plan details the approach the FOMC intends to use to reduce the Federal Reserve's holding of Treasury and agency securities. For payments of principal that the Federal Reserve receives from its holdings of agency debt and mortgage-backed securities, the Committee anticipates that the cap will be \$4 billion per month and will increase in steps of \$4 billion in three-month intervals over 12 months until it reaches \$20 billion per month. There is still considerable uncertainty concerning the speed at which the Federal Reserve will continue to raise rates. Such uncertainty and volatility often leads to asset price volatility, wider spreads and increased hedging costs, which in turn could adversely affect our business, financial condition, results of operation and our ability to make distributions to our stockholders.

The federal conservatorship of Fannie Mae and Freddie Mac and related efforts, along with any changes in laws and regulations affecting the relationship between these agencies and the U.S. Government, may adversely affect our business.

The payments of principal and interest we receive on our Agency RMBS, which depend directly upon payments on the mortgages underlying such securities, are guaranteed by Fannie Mae, Freddie Mac and Ginnie Mae. Fannie Mae and Freddie Mac are GSEs, but their guarantees are not backed by the full faith and credit of the United States. Ginnie Mae is part of a U.S. Government agency, and its guarantees are backed by the full faith and credit of the United States.

In response to general market instability and, more specifically, the financial conditions of Fannie Mae and Freddie Mac, in July 2008, the Housing and Economic Recovery Act of 2008, or HERA, established the FHFA as the new regulator for Fannie Mae and Freddie Mac. In September 2008, the U.S. Treasury Department, the FHFA and the U.S. Federal Reserve announced a comprehensive action plan to help stabilize the financial markets, support the availability of mortgage financing and protect taxpayers. Under this plan, among other things, the FHFA was appointed as conservator of both Fannie Mae and Freddie Mac, allowing the FHFA to control the actions of the two GSEs, without forcing them to liquidate, which would be the case under receivership. Importantly, the primary focus of the plan was to increase the availability of mortgage financing by allowing these GSEs to continue to grow their guarantee business without limit, while limiting the size of their retained mortgage and agency security portfolios and requiring that these portfolios be reduced over time.

Although the U.S. Government has committed to support the positive net worth of Fannie Mae and Freddie Mac, there can be no assurance that these actions will be adequate for their needs. These uncertainties lead to questions about the availability of, and trading market for, Agency RMBS. Despite the steps taken by the U.S. Government, Fannie Mae and Freddie Mac could default on their guarantee obligations, which would adversely affect the value of our Agency RMBS. Accordingly, if these government actions are inadequate and the GSEs continue to suffer losses or cease to exist, our business, financial condition, results of operations and our ability to make distributions to our stockholders could be adversely affected.

In addition, the problems faced by Fannie Mae and Freddie Mac resulting in their being placed into federal conservatorship and receiving significant U.S. Government support have sparked serious debate among federal policy makers regarding the continued role of the U.S. Government in providing liquidity for mortgage loans. The current Treasury Secretary has created additional uncertainty by expressing support for ending government control of Fannie Mae and Freddie Mac, but varying his previous statements during his confirmation hearing. The future roles of Fannie Mae and Freddie Mac could be significantly reduced and the nature of their guarantee obligations could be considerably limited relative to historical measurements. Any such changes to the nature of their guarantee obligations could redefine what constitutes an agency security and could have broad adverse implications for the market and our business, financial condition, results of operations and our ability to make distributions to our stockholders. If Fannie Mae or Freddie Mac were eliminated, or their structures were to change radically (i.e., limitation or removal of the guarantee obligation), or their market share reduced because of required price increases or lower limits on the loans they can guarantee, we could be unable to acquire additional Agency RMBS and our existing Agency RMBS could be adversely impacted.

We could be negatively affected in a number of ways depending on the manner in which related events unfold for Fannie Mae and Freddie Mac. We rely on our Agency RMBS (as well as Non-Agency RMBS) as collateral for our financings under our repurchase agreements. Any decline in their value, or perceived market uncertainty about their value, would make it more difficult for us to obtain financing on our Agency RMBS on acceptable terms or at all, or to maintain our compliance with the terms of any financing transactions. Further, the current support provided by the U.S. Treasury Department to Fannie Mae and Freddie Mac, and any additional support it may provide in the future, could have the effect of lowering the interest rates we expect to receive from Agency RMBS, thereby tightening the spread between the interest we earn on our Agency RMBS and the cost of financing those assets. A reduction in the supply of Agency RMBS could also negatively affect the pricing of Agency RMBS by reducing the spread between the interest we earn on our investment portfolio of Agency RMBS and our cost of financing that portfolio.

As indicated above, legislation has changed the relationship between Fannie Mae and Freddie Mac and the U.S. Government and the current Treasury Secretary has indicated that the relationship may change again in the future. Future legislation that further changes the relationship between Fannie Mae and Freddie Mac and the U.S. Government could also nationalize, privatize or eliminate such entities entirely. Any law affecting these GSEs may create market uncertainty and have the effect of reducing the actual or perceived credit quality of securities issued or guaranteed by Fannie Mae or Freddie Mac. As a result, such laws could increase the risk of loss on our investments in Agency RMBS guaranteed by Fannie Mae and/or Freddie Mac. It also is possible that such laws could adversely impact the market for such securities and spreads at which they trade. All of the foregoing could adversely affect our business, financial condition, results of operations and our ability to make distributions to our stockholders.

Future legislation may, among other things, revoke the charters of Fannie Mae and Freddie Mac, and we could be adversely affected if these proposed laws were enacted.

Bills calling for the revocation of the charters of Fannie Mae and Freddie Mac and seeking to increase the opportunities for private capital to participate in, and consequently bear the risk of loss in connection with, government-guaranteed MBS have been introduced in both the House and the Senate. If the charters of Fannie Mae and Freddie Mac were revoked, it is unclear what effect, if any, this would have on the value of our Agency RMBS guaranteed by Fannie Mae and Freddie Mac. It is also possible that the above-referenced proposed legislation, if made law, could adversely impact the market for securities issued or guaranteed by the U.S. Government and the spreads at which they trade. The foregoing could adversely affect the pricing, supply, liquidity and value of our target assets and otherwise adversely affect our business, operations and financial condition.

Certain of the mortgage loans underlying the RMBS assets may be subject to the new “know before you owe” TRID disclosures.

Mortgage loans underlying the RMBS assets may be subject to the CFPB’s Know Before You Owe TILA – RESPA Integrated Disclosure, or TRID, rule, which became effective for mortgage loans whose applications were received on or after October 3, 2015. The purpose of the TRID rule was to reconcile overlapping disclosure obligations under TILA and the Real Estate Settlement Procedures Act, or RESPA, and to provide for integrated closing disclosure and loan estimate forms that would satisfy those requirements under both TILA and RESPA.

Regular instances of potential non-compliance with the TRID rule have been reported in the marketplace since it became effective. Certain TILA-based disclosure provisions of the TRID rule carry assignee liability. Violations of the TILA-based disclosure provisions of the TRID rule are limited in individual actions to actual damages, statutory damages for certain violations of not more than \$4,000 per mortgage loan plus attorney’s fees and court costs, and can potentially result in liability for assignees where the violation is apparent on the face of the disclosure and the assignment was voluntary. While the statute of limitations under TILA is generally one-year from the date of origination for most TRID violations, mortgagors may raise a violation of the TRID rules as a matter of defense by recoupment or set-off to an action to collect the debt beyond the one-year period, if permitted by state law. Further, for certain mortgage loans, while not changed by TRID requirements, TILA’s right of rescission may be extended to three years from consummation if there are errors in certain “material disclosures” such as the required disclosures of finance charges and payment schedule, which are contained within the TRID closing disclosure.

Although the TRID rule provides for multiple mechanisms to cure certain errors in the closing disclosure, uncertainties remain as to liability for violating other requirements in the closing disclosure and in the loan estimate, including violations that may not be expressly covered by the cure mechanisms of the TRID rule. On December 29, 2015, the Director of the CFPB released a letter that provides informal guidance with respect to some of these uncertainties (the “CFPB Director’s Letter”). The CFPB Director’s Letter is not binding upon the CFPB, any other regulator or the courts and does not necessarily reflect how courts and regulators, including the CFPB, may view liability for TRID violations in the future.

On July 29, 2016, the CFPB proposed amendments to the TRID rule, or the Proposed Rule. Comments on the Proposed Rule were due by October 18, 2016. The CFPB stated in its Proposed Rule that it does not intend to further clarify the curative provisions contained in TRID, and the Proposed Rule does not address any TILA liability issues. No assurance can be given that the results of any final rulemaking by the CFPB will clarify the ambiguities of the requirements of the TRID rule, or that future CFPB rulemaking, if any, will be consistent with the CFPB Director’s Letter.

Various state and local jurisdictions may adopt similar or more onerous provisions in the future. No prediction can be made as to how these laws and regulations relating to assignee liability may affect the market value of the RMBS assets. In addition, the TRID rule may adversely affect the market generally for mortgage-backed securities and the liquidity thereof if investors are not willing to invest in securitizations with mortgage loans originated with exceptions



to the TRID rule.

Drug, RICO and money laundering violations could lead to property forfeitures.

Federal law provides that property purchased or improved with assets derived from criminal activity or otherwise tainted, or used in the commission of certain offenses, can be seized and ordered forfeited to the United States. The offenses which can trigger such a seizure and forfeiture include, among others, violations of the Racketeer Influenced and Corrupt Organizations Act, the Bank Secrecy Act, the anti-money laundering laws and regulations, including the USA Patriot Act of 2001 and the regulations issued pursuant to that act, as well as the narcotic drug laws. In many instances, the United States may seize the property even before a conviction occurs.

In the event of a forfeiture proceeding, a lender may be able to establish its interest in the property by proving that (i) its mortgage was executed and recorded before the commission of the illegal conduct from which the assets used to purchase or improve the property were derived or before the commission of any other crime upon which the forfeiture is based, or (ii) the lender, at the time of the execution of the mortgage, did not know or was reasonably without cause to believe that the property was subject to forfeiture. However, there is no assurance that such a defense would be successful and therefrom the related RMBS assets may be adversely affected.

We may be subject to lender liability claims, and if we are held liable under such claims, we could be subject to losses.

In recent years, a number of judicial decisions have upheld the right of borrowers to sue lending institutions on the basis of various evolving legal theories, collectively termed “lender liability.” Generally, lender liability is founded on the premise that a lender has either violated a duty, whether implied or contractual, of good faith and fair dealing owed to the borrower or has assumed a degree of control over the borrower resulting in the creation of a fiduciary duty owed to the borrower or its other creditors or stockholders. We cannot assure prospective investors that such claims will not arise or that we will not be subject to significant liability if a claim of this type did arise.

Homeowner association super priority liens, special assessment liens and energy efficiency liens may take priority over the mortgage loans underlying our RMBS assets.

In some states it is possible that the first lien of the mortgages may be extinguished by super priority liens of homeowner associations, potentially resulting in a loss of the mortgage loan’s outstanding principal balance. In at least 20 states, and the District of Columbia, homeowner association, or HOA, or condominium association assessment liens can take priority over first lien mortgages under certain circumstances. The number of these so called “super lien” states has increased in the past few decades and may increase further. Prior rulings by the highest courts of Nevada and the District of Columbia have held that the “super lien statute” provides the HOA or condominium association with a true lien priority rather than a payment priority from the proceeds of the sale, creating the ability to extinguish the senior mortgage and greatly increasing the risk of losses on mortgage loans secured by homes whose owners fail to pay HOA or condominium fees.

The laws of these “super lien” states that provide for HOA super liens vary in terms of: (a) the duration of the priority period (with many at six months and some with no limitations); (b) the assessments secured by the HOA lien (charges can include not only unpaid HOA assessments, but also late charges, collection

costs, attorney fees, foreclosure costs, fines, and interest); (c) whether the HOA must give lenders with liens encumbering the mortgaged property notice of the homeowner's failure to pay the assessment; and (d) the statute of limitations on HOA foreclosure rights.

On May 28, 2015, Nevada adopted a new law which took effect on October 1, 2015, that provides clarity to the superpriority statutes in Nevada with respect to: (a) the type of notice that must be provided to lien holders by an HOA regarding the HOA deficiency and the HOA sale; (b) the manner of notification of the HOA deficiency and HOA sale; (c) amounts that can lawfully be included in the superpriority amount that can extinguish a first deed; and (d) the location of an HOA sale. The revised law also provides a 60-day redemption period for the owner of the property and first lien holder following an HOA sale.

There is currently no efficient mechanism available to loan servicers of RMBS securities to track the status of borrowers' payments of HOA assessments that are governed by state super lien statutes. In fact, there is neither a unified database for HOA information, nor a centralized place for HOAs and loan servicers to contact one another. Consequently, in some of the super lien states there often is no practical, systematic method for loan servicers to determine when an HOA assessment is unpaid or when the HOA initiates foreclosure of its lien. In some circumstances the servicer may make servicing advances to pay delinquent homeowner association assessments or for the costs of determining whether any mortgaged property is subject to a homeowner association assessment or a related lien. If such servicing advances are not recovered from the related mortgagor or liquidation proceeds, they will be paid to the servicer from collections on the mortgage loans and reduce amounts payable on the related RMBS asset.

If an HOA, or a purchaser of an HOA super lien, completes a foreclosure on an HOA super lien on a mortgaged property, the underlying mortgage loan will be extinguished. In those instances, the related RMBS assets could suffer a loss of the entire outstanding principal balance of the mortgage loan, plus interest. A servicer might be able to attempt to recover on an unsecured basis by suing the borrower personally for the balance, but recovery in these circumstances will be problematic if the borrower has no meaningful assets to recover against.

Mortgaged properties securing the mortgage loans underlying the RMBS assets may also be subject to the lien of special property taxes and/or special assessments. These liens may be superior to the liens securing the mortgage loans, irrespective of the date of the mortgage. In some instances, individual borrowers may be able to elect to enter into contracts with governmental agencies for Property Assessed Clean Energy (PACE) or similar assessments that are intended to secure the payment of energy and water efficiency and distributed energy generation improvements that are permanently affixed to their properties, possibly without notice to or the consent of the mortgagee. These assessments may also have lien priority over the mortgages securing mortgage loans. No assurance can be given that any mortgaged property so assessed will increase in value to the extent of the assessment lien. Additional indebtedness secured by the assessment lien would reduce the amount of the value of the mortgaged property available to satisfy the affected mortgage loan and thereby reduce the amount available for distributions on the related underlying RMBS asset.

The increasing number of proposed U.S. federal, state and local laws and regulations may affect certain mortgage-related assets in which we intend to invest and could increase our cost of doing business.

Additional legislation has been considered, proposed or adopted which, among other provisions, could further hinder the ability of a servicer to foreclose promptly on defaulted mortgage loans or would permit limited assignee liability for certain violations in the mortgage loan origination process. For example, the Dodd-Frank Act created the CFPB, which supervises consumer financial services companies (including bank and non-bank mortgage lenders and mortgage servicers) and enforces U.S. federal consumer protection laws as they apply to banks, credit unions and other financial services companies, including mortgage servicers, and which has issued many regulations regarding mortgage origination and servicing. These regulations provide for special remedies in favor of consumer mortgage

borrowers, particularly upon default and foreclosure. It remains uncertain whether any of these measures will have a significant impact on foreclosure volumes or what the timing of that impact would be, as well as whether these measures will remain in effect. If foreclosure volumes were to decline significantly, we may experience difficulty in finding target assets at attractive prices, which will adversely affect our business, financial condition, results of operations and our ability to make distributions to our stockholders.

We cannot predict whether or in what form the U.S. Congress, the various state and local legislatures or the various federal, state or local regulatory agencies may enact legislation affecting our business. We will evaluate the potential impact of any initiatives which, if enacted, could affect our practices and results of operations. We are unable to predict whether U.S. federal, state or local authorities will enact laws, rules or regulations that will require changes in our practices in the future, and any such changes could adversely affect our business, financial condition, results of operations and our ability to make distributions to our stockholders.

We have identified material weaknesses in our internal control over financial reporting as well as significant deficiencies in our disclosure controls and procedures, and we may identify additional material weaknesses in internal controls or significant deficiencies in our disclosure controls and procedures in the future. If we fail to remediate the identified material weaknesses, or if we otherwise fail to maintain effective internal control over financial reporting and disclosure controls and procedures, we may not be able to accurately report our financial results, detect or prevent fraud, or file our periodic reports in a timely manner, which may, among other adverse consequences, cause investors to lose confidence in our reported financial information and lead to a decline in our stock price.

The Sarbanes-Oxley Act of 2002, or SOX, requires, among other things, ongoing review of our disclosure controls and procedures and internal control over financial reporting. Section 404 of SOX requires us to include a management report on our internal control over financial reporting in our Annual Reports on Form 10-K, which report must include management's assessment of the effectiveness of our internal control over financial reporting. In addition, we are required, on a quarterly and annual basis, to disclose the conclusions of our principal executive and principal financial officer on the effectiveness of our disclosure controls and procedures.

These reviews and assessments have resulted in our identifying the material weaknesses in our internal control over financial reporting and significant deficiencies in our disclosure controls and procedures described below. A "material weakness" is a deficiency, or a combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis. We believe the actions described below will be sufficient to remediate the identified material weaknesses that have not yet been remediated, and strengthen our internal control over financial reporting as well as our disclosure controls and procedures. However, while we believe meaningful progress has been made, certain of the new and enhanced systems and controls are not as yet fully operational, and we may determine to take additional measures to address our control deficiencies or to modify the remediation plans described below. The identified material weakness in our internal control over financial reporting will not be considered remediated until the new controls are fully implemented, in operation for a sufficient period of time, tested and concluded by management to be designed and operating effectively. We cannot currently estimate when all such remediation will be complete, nor can we currently ascertain whether additional actions will be required, or the costs therefor.

2017 and Prior Determinations and Actions. In connection with the preparation of our financial statements for inclusion in our Annual Report on Form 10-K for the year ended December 31, 2015, or the 2015 10-K, we identified a material weakness in our internal control over financial reporting. Such material weakness did not result in any misstatements in our audited consolidated financial statements included in our 2015 10-K, but did require adjustments during the 2015 annual audit with respect to net income (loss) attributable to common stockholders, total other comprehensive income, and basic and diluted income (loss) per share in our preliminary 2015 consolidated financial statements, and required the restatement of the unaudited condensed consolidated financial statements for the periods ended June 30, 2015 and September 30, 2015, originally included in our Quarterly Reports on Form 10-Q for the second and third quarters of 2015, respectively.

The material weakness consisted of a failure of our control over the critical timely review of account balances to determine whether the appropriate accounting policy and methodology had been applied, which in turn resulted in the incorrect reporting of unrealized losses on two Non-Agency RMBS IOs for which we had elected the fair value option at the inception of each transaction. Such losses were incorrectly reported through other comprehensive income (OCI) instead of through our statements of operations for each of the quarter and year-to-date periods ended June 30, 2015 and September 30, 2015, respectively. The first IO was acquired in the Oaks Mortgage Trust Series 2015-1 transaction completed in April 2015, and the second IO was acquired in the Oaks Mortgage Trust Series 2015-2 transaction completed in November 2015.

In connection with the preparation of our third quarter financial statements for the period ended September 30, 2017, we identified a further instance of a failure of our internal control over the depth and timeliness of review of account balances, specifically relating to the asset and liability balances of securitizations that we consolidate in our financial statements. A discrepancy between the liability balance reported in a consolidation workbook required an adjustment to the asset and liability balances during the preparation of our consolidated balance sheet for the period ended September 30, 2017. While the adjustment did not impact our stockholders' equity or our net income, if uncorrected, such a discrepancy could cause our reported total asset and liability balances to be inaccurate, possibly by material amounts.

As a consequence of this material weakness, management concluded that our internal control over financial reporting, and consequently our disclosure controls and procedures, were not effective as of December 31, 2017.

To remediate the material weakness in our internal control over financial reporting related to timely review of account balances (and consequent deficiencies in our disclosure controls and procedures), we have continued to implement certain changes to the design of our internal controls. Specifically, we previously contracted with a nationally recognized accounting systems and services provider to provide us with a more robust accounting system that has improved the effectiveness of correct accounting treatment for transactions that we enter into. Implementation of the new system was completed effective January 1, 2017, and we have substantially completed the process, with the assistance of an experienced financial reporting consultant, of formalizing enhanced written policies and procedures appropriate to the design and operation of controls and procedures applicable to the new system. We began the testing of controls during the fourth quarter, and also enhanced the timeliness and strengthened the review process in respect of consolidated trust account balances to ensure that the related control operated at the level of precision necessary to effectively and timely identify, investigate and resolve any discrepancies. We believe the actions described above will be sufficient to remediate the identified material weaknesses and strengthen our internal control over financial reporting, as well as our disclosure controls and procedures. However, while we believe meaningful progress has been made, and the new and enhanced systems and controls are now fully operational, we may determine to take additional measures to address our control deficiencies or to modify the remediation plans described above. The identified material weakness in our internal control over financial reporting will not be considered remediated until the new controls have been in operation for a sufficient period of time, tested and concluded by management to be designed and operating effectively. We intend that such remediation will be complete by December 31, 2018, but we cannot

currently ascertain whether additional actions will be required, or the costs therefor.

2016 Determinations and Actions. In connection with our determination of an inability to offset net gains realized on certain hedging transactions in 2013 for federal income tax purposes with net capital losses realized in 2013 on the sale of certain securities, during the quarter ended September 30, 2016, management and our Audit Committee identified a material weakness in our internal control over financial reporting. The material weakness consisted of a failure to ensure adequate timely technical review of the position proposed and analysis undertaken by our nationally recognized tax-consulting specialist and taken by us in calculating our REIT taxable income for 2013. As a result, we declared on November 9, 2016, and paid on December 27, 2016, a deficiency dividend to reduce our 2013 undistributed taxable income, as adjusted, and satisfy the REIT distribution requirements. We also recorded a charge of \$1.86 million in the third quarter of 2016 for interest charges expected to be payable to the IRS following the payment of the dividend. The material weakness did not impact any prior period GAAP financial statements, and thus did not result in any misstatements of our annual audited or interim financial statements. Nonetheless, when taken together with the material weakness described below, management and our Audit Committee concluded that additional remediation measures described below are necessary to enhance our control environment.

As a consequence of this material weakness, management concluded that our internal control over financial reporting, and consequently our disclosure controls and procedures, were not effective as of December 31, 2016, nor were they effective for the quarters ended March 31, 2016, June 30, 2016 or September 30, 2016.

To remediate this material weakness, we have implemented certain changes to the design of our internal controls. Specifically, for any REIT tax matters that we have not previously addressed, we are now required to obtain a written technical review and conclusion from a nationally recognized accounting firm or law firm, which must be presented to and approved by our Audit Committee prior to our adoption of the related conclusion.

Because of our status as an emerging growth company, our independent registered public accounting firm will not be required to attest to the effectiveness of our internal control over financial reporting until after December 31, 2018. Our independent registered public accounting firm will not be required to attest to the effectiveness of our internal control over financial reporting until our Annual Report on Form 10-K following the date on which we are no longer an “emerging growth company.” We will remain an emerging growth company until the earlier of (a) December 31, 2018, (b) the last day of any fiscal year in which we have total annual gross revenue of at least \$1.0 billion, or (c) the last day of any fiscal year in which we are deemed to be a large accelerated filer, which means the market value of our common stock that is held by non-affiliates exceeds \$700 million as of the prior June 30th, and (d) the date on which we have issued more than \$1.0 billion in non-convertible debt during the prior three-year period. For as long as we remain an emerging growth company, we intend to take advantage of the exemption permitting us not to comply with the independent registered public accounting firm attestation requirement. At such time that an attestation is required, however, our independent registered public accounting firm may issue a report that is qualified if it is not satisfied with our controls or the level at which our controls are documented, designed, operated or reviewed, or if it interprets the relevant requirements differently from us. Material weaknesses and significant deficiencies may be identified during the audit process or at other times. During the course of the evaluation, documentation or attestation, we or our independent registered public accounting firm may identify weaknesses and deficiencies that we may not be able to remedy in time to meet the deadline imposed by the Sarbanes-Oxley Act for compliance with Section 404, or at all.

We depend on our accounting services provider for assistance with the preparation of our financial statements, access to appropriate accounting technology and assistance with portfolio valuation.

Pursuant to our agreement with SS&C Technologies, or SS&C, SS&C currently provides a monthly calculation of our net asset value, maintains our general ledger and all related accounting records, reconciles all broker and custodial statements we routinely receive, provides us with monthly portfolio, cash and position reports, assists us with portfolio valuations, prepares draft quarterly financial statements for our review and provides us with access to data and technology services to facilitate the preparation of our annual financial statements. If our agreement with SS&C were to be terminated and no suitable replacement can be timely engaged, we may not be able to timely and accurately prepare our financial statements.

We may be subject to fines or other penalties based on the conduct of the mortgage loan originators and brokers that originated the residential mortgage loans that we previously acquired, and the third-party servicers which service the loans we acquired.

Mortgage loan originators and brokers are subject to strict and evolving consumer protection laws and other legal obligations with respect to the origination of residential mortgage loans. These laws and regulations include the CFPB's "ability-to-repay" and "qualified mortgage" regulations, which became effective on January 10, 2014. In addition, there are various other federal, state and local laws and regulations that are intended to discourage predatory lending practices by residential mortgage loan originators. For example, the federal Home Ownership and Equity Protection Act of 1994, or HOEPA, requires lenders to make certain disclosures and comply with certain limitations with respect to loans that are considered to be "high cost" loans. These requirements, as well as certain standards set forth in the "ability-to-repay" and "qualified mortgage" regulations, may be highly subjective and open to interpretation. As a result, a court may determine that a residential mortgage loan did not meet an applicable standard or test even if the mortgage loan originator reasonably believed such standard or test had been satisfied. Failure or alleged failure of residential mortgage loan originators to comply with these laws and regulations could subject us, as an assignee or purchaser of these loans or securities backed by these loans, to delays in foreclosure proceedings, increased litigation expenses, monetary penalties and defenses to foreclosure, including by recoupment or setoff of finance charges and fees collected, and in some cases could also result in rescission of the affected residential mortgage loans, which could adversely impact our business and financial results.

We may be required to make servicing advances and may be exposed to a risk of loss if such advances become non-recoverable and such advances and risk could adversely affect our liquidity or cash flow.

In connection with most (as currently anticipated) securitization transactions wherein FOAC sells mortgage loans to the securitization trust and holds the MSRs with respect to those mortgage loans, FOAC has entered into and expects to continue to enter into sub-servicing agreements with one or more sub-servicers. Pursuant to the terms of the sub-servicing agreements, FOAC will be required to refund or to fund any servicing advances that are obligated to be made by the sub-servicers. FOAC will therefore be exposed to the potential loss of any servicing advance that becomes a non-recoverable. It is expected that the aggregate amount of servicing advances, and FOAC's exposure to the risk of loss related to such servicing advances, will increase as FOAC enters into additional securitization transactions. Such advances and exposure going forward could adversely affect our liquidity or cash flow during a financial period.

When we have acquired and subsequently re-sold any mortgage loans, we may be required to repurchase such loans or indemnify investors if we breach certain representations and warranties.

When we have acquired and subsequently re-sold any mortgage loans, we are generally required to make customary representations and warranties about such loans to the loan purchaser. Residential mortgage loan sale agreements and

the terms of any securitizations into which we have sold or deposited loans generally require us to repurchase or substitute loans in the event that we breach a representation or warranty given to the loan purchaser or the securitization trust. In addition, we may be required to repurchase loans as a result of borrower fraud or in the event of an early payment default by a borrower. Repurchased loans are typically worth only a fraction of the original price. Significant repurchase activity could adversely affect our business, financial condition and results of operations and our ability to make distributions.

Government use of eminent domain to seize underwater mortgages could materially adversely affect the value of, and the returns on, our RMBS.

The mortgages securing our investments are located in many geographic regions across the United States, with significantly higher exposure in California, and Washington. Several county and municipal governments have discussed using eminent domain to seize from mortgage holders the mortgages of borrowers who are underwater, but not in default. Legislation enacted in 2014 prohibits the FHFA and the Department of Housing and Urban Development from using federal funds to facilitate the seizure of mortgage loans by a state or local municipality. However, if definitive action is taken by any local governments and such actions withstand Constitutional and other legal challenges, resulting in mortgages securing certain of our investments being seized using eminent domain, the consideration received from the seizing authorities for such mortgages may be substantially less than the outstanding principal balance, which would result in a realized loss and a corresponding write-down of the principal balance of those mortgages. The result of these seizures would be that the amounts we receive on our investments would be less than we would otherwise have received if the mortgage loans had not been seized, which may result in a lower return on such assets or require charges for “other-than-temporary impairment” or loan loss reserves. If governments ultimately adopt such plans and mortgages securing certain of our investments are seized on a widespread scale, it could have an adverse effect on the value of and/or returns on our assets and our results of operations more generally.

We operate in a highly competitive market for investment opportunities and competition may limit our ability to acquire desirable investments in RMBS, Multi-Family MBS, MSRs and other mortgage related investments and could also affect the pricing of these securities.

We operate in a highly competitive market for investment opportunities. Our profitability depends, in large part, on our ability to acquire RMBS, Multi-Family MBS, MSRs and other mortgage related investments at favorable prices. In acquiring these assets, we will compete with a variety of institutional investors, including other REITs, specialty finance companies, public and private funds (including funds that our Manager may now or in the future sponsor, advise or manage), hedge funds, commercial and investment banks, commercial finance and insurance companies and other financial institutions. Many of our competitors are substantially larger and have considerably greater financial, technical, marketing and other resources than we do. New companies, including REITs, have recently raised, or are expected to raise, significant amounts of capital, and may have investment objectives that overlap with ours, which may create additional competition for investment opportunities. Some competitors may have a lower cost of funds and access to funding sources that may not be available to us, such as funding from the U.S. Government. Many of our competitors are not subject to the operating constraints associated with REIT tax compliance or maintenance of an exclusion from the Investment Company Act. In addition, some of our competitors may have higher risk tolerances or different risk assessments, which could allow them to consider a wider variety of investments and establish more relationships than us. Furthermore, competition for investments in RMBS, Multi-Family MBS, MSRs and other mortgage related investments may lead to the price of such assets increasing, which may further limit our ability to generate desired returns. We cannot assure you that the competitive pressures we face will not have a material adverse effect on our business, financial condition, results of operations and our ability to make distributions to our stockholders. Also, as a result of this competition, desirable investments in these assets may be limited in the future

and we may not be able to take advantage of attractive investment opportunities from time to time, as we can provide no assurance that we will be able to identify and make investments that are consistent with our investment objectives.

Adverse developments in the broader residential mortgage market may adversely affect the value of the assets in which we invest.

Since 2007, the residential mortgage market in the United States has experienced a variety of unprecedented difficulties and significant adverse changes in economic conditions, including defaults, credit losses and liquidity concerns. Certain commercial banks, investment banks and insurance companies announced extensive losses from exposure to the residential mortgage market. These losses reduced financial industry capital, leading to reduced liquidity for some institutions. These factors have impacted investor perception of the risk associated with real estate-related assets, including Agency RMBS and other high-quality RMBS assets. As a result, values for RMBS assets, including some Agency RMBS and other AAA-rated RMBS assets, have experienced a certain amount of volatility. Further increased volatility and deterioration in the broader residential mortgage and RMBS markets may adversely affect the performance and market value of the Agency and Non-Agency RMBS in which we invest. Accordingly, our results of operations may be materially affected by conditions in the residential mortgage market, including MBS.

We invest in Agency and Non-Agency RMBS. We rely on our securities as collateral for our financings. Any decline in their value, or perceived market uncertainty about their value, would likely make it difficult for us to obtain financing on favorable terms or at all, or maintain our compliance with terms of any financing arrangements already in place. The securities we acquire will be classified for accounting purposes as available-for-sale. All assets classified as available-for-sale will be reported at fair value, based on market prices from third-party sources, with unrealized gains and losses excluded from earnings and reported as a separate component of stockholders' equity. As a result, a decline in fair values may reduce the book value of our assets. Moreover, if the decline in fair value of an available-for-sale security is other-than-temporarily impaired, such decline will reduce earnings. If market conditions result in a decline in the fair value of our assets, our business, financial condition, results of operations and our ability to make distributions to our stockholders could be adversely affected.

A prolonged economic recession and further declining real estate values could impair our assets and harm our operations.

The risks associated with our business are more severe during economic recessions and are compounded by declining real estate values. The Multi-Family MBS and Non-Agency RMBS in which we invest part of our capital will be particularly sensitive to these risks. Declining real estate values will likely reduce the level of new mortgage loan originations since borrowers often use appreciation in the value of their existing properties to support the purchase of additional properties. Borrowers will also be less able to pay principal and interest on loans underlying the securities in which we invest if the value of residential real estate weakens further. Further, declining real estate values significantly increase the likelihood that we will incur losses on Multi-Family MBS and Non-Agency RMBS in the event of default because the value of collateral on the mortgages underlying such securities may be insufficient to cover the outstanding principal amount of the loan. Any sustained period of increased payment delinquencies, foreclosures or losses could adversely affect our net interest income from Non-Agency RMBS in our portfolio, which could have an adverse effect on our business, financial condition, results of operations and our ability to make distributions to our stockholders.

The lack of liquidity in our investments may adversely affect our business.

We acquire assets that are not liquid or publicly traded. A lack of liquidity may result from the absence of a willing buyer or an established market for these assets, as well as legal or contractual restrictions on resale or the



unavailability of financing for these assets. In addition, mortgage-related assets generally experience periods of illiquidity. Further, validating third-party pricing for illiquid assets may be more subjective than for liquid assets. Any illiquidity of our investments may make it difficult for us to sell such investments if the need or desire arises. In addition, if we are required to liquidate all or a portion of our portfolio quickly, we may realize significantly less than the value at which we have previously recorded our investments. Further, we may face other restrictions on our ability to liquidate an investment in a business entity to the extent that we or our Manager has or could be attributed with material, non-public information regarding such business entity. If we are unable to sell our assets at favorable prices or at all, it could adversely affect our business, financial condition and results of operations and our ability to make distributions to our stockholders. Assets that are illiquid are more difficult to finance, and to the extent that we use leverage to finance assets that become illiquid, we may lose that leverage or have it reduced. Assets tend to become less liquid during times of financial stress, which is often the time that liquidity is most needed. As a result, our ability to vary our portfolio in response to changes in economic and other conditions may be relatively limited, which could adversely affect our business, financial condition, results of operations and our ability to make distributions to our stockholders.

Changes in the underwriting standards by Freddie Mac or Fannie Mae could have an adverse impact on agency mortgage investments in which we may invest or make it more difficult to acquire attractive Non-Agency mortgage investments.

In April 2010, Freddie Mac and Fannie Mae announced tighter underwriting guidelines for ARMs and hybrid interest-only ARMs in particular. Specifically, Freddie Mac announced that it would no longer purchase interest-only mortgages and Fannie Mae changed its eligibility criteria for purchasing and securitizing ARMs to protect consumers from potentially dramatic payment increases. Our target assets include ARMs and hybrid ARMs. Tighter underwriting standards by Freddie Mac or Fannie Mae could reduce the supply of ARMs, resulting in a reduction in the availability of the asset class. More lenient underwriting standards could also substantially reduce the supply and attractiveness of investments in Non-Agency RMBS.

We will be subject to the risk that U.S. Government agencies and/or GSEs may not be able to fully satisfy their guarantees of Agency RMBS or that these guarantee obligations may be repudiated, which may adversely affect the value of our assets and our ability to sell or finance these securities.

The interest and principal payments we receive on the Agency RMBS in which we invest is guaranteed by Fannie Mae, Freddie Mac or Ginnie Mae. Unlike the Ginnie Mae securities in which we invest, the principal and interest on securities issued by Fannie Mae and Freddie Mac are not guaranteed by the U.S. Government. All the Agency RMBS in which we invest depend on a steady stream of payments on the mortgages underlying the securities.

As conservator of Fannie Mae and Freddie Mac, the FHFA may disaffirm or repudiate contracts (subject to certain limitations for qualified financial contracts) that Freddie Mac or Fannie Mae entered into prior to the FHFA's appointment as conservator if it determines, in its sole discretion, that performance of the contract is burdensome and that disaffirmation or repudiation of the contract promotes the orderly administration of its affairs. HERA requires the FHFA to exercise its right to disaffirm or repudiate most contracts within a reasonable period of time after its appointment as conservator. Fannie Mae and Freddie Mac have disclosed that the FHFA has disaffirmed certain consulting and other contracts that these entities entered into prior to the FHFA's appointment as conservator. Freddie Mac and Fannie Mae have also disclosed that the FHFA has advised that it does not intend to repudiate any guarantee obligation relating to Fannie Mae and Freddie Mac's mortgage-related securities, because the FHFA views repudiation as incompatible with the goals of the conservatorship. In addition, HERA provides that mortgage loans and mortgage-related assets that have been transferred to a Freddie Mac or Fannie Mae securitization trust must be held for the beneficial owners of the related mortgage-related securities and cannot be used to satisfy the general creditors of Freddie Mac or Fannie Mae.



If the guarantee obligations of Freddie Mac or Fannie Mae were repudiated by the FHFA, payments of principal and/or interest to holders of Agency RMBS issued by Freddie Mac or Fannie Mae would be reduced in the event of borrowers' late payments or failure to pay or a servicer's failure to remit borrower payments to the trust. In that case, trust administration and servicing fees could be paid from mortgage payments prior to distributions to holders of Agency RMBS. Any actual direct compensatory damages owed due to the repudiation of Freddie Mac or Fannie Mae's guarantee obligations may not be sufficient to offset any shortfalls experienced by holders of Agency RMBS. The FHFA also has the right to transfer or sell any asset or liability of Freddie Mac or Fannie Mae, including its guarantee obligation, without any approval, assignment or consent. If the FHFA were to transfer Freddie Mac or Fannie Mae's guarantee obligations to another party, holders of Agency RMBS would have to rely on that party for satisfaction of the guarantee obligation and would be exposed to the credit risk of that party.

Our investments in Non-Agency RMBS and Multi-Family MBS are generally subject to losses.

We acquire Non-Agency RMBS and Multi-Family MBS. In general, losses on a mortgaged property securing a mortgage loan included in a securitization will be borne first by the equity holder of the property, then by a cash reserve fund or letter of credit, if any, then by the holder of a mezzanine loan or B-Note, if any, then by the "first loss" subordinated security holder and then by the holder of a higher-rated security. In the event of default and the exhaustion of any equity support, reserve fund, letter of credit, mezzanine loans or B-Notes, and any classes of securities junior to those in which we invest, we will not be able to recover all of our investment in the securities we purchase. In addition, if the underlying mortgage portfolio has been overvalued by the originator, or if the values subsequently decline, less collateral is available to satisfy interest and principal payments due on the related Non-Agency RMBS or Multi-Family MBS. The prices of lower credit quality securities are generally less sensitive to interest rate changes than more highly rated investments, but more sensitive to adverse economic downturns or individual issuer developments.

To the extent that due diligence is conducted on potential assets, such due diligence may not reveal all of the risks associated with such assets and may not reveal other weaknesses in such assets, which could lead to losses.

Before acquiring certain assets, such as Multi-Family MBS or other mortgage-related assets, our Manager conducts (either directly or using third parties) due diligence. Such due diligence may include (1) an assessment of the strengths and weaknesses of the asset's credit profile, (2) a review of all or merely a subset of the documentation related to the asset, or (3) other reviews that we or our Manager may deem appropriate to conduct. There can be no assurance that we or our Manager will conduct any specific level of due diligence, or that, among other things, the due diligence process will uncover all relevant facts and potential liabilities or that any purchase will be successful, which could result in losses on these assets, which, in turn, could adversely affect our financial condition and results of operations.

Our Manager utilizes analytical models and data in connection with the valuation of certain of our assets, and any incorrect, misleading or incomplete information used in connection therewith would subject us to potential risks.

Given the complexity of certain of our target assets, such as Multi-Family MBS, our Manager must rely heavily on analytical models and information and data supplied by third parties. Models and data are used to value potential target assets, potential credit risks and reserves and also in connection with hedging our acquisitions. Many of the models are based on historical trends. These trends may not be indicative of future results. Furthermore, the assumptions underlying the models may prove to be inaccurate, causing the models to also be incorrect. In the event models and data prove to be incorrect, misleading or incomplete, any decisions made in reliance thereon expose us to potential risks. For example, by relying on incorrect models and data, especially valuation models, our Manager may be induced to buy for us certain target assets at prices that are too high, to sell certain other assets at prices that are too low or to miss favorable opportunities altogether. Similarly, any hedging based on faulty models and data may prove

to be unsuccessful.

Any credit ratings assigned to our investments will be subject to ongoing evaluations and revisions and we cannot assure you that those ratings will not be downgraded.

Some of our investments may be rated by Moody's Investors Service, Fitch Ratings, Standard & Poor's or other rating agencies. Any credit ratings on our investments are subject to ongoing evaluation by credit rating agencies, and we cannot assure you that any such ratings will not be changed or withdrawn by a rating agency in the future if, in its judgment, circumstances warrant. If rating agencies assign a lower-than-expected rating or reduce or withdraw, or indicate that they may reduce or withdraw, their ratings of our investments in the future, the value of these investments could significantly decline, which would adversely affect the value of our investment portfolio and could result in losses upon disposition or the failure of borrowers to satisfy their debt service obligations to us.

The mortgage loans underlying the Non-Agency RMBS that we have acquired will be subject to defaults, foreclosure timeline extension, fraud and residential price depreciation and unfavorable modification of loan principal amount, interest rate and amortization of principal, which could result in losses to us.

Our investments in Non-Agency RMBS and residential mortgage loans underlying the Non-Agency RMBS are subject to the risks of defaults, foreclosure timeline extension, fraud and home price depreciation and unfavorable modification of loan principal amount, interest rate and amortization of principal, which could result in loss to us. The ability of a borrower to repay a mortgage loan secured by a residential property is dependent upon the income or assets of the borrower. A number of factors may impair borrowers' abilities to repay their loans, including:

- adverse changes in national and local economic and market conditions;
- changes in governmental laws and regulations, fiscal policies and zoning ordinances and the related costs of compliance with laws and regulations, fiscal policies and ordinances;
- costs of remediation and liabilities associated with environmental conditions such as indoor mold;
- the potential for uninsured or under-insured property losses;
- acts of God, including earthquakes, floods and other natural disasters, which may result in uninsured losses;
- acts of war or terrorism, including the consequences of terrorist attacks; and
- social unrest and civil disturbances.

In the event of defaults on the residential mortgage loans that underlie our investments in Non-Agency RMBS and the exhaustion of any underlying or any additional credit support, we may not realize our anticipated return on our investments and we may incur a loss on these investments. In addition, our investments in Non-Agency RMBS are backed by residential real property but, in contrast to Agency RMBS, their principal and interest are not guaranteed by a U.S. Government agency or a GSE. The ability of a borrower to repay these loans or other financial assets is dependent upon the income or assets of these borrowers.

The failure of servicers to effectively service the mortgage loans underlying the RMBS in our investment portfolio would adversely affect our business, financial condition, results of operations and our ability to make distributions to our stockholders.

Most securitizations of residential mortgage loans require a servicer to manage collections on each of the underlying loans. Both default frequency and default severity of loans may depend upon the quality of the servicer. If servicers are not vigilant in encouraging borrowers to make their monthly payments, the borrowers may be far less likely to make these payments, which could result in a higher frequency of default. If servicers take longer to liquidate non-performing assets, loss severities may tend to be higher than originally anticipated. The failure of servicers to effectively service the mortgage loans underlying the RMBS in our investment portfolio or any mortgage loans we own could negatively impact the value of our investments and our performance. Servicer quality is of prime importance in the default performance of RMBS. Many servicers have gone out of business in recent years, requiring a transfer of servicing to another servicer. This transfer takes time and loans may become delinquent because of confusion or lack of attention. When servicing is transferred, servicing fees may increase, which may have an adverse effect on the credit support of RMBS held by us. In the case of pools of securitized loans, servicers may be required to advance interest on delinquent loans to the extent the servicer deems those advances recoverable. In the event the servicer does not advance funds, interest may be interrupted even on more senior securities. Servicers may also advance more than is in fact recoverable once a defaulted loan is disposed, and the loss to the trust may be greater than the outstanding principal balance of that loan (greater than 100% loss severity).

We may be affected by deficiencies in foreclosure practices of third parties, as well as related delays in the foreclosure process.

There continues to be uncertainty around the timing and ability of servicers to remove delinquent borrowers from their homes, so that they can liquidate the underlying properties and ultimately pass the liquidation proceeds through to owners of the mortgage loans or related RMBS. Given the magnitude of the housing crisis, and in response to the well-publicized failures of many servicers to follow proper foreclosure procedures (such as “robo-signing”), mortgage servicers are being held to much higher foreclosure-related documentation standards than they previously were. However, because many mortgages have been transferred and assigned multiple times (and by means of varying assignment procedures) throughout the origination, warehouse and securitization processes, mortgage servicers may have difficulty furnishing the requisite documentation to initiate or complete foreclosures. This leads to stalled or suspended foreclosure proceedings, and ultimately additional foreclosure-related costs. Foreclosure-related delays also tend to increase ultimate loan loss severities as a result of property deterioration, amplified legal and other costs, and other factors. Many factors delaying foreclosure, such as borrower lawsuits and judicial backlog and scrutiny, are outside of servicers’ control and have delayed, and will likely continue to delay, foreclosure processing in both judicial states (where foreclosures require court involvement) and non-judicial states. A servicer’s failure to remove delinquent borrowers from their homes in a timely manner could increase our costs, adversely affect the value of the property and mortgage loans and have an adverse effect on our results of operations and business.

Our investments may benefit from private mortgage insurance, but this insurance may not be sufficient to cover losses.

In certain instances, Non-Agency mortgage loans may have private insurance. This insurance is often structured to absorb only a portion of the loss if a loan defaults and, as such, we may be exposed to losses on these loans in excess of the insured portion of the loans. The private mortgage insurance industry has been adversely affected by the housing market decline and this may limit an insurer’s ability to perform on its insurance. Lastly, rescission and denial of mortgage insurance has increased significantly, and this may affect our ability to collect on our insurance. If private mortgage insurers fail to remit insurance payments to us for insured portions of loans when losses are incurred and where applicable, whether due to breach of contract or to an insurer’s insolvency, we may experience a loss for the

amount that was insured by such insurers, though we may maintain claims against the insurers.

We may experience a decline in the market value of our assets.

A decline in the market value of our assets may require us to recognize an “other-than-temporary” impairment against such assets under GAAP if we were to determine that, with respect to any assets in unrealized loss positions, we do not have the ability and intent to hold such assets to maturity or for a period of time sufficient to allow for recovery to the amortized cost of such assets. If such a determination were to be made, we would recognize unrealized losses through earnings and write down the amortized cost of such assets to a new cost basis, based on the fair market value of such assets on the date they are considered to be other-than-temporarily impaired. Such impairment charges reflect non-cash losses at the time of recognition; subsequent disposition or sale of such assets could further affect our future losses or gains, as they are based on the difference between the sale price received and adjusted amortized cost of such assets at the time of sale. If we experience a decline in the fair value of our assets, our business, financial condition, results of operations and our ability to make distributions to our stockholders could be adversely affected.

The allocation of the net proceeds of any equity offering among our target assets, and the timing of the deployment of these proceeds is subject to, among other things, then prevailing market conditions and the availability of target assets.

Our allocation of the net proceeds from any equity offering among our target assets is subject to our investment guidelines and maintenance of our REIT qualification. Our Manager will make determinations as to the percentage of our equity that will be invested in each of our target assets and the timing of the deployment of the net proceeds of our equity offerings. These determinations will depend on then prevailing market conditions and may change over time in response to opportunities available in different interest rate, economic and credit environments. Until appropriate assets can be identified, our Manager may decide to use the net proceeds of our offerings to pay down our short-term debt or to invest the net proceeds in interest-bearing short-term investments, including funds, which are consistent with maintenance of our REIT qualification. These investments are expected to provide a lower net return than we seek to achieve from our target assets. Prior to the time we have fully used the net proceeds of our offerings to acquire our target assets, we may fund our monthly and/or quarterly distributions out of such net proceeds.

Many of our investments are recorded at fair value, and quoted prices or observable inputs may not be available to determine such value, resulting in the use of significant unobservable or subjective judgment inputs to determine value.

We expect that the values of some of our investments may not be readily determinable. We will measure the fair value of these investments quarterly, in accordance with guidance set forth in the Financial Accounting Standards Board Accounting Standards Codification, or ASC, Topic 820, Fair Value Measurements and Disclosures. The fair value at which our assets may be recorded may not be an indication of their realizable value. Ultimate realization of the value of an asset depends to a great extent on economic and other conditions that are beyond the control of our Manager, us or our board of directors. Further, fair value is only an estimate based on good faith judgment of the price at which an investment can be sold since market prices of investments can only be determined by negotiation between a willing buyer and seller. If we were to liquidate a particular asset, the realized value may be more than or less than the amount at which such asset is valued. Accordingly, the value of our equity securities could be adversely affected by our determinations regarding the fair value of our investments, whether in the applicable period or in the future. Additionally, such valuations may fluctuate over short periods of time.

In certain cases, our Manager's determination of the fair value of our investments will include inputs provided by third-party dealers and pricing services. Valuations of certain investments in which we may invest are often difficult to obtain or unreliable. In general, dealers and pricing services heavily disclaim their valuations. Dealers may claim to furnish valuations only as an accommodation and without special compensation, and so they may disclaim any and all liability for any direct, incidental or consequential damages arising out of any inaccuracy or incompleteness in valuations, including any act of negligence or breach of any warranty. Depending on the complexity and illiquidity of a security, valuations of the same security can vary substantially from one dealer or pricing service to another. Therefore, our results of operations for a given period could be adversely affected if our determinations regarding the fair market value of these investments are materially different than the values that we ultimately realize upon their disposal. The valuation process involves a significant degree of management judgment and is particularly challenging during periods of market instability, unpredictability and volatility.

Real estate valuation is inherently subjective and uncertain.

The valuation of real estate and therefore the valuation of any collateral underlying our loans is inherently subjective due to, among other factors, the individual nature of each property, its location, the expected future rental revenues from that particular property and the valuation methodology adopted. As a result, the valuations of the real estate assets against which we will make or acquire loans are subject to a large degree of uncertainty and are made on the basis of assumptions and methodologies that may not prove to be accurate, particularly in periods of volatility, low transaction flow or restricted debt availability in the commercial or residential real estate markets.

Because we acquire fixed-rate securities, an increase in interest rates on our borrowings adversely affects our book value.

Increases in interest rates negatively affect the market value of our assets. Any fixed-rate securities that we invest in generally are more negatively affected by these increases than adjustable-rate securities or loans. In accordance with accounting rules, we are required to reduce our book value by the amount of any decrease in the market value of our assets that are classified for accounting purposes as available-for-sale or for which we have elected the fair value option. Our entire investment portfolio is priced by independent pricing providers or by third-party brokers. If the fair value of a security is not available from a third-party pricing service or dealer, we estimate the fair value of the security using a variety of models and analyses, taking into consideration aggregate characteristics including, but not limited to, type of collateral, index, margin, periodic interest rate caps, lifetime interest rate caps, underwriting standards, age and delinquency experience. However, the fair value reflects estimates and may not be indicative of the amounts we would receive in a current market exchange. If we determine that a security is other-than-temporarily impaired, we would be required to reduce the value of such security on our balance sheet by recording an impairment charge in our income statement and our stockholders' equity would be correspondingly reduced. Reductions in stockholders' equity decrease the amounts that we may borrow to purchase additional assets, which could restrict our ability to increase our net income.

An increase in interest rates may cause a decrease in the volume of certain of our assets, which could adversely affect our ability to acquire assets that satisfy our investment objectives and to generate income and make distributions to our stockholders.

Rising interest rates generally reduce the demand for mortgage loans due to the higher cost of borrowing. A reduction in the volume of mortgage loans originated may affect the volume of RMBS, Multi-Family MBS, MSRs and other mortgage related investments available to us, which could adversely affect our ability to acquire assets that satisfy our investment objectives. Rising interest rates may also cause our assets that were issued prior to an interest rate increase to provide yields that are below prevailing market interest rates. If rising interest rates cause us to be unable to acquire a sufficient volume of RMBS, Multi-Family MBS, MSRs and other mortgage related investments with a yield that is

above our borrowing cost, our ability to satisfy our investment objectives and to generate income and make distributions to our stockholders may be adversely affected.

The relationship between short-term and longer-term interest rates is often referred to as the “yield curve.” Ordinarily, short-term interest rates are lower than longer-term interest rates. If short-term interest rates rise disproportionately relative to longer-term interest rates (a flattening of the yield curve), our borrowing costs may increase more rapidly than the interest income earned on our assets. Because we expect our investments, on average, generally will bear interest based on longer-term rates than our borrowings, a flattening of the yield curve would tend to decrease our net income and the market value of our net assets. Additionally, to the extent cash flows from investments that return scheduled and unscheduled principal are reinvested, the spread between the yields on the new investments and available borrowing rates may decline, which would likely decrease our net income. It is also possible that short-term interest rates may exceed longer-term interest rates (a yield curve inversion), in which event our borrowing costs may exceed our interest income and we could incur operating losses. Given the volatile nature of the U.S. economy since the end of the third round of quantitative easing, or QE3, and the Fed’s recent increase in short-term interest rates, there can be no guarantee that the yield curve will not become and/or remain inverted.

Increases in interest rates typically adversely affect the value of our investments and cause our interest expense to increase, which could result in reduced earnings or losses and negatively affect our profitability as well as the cash available for distribution to our stockholders.

We invest in RMBS, Multi-Family MBS, MSRs and other mortgage related investments. In a normal yield curve environment, an investment in the fixed-rate component of such assets will generally decline in value if future long-term interest rates increase. Declines in market value may ultimately reduce earnings or result in losses to us, which may negatively affect cash available for distribution to our stockholders.

A significant risk associated with RMBS, Multi-Family MBS, MSRs and other mortgage related investments is the risk that both long-term and short-term interest rates will increase significantly. If long-term rates increased significantly, the market value of these investments would decline, and the duration and weighted average life of the investments would increase. We could realize a loss if the securities were sold. At the same time, an increase in short-term interest rates would increase the amount of interest owed on any repurchase agreements we may enter into.

Market values of our investments may decline without any general increase in interest rates for a number of reasons, such as increases or expected increases in defaults, or increases or expected increases in voluntary prepayments for those investments that are subject to prepayment risk or widening of credit spreads.

In addition, in a period of rising interest rates, our operating results will depend in large part on the difference between the income from our assets and our financing costs. We anticipate that, in most cases, the income from such assets will respond more slowly to interest rate fluctuations than the cost of our borrowings. Consequently, changes in interest rates, particularly short-term interest rates, may significantly influence our net income. Increases in these rates will tend to decrease our net income and market value of our assets.

Interest rate mismatches between our RMBS backed by ARMs or hybrid ARMs and our borrowings used to fund our purchases of these assets may cause us to suffer losses.



We may fund our RMBS with borrowings that have interest rates that adjust more frequently than the interest rate indices and repricing terms of RMBS backed by ARMs or hybrid ARMs. Accordingly, if short-term interest rates increase, our borrowing costs may increase faster than the interest rates on RMBS backed by ARMs or hybrid ARMs adjust. As a result, in a period of rising interest rates, we could experience a decrease in net income or a net loss.

In most cases, the interest rate indices and repricing terms of RMBS backed by ARMs or hybrid ARMs and our borrowings will not be identical, thereby potentially creating an interest rate mismatch between our investments and our borrowings. While the historical spread between relevant short-term interest rate indices has been relatively stable, there have been periods when the spread between these indices was volatile. During periods of changing interest rates, these interest rate index mismatches could reduce our net income or produce a net loss and adversely affect the level of our distributions to our stockholders and the market price of our equity securities.

In addition, RMBS backed by ARMs or hybrid ARMs will typically be subject to lifetime interest rate caps that limit the amount an interest rate can increase through the maturity of the RMBS. However, our borrowings under repurchase agreements typically will not be subject to similar restrictions. Accordingly, in a period of rapidly increasing interest rates, the interest rates paid on our borrowings could increase without limitation while caps could limit the interest rates on these types of RMBS. This problem is magnified for RMBS backed by ARMs or hybrid ARMs that are not fully indexed. Further, some RMBS backed by ARMs or hybrid ARMs may be subject to periodic payment caps that result in a portion of the interest being deferred and added to the principal outstanding. As a result, we may receive less cash income on these types of RMBS than we need to pay interest on our related borrowings. These factors could reduce our net interest income and cause us to suffer a loss during periods of rising interest rates.

Interest rate fluctuations may adversely affect our business, financial condition, results of operations and our ability to make distributions to our stockholders.

Interest rates are highly sensitive to many factors, including governmental, monetary and tax policies, domestic and international economic and political considerations and other factors beyond our control. Our success will depend on our ability to analyze the relationship changing interest rates may have on our financial position and results of operations in general and the impact such rate changes may have on critical elements underlying our target assets and borrowings. In particular,

Changes in interest rates typically inversely affect the fair value of our target assets, which consist of primarily RMBS, Multi-Family MBS, residential mortgage loans, MSRs and other mortgage related investments. When interest rates rise, the value of our fixed-rate target assets generally decline, and when interest rates fall, the value of our fixed-rate target assets generally increase.

Changes in interest rates may inversely affect prepayment speeds. Typically, as interest rates rise, prepayments on the underlying mortgages tend to slow; conversely, as interest rates fall, prepayments on the underlying mortgages tend to accelerate. The effect that rising or falling interest rates has on these prepayments affects the price of our target assets, and the effect can be particularly pronounced with fixed-rate Agency RMBS.

Changes in interest rates may create mismatches between our target assets, which will consist primarily of Agency RMBS, Non-Agency RMBS, Multi-Family MBS, residential mortgage loans and other mortgage-related investments, and our borrowings used to fund our purchases of those assets. The risk of these mismatches may be pronounced in that, should interest rates increase, interest rate caps on our hybrid ARMs and adjustable rate RMBS would limit the income stream on those investments while our borrowing would not be subject to similar restrictions.

In accordance with accounting rules, we are required to reduce our stockholders' equity, or book value, by the amount of any decrease in the market value of our securities that are classified for accounting purposes as available-for-sale.

We are required to evaluate our securities on a quarterly basis to determine their fair value by using third-party bid price indications provided by dealers who make markets in these securities or by third-party pricing services. If the fair value of a security is not available from a dealer or third-party pricing service, we will estimate the fair value of

the security using a variety of methods including, but not limited to, discounted cash flow analysis, matrix pricing, option-adjusted spread models and fundamental analysis. Aggregate characteristics taken into consideration include, but are not limited to, type of collateral, index, margin, periodic cap, lifetime cap, underwriting standards, age and delinquency experience. However, the fair value reflects estimates and may not be indicative of the amounts we would receive in a current market sale transaction. If we determine that a security is other-than-temporarily impaired, we are required to reduce the value of such security on our balance sheet by recording an impairment charge in our income statement, and our stockholders' equity is correspondingly reduced. Reductions in stockholders' equity decrease the amounts we may borrow to purchase additional securities, which could restrict our ability to implement our investment strategy, which could adversely affect our business, financial condition, results of operations and our ability to make distributions to our stockholders. In addition, rising interest rates generally reduce the demand for consumer credit, including mortgage loans, due to the higher cost of borrowing. A reduction in the volume of mortgage loans originated may affect the volume of RMBS available to us, which could affect our ability to acquire assets that satisfy our investment objectives.

Changes in prepayment rates may adversely affect our profitability.

The RMBS assets we acquire are backed by pools of residential mortgage loans. We also invest in residential mortgage loans. We receive payments, generally, from the payments that are made on these underlying residential mortgage loans. When residential mortgage loans are prepaid (including by way of voluntary prepayments by borrowers, loan buyouts and liquidations due to defaults and foreclosures) at rates that are faster than expected, this results in prepayments that are faster than expected on the related RMBS. These faster than expected payments may adversely affect our profitability. In addition, a decrease in prepayment rates may adversely affect our results of operations. When residential mortgage loans are prepaid at slower than expected rates, prepayments on the RMBS may be slower than expected. These slower than expected payments may adversely affect our profitability.

We purchase RMBS assets, and purchase residential mortgage loans, that have a higher interest rate than the then prevailing market interest rate. In exchange for this higher interest rate, we may pay a premium to par value to acquire the asset. In accordance with GAAP, we amortize this premium over the expected term of the asset based on our prepayment assumptions or its contractual terms, depending on the type of asset. If the asset is prepaid in whole or in part at a faster than expected rate or contractual term (as applicable), however, we must expense all or a part of the remaining unamortized portion of the premium that was paid at the time of the purchase, which will adversely affect our profitability.

We also purchase RMBS assets or residential mortgage loans that have a lower interest rate than the then prevailing market interest rate. In exchange for this lower interest rate, we may pay a discount to par value to acquire the asset. In accordance with GAAP, we accrete this discount over the expected term of the asset based on our prepayment assumptions or its contractual terms. If the asset is prepaid at a slower than expected rate, however, we must accrete the remaining portion of the discount at a slower than expected rate. This will extend the expected life of the asset and result in a lower than expected yield on assets purchased at a discount to par.

Prepayment rates generally increase when interest rates fall and decrease when interest rates rise, but changes in prepayment rates are difficult to predict. Prepayments can also occur when borrowers default on their residential mortgages and the mortgages are prepaid from the proceeds of a foreclosure sale of the property, or when borrowers sell the property and use the sale proceeds to prepay the mortgage as part of a physical relocation. Prepayment rates also may be affected by conditions in the housing and financial markets, general economic conditions and the relative interest rates on fixed-rate mortgages and ARMs and increasing defaults on residential mortgage loans, which could lead to an acceleration of the payment of the related principal. While we will seek to manage prepayment risk, in selecting RMBS investments we must balance prepayment risk against other risks, the potential returns of each investment and the cost of hedging our risks. No strategy can completely insulate us from prepayment or other such risks, and we may deliberately retain exposure to prepayment or other risks.

Changing market conditions may upset the historical relationship between interest rate changes and prepayment trends, which would make it more difficult for us to analyze our portfolio.

Our success will depend on our ability to analyze the relationship of changing interest rates and prepayments of the mortgages that underlie our target assets. Changes in interest rates and prepayments will affect the market price of the target assets that we purchase and any target assets that we hold at a given time. As part of our overall portfolio risk management, we analyze interest rate changes and prepayment trends separately and collectively to assess their effects on our portfolio. In conducting our analysis, we depend on industry-accepted assumptions with respect to the relationship between interest rates and prepayments under normal market conditions. If the dislocation in the residential mortgage market or other developments change the way that prepayment trends have historically responded to interest rate changes, our ability to assess the market value of our portfolio would be significantly affected and could adversely affect our financial position and results of operations.

We are highly dependent on communications and information systems and systems failures could significantly disrupt our operations, which may, in turn, negatively affect the market price of our equity securities and our ability to make distributions.

Our business is highly dependent on the communications and information systems of our Manager that allow it to monitor, value, buy, sell, finance and hedge our investments. Any failure or interruption of our Manager's systems could cause delays or other problems in our securities trading activities, which could have a material adverse effect on our operating results and negatively affect the market price of our equity securities and our ability to make distributions.

The occurrence of cyber-incidents, or a deficiency in our Manager's cybersecurity or in those of any of our third party service providers, could negatively impact our business by causing a disruption to our operations, a compromise of our confidential information or damage to our business relationships or reputation, all of which could negatively impact our business and results of operations.

A cyber-incident is considered to be any adverse event that threatens the confidentiality, integrity or availability of our or Manager's information resources or those of our third party service providers. A cyber-incident can be an intentional attack or an unintentional event and can include gaining unauthorized access to a system to disrupt operations, corrupt data or steal confidential information. The primary risks that could directly result from a cyber-incident include operational interruption and private data exposure. Our Manager has implemented processes, procedures and controls to help mitigate these risks, but these measures, as well as our increased awareness of the risk of a cyber-incident, do not guarantee that our business and results of operations will not be negatively impacted by such an incident.

Rapid changes in the values of our real estate-related assets may make it more difficult for us to maintain our qualification as a REIT or exclusion from registration under the Investment Company Act.

If the market value or income potential of our real estate-related assets declines as a result (i) of increased interest rates, prepayment rates or other factors; or (ii) we determine based on subsequently available guidance from the SEC or SEC staff that our treatment as qualified interests in real estate of certain subordinated certificates we acquire (a) in the secondary market issued by K-Series trusts, or (b) from securitization trusts into which we sell residential mortgage loans, is no longer correct; we may need to increase certain real estate investments and income and/or liquidate our non-qualifying assets in order to maintain our REIT qualification or exclusion from registration under the Investment Company Act. If the decline in real estate asset values and/or income occurs quickly, this may be especially difficult to accomplish. This difficulty may be exacerbated by the illiquid nature of our investments. We may have to make investment decisions that we otherwise would not make absent our REIT and Investment Company Act considerations.

Any downgrades, or perceived potential of downgrades, of the credit ratings of the U.S. Government, GSEs or certain European countries may adversely affect our business, financial condition, results of operations and our ability to make distributions to our stockholders.

On August 5, 2011, Standard & Poor's downgraded the U.S. Government's credit rating for the first time in history, and on October 15, 2013, Fitch Ratings placed the ratings of all outstanding U.S. sovereign debt securities on Rating Watch Negative. Because Fannie Mae and Freddie Mac are in conservatorship of the U.S. Government, downgrades to the U.S. Government's credit rating could impact the credit risk associated with our target assets and, therefore, decrease the value of the target assets in our portfolio. In addition, downgrades of the credit ratings of the U.S. Government, GSEs and certain European countries could create broader financial turmoil and uncertainty, which could weigh heavily on the global banking system. Therefore, any downgrades of the credit ratings of the U.S. Government, GSEs or certain European countries may adversely affect the value of our target assets and our business, financial condition, results of operations and our ability to make distributions to our stockholders.

#### Risks Related to Financing and Hedging

Our strategy involves significant leverage, which may amplify losses; while we currently expect to incur approximately one to three times leverage on our New Issue Non-Agency RMBS, approximately one to four times leverage on our Multi-Family MBS, approximately one to two times leverage on our Legacy Non-Agency RMBS and approximately six to nine times leverage on our Agency RMBS there is no specific limit on the amount of leverage that we may use.

We leverage our portfolio investments in our target assets principally through borrowings under repurchase agreements. Our leverage (on both a GAAP and non-GAAP basis) currently ranges, and we expect that it will continue to range, between three and six times the amount of our stockholders' equity. Additionally, we currently borrow, and expect that we will continue to borrow, between one to three times when acquiring New Issue Non-Agency RMBS, between one to four times when acquiring Multi-Family MBS, between one and two times when acquiring Legacy Non-Agency RMBS and between six to nine times the amount of our stockholders' equity in acquiring Agency RMBS. The leverage our Manager is comfortable applying to each asset class at any point in time is a function of the yield profile across housing environments and also a function of price or market values in environments of excessive volatility, which cannot be ruled out. We

will incur this leverage by borrowing against a substantial portion of the market value of our assets. Our leverage, which is fundamental to our investment strategy, creates significant risks.

To the extent that we incur significant leverage, we may incur substantial losses if our borrowing costs increase. Our borrowing costs may increase for any of the following, or other, reasons:

- short-term interest rates increase;
- the market value of our securities decreases;
- interest rate volatility increases; or
- the availability of financing in the market decreases.

Our return on our investments and cash available for distributions may be reduced if market conditions cause the cost of our financing to increase relative to the income that can be derived from the assets acquired, which could adversely affect the price of our equity securities. In addition, our debt service payments will reduce cash flow available for distributions to stockholders. In addition, if the cost of our financing increases, we may not be able to meet our debt service obligations. To the extent that we cannot meet our debt service obligations, we risk the loss of some or all of our assets to satisfy our debt obligations. To the extent we are compelled to liquidate qualified REIT assets to repay debts, our compliance with the REIT rules regarding our assets and our sources of income could be negatively affected, which would jeopardize our qualification as a REIT. Losing our REIT status would cause us to lose tax advantages applicable to REITs and would decrease our overall profitability and distributions to our stockholders.

We may continue to incur significant additional debt in the future, which will subject us to increased risk of loss and may reduce cash available for distributions to our stockholders.

Subject to market conditions and availability, we may continue to incur significant additional debt in the future. Although we are not required to maintain any particular assets-to-equity leverage ratio, the amount of leverage we may deploy for particular assets will depend upon our Manager's assessment of the credit and other risks of those assets. Our board of directors may establish and change our leverage policy at any time without stockholder approval. Incurring debt could subject us to many risks that, if realized, would adversely affect us, including the risk that:

- our cash flow from operations may be insufficient to make required payments of principal of and interest on the debt or we may fail to comply with all of the other covenants contained in the debt, which is likely to result in (1) acceleration of such debt (and any other debt containing a cross-default or cross-acceleration provision) that we may be unable to repay from internal funds or to refinance on favorable terms, or at all, (2) our inability to borrow unused amounts under our financing arrangements, even if we are current in payments on borrowings under those arrangements, and/or (3) the loss of some or all of our assets to foreclosure or sale;
- our debt may increase our vulnerability to adverse economic and industry conditions with no assurance that investment yields will increase with higher financing costs;
- we may be required to dedicate a substantial portion of our cash flow from operations to payments on our debt, thereby reducing funds available for operations, investments, stockholder distributions or other purposes; and
- we may not be able to refinance debt that matures prior to the investment it was used to finance on favorable terms or at all.

There can be no assurance that our Manager will be able to prevent mismatches in the maturities of our assets and liabilities.

Because we employ financial leverage in funding our portfolio, mismatches in the maturities of our assets and liabilities can create risk in the need to continually renew or otherwise refinance our liabilities. Our net interest margins will be dependent upon a positive spread between the returns on our asset portfolio and our overall cost of funding. Our Manager's risk management tools include software and services licensed or purchased from third parties,

in addition to proprietary systems and analytical methods developed internally. There can be no assurance that these tools and the other risk management techniques described above will protect us from asset/liability risks.

We are subject to margin calls under our master repurchase agreements, which could result in defaults or force us to sell assets under adverse market conditions or through foreclosure.

We enter into master repurchase agreements with various financial institutions and borrow under these master repurchase agreements to finance the acquisition of assets for our investment portfolio. Pursuant to the terms of borrowings under our master repurchase agreements, a decline in the value of the subject assets typically results in our lenders initiating margin calls. A margin call means that the lender requires us to pledge additional collateral to re-establish the ratio of the value of the collateral to the amount of the borrowing. The specific collateral value to borrowing ratio that would trigger a margin call is not set in the master repurchase agreements and will not be determined until we engage in a repurchase transaction under these agreements. Our fixed-rate securities generally are more susceptible to margin calls as increases in interest rates tend to more negatively affect the market value of fixed-rate securities. If we are unable to satisfy margin calls, our lenders may foreclose on our collateral. The threat of or occurrence of a margin call could force us to sell our assets, either directly or through a foreclosure, under adverse market conditions. Because of the significant leverage we have, we may incur substantial losses upon the threat or occurrence of a margin call.

If a counterparty to our repurchase transactions defaults on its obligation to resell the underlying security back to us at the end of the transaction term, or if the value of the underlying security has declined as of the end of that term, or if we default on our obligations under the repurchase agreement, we will lose money on our repurchase transactions.

When we engage in repurchase transactions, we generally sell securities to lenders (repurchase agreement counterparties) and receive cash from these lenders. The lenders are obligated to resell the same securities back to us at the end of the term of the transaction. Because the cash we receive from the lender when we initially sell the securities to the lender is less than the value of those securities (this difference is the haircut), if the lender defaults on its obligation to resell the same securities back to us we may incur a loss on the transaction equal to the amount of the haircut (assuming there was no change in the value of the securities). We would also lose money on a repurchase transaction if the value of the underlying securities has declined as of the end of the transaction term, as we would have to repurchase the securities for their initial value but would receive securities worth less than that amount. Further, if we default on one of our obligations under a repurchase transaction, the lender can terminate all of the outstanding repurchase transactions with us and can cease entering into any other repurchase transactions with us. Our repurchase agreements contain cross-default provisions, so that if a default occurs under any one agreement, the lenders under our other

agreements could also declare a default. Any losses we incur on our repurchase transactions could adversely affect our earnings and thus our cash available for distribution to our stockholders.

Our use of derivative instruments and repurchase agreements may expose us to counterparty risk.

We enter into transactions to mitigate interest rate risks associated with our business with counterparties that have a high-quality credit rating or in the assessment of our management team represent an acceptable counterparty risk. If counterparties cannot perform under the terms of our futures contracts, for example, we would not receive payments due under those contracts, and may lose any unrealized gain associated with such contracts, and the mitigated liability would cease to be mitigated by such contracts. We may also be at risk for any collateral we have pledged to secure our obligations under a futures contract if the counterparty became insolvent or filed for bankruptcy. Similarly, if an interest rate cap agreement counterparty fails to perform under the terms of the interest rate cap agreement, in addition to not receiving payments due under that agreement that would offset our interest expense, we would also incur a loss for all remaining unamortized premium paid for that agreement. Our derivative instrument agreements require our counterparties to post collateral in certain events, generally related to their credit condition, to provide us some protection against their potential failure to perform. We, in turn, are subject to similar requirements. In addition, we enter into repurchase agreements to finance our target assets with certain counterparties. A failure or insolvency of any of these counterparties under such agreements could result in a loss of our collateral pledged to the counterparty or a loss of the securities that have not yet been repurchased from such counterparty, which, in either case, could adversely affect our business, financial condition, results of operations and our ability to make distributions to our stockholders.

Failure to procure adequate repurchase agreement financings, which generally have short terms, or to renew or replace such financing as it matures, would adversely affect our results of operations.

We use repurchase agreements as a strategy to increase the return on our investment portfolio. However, we may not be able to achieve our desired leverage ratio for a number of reasons, including if the following events occur:

- our lenders do not make repurchase agreement financing available to us at acceptable rates;
- certain of our lenders exit the repurchase market;
- our lenders require that we pledge additional collateral to cover our borrowings, which we may be unable to do; or
- we determine that the leverage would expose us to excessive risk.

Indeed, our access to financing depends on a number of factors over which we have no or little control, including:

- general market conditions;
- the lender's view of the quality of our assets;
- the lender's perception of the credit risk of the Company;
- our current and potential earnings and cash distributions; and
- the market prices for shares of our common stock.

We cannot assure you that any, or sufficient, repurchase agreement financing will continue to be available to us on terms that are acceptable to us. In recent years, investors and financial institutions that lend in the securities repurchase market have tightened lending standards in response to the difficulties and changed economic conditions that have adversely affected the RMBS and mortgage market. These market disruptions have been pronounced in the Non-Agency RMBS market and loan market, and the impact has also extended to Agency RMBS, which has made the value of these assets unstable and relatively illiquid compared to prior periods. Any decline in their value, or perceived market uncertainty about their value, would make it more difficult for us to obtain financing on favorable terms, or at all, or maintain our compliance with terms of any financing arrangements then in place. Additionally, the lenders from which we may seek to obtain repurchase agreement financing may have owned or financed RMBS that

have declined in value and caused the lender to suffer losses. If these conditions persist, these institutions may be forced to exit the repurchase market, become insolvent or further tighten lending standards or increase the amount of equity capital or haircut required to obtain financing, and in such event, could make it more difficult for us to obtain financing on favorable terms or at all. In the event that we cannot obtain sufficient funding on acceptable terms, there may be a negative impact on the value of our equity securities and our ability to make distributions, and you may lose part or all of your investment.

In addition, in response to certain interest rate and investment environments or to changes in market liquidity, we could adopt a strategy of reducing our leverage by selling assets or not reinvesting principal payments as RMBS amortize or prepay, thereby decreasing the outstanding amount of our related borrowings. Such a strategy could reduce interest income, interest expense and net income, the extent of which would be dependent on the level of reduction in assets and liabilities, as well as the sale prices for which the assets were sold.

While the overall financing environment has remained relatively stable over the last 12 months, further credit losses or mergers, acquisitions or bankruptcies of investment banks and commercial banks that have historically acted as repurchase agreement counterparties may occur. This would result in a fewer number of potential repurchase agreement counterparties operating in the market and could potentially impact the pricing and availability of financing for our business.

Furthermore, because we rely primarily on short-term borrowings, our ability to achieve our investment objective will depend not only on our ability to borrow money in sufficient amounts and on favorable terms, but also on our ability to renew or replace on a continuous basis our maturing short-term borrowings. If we are not able to renew or replace maturing borrowings, we will have to sell some or all of our assets, possibly under adverse market conditions. In addition, if the regulatory capital requirements imposed on our lenders change, as they are expected to under the Basel III standards adopted by the Basel Committee on Banking Supervision, they may be required to significantly increase the cost of the financing that they provide to us. Our lenders also may revise their eligibility requirements for the types of assets they are willing to finance or the terms of such financings, based on, among other factors, the regulatory environment and their management of perceived risk, particularly with respect to assignee liability.

Our repurchase agreement financing may require us to provide additional collateral and may restrict us from leveraging our assets as fully as desired.

We use repurchase agreements to finance acquisitions of RMBS, Multi-Family MBS, MSRs and other mortgage related investments. If the market value of the asset pledged or sold by us to a financing institution pursuant to a repurchase agreement declines, we may be required by the financing institution to provide additional collateral or pay down a portion of the funds advanced, but we may not have the funds available to do so, which could result in defaults. Posting additional collateral to support our credit will reduce our liquidity and limit our ability to leverage our assets, which could adversely affect our business. In the event we do not have sufficient liquidity to meet such requirements, financing institutions can accelerate repayment of our indebtedness, increase interest rates,



liquidate our collateral or terminate our ability to borrow. Such a situation would likely result in a rapid deterioration of our financial condition and possibly necessitate a filing for bankruptcy protection.

Further, financial institutions providing the repurchase facilities may require us to maintain a certain amount of cash uninvested or to set aside non-levered assets sufficient to maintain a specified liquidity position which would allow us to satisfy our collateral obligations. As a result, we may not be able to leverage our assets as fully as we would choose, which could reduce our return on equity. If we are unable to meet these collateral obligations, our financial condition could deteriorate rapidly.

Lenders generally require us to enter into restrictive covenants relating to our operations.

When we obtain financing, lenders typically impose restrictions on us that would affect our ability to incur additional debt, our capability to make distributions to stockholders and our flexibility to determine our operating policies. Loan documents we execute may contain negative covenants that limit, among other things, our ability to repurchase stock, distribute more than a certain amount of our funds from operations and employ leverage beyond certain amounts.

Our inability to meet certain financial covenants related to our repurchase agreements could adversely affect our business, financial condition and results.

In connection with certain of our repurchase agreements, we are required to maintain certain financial covenants with respect to our net worth, the most restrictive of which requires that, on the last day of any fiscal quarter, our total stockholders' equity shall not be less than the greater of (1) \$75,000,000 or (2) 50% of the highest stockholders' equity on the last day of the preceding eight fiscal quarters. Compliance with these financial covenants will depend on market factors and the strength of our business and operating results. Various risks, uncertainties and events beyond our control could affect our ability to comply with our financial covenants. Failure to comply with our financial covenants could result in an event of default, termination of the repurchase facility and acceleration of all amounts owing under the repurchase facility and gives the counterparty the right to exercise certain other remedies under the repurchase agreement, including the sale of the asset subject to repurchase at the time of default, unless we were able to negotiate a waiver. Any such waiver could be conditioned on an amendment to the repurchase facility and any related guaranty agreement on terms that may be unfavorable to us. If we are unable to negotiate a covenant waiver or replace or refinance our assets under a new repurchase facility on favorable terms or at all, our financial condition, results of operations and cash flows could be adversely affected.

Our rights under repurchase agreements may be subject to the effects of the bankruptcy laws in the event of the bankruptcy or insolvency of us or our counterparties under the repurchase agreements.

In the event of our insolvency or bankruptcy, certain repurchase agreements may qualify for special treatment under Title 11 of the United States Code, as amended, or the U.S. Bankruptcy Code, the effect of which, among other things, would be to allow the lender under the applicable repurchase agreement to avoid the automatic stay provisions of the U.S. Bankruptcy Code and to take possession of and liquidate the assets that we have pledged under their repurchase agreements. In the event of the insolvency or bankruptcy of a lender during the term of a repurchase agreement, the lender may be permitted, under applicable insolvency laws, to repudiate the contract, and our claim against the lender for damages may be treated simply as an unsecured creditor. In addition, if the lender is a broker or dealer subject to the Securities Investor Protection Act of 1970, or an insured depository institution subject to the Federal Deposit Insurance Act, our ability to exercise our rights to recover our securities under a repurchase agreement or to be compensated for any damages resulting from the lender's insolvency may be further limited by those statutes. These claims would be subject to significant delay and, if and when received, may be substantially less than the damages we actually incur.

An increase in our borrowing costs relative to the interest that we receive on investments in RMBS, Multi-Family MBS, MSRs and other mortgage related investments may adversely affect our profitability and cash available for distribution to our stockholders.

As our financings mature, we will be required either to enter into new borrowings or to sell certain of our investments. An increase in short-term interest rates at the time that we seek to enter into new borrowings would reduce the spread between our returns on our assets and the cost of our borrowings. This would adversely affect our returns on our assets, which might reduce earnings and, in turn, cash available for distribution to our stockholders.

If a counterparty to one of our swap agreements or TBAs defaults on its obligations, we may incur losses.

If a counterparty to one of the swap agreements or TBAs that we enter into defaults on its obligations under the agreement, we may not receive payments due under the agreement, and thus, we may lose any unrealized gain associated with the agreement. If any such swap agreement hedged a liability, such liability could cease to be hedged upon the default of a counterparty. Additionally, we may also risk the loss of any collateral we have pledged to secure our obligations under a swap agreement if the counterparty becomes insolvent or files for bankruptcy.

Clearing facilities or exchanges upon which some of our hedging instruments are traded may increase margin requirements on our hedging instruments in the event of adverse economic developments.

In response to events having or expected to have adverse economic consequences or which create market uncertainty, clearing facilities or exchanges upon which some of our hedging instruments are traded may require us to post additional collateral against our hedging instruments. For example, in response to the U.S. approaching its debt ceiling without resolution and the federal government shutdown in October 2013, the Chicago Mercantile Exchange announced that it would increase margin requirements by 12% for all over-the-counter interest rate swap portfolios that its clearinghouse guaranteed. This increase was subsequently rolled back shortly thereafter upon the news that Congress passed legislation to temporarily suspend the national debt ceiling, reopened the federal government, and provided a time period for broader negotiations concerning federal budgetary issues. In the event that future adverse economic developments or market uncertainty (including those due to governmental, regulatory, or legislative action or inaction) result in increased margin requirements for our hedging instruments, it could adversely affect our liquidity position, business, financial condition and results of operations.

We enter into hedging transactions that expose us to contingent liabilities in the future, which may adversely affect our financial results or cash available for distribution to stockholders.

We engage in hedging transactions intended to hedge various risks to our portfolio, including the exposure to adverse changes in interest rates. Our hedging activity varies in scope based on, among other things, the level and volatility of interest rates, the type of assets held and other changing market conditions. Although these transactions are intended to reduce our exposure to various risks, hedging may fail to protect or could adversely affect us because, among other things:

- hedging can be expensive, particularly during periods of volatile or rapidly changing interest rates;
- available hedges may not correspond directly with the risks for which protection is sought;
- the duration of the hedge may not match the duration of the related liability;
- the amount of income that a REIT may earn from certain hedging transactions is limited by U.S. federal income tax provisions governing REITs;
- the credit quality of a hedging counterparty may be downgraded to such an extent that it impairs our ability to sell or assign our side of the hedging transaction; and
- the hedging counterparty may default on its obligation to pay.

Subject to maintaining our qualification as a REIT, there are no current limitations on the hedging transactions that we may undertake. However, our Manager's reliance on the CFTC's December 7, 2012 no action letter relieving CPOs of mortgage REITs from the obligation to register with the CFTC as CPOs depends on the satisfaction of several conditions, including that we comply with additional limitations on our hedging activity. The letter limits the initial margin and premiums required to establish our Manager's commodity interest positions to no more than 5% of the fair market value of our total assets and limits the net income derived annually from our commodity interest positions that are not qualifying hedging transactions to less than 5% of our gross income.

Therefore, our and our Manager's reliance on this no action letter places additional restrictions on our hedging activity. Our hedging transactions could require us to fund large cash payments in certain circumstances (e.g., the early termination of the hedging instrument caused by an event of default or other early termination event or a demand by a counterparty that we make increased margin payments). Our ability to fund these obligations will depend on the liquidity of our assets and access to capital at the time. The need to fund these obligations could adversely affect our financial condition. Further, hedging transactions, which are intended to limit losses, may actually result in losses, which would adversely affect our earnings and could in turn reduce cash available for distribution to stockholders.

Hedging instruments involve various kinds of risk because they are not always traded on regulated exchanges, guaranteed by an exchange or its clearinghouse or regulated by any U.S. or foreign governmental authorities. The CFTC is still in the process of proposing rules under the Dodd-Frank Act that may make our hedging more difficult or increase our costs. Furthermore, the enforceability of agreements underlying hedging transactions may depend on compliance with applicable statutory and commodity and other regulatory requirements and, depending on the identity of the counterparty, applicable international requirements. The business failure of a hedging counterparty will most likely result in its default. Default by a hedging counterparty may result in the loss of unrealized profits and force us to cover our commitments, if any, at the then current market price. Although we generally seek to reserve the right to terminate our hedging positions, it may not always be possible to dispose of or close out a hedging position without the consent of the hedging counterparty, and we may not be able to enter into an offsetting contract in order to cover our risk. We cannot assure you that a liquid secondary market will exist for hedging instruments purchased or sold, and we may be required to maintain a position until exercise or expiration, which could result in losses.

Hedging against interest rate exposure may adversely affect our earnings, which could reduce our cash available for distribution to our stockholders, and such transactions may fail to protect us from the losses that they were designed to offset.

Subject to maintaining our qualification as a REIT and exemption from registration under the Investment Company Act, we employ techniques that limit the adverse effects of rising interest rates on a portion of our short-term repurchase agreements and on a portion of the value of our assets. In general, our interest rate risk mitigation strategy depends on our view of our entire portfolio, consisting of assets, liabilities and derivative instruments, in light of prevailing market conditions. We could misjudge the condition of our portfolio or the market. Our interest rate risk mitigation activity varies in scope based on the level and volatility of interest rates and principal repayments, the type of securities held and other changing market conditions. Our actual interest rate risk mitigation decisions are

determined in light of the facts and circumstances existing at the time and may differ from our currently anticipated strategy. These techniques may include purchasing or selling futures contracts, entering into interest rate swap, interest rate cap or interest rate floor agreements, swaptions, purchasing put and call options on securities or securities underlying futures contracts, or entering into forward rate agreements.

Because a mortgage borrower typically has no restrictions on when a loan may be paid off either partially or in full, there are no perfect interest rate risk mitigation strategies, and interest rate risk mitigation may fail to protect us from loss. Alternatively, we may fail to properly assess a risk to our portfolio or may fail to recognize a risk entirely leaving us exposed to losses without the benefit of any offsetting interest rate mitigation activities. The derivative instruments we select may not have the effect of reducing our interest rate risk. The nature and timing of interest rate risk mitigation transactions may influence the effectiveness of these strategies. Poorly designed strategies or improperly executed transactions could actually increase our risk and losses. In addition, interest rate risk mitigation activities could result in losses if the event against which we mitigate does not occur.

Changes in regulations relating to swaps activities may cause us to limit our swaps activity or subject us to additional disclosure, recordkeeping, and other regulatory requirements.

The enforceability of agreements underlying hedging transactions may depend on compliance with applicable statutory and commodity and other regulatory requirements and, depending on the identity of the counterparty, applicable international requirements. Updated regulations have been promulgated by U.S. and foreign regulators to strengthen oversight of derivative contracts. Any actions taken by regulators could constrain our strategy and could increase our costs, either of which could adversely affect our business, financial condition and results of operations and our ability to make distributions to our stockholders.

Our results may experience greater fluctuations by not electing hedge accounting treatment on the derivatives that we enter into.

We have elected to not qualify for hedge accounting treatment under ASC 815, Derivatives and Hedging, for our current derivative instruments. The economics of our derivative hedging transactions are not affected by this election; however, our GAAP earnings may be subject to greater fluctuations from period to period as a result of this accounting treatment for changes in fair value of certain interest rate swap agreements or for the accounting of the underlying hedged assets or liabilities in our financial statements, if it does not necessarily match the accounting used for interest rate swap agreements.

Our adoption of fair value option accounting could result in income statement volatility, which in turn, could cause significant market price and trading volume fluctuations for our securities.

We have determined that the securitization trusts that have issued certain of our Multi-Family MBS and Non-Agency RMBS are variable interest entities, or VIEs, of which we are the primary beneficiary, and elected the fair value option on the assets and liabilities held within these securitization trusts. As a result, we are required to consolidate the underlying multi-family and residential mortgage loans or securities, as applicable, related debt, interest income and interest expense of the securitization trusts in our financial statements, although our actual investment in these securitization trusts generally represents a small percentage of the total assets of the trusts. We historically accounted for the Multi-Family MBS and Non-Agency RMBS in our investment portfolio through other comprehensive income, pursuant to which unrealized gains and losses on those MBS were reflected as an adjustment to stockholders' equity. The fair value option, however,

requires that changes in valuations in the assets and liabilities of those VIEs of which we are the primary beneficiary be reflected through our consolidated earnings. As we continue to acquire subordinate Non-Agency RMBS and additional Multi-Family MBS assets in the future that are similar in structure and form to those already acquired, we may be required to consolidate the assets and liabilities of the issuing or securitization trusts and would expect to elect the fair value option for those assets. Because of this, our earnings may experience greater volatility in the future as a decline in the fair value of the assets of any VIE that we consolidate in our financial statements could reduce both our earnings and stockholders' equity, which in turn, could cause significant market price and trading volume fluctuations for our securities.

We may be exposed to environmental liabilities with respect to properties to which we take title.

In the course of our business, we may take title to real estate, and, if we do take title, we could be subject to environmental liabilities with respect to these properties. In such a circumstance, we may be held liable to a governmental entity or to third parties for property damage, personal injury, investigation and clean-up costs incurred by these parties in connection with environmental contamination, or we may be required to investigate or clean up hazardous or toxic substances or chemical releases at a property. The costs associated with investigation or remediation activities could be substantial. If we ever become subject to significant environmental liabilities, our business, financial condition, results of operations and our ability to make distributions to our stockholders could be adversely affected.

#### Risks Associated with Our Relationship with Our Manager

Our board of directors has approved very broad investment guidelines for our Manager and will not approve each investment and financing decision made by our Manager.

Our Manager is authorized to follow very broad investment guidelines. Our board of directors periodically reviews and updates our investment guidelines and also reviews our investment portfolio but does not generally review or approve specific investments. In addition, in conducting periodic reviews, our board of directors may rely primarily on information provided to them by our Manager. Furthermore, our Manager may use complex strategies, and transactions entered into by our Manager may be costly, difficult or impossible to unwind by the time they are reviewed by our board of directors. Our Manager will have great latitude within the broad parameters of our investment guidelines in determining the types and amounts of RMBS, Multi-Family MBS, MSRs and other mortgage related investments it may decide are attractive investments for us, which could result in investment returns that are substantially below expectations or that result in losses, which would adversely affect our business operations and results. In addition, our Manager may invest in any investment on our behalf without restriction as to the dollar amount of such investment and generally without prior approval of our board of directors. Our Manager is generally permitted to invest our assets in its discretion, provided that such investments comply with our investment guidelines. Our Manager's failure to generate attractive risk-adjusted returns on an investment which represents a significant dollar amount would adversely affect us. Further, decisions made and investments and financing arrangements entered into by our Manager may not fully reflect the best interests of our stockholders.

The incentive fee payable to our Manager under the management agreement is payable quarterly and is based on our core earnings and, therefore, may cause our Manager to select investments in more risky assets to increase its incentive compensation.

Our Manager is entitled to receive incentive compensation based upon our achievement of targeted levels of core earnings. In evaluating investments and other management strategies, the opportunity to earn incentive compensation based on core earnings may lead our Manager to place undue emphasis on the maximization of core earnings at the expense of other criteria, such as preservation of capital, in order to achieve higher incentive compensation.

Investments with higher yield potential are generally riskier or more speculative. This could result in increased risk to the value of our investment portfolio.

Core earnings is not a measure calculated in accordance with accounting principles generally accepted in the United States of America ("GAAP") and is defined in our management agreement in this Annual Report on Form 10-K.

We are dependent on our Manager and its key personnel for our success.

We have no separate facilities and are completely reliant on our Manager. All of our officers are employees of our Manager. Our Manager has significant discretion as to the implementation of our investment and operating policies and strategies. Accordingly, we believe that our success will depend to a significant extent upon the efforts, experience, diligence, skill and network of business contacts of the officers and key personnel of our Manager. The officers and key personnel of our Manager evaluate, negotiate, close and monitor our investments; therefore, our success will depend on their continued service. The departure of any of the officers or key personnel of our Manager could have a material adverse effect on our performance. In addition, there can be no assurance that our Manager will remain our investment manager or that we will continue to have access to our Manager's officers and professionals. The initial term of our management agreement with our Manager only extends until January 18, 2021, with automatic one-year renewals thereafter. If the management agreement is terminated and no suitable replacement is found to manage us, we may not be able to execute our business plan.

The management agreement with our Manager may be costly and difficult to terminate, including for our Manager's poor performance.

The initial term of the Management Agreement ends on January 18, 2021. The Management Agreement automatically renews for successive one year terms beginning January 18, 2021 and each January 18 thereafter, unless it is sooner terminated upon written notice delivered no later than 180 days prior to a renewal date by the affirmative vote of at least two-thirds (2/3) of the independent directors of the Board or by a vote of at least two-thirds of our outstanding shares of common stock, based upon a determination that (a) the Manager's performance is unsatisfactory and materially detrimental to us or (b) the compensation payable to the Manager under the Management Agreement is not fair to us (provided that in the instance of (b), we shall not have the right to terminate the Management Agreement if the Manager agrees to continue to provide services under the Management Agreement at fees that at least two-thirds of the independent directors of the Board determine to be fair, provided further that in the instance of (b), the Manager will be afforded the opportunity to renegotiate its compensation prior to termination). We may also terminate the Management Agreement at any time, including during the initial term, without the payment of any termination fee, with at least 30 days' prior written notice from us "for cause" as described in the Management Agreement. In the event of a termination of the Manager other than a termination for cause, we are required to pay a termination fee to the Manager. The termination fee is equal to three times the sum of (a) the average annual Base Management Fee and (b) the average annual Incentive Fee, in each case, earned by the Manager during the 24-month period immediately preceding the effective date of termination, calculated as of the end of the most recently completed fiscal quarter before the effective date of termination. Our Manager may terminate the Management Agreement upon written notice delivered no later than 180 days prior to a renewal date.

Our Manager's liability is limited under the management agreement and we have agreed to indemnify our Manager and its affiliates against certain liabilities. As a result, we could experience poor performance or losses for which our Manager would not be liable.

Pursuant to the management agreement, our Manager does not assume any responsibility other than to render the services called for thereunder and will not be responsible for any action of our board of directors in following or declining to follow its advice or recommendations. Our Manager maintains a contractual as opposed to a fiduciary relationship with us, although our officers who are also employees of our Manager will have a fiduciary duty to us under the Maryland General Corporation Law, or the MGCL, as our officers. Under the terms of the management agreement, our Manager, its officers, members, managers, directors, personnel, trustees, partners, stockholders, equity holders, any person controlling or controlled by our Manager and any person providing sub-advisory services to our Manager will not be liable to us, our directors, our stockholders or any partners for acts or omissions performed in accordance with and pursuant to the management agreement, except because of acts or omissions constituting bad faith, willful misconduct, gross negligence or reckless disregard of their duties under the management agreement, as determined by a final non-appealable order of a court of competent jurisdiction. In addition, we have agreed to indemnify our Manager, its officers, stockholders, members, managers, directors, personnel, trustees, partners, stockholders, equity holders, any person controlling or controlled by our Manager and any person providing sub-advisory services to our Manager with respect to all expenses, losses, damages, liabilities, demands, charges and claims arising from acts or omissions of our Manager not constituting bad faith, willful misconduct, gross negligence or reckless disregard of duties, performed in good faith in accordance with and pursuant to the management agreement. As a result, we could experience poor performance or losses for which our Manager would not be liable.

Our Manager is subject to extensive regulation as an investment adviser, which could adversely affect its ability to manage our business.

Our Manager is an investment adviser registered with the SEC and is subject to regulation by various regulatory authorities that are charged with protecting the interests of its clients, including us. Our Manager could be subject to civil liability, criminal liability or sanction, including revocation or denial of its registration as an investment adviser, revocation of the licenses of its employees, censures, fines or temporary suspension or permanent bar from conducting business, if it is found to have violated any of laws or regulations applicable to it. Any such liability or sanction could adversely affect its ability to manage our business.

There are conflicts of interest in our relationship with Hunt, including with our Manager and in the allocation of investment opportunities to Hunt affiliates and us, which could result in decisions that are not in the best interests of our stockholders.

We are subject to conflicts of interests arising out of our relationship with Hunt, including our Manager and its affiliates. Hunt owns approximately 9.5% of our outstanding common shares and, pursuant to our shareholder agreement, so long as Hunt and its affiliates own at least 5% of our outstanding common shares, Hunt will have the right to designate one designee to our board of directors. In addition, we are managed by our Manager, a Hunt affiliate, and our executive officers are employees of our Manager or one or more of its affiliates. There is no guarantee that the policies and procedures adopted by us, the terms and conditions of the Management Agreement or the policies and procedures adopted by our Manager, Hunt and their respective affiliates, will enable us to identify, adequately address or mitigate all potential conflicts of interest.

#### Risks Related to Our Securities

The market price and trading volume of our securities may vary substantially.

Our common stock is listed on the NYSE under the symbol "OAKS." Our Series A Preferred Stock is listed on the NYSE under the symbol "OAKS-PRA." Stock markets, including the NYSE, have experienced significant price and

volume fluctuations over the past several years. As a result, the market price of our securities has been and is likely to continue to be similarly volatile, and investors in our securities have experienced since the initial offering of our securities and may continue to experience a decrease in the value of their securities. Accordingly, no assurance can be given as to the ability of our stockholders to sell their securities or the price that our stockholders may obtain for their securities.

Some of the factors that negatively affect the market price of our securities include:

- changes in our dividend rates or frequency of payments thereof;
- actual or anticipated variations in our quarterly operating results;
- changes in our earnings estimates or publication of research reports about us or the real estate industry;
- changes in market valuations of similar companies;
- adverse market reaction to any increased indebtedness we incur in the future;
- additions to or departures of our Manager's key personnel;
- actions by our stockholders;
- speculation in the press or investment community;
- trading prices of common and preferred equity securities issued by REITs and other similar companies;
- in the case of our Series A Preferred Stock, prevailing interest rates, increases in which may have an adverse effect on the market price of the Series A Preferred Stock, and the annual yield from distributions on the Series A Preferred Stock as compared to yields on other financial instruments;
- general economic and financial conditions;
- government action or regulation; and
- our issuance of additional preferred equity or debt securities.

Market factors unrelated to our performance could negatively impact the market price of our securities, and broad market fluctuations could also negatively impact the market price of our securities.

Market factors unrelated to our performance could negatively impact the market price of our securities. One of the factors that investors may consider in deciding whether to buy or sell our securities is our distribution rate as a percentage of our stock price relative to market interest rates. If market interest rates increase, prospective investors may demand a higher distribution rate or seek alternative investments paying higher distributions or interest. As a result, interest rate fluctuations and conditions in the capital markets can affect the market value of our securities. In addition, the stock market has experienced extreme price and volume fluctuations that have affected the market price of many companies in industries similar or related to ours and that have been unrelated to these companies' operating performances. These broad market fluctuations could reduce the market price of our securities. Furthermore, our operating results and prospects may be below the expectations of public market analysts and investors or may be lower than those of companies with comparable market capitalizations, which could lead to a material decline in the market price of our securities.



The performance of our securities may be affected by the performance of our investments, which may be speculative and aggressive compared to other types of investments.

The investments we make in accordance with our investment objectives may result in a greater amount of risk as compared to alternative investment options, including relatively higher risk of volatility or loss of principal. Our investments may be speculative and aggressive, and therefore an investment in our securities may not be suitable for someone with lower risk tolerance.

One of the factors that investors may consider in deciding whether to buy or sell shares of our securities is our distribution rate as a percentage of the trading price of our securities relative to market interest rates and distribution rates of our competitors. If the market price of our securities is based primarily on the earnings and return that we derive from our investments and income with respect to our investments and our related distributions to stockholders, and not from the market value of the investments themselves, then interest rate fluctuations and capital market conditions are likely to affect adversely the market price of our securities. For instance, if market rates rise without an increase in our distribution rate, the market price of our securities could decrease as potential investors may require a higher distribution yield on our securities or seek other securities paying higher distributions or interest. In addition, rising interest rates would result in increased interest expense on our variable rate debt, thereby reducing cash flow and our ability to service our indebtedness and make distributions to our stockholders.

An increase in interest rates may have an adverse effect on the market price of our stock and our ability to make distributions to our stockholders.

One of the factors that investors may consider in deciding whether to buy or sell shares of our stock is our dividend rate, or our future expected dividend rate, as a percentage of our common stock price, relative to market interest rates. If market interest rates increase, prospective investors may demand a higher dividend rate on our shares or seek alternative investment paying higher dividends or interest. As a result, interest rate fluctuations and capital market conditions can affect the market price of our stock independent of the effects such conditions may have on our portfolio.

We have not established a minimum distribution payment level on our common stock and we cannot assure you of our ability to make distributions in the future, or that our board of directors will not reduce distributions in the future regardless of such ability.

As announced on March 16, 2018, the dividend to holders of our common stock will be paid monthly for the months of April, May and June, 2018 and will thereafter change to such dividends being paid on a quarterly basis in arrears. Thereafter, we intend to announce quarterly dividends in arrears on a quarterly basis for our common stock and continue to announce in advance monthly dividends to be paid during each calendar quarter. If substantially all of our taxable income has not been paid by the close of any calendar year, we intend to declare a special dividend to holders of our common stock prior to September 15th of the following year, to achieve this result.

Even though our board of directors has declared these dividends, we have not established a minimum distribution payment level on our common stock and our ability to make distributions may be adversely affected by the risk factors described in this Annual Report on Form 10-K. All distributions to our common stockholders will be made at the discretion of our board of directors and will depend on our earnings, our financial condition, maintenance of our REIT status and such other factors as our board of directors may deem relevant from time to time. There can be no assurance of our ability to make distributions to our common stockholders, or that our board of directors will not determine to reduce such distributions, in the future. In addition, some of our distributions to our common stockholders may continue to include a return of capital.

We may not be able to pay dividends or other distributions on the Series A Preferred Stock.

Under Maryland law, no distributions on capital stock may be made if, after giving effect to the distribution, (1) the corporation would not be able to pay the indebtedness of the corporation as such indebtedness becomes due in the usual course of business or, (2) except in certain limited circumstances when distributions are made from net earnings, the corporation's total assets would be less than the sum of the corporation's total liabilities plus, unless the charter provides otherwise (which our charter does, with respect to the Series A Preferred Stock), the amount that would be needed, if the corporation were to be dissolved at the time of the distribution, to satisfy the preferential rights upon dissolution of stockholders whose preferential rights on dissolution are superior to those receiving the distribution. There can be no guarantee that we will have sufficient cash to pay dividends on the Series A Preferred Stock. In addition, payment of our dividends depends upon our earnings, our financial condition, maintenance of our REIT qualification and other factors as our board of directors may deem relevant from time to time.

We cannot assure you that our business will generate sufficient cash flow from operations or that future borrowings will be available to us in an amount sufficient to enable us to make distributions on our securities, to pay our indebtedness or to fund our other liquidity needs.

Future offerings of debt or equity securities that rank senior to our common stock may adversely affect the market price of our common stock.

If we decide to issue additional equity securities or to issue debt in the future that rank senior to our common stock, it is likely that they will be governed by an indenture or other instrument containing covenants restricting our operating flexibility. Additionally, any convertible or exchangeable securities that we issue in the future may have rights, preferences and privileges more favorable than those of our common stock and may result in dilution to owners of our common stock. We and, indirectly, our stockholders, will bear the cost of issuing and servicing such securities. Because our decision to issue debt or equity securities in any future offering will depend on market conditions and other factors beyond our control, we cannot predict or estimate the amount, timing or nature of our future offerings. Thus holders of our common stock will bear the risk of our future offerings reducing the market price of our common stock and diluting the value of their stock holdings in us. Furthermore, the compensation payable to our Manager will increase as a result of future issuances of our equity securities even if the issuances are dilutive to existing stockholders.

#### Risks Related to Our Organization and Structure

Maintenance of our exclusion from the Investment Company Act will impose limits on our business; we have not sought formal guidance from the staff of the SEC as to our treatment of loans in securitization trusts and there can be no assurance that the staff will not adopt a contrary interpretation which could cause us to sell material amounts of our assets and to change our investment strategy.

We conduct our business so as not to become regulated as an investment company under the Investment Company Act. If we were to fall within the definition of an investment company, we would be unable to conduct our business as described in this Annual Report on Form 10-K. Section 3(a)(1)(A) of the Investment Company Act defines an investment company as any issuer that is or holds itself out as being engaged primarily in the business of investing, reinvesting or trading in securities. Section 3(a)(1)(C) of the Investment Company Act also defines an investment company as any issuer that is engaged or proposes to engage in the business of investing, reinvesting, owning, holding or trading in securities and owns or proposes to acquire investment securities having a value exceeding 40%

of the value of the issuer's total assets (exclusive of U.S. Government securities and cash items) on an unconsolidated basis. Excluded from the term "investment securities," among other things, in Section 3(a)(1)(C) of the Investment Company Act are U.S. Government securities and securities issued by majority owned subsidiaries that are not themselves investment companies and are not relying on the exception from the definition of investment company set forth in Section 3(c)(1) or Section 3(c)(7) of the Investment Company Act.

We conduct our business so as not to become regulated as an investment company under the Investment Company Act in reliance on the exclusion provided by Section 3(c)(5)(C) of the Investment Company Act. Section 3(c)(5)(C), as interpreted by the staff of the SEC, requires us to invest at least 55% of our assets in "mortgages and other liens on and interest in real estate," or "qualifying real estate interests," and at least 80% of our assets in qualifying real estate interests plus "real estate-related assets." In satisfying this 55% requirement, based on SEC staff guidance, we may treat Agency RMBS issued with respect to an underlying pool of mortgage loans in which we hold all of the certificates issued by the pool as qualifying real estate interests. Neither the SEC nor its staff has issued guidance with respect to whole pool Non-Agency RMBS. Accordingly, based on our own judgment and analysis of the SEC staff's guidance with respect to whole pool Agency RMBS, we may also treat Non-Agency RMBS issued with respect to an underlying pool of mortgage loans in which we hold all of the certificates issued by the pool as qualifying real estate interests. We may also treat whole mortgage loans that we acquire directly as qualifying real estate interests provided that 100% of the loan is secured by real estate when we acquire it and we have the unilateral right to foreclose on the mortgage. We currently treat partial pool Agency and Non-Agency RMBS as real estate-related assets. We treat any interest rate swaps or other derivative hedging transactions we enter into as miscellaneous assets that will not exceed 20% of our total assets. We generally rely on guidance published by the SEC or its staff or on our analyses of guidance published with respect to other types of assets to determine which assets are qualifying real estate assets and real estate-related assets.

When we acquire (i) 100% of the expected loss exposure and all of the directing certificate holder's rights in a K-Series trust; or (ii) 100% of the subordinated certificates issued by a securitization trust into which we sell loans, which certificates have the sole ability, inter alia, to foreclose against defaulting loans and have all of the interests in the trust's expected loss disclosure; we may treat the full amount of loans in the trust as qualifying real estate. When we acquire less than 100% of the subordinated certificates in a K-Series trust (and accordingly have less than 100% of the trust's expected loss exposure), we will treat our net investment amount in such trust as real estate related assets.

The foregoing treatments are not based on specific and particular guidance from the SEC staff. Accordingly, there can be no assurance that such treatments, particularly as to the treatment of the loans in a trust described by "(i)" or "(ii)" above as qualified real estate interests and in such amounts as described above, will continue to be appropriate. Additionally, we use our net investment amount in any K-Series trust (rather than the amount of loans in such trust) that is not described by "(i)" above when calculating whether we continue to meet the requirements of the exclusion provided by Section 3(c)(5)(C) of the Investment Company Act. If we were required to use the aggregate face amount of loans in any such K-Series trust in making such calculation, it is likely that the exclusion would no longer be available to us given the large amount of those loans vis-a-vis our current and expected holdings of other qualifying real estate interests. Similarly, if we were required to use the aggregate face amount of loans in future securitization trusts where we own 100% of the subordinated certificates but do not own the rights, inter alia, to foreclose against defaulting loans, it is likely that the exclusion would no longer be available to us as the aggregate amount of the loans in such securitization trust increases over time. If the SEC or its staff determines that any of these securities are not qualifying real estate interests or real estate-related assets, adopts a contrary interpretation with respect to these securities or otherwise believes we do not satisfy the above exclusions or changes its interpretation of the above exclusions based on our methodology for calculating compliance or otherwise, we could be required to substantially restructure our activities including selling material amounts of our assets and to adopt changes to our investment strategy.

Although we monitor our portfolio for compliance with the Section 3(c)(5)(C) exclusion periodically and prior to each acquisition and disposition, there can be no assurance that we will be able to maintain this exclusion.

To the extent that we elect in the future to conduct our operations through majority owned subsidiaries, such business will be conducted in such a manner as to ensure that we do not meet the definition of investment company under either Section 3(a)(1)(A) or Section 3(a)(1)(C) of the 1940 Act, because less than 40% of the value of our total assets on an unconsolidated basis would consist of investment securities. We intend to monitor our portfolio periodically to insure compliance with the 40% test, to the extent we have made such election. In such case, we would be a holding company which conducts business exclusively through majority owned subsidiaries and we would be engaged in the non-investment company business of our subsidiaries.

Loss of our exclusion from regulation pursuant to the Investment Company Act would adversely affect us.

On August 31, 2011, the SEC issued a concept release requesting comments to a number of matters relating to the Section 3(c)(5)(C) exclusion from the Investment Company Act, including the nature of assets that qualify for purposes of the exclusion and whether mortgage-related REIT's should be regulated as investment companies. There can be no assurance that the laws and regulations governing the Investment Company Act status of REITs, including guidance and interpretations from the SEC or its staff regarding the Section 3(c)(5)(C) exclusion, will not change in a manner that adversely affects our operations or business. As a result of this release, the SEC or its staff may issue new interpretations of the Section 3(c)(5)(C) exclusion causing us to change the way we conduct our businesses, including changes that may adversely affect our ability to achieve our investment objective. We may be required at times to adopt less efficient methods of financing certain of our mortgage related investments and we may be precluded from acquiring certain types of higher yielding securities. The net effect of these factors would be to lower our net interest income. If we fail to qualify for an exemption from registration as an investment company or an exclusion from the definition of an investment company, our ability to use leverage would be substantially reduced. Our businesses will be adversely affected if we fail to qualify for an exemption or exclusion from regulation under the Investment Company Act.

Our authorized but unissued shares of common and preferred stock may prevent a change in our control.

Our charter authorizes us to issue additional authorized but unissued shares of common or preferred stock. In addition, our board of directors may, without stockholder approval, amend our charter to increase the aggregate number of our shares of stock or the number of shares of stock of any class or series that we have authority to issue and classify or reclassify any unissued shares of common or preferred stock and set the preferences, rights and other terms of the classified or reclassified shares. As a result, our board of directors may establish a series of shares of common or preferred stock that could delay or prevent a transaction or a change in control that might involve a premium price for our shares of common stock or otherwise be in the best interest of our stockholders.

Ownership limitations may restrict change of control or business combination opportunities in which our stockholders might receive a premium for their shares.

In order for us to maintain our REIT qualification for each taxable year after December 31, 2012, during the last half of any taxable year no more than 50% in value of our outstanding capital stock may be owned, directly or indirectly, by five or fewer individuals. "Individuals" for this purpose include natural persons, private foundations, some employee benefit plans and trusts, and some charitable trusts. To assist us in maintaining our qualification as a REIT and subject to

certain exceptions, our charter generally prohibits any person from directly or indirectly owning more than 9.8% in value or in number of shares, whichever is more restrictive, of the outstanding shares of our capital stock or more than 9.8% in value or in number of shares, whichever is more restrictive, of the outstanding shares of our equity securities. This ownership limitation could have the effect of discouraging a takeover or other transaction in which holders of our equity securities might receive a premium for their shares over the then prevailing market price or which holders might believe to be otherwise in their best interests. Our board of directors has granted XL Investments Ltd an exemption from the 9.8% ownership limitation. As of March 1, 2018, XL Investments Ltd, together with XL Global, Inc., owned 14.1% of our common stock.

Certain provisions of Maryland law may limit the ability of a third-party to acquire control of our company.

Certain provisions of the MGCL may have the effect of delaying, deferring or preventing a transaction or a change of control of our company that might involve a premium price for holders of our equity securities or otherwise be in their best interests.

Subject to certain limitations, provisions of the MGCL prohibit certain business combinations between us and an “interested stockholder” (defined generally as any person who beneficially owns 10% or more of the voting power of our outstanding voting stock or an affiliate or associate of ours who beneficially owned 10% or more of the voting power of our then outstanding stock during the two-year period immediately prior to the date in question) or an affiliate of the interested stockholder for five years after the most recent date on which the stockholder became an interested stockholder. After the five-year period, business combinations between us and an interested stockholder or an affiliate of the interested stockholder must generally either provide a minimum price to our stockholders (as defined in the MGCL) in the form of cash or other consideration in the same form as previously paid by the interested stockholder or be recommended by our board of directors and approved by the affirmative vote of at least 80% of the votes entitled to be cast by holders of our outstanding shares of voting stock and at least two-thirds of the votes entitled to be cast by stockholders other than the interested stockholder and its affiliates and associates. These provisions of the MGCL relating to business combinations do not apply, however, to business combinations that are approved or exempted by our board of directors prior to the time that the interested stockholder becomes an interested stockholder. Pursuant to the statute, our board of directors has by resolution exempted business combinations between us and any member of the XL group of companies, the parent of which is XL Group Ltd. Consequently, the five-year prohibition and the supermajority vote requirements will not apply to business combinations with the XL group of companies. As a result, the members of the XL group of companies may be able to enter into business combinations with us that may not be in the best interest of our stockholders without compliance by us with the supermajority vote requirements and other provisions of the statute. However, our board of directors may repeal or modify this exemption at any time in the future, in which case the applicable provisions of this statute will become applicable to business combinations between us and the XL group of companies.

The “control share” provisions of the MGCL provide that holders of “control shares” of a Maryland corporation (defined as shares which, when aggregated with other shares controlled by the stockholder (except solely by virtue of a revocable proxy), entitle the stockholder to exercise one of three increasing ranges of voting power in electing directors) acquired in a “control share acquisition” (defined as the direct or indirect acquisition of ownership or control of “control shares”) have no voting rights with respect to such shares except to the extent approved by our stockholders by the affirmative vote of at least two-thirds of all the votes entitled to be cast on the matter, excluding votes entitled to be cast by the acquirer of control shares, our officers and our employees who are also our directors. Our bylaws contain a provision exempting from the control share acquisition statute any and all acquisitions by any person of shares of our stock. There can be no assurance that this provision will not be amended or eliminated at any time in the future.

Additionally, Title 3, Subtitle 8 of the MGCL permits our board of directors, without stockholder approval and regardless of what is currently provided in our charter or bylaws, to elect to be subject to certain provisions relating to corporate governance that may have the effect of delaying, deferring or preventing a transaction or a change of control of our company that might involve a premium to the market price of our equity securities or otherwise be in our stockholders' best interests. Upon the completion of our IPO, we became subject to some of these provisions, either by provisions of our charter and bylaws unrelated to Subtitle 8 or by reason of an election in our charter to be subject to certain provisions of Subtitle 8.

Stockholders have limited control over changes in our policies and operations.

Our board of directors determines our major policies, including with regard to financing, growth, debt capitalization, REIT qualification and distributions. Our board of directors may amend or revise these and other policies without a vote of the stockholders. Under our charter and the MGCL, our common stockholders generally have a right to vote only on the following matters:

- the election or removal of directors;
- the amendment of our charter, except that our board of directors may amend our charter without stockholder approval to:

- change our name;
- change the name or other designation or the par value of any class or series of stock and the aggregate par value of our stock;
- increase or decrease the aggregate number of shares of stock that we have the authority to issue; and
- increase or decrease the number of our shares of any class or series of stock that we have the authority to issue;

- our liquidation and dissolution; and
- our being a party to a merger, consolidation, sale or other disposition of all or substantially all of our assets or statutory share exchange.

All other matters are subject to the discretion of our board of directors.

Our charter contains provisions that make removal of our directors difficult, which could make it difficult for stockholders to effect changes in management.

Our charter provides that, subject to the rights of any series of preferred stock, a director may be removed only by the affirmative vote of at least two-thirds of all the votes entitled to be cast generally in the election of directors. Our charter and bylaws provide that vacancies generally may be filled only by a majority of the remaining directors in office, even if less than a quorum. These requirements make it more difficult to change management by removing and replacing directors and may prevent a change in control that is in the best interests of stockholders.

Our rights and stockholders' rights to take action against directors and officers are limited, which could limit recourse in the event of actions not in the best interests of stockholders.

As permitted by Maryland law, our charter eliminates the liability of our directors and officers to us and our stockholders for money damages, except for liability resulting from:

- actual receipt of an improper benefit or profit in money, property or services; or
- a final judgment based upon a finding of active and deliberate dishonesty by the director or officer that was material to the cause of action adjudicated.

In addition, our charter requires us, to the maximum extent permitted by Maryland law, to indemnify and, without requiring a preliminary determination of the ultimate entitlement to indemnification, pay or reimburse reasonable expenses in advance of final disposition of a proceeding to any individual who is a present or former director or officer and who is made or threatened to be made a party to the proceeding by reason of his or her service in that capacity or any individual who, while a director or officer and at our request, serves or has served as a director, officer, partner, trustee of another corporation, REIT, partnership, joint venture, trust, employee benefit plan or any other enterprise and who is made or threatened to be made a party to the proceeding by reason of his or her service in that capacity. As part of these indemnification obligations, we may be obligated to fund the defense costs incurred by our directors and officers.

We also are permitted to purchase and maintain insurance or provide similar protection on behalf of any directors, officers, employees and agents, including our Manager and its affiliates, against any liability asserted which was incurred in any such capacity with us or arising out of such status. This may result in us having to expend significant funds, which will reduce the available cash for distribution to our stockholders.

We have made, and in the future may make, distributions of offering proceeds, borrowings or the sale of assets to the extent that distributions exceed earnings or cash flow from our operations.

We have made, and in the future may make, distributions of offering proceeds, borrowings or the sale of assets to the extent that distributions exceed earnings or cash flow from our operations. Such distributions reduce the amount of cash we have available for investing and other purposes and could be dilutive to our financial results. In addition, funding our distributions from our net proceeds may constitute a return of capital to our investors, which would have the effect of reducing each stockholder's basis in its shares of equity securities.

Because of its significant ownership of our common stock, XL Investments has the ability to influence the outcome of matters that require a vote of our stockholders, including a change of control.

XL Investments holds a significant interest in our outstanding common stock. As of March 1, 2018, XL Investments, together with XL Global, Inc., owned 14.1% of our common stock. As a result, XL Investments potentially has the ability to influence the outcome of matters that require a vote of our stockholders, including election of our board of directors and other corporate transactions, regardless of whether others believe that the transaction is in our best interests. We have agreed with XL Investments that, for so long as XL Investments and any other of the XL group of companies collectively beneficially owns at least 9.8% of our issued and outstanding common stock (on a fully diluted basis), XL Investments will have the right to appoint an observer to attend all board meetings, but such observer has no right to vote at any such board meetings.

We are an "emerging growth company" and the reduced disclosure requirements applicable to emerging growth companies may make it more difficult for you to evaluate an investment in our company and may make our equity securities less attractive to investors.

In April 2012, President Obama signed into law the Jumpstart Our Business Startups Act, or the JOBS Act. The JOBS Act contains provisions that, among other things, relax certain reporting requirements for "emerging growth companies," including certain requirements relating to accounting standards and compensation disclosure. We are classified as an emerging growth company. For as long as we are an emerging growth company, which may be up to

December 31, 2018, unlike other public companies, we will not be required to (1) provide an auditor's attestation report on management's assessment of the effectiveness of our system of internal control over financial reporting pursuant to Section 404 of the Sarbanes-Oxley Act, (2) comply with any new or revised financial accounting standards applicable to public companies until such standards are also applicable to private companies under Section 102(b)(1) of the JOBS Act, (3) comply with any new requirements adopted by the Public Company Accounting Oversight Board, or the PCAOB, requiring mandatory audit firm rotation or a supplement to the auditor's report in which the auditor would be required to provide additional information about the audit and the financial statements of the issuer, (4) comply with any new audit rules adopted by the PCAOB after April 5, 2012 unless the SEC determines otherwise, (5) provide certain disclosure regarding executive compensation required of larger public companies or (6) hold shareholder advisory votes on executive compensation. We cannot predict if investors will find our equity securities less attractive because we have chosen to rely on these exemptions. If some investors find our equity securities less attractive as a result of any choices to reduce future disclosure, there may be a less active trading market for our equity securities and the stock price of our equity securities may be more volatile.

Under the JOBS Act, emerging growth companies can delay adopting new or revised accounting standards that have different effective dates for public and private companies until such time as those standards apply to private companies. We have elected to take advantage of such extended transition period. Since we will not be required to comply with new or revised accounting standards on the relevant dates on which adoption of such standards are required for other public companies, our financial statements may not be comparable to the financial statements of companies that comply with public company effective dates. Our election is irrevocable pursuant to Section 107 of the JOBS Act.

The JOBS Act allows us to postpone the date by which we must comply with certain laws and regulations intended to protect investors and to reduce the amount of information we have provided to you in this Annual Report on Form 10-K, which may have an adverse effect on the trading price of our equity securities.

The JOBS Act is intended to reduce the regulatory burden on "emerging growth companies." As defined in the JOBS Act, a public company whose initial public offering of common equity securities occurred after December 8, 2011 and whose annual gross revenues are less than \$1.0 billion will, in general, qualify as an "emerging growth company" until the earliest of:

- the last day of its fiscal year following the fifth anniversary of the date of its initial public offering of common equity securities;
- the last day of its fiscal year in which it has annual gross revenue of \$1.0 billion or more;
- the date on which it has, during the previous three-year period, issued more than \$1.0 billion in non-convertible debt; and
- the date on which it is deemed to be a "large accelerated filer," which will occur at such time as the company (1) has an aggregate worldwide market value of common equity securities held by non-affiliates of \$700 million or more as of the last business day of its most recently completed second fiscal quarter, (2) has been required to file annual and quarterly reports under the Exchange Act for a period of at least 12 months, and (3) has filed at least one Annual Report on Form 10-K pursuant to the Exchange Act.



Under this definition, we are an “emerging growth company” and could remain an emerging growth company until as late as December 31, 2018. The market value of our common stock held by non-affiliates was \$71.6 million at December 31, 2017.

As a result, this Annual Report on Form 10-K includes less information about us than would otherwise be required if we were not an “emerging growth company,” which may make it more difficult for you to evaluate an investment in our company. We have elected to take advantage of some or all of the reduced regulatory and reporting requirements applicable to reports and proxy statements that we file with the SEC in the future, which will be available to us so long as we qualify as an “emerging growth company,” including, but not limited to, not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements, and exemptions from the requirements of holding a nonbinding advisory vote on executive compensation and shareholder approval of any golden parachute payments not previously approved. Among other things, this means that our independent registered public accounting firm will not be required to provide an attestation report on the effectiveness of our internal control over financial reporting so long as we qualify as an emerging growth company, which may increase the risk that material weaknesses or other deficiencies in our internal control over financial reporting go undetected. So long as we qualify as an “emerging growth company,” we may elect not to provide you with certain information, including certain financial information and certain information regarding compensation of our executive officers, that we would otherwise have been required to provide in filings we make with the SEC, which may make it more difficult for investors and securities analysts to evaluate our company. As a result, investor confidence in our company and the market price of our equity securities may be adversely affected.

We are subject to financial reporting and other requirements for which our accounting, internal audit and other management systems and resources may not be adequately prepared.

We are subject to reporting and other obligations under the Exchange Act, including the requirements of Section 404 of the Sarbanes-Oxley Act. These reporting and other obligations may place significant demands on our management, administrative, operational, internal audit and accounting resources and cause us to incur significant expenses. We may need to upgrade our systems or create new systems, implement additional financial and management controls, reporting systems and procedures, expand or outsource our internal audit function and hire additional accounting, internal audit and finance staff. If we are unable to accomplish these objectives in a timely and effective fashion, our ability to comply with the financial reporting requirements and other rules that apply to reporting companies could be impaired. Any failure to maintain effective internal controls could have a material adverse effect on our business, financial condition and results of operations and our ability to make distributions to our stockholders.

We are required to make critical accounting estimates and judgments, and our financial statements may be materially affected if our estimates or judgments prove to be inaccurate.

Financial statements prepared in accordance with GAAP require the use of estimates, judgments and assumptions that affect the reported amounts. Different estimates, judgments and assumptions reasonably could be used that would have a material effect on our financial statements, and changes in these estimates, judgments and assumptions are likely to occur from period to period in the future. Significant areas of accounting requiring the application of management’s judgment include, but are not limited to (1) determining the fair value of our investments, (2) assessing the adequacy of the allowance for loan losses or credit reserves and (3) appropriately consolidating VIEs for which we have determined we are the primary beneficiary. These estimates, judgments and assumptions are inherently uncertain, and, if they prove to be wrong, then we face the risk that charges to income will be required. In addition, because we have limited operating history in some of these areas and limited experience in making these estimates, judgments and assumptions, the risk of future charges to income may be greater than if we had more experience in these areas. Any such charges could significantly harm our business, financial condition, results of operations and our

ability to make distributions to our stockholders. See “Management’s Discussion and Analysis of Financial Condition and Results of Operations-Critical Accounting Policies” for a discussion of the accounting estimates, judgments and assumptions that we believe are the most critical to an understanding of our business, financial condition and results of operations.

#### Tax Risks

If we fail to remain qualified as a REIT, we will be subject to U.S. federal income tax as a regular corporation and could face a substantial tax liability, which would reduce the amount of cash available for distribution to our stockholders.

We elected to be taxed as a REIT commencing with our short taxable year ended December 31, 2012, and to comply with the provisions of the Internal Revenue Code with respect thereto. Our continued qualification as a REIT will depend on our satisfaction of certain asset, income, organizational, distribution, stockholder ownership and other requirements on a continuing basis. Our ability to satisfy the asset tests depends upon our analysis of the characterization and fair market values of our assets, some of which are not susceptible to a precise determination, and for which we will not obtain independent appraisals. Our compliance with the REIT income and quarterly asset requirements also depends upon our ability to successfully manage the composition of our income and assets on an ongoing basis. Further, there can be no assurance that the U.S. Internal Revenue Service, or the IRS, will not contend that our interests in subsidiaries or in securities of other issuers will not cause a violation of the REIT requirements.

If we were to fail to maintain our REIT qualification in any taxable year and were not able to qualify for certain statutory relief provisions, we would be subject to U.S. federal income tax, including any applicable alternative minimum tax, on our taxable income at regular corporate rates, and dividends paid to our stockholders would not be deductible by us in computing our taxable income. Any resulting corporate tax liability could be substantial and would reduce the amount of cash available for distribution to our stockholders, which in turn could have an adverse impact on the value of our equity securities. Unless we were entitled to relief under certain Internal Revenue Code provisions, we also would be disqualified from re-electing to be taxed as a REIT for the four taxable years following the year in which we failed to qualify as a REIT.

Dividends payable by REITs do not qualify for the reduced tax rates available for some dividends.

The maximum tax rate applicable to income from “qualified dividends” payable to U.S. stockholders that are individuals, trusts and estates is 20%, exclusive of a 3.8% investment tax surcharge. Dividends payable by REITs, however, generally are not eligible for the reduced rates. Thus, the more favorable rates applicable to regular corporate qualified dividends could cause investors who are individuals, trusts and estates to perceive investments in REITs to be relatively less attractive than investments in the stocks of non-REIT corporations that pay dividends, which could adversely affect the value of the stock of REITs, including our equity securities.

REIT distribution requirements could adversely affect our ability to execute our business plan.

We generally must distribute annually at least 90% of our REIT taxable income determined without regard to the deduction for dividends paid and excluding net capital gain and 90% of our net income, if any, (after tax) from foreclosure property, in order for us to maintain our REIT qualification. To the extent that we satisfy such distribution requirements but distribute less than 100% of our REIT taxable income we will be subject to U.S. federal income tax on our undistributed taxable income. In addition, we will be subject to a 4% nondeductible excise tax if the actual amount that we pay out to our stockholders in a calendar year is less than a minimum amount specified under U.S. federal income tax laws. We intend to make distributions to our stockholders to comply with the REIT requirements of the Internal Revenue Code.

From time to time, differences in timing between our recognition of taxable income and our actual receipt of cash may occur. If we do not have other funds available in these situations we could be required to borrow funds on unfavorable terms, sell investments at disadvantageous prices or distribute amounts that would otherwise be invested in future acquisitions, capital expenditures or repayment of debt, make a taxable distribution of our shares as part of a distribution in which stockholders may elect to receive shares or (subject to certain limits) cash or use cash reserves, in order to make distributions sufficient to enable us to pay out enough of our taxable income to satisfy the REIT distribution requirement and to avoid the U.S. federal income tax and the 4% excise tax in a particular year. These alternatives could increase our costs or reduce our equity. Thus, compliance with the REIT requirements may hinder our ability to grow, which could adversely affect the value of our equity securities.

Even if we remain qualified as a REIT, we may face other tax liabilities that reduce our cash flow.

Even if we remain qualified for taxation as a REIT, we may be subject to certain U.S. federal, state and local taxes on our income and assets, including taxes on any undistributed income, tax on income from some activities conducted as a result of a foreclosure, and state or local income, property and transfer taxes, such as mortgage recording taxes. Any of these taxes would decrease cash available for distribution to our stockholders.

Complying with REIT requirements may cause us to forgo otherwise attractive opportunities and may require us to dispose of our target assets sooner than originally anticipated.

To maintain our qualification as a REIT, we must satisfy five tests relating to the nature of our assets at the end of each calendar quarter. First, at least 75% of the value of our total assets must consist of cash, cash items, government securities and real estate assets, including certain mortgage loans and securities and debt instruments issued by publicly offered REITs. Second, we may not own more than 10% of any one issuer's outstanding securities, as measured by either value or voting power. Third, no more than 5% of the value of our total assets can consist of the securities of any one issuer. Fourth, no more than 20% of our total assets can be represented by securities of one or more TRSs. Fifth, not more than 25% of our assets may consist of debt instruments issued by publicly offered REITs to the extent that such debt instruments constitute "real estate assets" for purposes of the 75% asset test described above only because of the express inclusion of "debt instruments issued by publicly offered REITs" in the definition. If we fail to comply with these requirements at the end of any calendar quarter, we will lose our REIT qualification unless we are able to qualify for certain statutory relief provisions, which may involve paying taxes and penalties. In order to comply with the asset tests, we may be required to liquidate from our investment portfolio otherwise attractive investments. These actions could have the effect of reducing our income and the amount available for distribution to our stockholders.

In addition to the asset tests set forth above, to maintain our REIT qualification, we must continually satisfy tests concerning, among other things, the sources of our income, the amounts we distribute to our stockholders and the ownership of our stock. We may be unable to pursue investments that would be otherwise advantageous to us in order to satisfy the income test, the asset tests, and the other REIT requirements. Thus, compliance with the REIT requirements may hinder our ability to make certain attractive investments.

We may be required to report taxable income for certain investments in excess of the economic income we ultimately realize from them.

We may continue to acquire mortgage-backed securities in the secondary market for less than their face amount. In addition, as a result of our ownership of certain mortgage-backed securities, we may be treated for tax purposes as holding certain debt instruments acquired in the secondary market for less than their face amount. The discount at which such securities or debt instruments are acquired may reflect doubts about their ultimate collectability rather than current market interest rates. The amount of such discount will nevertheless generally be treated as “market discount” for U.S. federal income tax purposes. Accrued market discount is generally reported as income when, and to the extent that, any payment of principal of the mortgage-backed security or debt instrument is made. If we collect less on the mortgage-backed security or debt instrument than our purchase price plus the market discount we had previously reported as income, we may not be able to benefit from any offsetting loss deductions.

In addition, as a result of our ownership of certain mortgage-backed securities, we may be treated for tax purposes as holding distressed debt investments that are subsequently modified by agreement with the borrower. If the amendments to the outstanding debt are “significant modifications” under applicable U.S. Treasury Department regulations, the modified debt may be considered to have been reissued to us at a gain in a debt-for-debt exchange with the borrower. In that event, we may be required to recognize taxable gain to the extent the principal amount of the modified debt exceeds our adjusted tax basis in the unmodified debt, even if the value of the debt or the payment expectations have not changed.

Moreover, some of the mortgage-backed securities that we acquire may have been issued with original issue discount. We will be required to report such original issue discount based on a constant yield method and will be taxed based on the assumption that all future projected payments due on such mortgage-backed securities will be made. If such mortgage-backed securities turn out not to be fully collectable, an offsetting loss deduction will become available only in the later year that uncollectability is provable.

Finally, in the event that any debt instruments or mortgage-backed securities acquired by us are delinquent as to mandatory principal and interest payments, or in the event a borrower with respect to a particular debt instrument acquired by us encounters financial difficulty rendering it unable to pay stated interest as due, we may nonetheless be required to continue to recognize the unpaid interest as taxable income as it accrues, despite doubt as to its ultimate collectability. Similarly, we may be required to accrue interest income with respect to subordinate mortgage-backed securities at the stated rate regardless of whether corresponding cash payments are received or are ultimately collectable. In each case, while we would in general ultimately have an offsetting loss deduction available to us when such interest was determined to be uncollectable, the utility of that deduction could depend on our having taxable income in that later year or thereafter.

Certain apportionment rules may affect our ability to comply with the REIT asset and gross income tests.

The Internal Revenue Code provides that a regular or a residual interest in a real estate mortgage investment conduit, or REMIC, is generally treated as a real estate asset for the purpose of the REIT asset tests, and any amount includible in our gross income with respect to such an interest is generally treated as interest on an obligation secured by a mortgage on real property for the purpose of the REIT gross income tests. If, however, less than 95% of the assets of a REMIC in

which we hold an interest consist of real estate assets (determined as if we held such assets), we will be treated as holding our proportionate share of the assets of the REMIC for the purpose of the REIT asset tests and receiving directly our proportionate share of the income of the REMIC for the purpose of determining the amount of income from the REMIC that is treated as interest on an obligation secured by a mortgage on real property. In connection with the expanded Agency RMBS-backed HARP loan program, the IRS issued guidance providing that, among other things, if a REIT holds a regular interest in an “eligible REMIC,” or a residual interest in an “eligible REMIC” that informs the REIT that at least 80% of the REMIC’s assets constitute real estate assets, then the REIT may treat 80% of the interest in the REMIC as a real estate asset for the purpose of the REIT income and asset tests. Although the portion of the income from such a REMIC interest that does not qualify for purposes of the REIT 75% gross income test would likely be qualifying income for the purpose of the 95% REIT gross income test, the remaining 20% of the REMIC interest generally would not qualify as a real estate asset and the income therefrom generally would not qualify for purposes of the 75% REIT gross income test, which could adversely affect our ability to satisfy the REIT income and asset tests. Accordingly, owning such a REMIC interest could adversely affect our ability to maintain our REIT qualification.

The “taxable mortgage pool” rules may increase the taxes that we or our stockholders may incur, and may limit the manner in which we effect future securitizations.

Securitizations by us or our subsidiaries could result in the creation of taxable mortgage pools for U.S. federal income tax purposes, resulting in “excess inclusion income.” As a REIT, so long as we own 100% of the equity interests in a taxable mortgage pool, we generally would not be adversely affected by the characterization of the securitization as a taxable mortgage pool. Certain categories of stockholders, however, such as non-U.S. stockholders eligible for treaty or other benefits, stockholders with net operating losses, and certain tax-exempt U.S. stockholders that are subject to unrelated business income tax, could be subject to increased taxes on a portion of their dividend income from us that is attributable to the excess inclusion income. In the case of a stockholder that is a REIT, a regulated investment company, or RIC, common trust fund or other pass-through entity, our allocable share of our excess inclusion income could be considered excess inclusion income of such entity. In addition, to the extent that our stock is owned by tax-exempt “disqualified organizations,” such as certain government-related entities and charitable remainder trusts that are not subject to tax on unrelated business income, we may incur a corporate level tax on a portion of any excess inclusion income. Because this tax generally would be imposed on us, all of our stockholders, including stockholders that are not disqualified organizations, generally would bear a portion of the tax cost associated with the classification of us or a portion of our assets as a taxable mortgage pool. A RIC, or other pass-through entity owning our stock in record name will be subject to tax at the highest U.S. federal corporate tax rate on any excess inclusion income allocated to their owners that are disqualified organizations. Moreover, we could face limitations in selling equity interests in these securitizations to outside investors, or selling any debt securities issued in connection with these securitizations that might be considered to be equity interests for tax purposes. Finally, if we were to fail to maintain our REIT qualification, any taxable mortgage pool securitizations would be treated as separate taxable corporations for U.S. federal income tax purposes that could not be included in any consolidated U.S. federal income tax return. These limitations may prevent us from using certain techniques to maximize our returns from securitization transactions.

Our ability to invest in and dispose of “to be announced” securities could be limited by our election to be subject to tax as a REIT.

We purchase agency mortgage investments through TBAs and may recognize income or gains from the disposition of those TBAs, through dollar roll transactions or otherwise. There is no direct authority with respect to the qualification of TBAs as real estate assets or U.S. Government securities for purposes of the 75% asset test or the qualification of income or gains from dispositions of TBAs as gains from the sale of real property (including interests in real property and interests in mortgages on real property) or other qualifying income for purposes of the 75% gross income test, and

we would not treat these items as qualifying assets or income (as the case may be) unless we receive a reasoned, written opinion (within the meaning of applicable U.S. Treasury Department regulations) of our counsel that such items should be treated as qualifying assets or income. Consequently, our ability to enter into dollar roll transactions and other dispositions of TBAs could be limited. Moreover, even if we were to receive the opinion of counsel described above, it is possible that the IRS could assert that such assets or income are not qualifying assets or income, which could cause us to fail the 75% asset test or the 75% gross income test.

The failure of securities subject to repurchase agreements to qualify as real estate assets could adversely affect our ability to maintain our REIT qualification.

We enter into financing arrangements that are structured as sale and repurchase agreements pursuant to which we would nominally sell certain of our securities to a counterparty and simultaneously enter into an agreement to repurchase these securities at a later date in exchange for a purchase price. Economically, these agreements are financings which are secured by the securities sold pursuant thereto. We believe that we would be treated for REIT asset and income test purposes as the owner of the securities that are the subject of any such sale and repurchase agreement notwithstanding that such agreements may transfer record ownership of the securities to the counterparty during the term of the agreement. It is possible, however, that the IRS could assert that we did not own the securities during the term of the sale and repurchase agreement, in which case we could fail to maintain our REIT qualification.

Liquidation of our assets may jeopardize our REIT qualification.

To maintain our qualification as a REIT, we must comply with requirements regarding our assets and our sources of income. If we are compelled to liquidate our investments to repay obligations to our lenders, we may be unable to comply with these requirements, ultimately jeopardizing our qualification as a REIT, or we may be subject to a 100% tax on any resultant gain if we sell assets that are treated as dealer property or inventory.

Complying with REIT requirements may limit our ability to hedge effectively and may cause us to incur tax liabilities.

The REIT provisions of the Internal Revenue Code substantially limit our ability to hedge our assets and liabilities. Under these provisions, any income from a hedging transaction we enter into to manage risk of interest rate changes with respect to borrowings made or to be made to acquire or carry real estate assets does not constitute “gross income” for purposes of the 75% or 95% gross income tests, if certain requirements are met. To the extent that we enter into other types of hedging transactions, the income from those transactions is likely to be treated as non-qualifying income for purposes of both of the REIT gross income tests.

Qualifying as a REIT involves highly technical and complex provisions of the Internal Revenue Code.

Qualification as a REIT involves the application of highly technical and complex Internal Revenue Code provisions for which only limited judicial and administrative authorities exist. Even a technical or inadvertent violation could jeopardize our REIT qualification. Our qualification as a REIT will depend on our satisfaction of certain asset, income, organizational, distribution, stockholder ownership and other requirements on a continuing basis. In addition, our ability to satisfy the requirements to maintain our REIT qualification depends in part on the actions of third parties over which we have no control or only limited influence, including in cases where we own an equity interest in an entity that is classified as a partnership for U.S. federal income tax purposes. Thus, while we intend to continue to operate so that we will qualify as a REIT, given the highly complex nature of the rules governing REITs, the ongoing importance of factual determinations, and the possibility of future changes in our circumstances, no assurance can be given that we will maintain our qualification for any particular year.

We may incur a significant tax liability as a result of selling assets that might be subject to the prohibited transactions tax if sold directly by us.

A REIT's net income from "prohibited transactions" is subject to a 100% tax. In general, "prohibited transactions" are sales or other dispositions of assets held primarily for sale to customers in the ordinary course of business. There is a risk that certain loans that we are treating as owning for U.S. federal income tax purposes and certain property received upon foreclosure of these loans will be treated as held primarily for sale to customers in the ordinary course of business. Although we expect to avoid the prohibited transactions tax by contributing those assets to one of our TRSs and conducting the marketing and sale of those assets through that TRS, no assurance can be given that the IRS will respect the transaction by which those assets are contributed to our TRS. Even if those contribution transactions are respected, our TRS will be subject to U.S. federal, state and local corporate income tax and may incur a significant tax liability as a result of those sales.

We may be subject to adverse legislative or regulatory tax changes that could reduce the market price of shares of our equity securities.

At any time, the U.S. federal income tax laws or regulations governing REITs or the administrative interpretations of those laws or regulations may be changed, possibly with retroactive effect. We cannot predict if or when any new U.S. federal income tax law, regulation or administrative interpretation, or any amendment to any existing U.S. federal income tax law, regulation or administrative interpretation, will be adopted, promulgated or become effective or whether any such law, regulation or interpretation may take effect retroactively. We and our stockholders could be adversely affected by any such change in, or any new, U.S. federal income tax law, regulation or administrative interpretation.

Distributions to tax-exempt investors may be classified as unrelated business taxable income, or UBTI, as defined under Section 512(a) of the Internal Revenue Code.

Neither ordinary nor capital gain distributions with respect to our stock nor gain from the sale of stock should generally constitute UBTI to a tax-exempt investor. However, there are certain exceptions to this rule, including: (1) part of the income and gain recognized by certain qualified employee pension trusts with respect to our stock may be treated as UBTI if shares of our stock are predominantly held by qualified employee pension trusts, and we are required to rely on a special look-through rule for purposes of meeting one of the REIT ownership tests, and we are not operated in a manner to avoid treatment of such income or gain as UBTI; (2) part of the income and gain recognized by a tax-exempt investor with respect to our stock would constitute UBTI if the investor incurs debt in order to acquire the stock; (3) part or all of the income or gain recognized with respect to our stock by social clubs, voluntary employee benefit associations, supplemental unemployment benefit trusts and qualified group legal services plans which are exempt from U.S. federal income taxation under the Internal Revenue Code may be treated as UBTI; and (4) to the extent that we are (or a part of us, or a disregarded subsidiary of ours, is) a "taxable mortgage pool," or if we hold residual interests in a REMIC, a portion of the distributions paid to a tax-exempt stockholder that is allocable to excess inclusion income may be treated as UBTI.

The value of our assets represented by our TRS is required to be limited and a failure to comply with this and certain other rules governing transactions between a REIT and its TRSs would jeopardize our REIT qualification and may result in the application of a 100% excise tax.

A REIT may own up to 100% of the stock of one or more TRSs. Other than certain activities relating to lodging and healthcare facilities, a TRS generally may engage in any business and may hold assets and earn income that would not be qualifying assets or income if held or earned directly by a REIT. No more than 20% of the value of a REIT's assets

may consist of stock or securities of one or more TRSs. In addition, the TRS rules limit the deductibility of interest paid or accrued by a TRS to its parent REIT to assure that the TRS is subject to an appropriate level of corporate taxation. The rules also impose a 100% excise tax on certain transactions between a TRS and its parent REIT, or by a TRS on behalf of its parent REIT, that are not conducted on an arm's-length basis.

Our current TRS, and any future TRSs, will pay U.S. federal, state and local income tax on their respective taxable incomes, if any. We anticipate that the aggregate value of the securities of our TRS will be less than 20% of the value of our total assets (including our TRS securities). Furthermore, we intend to monitor the value of our investments in our TRS for the purpose of ensuring compliance with TRS-ownership limitations. In addition, we will review all our transactions with our TRS to ensure that they are entered into on arm's-length terms to avoid incurring the 100% excise tax described above. There can be no assurance, however, that we will be able to continue to comply with the TRS-ownership limitation or to avoid application of the 100% excise tax discussed above.

Your investment has various U.S. federal income tax risks.

We urge you to consult your tax advisor concerning the effects of U.S. federal, state, local and foreign tax laws to you with regard to an investment in shares of our stock.

#### ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

#### ITEM 2. PROPERTIES

We do not own any real estate or other physical properties. We maintain our corporate headquarters at 230 Park Avenue, 19th Floor, New York, NY 10169 in office space furnished to us by our Manager. We reimburse our Manager under the management agreement between us for lease and other related expenses incurred in furnishing us with our offices. We believe that our property is maintained in good condition and is suitable and adequate for our purposes.

#### ITEM 3. LEGAL PROCEEDINGS

As of the date of this filing, we are not party to any litigation or legal proceeding or, to the best of our knowledge, any threatened litigation or legal proceeding.

#### ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

#### PART II



## ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

### Market Information

Our common stock is traded on the NYSE under the symbol "OAKS." The following table sets forth, for the periods indicated during the calendar year 2016 and 2017, the high and low sale price of our common stock as reported on the NYSE:

	High	Low
Year Ended December 31, 2017		
Fourth Quarter	\$4.70	\$3.92
Third Quarter	\$4.98	\$3.80
Second Quarter	\$5.61	\$4.58
First Quarter	\$5.38	\$4.52
Year Ended December 31, 2016		
Fourth Quarter	\$6.15	\$4.81
Third Quarter	\$6.19	\$5.45
Second Quarter	\$6.29	\$4.86
First Quarter	\$5.90	\$3.82

On March 15, 2018, the last reported sales price for our common stock on the New York Stock Exchange was \$3.37.

### Holders

At December 31, 2017, there were 22,143,758 shares of our common stock outstanding. As of March 15, 2018, there were 24 registered holders. The number of beneficial stockholders is substantially greater than the number of holders of record as a large portion of our stock is held through brokerage firms.

### Dividends

No dividends may be paid on our common stock unless full cumulative dividends have been paid on our preferred stock. We have paid full cumulative dividends on our preferred stock on a monthly basis since it was first issued in December 2013. From and after June 2018, the dividend on our common stock will be paid on a quarterly basis, a change from previously being paid on a monthly basis.

All dividend distributions are made with the authorization of the board of directors at its discretion and depend on such items as our REIT taxable earnings, financial condition, maintenance of REIT status, and other factors that the board of directors may deem relevant from time to time.

The holders of our common stock share proportionally on a per share basis in all declared dividends on our common stock. We intend to declare and pay on a quarterly basis dividends to holders of our common stock and declare on a quarterly basis and pay monthly dividends to holders of our preferred stock and are required to distribute to our stockholders as dividends at least 90% of our REIT taxable income, computed without regard to our net capital gains and the deduction for dividends paid, and 90% of our net income, if any (after tax) from foreclosure property in order to maintain our qualification as a REIT. See Item 1A, "Risk Factors," and Item 7, "Management's Discussion and Analysis of Financial Conditions and Results of Operations," of this Annual Report on Form 10-K, for information regarding the sources of funds used for dividends and for a discussion of factors, if any, which may adversely affect our ability to pay dividends at the same level in 2018 and thereafter.

The following table presents cash dividends declared on our common stock from January 1, 2016 through December 31, 2017:

34

---

Common Dividends			
Declared per Share			
Declaration Date	Amount	Record Date	Date of Payment
March 16, 2016	\$0.06	April 15, 2016	April 28, 2016
March 16, 2016	\$0.06	May 16, 2016	May 27, 2016
March 16, 2016	\$0.06	June 15, 2016	June 29, 2016
June 15, 2016	\$0.06	July 15, 2016	July 28, 2016
June 15, 2016	\$0.06	August 15, 2016	August 30, 2016
June 15, 2016	\$0.06	September 15, 2016	September 29, 2016
September 16, 2016	\$0.06	October 17, 2016	October 28, 2016
September 16, 2016	\$0.06	November 15, 2016	November 29, 2016
September 16, 2016	\$0.06	December 15, 2016	December 29, 2016
November 9, 2016 <sup>(1)</sup>	\$1.33	November 21, 2016	December 27, 2016
December 27, 2016	\$0.05	January 17, 2017	January 30, 2017
December 27, 2016	\$0.05	February 15, 2017	February 27, 2017
December 27, 2016	\$0.05	March 15, 2017	March 30, 2017
March 16, 2017	\$0.05	April 17, 2017	April 27, 2017
March 16, 2017	\$0.05	May 15, 2017	May 30, 2017
March 16, 2017	\$0.05	June 15, 2017	June 29, 2017
June 14, 2017	\$0.05	July 17, 2017	July 28, 2017
June 14, 2017	\$0.05	August 15, 2017	August 30, 2017
June 14, 2017	\$0.05	September 15, 2017	September 28, 2017
September 15, 2017	\$0.05	October 16, 2017	October 30, 2017
September 15, 2017	\$0.05	November 15, 2017	November 29, 2017
September 15, 2017	\$0.05	December 15, 2017	December 28, 2017

(1) One-time deficiency dividend, subject to stockholder election to receive entirely in stock or in cash. If no election was made, the entire dividend was paid in shares of common stock based on the average closing stock price of the Company for the ten trading days ending December 22, 2016. To the extent the cash alternative was oversubscribed, each stockholder electing the cash alternative received a pro-rata amount of cash and stock with such cash component being no less than \$0.2655 per share. On December 27, 2016, the cash portion of the deficiency paid was \$3,878,042 and the stock portion of the deficiency dividend was represented by the issuance of 2,936,864 common shares at a price of \$5.28 per share.

#### Securities Authorized for Issuance under Equity Compensation Plan

The Five Oaks Investment Corp. Manager Equity Plan, or the Manager Equity Plan, includes provisions for grants of restricted common stock and other equity based awards to our Manager and to our independent directors, consultants or officers whom we may directly employ in the future, if any. In turn, our Manager grants such awards to its employees, officers (including our current officers), members, directors or consultants. The total number of shares that may be granted subject to awards under the Manager Equity Plan is equal to an aggregate of 3.0% of the total number of issued and outstanding shares of our common stock (on a fully diluted basis) at the time of each award (other than any shares issued or subject to awards made pursuant to the Manager Equity Plan).

#### Purchases of Equity Securities by the Issuer and Affiliated Purchasers

On December 16, 2015, we announced a share repurchase program, pursuant to which our Board authorized us to repurchase up to \$10 million of our common shares. Under this program, we have discretion to determine the dollar amount of common shares to be repurchased and the timing of any repurchases in compliance with applicable law and

regulations. The program does not have an expiration date.

As of December 31, 2017, we had repurchased 126,856 shares under the program for a total cost of \$645,394. The Company did not purchase any common shares under the plan during the three months ended December 31, 2017.

#### Performance Graph

The following line graph sets forth, for the period from March 22, 2013 through December 31, 2017, a comparison of the percentage change in the cumulative total stockholder return on our common stock compared to the cumulative total return of the Standard and Poor's 500 Stock Index, or the S&P 500, and the FTSE National Association of Real Estate Investment Trusts Mortgage REIT Index, or the NAREIT Mortgage REIT Index.

Index	03/22/2013	12/31/2013	12/31/2014	12/31/2015	12/31/2016	12/31/2017
Five Oaks Investment Corp	100	77	91	54	71	65
S&P 500	100	122	138	140	157	191
NAREIT Mortgage REIT Index	100	85	99	90	110	130

The foregoing graph shall not be deemed incorporated by reference by any general statement incorporating by reference this Annual Report on Form 10-K into any filing under the Securities Act of 1933 or under the Securities Exchange Act of 1934, except to the extent we specifically incorporate this information by reference, and shall not otherwise be deemed filed under those acts.

This information is derived from sources which management believes to be reliable. The historical information set forth above is not necessarily indicative of future performance. Accordingly, we do not make or endorse any predictions as to future share performance.

## ITEM 6. SELECTED FINANCIAL DATA

Our selected financial data set forth below is derived from our audited financial statements and should be read in conjunction with our consolidated financial statements and the accompanying notes, included under Item 8 of this Annual Report on Form 10-K.

Balance Sheet Data<sup>(1) (2)</sup>

	December 31, 2017	December 31, 2016	December 31, 2015	December 31, 2014	December 31, 2013
Available-for-sale securities	\$1,290,825,648	\$870,929,601	\$571,466,581	\$368,315,738	\$444,984,955
Mortgage loans held-for-sale	—	2,849,536	10,900,402	54,678,382	—
Multi-family loans held in securitization trusts	1,130,874,274	1,222,905,433	1,449,774,383	1,750,294,430	—
Residential loans held in securitization trusts	119,756,455	141,126,720	411,881,097	631,446,984	—
Mortgage servicing rights	2,963,861	3,440,809	4,268,673	—	—
Linked Transaction, net	—	—	—	60,818,111	33,352,562
Cash and cash equivalents	34,347,339	27,534,374	26,140,718	32,274,285	33,062,931
Other assets <sup>(2)</sup>	33,773,539	30,814,730	23,934,807	24,381,627	16,800,957
Total assets	\$2,612,541,116	\$2,299,601,203	\$2,498,366,661	\$2,922,209,557	\$528,201,405
Repurchase agreements					
Available-for-sale securities	1,234,522,000	804,811,000	509,231,000	544,614,000	412,172,000
Mortgage loans held-for-sale	—	—	9,504,457	50,263,852	—
FHLBI advances	—	—	49,697,000	—	—
Multi-family securitized debt obligations	1,109,204,743	1,204,583,678	1,364,077,012	1,670,573,456	—
Residential securitized debt obligations	114,418,318	134,846,348	380,638,423	432,035,976	—
Other liabilities	8,604,778	12,893,312	7,724,241	11,924,143	2,104,043
Total stockholders' equity	145,791,277	142,466,865	177,494,528	212,798,130	113,925,362
Total liabilities and stockholders' equity	\$2,612,541,116	\$2,299,601,203	\$2,498,366,661	\$2,922,209,557	\$528,201,405

(1) Our consolidated balance sheets include assets and liabilities of consolidated variable interest entities ("VIEs") as the Company is the primary beneficiary of these VIEs. As of December 31, 2017, 2016, 2015, 2014 and 2013, assets of consolidated VIEs totaled \$1,255,404,335, \$1,369,120,941, \$1,868,482,556, \$2,389,784,101 and \$0, respectively, and the liabilities of consolidated VIEs totaled \$1,228,295,517, \$1,344,404,080, \$1,750,916,265, \$2,180,936,221 and \$0, respectively.

(2) Includes \$11,275,263, \$10,355,222, \$8,174,638, \$11,400,645 and \$13,343,173 in restricted cash for December 31, 2017, 2016, 2015, 2014 and 2013, respectively; restricted cash represents our cash held by counterparties as collateral against our securities, derivatives and/or repurchase agreements.

## Statement of Operation Data

\$ in thousands, except per share data

Year Ended December	Year Ended December	Year Ended December	Year Ended December	Year Ended December
---------------------------	---------------------------	---------------------------	---------------------------	---------------------------

Edgar Filing: Five Oaks Investment Corp. - Form 10-K

	31, 2017	31, 2016	31, 2015	31, 2014	31, 2013
Interest income	\$ 89,133	\$ 93,122	\$ 114,415	\$ 45,813	\$ 16,424
Interest expense	(68,994 )	(69,533 )	(83,105 )	(27,841 )	(2,244 )
Net interest income	20,139	23,589	31,310	17,972	14,180
Other-than-temporary impairment	—	(725 )	(3,636 )	—	—
Other income (loss)	(2,574 )	(16,088 )	(10,102 )	(3,123 )	(6,052 )
Total expenses	12,859	14,765	17,121	11,535	4,902
Net income (loss)	4,707	(7,990 )	450	3,314	3,226
Net income (loss) attributable to common stockholders (basic and diluted)	1,185	(11,512 )	(3,072 )	426	3,182
Earnings (loss) per share:					
Net income (loss) attributable to common stockholders (basic and diluted)	1,185	(11,512 )	(3,072 )	426	3,182
Dividends declared on common stock	(11,904 )	(29,899 )	(19,875 )	(18,230 )	(10,083 )
Weighted average number of shares of common stock	20,048,128	14,641,701	14,721,074	12,358,587	6,132,702
Basic and diluted income (loss) per share	0.06	(0.79 )	(0.21 )	0.03	0.52

## ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with our consolidated financial statements and the accompanying notes included in this Annual Report on Form 10-K. The following discussion contains forward-looking statements that reflect our current expectations, estimates, forecasts and projections.

### Overview

We are a Maryland corporation that, together with our subsidiaries, is focused on investing on a leveraged basis in mortgage-backed securities, or MBS, mortgage loans and other real estate-related assets. Our capital has primarily been invested in Agency RMBS, with a particular focus on shorter duration Agency securities backed by hybrid ARMs. Additionally, we have continued to maintain exposure to Multi-Family MBS, principally through owning subordinated and first-loss tranches in Freddie Mac K-series securitizations. We have sought to do so while reducing our reliance on short-term repurchase agreement financing, including through the use of re-securitization, or re-REMIC, financings.

In January 2018 we entered into a series of transactions with subsidiaries of the Hunt Companies, Inc., a holding company that invests in businesses focused in the real estate and infrastructure markets, including investment management, mortgage banking, direct lending, loan servicing, asset management, property management, development, construction, consulting and advisory. We entered into a new management agreement with Hunt Investment Management, LLC, while another affiliate of Hunt purchased an ownership stake of approximately 9.5% through a combination of a privately-placed stock issuance and a purchase from our largest stockholder, XL Investments Ltd. The transactions are expected to provide us with a new strategic direction through the reallocation of capital into new investment opportunities in the commercial real estate space, and in particular direct access to Hunt's significant pipeline of specified transitional floating-rate multi-family and commercial real estate loans. Hunt and its affiliates have extensive experience in the origination, servicing, risk management and financing of this asset class and the floating-rate nature of the loans should reduce or eliminate the need for complex interest-rate hedging. Subject to our ability to put in place term repurchase facilities and/or collateralized loan obligations of the type Hunt has historically used to finance this asset class, we intend to transition the portfolio towards loan assets that are positively correlated with rising interest rates and that have exhibited strong historical credit performance.

Accordingly, in furtherance of our objective to provide attractive cash flow returns over time to our investors, our investment strategy is to invest in the following assets:

- Transitional multi-family and other commercial real estate loans, which are floating-rate loans secured by multi-family and other commercial real estate properties that are not guaranteed by a U.S. Government sponsored entity, or securitizations backed by such loans;
- Securitizations backed by multi-family mortgage loans, or Multi-Family MBS;
- Agency RMBS, which are residential mortgage-backed securities, for which a U.S. Government agency such as Ginnie Mae or a federally chartered corporation such as Fannie Mae or Freddie Mac, guarantees payments of principal and interest on the securities;
- To a limited extent, Non-Agency RMBS, which are RMBS that are not issued or guaranteed by a U.S. Government-sponsored entity; and
- Other mortgage-related investments, including mortgage servicing rights, or MSRs, CMBS, or other loans or securities backed by real estate.

We finance our current investments in Agency RMBS, Multi-Family MBS and Non-Agency RMBS primarily through short-term borrowings structured as repurchase agreements. We intend to finance our intended investments in transitional multi-family and other commercial real estate loans primarily through medium term borrowings structured



either as repurchase agreements or secured loan facilities. Our primary sources of income are net interest income from our investment portfolio and non-interest income from our mortgage loan-related activities. Net interest income represents the interest income we earn on investments less the expenses of funding these investments.

With effect from January 18, 2018, we are now externally managed and advised by Hunt Investment Management, LLC (“HIM”), pursuant to a management agreement between us and HIM, and the simultaneous termination of our previous management agreement with Oak Circle. As our Manager, HIM implements our business strategy, performs investment advisory services and activities with respect to our assets and is responsible for performing all of our day-to-day operations. HIM is an investment adviser registered with the SEC.

Pursuant to the terms of the new management agreement, we are required to pay our Manager an annual base management fee of 1.50% of Stockholders’ Equity (as defined in the management agreement, payable quarterly (0.375% per quarter) in arrears. Starting in the first full calendar quarter following January 18, 2019, we are also required to pay our Manager a quarterly incentive fee equal to 20% of the excess of Core Earnings (as defined in the management agreement) over a hurdle rate of 8% per annum. We are required to reimburse the Manager for costs associated with (i) an allocable share of the costs of non-investment personnel of the Manager and its affiliates who spend all or a portion of their time managing our affairs and operations, (ii) our CFO, (iii) our general counsel, in each case, based on a percentage of his time spent on the Company’s affairs. Such reimbursement is subject to a cap of 1.5% of the average Stockholders’ Equity (as defined in the management agreement) for the applicable fiscal year. We are also required to reimburse the Manager for other costs and expenses associated with our operations, including but not limited to, the costs and expenses associated with our formation and capital raising activities, rent, utilities, office furniture, equipment, machinery and other overhead type expenses, the costs of legal, accounting, auditing, tax planning and tax return preparation, consulting services and insurance.

On January 18, 2018, we and Oak Circle, entered into a Termination Agreement (“Termination Agreement”) pursuant to which we and Oak Circle agreed to mutually and immediately terminate that certain management agreement, dated May 16, 2012, by and between us and Oak Circle. Under the terms of the Termination Agreement, the termination of the management agreement with Oak Circle did not trigger, and Oak Circle was not paid, a termination fee by us. Hunt separately agreed to pay Oak Circle a negotiated payment in connection with the foregoing.

We have elected to be taxed as a REIT and comply with the provisions of the Internal Revenue Code with respect thereto. Accordingly, we are generally not subject to federal income tax on our REIT taxable income that we currently distribute to our stockholders so long as we maintain our qualification as a REIT. Our continued qualification as a REIT depends on our ability to meet, on a continuing basis, various complex requirements under the Internal Revenue Code relating to, among other things, the source of our gross income, the composition and values of our assets, our distribution levels and the concentration of ownership of our capital stock. Even if we maintain our qualification as a REIT, we may become subject to some federal, state and local taxes on our income generated in our wholly owned taxable REIT subsidiary, Five Oaks Acquisition Corp., or FOAC.

## 2017 Highlights

- We reported an economic loss on common equity of 8.2%, comprised of a \$1.09 decrease in net book value per share that more than offset a \$0.60 dividend per common share.
- We continued the reduction of our credit risk MBS exposure during 2017. We reduced our Non-Agency exposure from \$12.8 million at December 31, 2016 to \$4.4 million at December 31, 2017 (on a non-GAAP, combined basis), and reduced our Multi-Family MBS exposure from \$91.5 million at December 31, 2016 to \$27.4 million at December 31, 2017 (on a non-GAAP combined basis); since year end, we have sold \$5.9 million of the remaining Multi-Family exposure. We also completed the sale of all remaining residential mortgage loans prior to year-end.
- We continued to redeploy the capital released from selling down our credit exposure into Agency RMBS, which increased from \$790.2 million at December 31, 2016 to \$1,285.1 million at December 31, 2017. In order to minimize the potential impact of interest rate volatility, the increase was composed of purchases of Agency hybrid-ARMs.
- On June 16, 2017, we issued 4,600,000 shares of common stock, inclusive of the underwriters' overallotment option, for \$4.60 per share, raising net proceeds of approximately \$19.8 million.
- The Hunt Transaction

On January 18, 2018, we announced a new strategic direction, and the entry into a new external management agreement with Hunt Investment Management, LLC, an affiliate of the Hunt Companies, Inc. ("Hunt") and the concurrent mutual termination of our management agreement with Oak Circle. Management by Hunt is expected to provide Five Oaks with a new strategic direction through the reallocation of capital into new investment opportunities focused in the commercial real estate mortgage space and direct access to Hunt's significant pipeline of transitional floating-rate multi-family and commercial real estate loans. Hunt and its affiliates have extensive experience in the origination, servicing, risk management and financing of this asset class and the floating-rate nature of the loans should reduce or eliminate the need for complex interest-rate hedging. The new management agreement is expected to better align our interests with those of our new manager through an incentive fee arrangement and agreed upon limitations on manager expense reimbursements from us, as further described below. Pursuant to the terms of the termination agreement between Five Oaks and Oak Circle, the termination of the prior management agreement did not trigger, and Oak Circle was not paid, a termination fee by us. Hunt separately agreed to pay Oak Circle a negotiated payment in connection with the termination agreement.

In connection with the transaction, an affiliate of Hunt purchased 1,539,406 shares of our common stock in a private placement, at a purchase price of \$4.77 per share resulting in an aggregate capital raise of \$7,342,967. In addition, such Hunt affiliate also purchased 710,495 Five Oaks shares from our largest shareholder, XL Investments Ltd. ("XL Investments"), for the same price per share. The purchase price per share represents a 56.9% premium over the Five Oaks common share price as of the closing on January 17, 2018. In connection with the acquisition of shares from XL Investments, XL Investments agreed to terminate all of its currently held Five Oaks warrants. After completion of these share purchases, Hunt and its affiliates own approximately 9.5% of Five Oaks outstanding common shares. Also in connection with the transaction, and as further described in Sections 10 hereof and in our Current Report on Form 8-K filed with the Securities and Exchange Commission on January 18, 2018, David Carroll resigned as a director, Chairman and CEO of the Company and the Five Oaks board appointed James C. ("Chris") Hunt as a director and Chairman of the board and named James P. Flynn as CEO of Five Oaks and Michael P. Larsen President of Five Oaks.

## FOAC and Changes to Our Residential Mortgage Loan Business

In June 2013, we established FOAC as a Taxable REIT Subsidiary, or TRS, to increase the range of our investments in mortgage-related assets. Until August 1, 2016, FOAC aggregated mortgage loans primarily for sale into securitization transactions, with the expectation that we would purchase the subordinated tranches issued by the related securitization trusts, and that these will represent high quality credit investments for our portfolio. Residential

mortgage loans for which FOAC owns the MSR continue to be directly serviced by one or more licensed sub-servicers since FOAC does not directly service any residential mortgage loans.

As noted earlier, we previously determined to cease the aggregation of prime jumbo loans for the foreseeable future, and therefore no longer maintain warehouse financing to acquire prime jumbo loans. We do not expect the changes to our mortgage loan business strategy to impact the existing MSRs that we own, or the securitizations we have sponsored to date.

#### Multi-Family and Residential Mortgage Loan Consolidation Reporting Requirements

As of December 31, 2017, we have determined that we are the primary beneficiary of two Multi-Family MBS securitization trusts, the FREMF 2011-K13 Trust and the FREMF 2012-KF01 Trust, and one prime jumbo residential mortgage securitization trust, CSMC 2014-OAK1, based in each case on our ownership of all or substantially all of the most subordinated, or first-loss, tranches in each transaction as well as the related control rights.

We have elected the fair value option on the assets and liabilities held within each of the three trusts. In accordance with ASU 2014-13, we are required to determine whether the fair value of the financial assets or the fair value of the financial liabilities of each trust is more observable, but in either case, the methodology results in the fair value of the assets of each trust being equal to the fair value of the respective trust's liabilities.

Securitization trusts are structured as pass through entities that receive principal and interest on the underlying collateral and distribute those payments to the certificate holders. Although our consolidated balance sheet at December 31, 2017 includes the gross assets and liabilities of the three trusts, the assets of each trust are restricted and can only be used to fulfill the obligations of the individual entity. Additionally, the obligations of the trusts do not have any recourse to us as the consolidator of the trusts. Accordingly, we are only exposed to the risk of loss on our net investment in the trusts.

We do not have any claims to the assets (other than the security represented by our first loss piece) or obligations for the liabilities of any of the trusts. Our maximum exposure to loss from our consolidation is our carrying value of \$27.1 million as of December 31, 2017, which represents our net aggregate investment in the trusts as set out below. As a result, for the purpose of describing our investment activities, we may present them on a net investment basis.

As of December 31, 2017, we had \$2,612,541,116 of total assets on a GAAP basis, as compared to \$2,299,601,203 as of December 31, 2016. A reconciliation of our net investment in the trusts with our consolidated financial statements as of December 31, 2017 and December 31, 2016 follows:

	December 31, 2017	December 31, 2016
Multi-family mortgage loans held in securitization trusts, at fair value <sup>(1)</sup>	\$1,135,251,880	\$1,227,523,075
Multi-family securitized debt obligations <sup>(2)</sup>	\$1,113,556,782	\$1,209,181,035
Net investment amount of Multi-Family MBS trusts held by us	\$21,695,098	\$18,342,040
Residential mortgage loans held in securitization trusts, at fair value <sup>(1)</sup>	\$120,152,455	\$141,597,866
Residential securitized debt obligations <sup>(2)</sup>	\$114,738,735	\$135,223,045
Net investment amount of residential mortgage loan trusts held by us	\$5,413,720	\$6,374,821

(1) Includes related receivables

(2) Includes related payables

### Five Oaks Insurance

On January 12, 2016, the regulator of the FHLB system, the Federal Housing Finance Agency, or the FHFA, published a Final Rule that amended FHLB membership regulations for captive insurance subsidiaries. Under the regulations, FOI was required to terminate its membership and repay its advances on or before February 19, 2017 in order to be eligible for timely full stock redemption. On July 18, 2016, the State of Michigan Department of Financial Services approved FOI's order for voluntary dissolution. All FHLBI advances were repaid and all of the FHLBI stock had been redeemed prior to the end of 2016.

### Factors Impacting Our Operating Results

**Market conditions.** The results of our operations are and will continue to be affected by a number of factors and primarily depend on, among other things, the level of our net interest income, the market value of our assets and the supply of, and demand for, our target assets in the marketplace. Our net interest income, which reflects the amortization of purchase premiums and accretion of purchase discounts, will vary primarily as a result of changes in market interest rates and prepayment speeds, as measured by the constant prepayment rate, or CPR, on our MBS and mortgage loans. Interest rates vary according to the type of investment, conditions in the financial markets, competition and other factors, none of which can be predicted with any certainty. Our operating results are also impacted by unanticipated credit events experienced by borrowers whose mortgage loans are included in our MBS, or whose loans we own directly. Our operating results will also be affected by general U.S. residential real estate fundamentals and the overall U.S. economic environment. In particular, our strategy is influenced by the specific characteristics of the residential real estate markets, including prepayment rates, credit market conditions and interest rate levels.

On December 13, 2017, based on its outlook for economic activity, the labor market and inflation and weighing the uncertainties associated with this outlook, the Federal Reserve raised its target range for the federal funds rate to 1-¼ to 1-½ percent and on January 31, 2018, maintained the target range at 1-¼ to 1-½ percent. The Federal Reserve also indicated that it would likely contemplate additional rate increases in 2018 and beyond in a manner consistent with policy normalization, while indicating that such additional increases would likely be gradual and data dependent. Additionally, the Federal Reserve initiated its balance sheet normalization program in October 2017 that was announced in June 2017. This plan details the approach the FOMC intends to use to reduce the Federal Reserve's holding of Treasury and agency securities. For payments of principal that the Federal Reserve receives from its holdings of agency debt and mortgage-backed securities, the Committee anticipates that the cap will be \$4 billion per month and will increase in steps of \$4 billion in three-month intervals over 12 months until it reaches \$20 billion per month. There is still considerable uncertainty concerning the speed at which the Federal Reserve will continue to raise rates. Such uncertainty and volatility often leads to asset price volatility, wider spreads and increased hedging costs, which in turn could adversely affect our business, financial condition, results of operation and our ability to make

distributions to our stockholders.

**Changes in market interest rates.** With respect to our business operations, increases in interest rates, in general, may over time cause: (1) the value of our MBS and loan portfolio to decline; (2) coupons on our adjustable-rate and hybrid RMBS to reset, although on a delayed basis, to higher interest rates; (3) prepayments on our MBS and loan portfolio to slow, thereby slowing the amortization of our purchase premiums and the accretion of our purchase discounts; (4) the interest expense associated with our borrowings to increase; and (5) to the extent we enter into Eurodollar futures contracts or other derivative contracts as part of our hedging strategy, the value of these agreements to increase. Conversely, decreases in interest rates, in general, may over time cause: (1) prepayments on our MBS and loan portfolio to increase, thereby accelerating the amortization of our purchase premiums and the accretion of our purchase discounts; (2) the value of our MBS and loan portfolio to increase; (3) coupons on our adjustable-rate and hybrid RMBS to reset, although on a delayed basis, to lower interest rates; (4) the interest expense associated with our borrowings to decrease; and (5) to the extent we enter into Eurodollar futures contracts or other derivative contracts as part of our hedging strategy, the value of these agreements to decrease.

**Credit risk.** We are subject to varying degrees of credit risk in connection with our Non-Agency RMBS and Multi-Family MBS investments. Our Manager seeks to mitigate this credit risk by estimating expected losses on these assets and purchasing such assets at appropriate discounted prices, e.g. for Non-Agency RMBS. Nevertheless, unanticipated credit losses could occur, which could adversely impact our operating results. Additionally, if the market's view of credit risk deteriorates, or the yield required to invest in such credit risk increases, this will generally lead to an increase in credit spreads, and a resultant decline in the market prices of such assets, even if our estimate of expected losses does not change. In turn, this can be expected to lead to a reduction in our stockholders' equity, and may also trigger margin calls under our repurchase agreements used to finance our credit sensitive assets.

**Liquidity and financing markets.** Liquidity is a measurement of our ability to meet potential cash requirements, including ongoing commitments to pay dividends, fund investments and repay borrowings and other general business needs. Our primary sources of liquidity are net proceeds of common or preferred stock issuance, net cash provided by operating activities, cash from repurchase agreements, and other financing arrangements. We previously noted a tightening trend in the balance sheet capacity of repurchase agreement counterparties due to a combination of higher capital requirements such as Basel III capital reforms, other regulatory restrictions, enhanced risk management and generally lower risk appetite among many financial institutions. Consequently, we have observed a reduced willingness of certain financial institutions to commit capital to support the trading of fixed income securities, and in turn, a consequent reduction in certain cases in the availability of financing for certain credit-sensitive MBS. We anticipate our primary sources of financing in 2018 will be repurchase agreements and other similar financing arrangements.

**Prepayment speeds.** Prepayment speeds, as reflected by the CPR, vary according to interest rates, the type of residential mortgage loan, conditions in financial markets and housing markets, availability of residential mortgages, borrowers' credit profiles, competition and other factors, none of which can be predicted with any certainty. CPR, expressed as a percentage over a pool of residential mortgages, is the rate at which principal is expected to prepay in the given

year (usually the next one). For example, if a certain residential mortgage loan pool has a CPR of 9%, then 9% of the existing pool principal outstanding is expected to prepay over the next year. In general, when interest rates rise, it is relatively less attractive for borrowers to refinance their residential mortgage loans, and as a result, prepayment speeds tend to decrease. When interest rates fall, however, prepayment speeds tend to increase. When house price appreciation is positive, prepayment rates may increase, and when house prices depreciate in value, prepayment rates may decline. For RMBS and loans purchased at a premium, as prepayment speeds increase, the amount of income we will earn on these investments will be less than expected because the purchase premium we will pay for the bonds amortizes faster than expected. Conversely, decreases in prepayment speeds result in income greater than expected and can extend the period over which we amortize the purchase premium. For RMBS and loans purchased at a discount, as prepayment speeds increase, the amount of income we will earn will be greater than expected because of the acceleration of the accretion of the discount into interest income. Conversely, decreases in prepayment speeds result in income less than expected and can extend the period over which we accrete the purchase discount into interest income. Generally, our Multi-Family MBS investments are not subject to prepayment risk, because scheduled repayments on the underlying multi-family mortgage loans are allocated to the most senior security in each transaction, and unscheduled repayments are held in the trust until the maturity date of the MBS securities. As a result, our Multi-Family MBS investments are generally scheduled to be repaid in full on a bullet maturity date.

**Changes in market value of our assets.** Other than residential mortgage loans that we previously owned, as discussed below, it is our business strategy to hold our target assets as long-term investments. As such, our investment securities (with the exception of Non-Agency RMBS IOs) are carried at their fair value, as available-for-sale, or AFS, when applicable, in accordance with ASC 320-10 "Investments-Debt and Equity Securities," with changes in fair value recorded through accumulated other comprehensive income/(loss), a component of stockholders' equity, rather than through earnings. However, at least on a quarterly basis, we monitor our target assets for other-than-temporary impairment, which could result in our recognizing a charge through earnings. See "Critical Accounting Policies" for further details. The primary exception to this accounting policy relates to residential mortgage loans, which we previously held with the intent to sell, either into a securitization transaction, or into the secondary market. We have elected the fair value option for mortgage loan assets, as well as Non-Agency RMBS IOs, and as such, changes in the market value of these assets will directly impact our earnings. In addition, to the extent that as a result of our purchase of subordinated securities issued by Multi-Family MBS and residential mortgage loan securitization trusts, we determine that we are the primary beneficiary of these trusts and accordingly consolidate their assets and liabilities; we have elected the fair value option in respect of these trusts. As such, changes in the market values of the consolidated trusts will also directly impact our earnings.

**Governmental actions.** Since 2008, when both Fannie Mae and Freddie Mac were placed under the conservatorship of the U.S. government, there have been a number of proposals to reform the U.S. housing finance system in general, and Fannie Mae and Freddie Mac in particular. As a result of the recent change in the presidential administration, we anticipate debate on residential housing and mortgage reform to continue into 2018 and beyond, but a deep divide persists between factions in Congress and as such it remains unclear what shape any reform would take and what impact, if any, reform would have on mortgage REITs.

#### Investment Portfolio

On a GAAP basis, we had increased our overall investments in MBS from \$870.9 million as of December 31, 2016 to \$1,290.8 million as of December 31, 2017. Within this total, on a year-over-year basis we had increased our Agency RMBS from \$790.2 million to \$1,285.1 million, decreased our Non-Agency RMBS from \$7.6 million to \$0.0 million and decreased our Multi-Family MBS from \$73.1 million to \$5.7 million. These changes reflect the application of our current investment strategy discussed under "Overview".

On a non-GAAP basis, our MBS investments increased from \$894.5 million as of December 31, 2016 to \$1,316.9 million as of December 31, 2017. The non-GAAP total includes our net investment in our consolidated Multi-Family MBS and residential mortgage loan trusts. Within these totals, on a year-over-year basis we had increased our Agency RMBS from \$790.2 million to \$1,285.1 million, decreased our Non-Agency RMBS from \$12.8 million to \$4.4 million and decreased our Multi-Family MBS from \$91.5 million to \$27.4 million. As of December 31, 2017, on a GAAP and non-GAAP basis, our investment in residential mortgage loans decreased from \$2.8 million at December 31, 2016 to \$0.0 million December 31, 2017.

We use leverage to increase potential returns to our stockholders. To that end, subject to maintaining our qualification as a REIT and our exclusion from registration under the Investment Company Act, we use borrowings to fund the origination or acquisition of our target assets. We accomplish this by borrowing against existing assets through repurchase agreements. Neither our organizational documents nor our investment guidelines place any limit on the maximum amount of leverage that we may use, and we are not required to maintain any particular debt-to-equity leverage ratio. We may also change our financing strategy and leverage without the consent of our stockholders.

The leverage that we employ is specific to each asset class in which we invest and will be determined based on several factors, including potential asset price volatility, margin requirements, the current cycle for interest rates, the shape of the yield curve, credit, security price, the outlook for interest rates and our ability to use and the effectiveness of interest rate hedges. We analyze both historical interest rate and credit volatility and market-driven implied volatility for each asset class in order to determine potential asset price volatility. Our leverage targets attempt to risk-adjust asset classes based on each asset class's potential price volatility. The goal of our leverage strategy is to ensure that, at all times, our investment portfolio's leverage ratio is appropriate for the level of risk inherent in the investment portfolio and that each asset class has individual leverage targets that are appropriate for its potential price volatility.

The following tables summarize certain characteristics of our investment portfolio as of December 31, 2017 and December 31, 2016 (i) as reported in accordance with GAAP, which excludes our net investment in Multi-Family MBS and prime jumbo mortgage securitization trusts; (ii) to show separately our net investments in Multi-Family MBS and prime jumbo mortgage securitization trusts; and (iii) on a non-GAAP combined basis (which reflects the inclusion of our net investment in Multi-Family MBS and prime jumbo mortgage securitization trusts combined with our GAAP-reported MBS):

December 31, 2017  
GAAP Basis

	Principal Balance	Unamortized Premium (Discount)	Designated Credit Reserve	Amortized Cost	Unrealized Gain/ (Loss)	Fair Value	Net Weighted Average Average Yield <sup>(2)</sup> Coupon <sup>(1)</sup>		
\$ in thousands									
Agency RMBS									
15 year fixed-rate	\$842	\$20	\$	—\$862	\$(16)	) \$846	2.50 %	1.83 %	
Hybrid RMBS	1,273,487	23,308	—	1,296,795	(12,557)	) 1,284,238	2.66 %	2.49 %	
Total Agency RMBS	1,274,329	23,328	—	1,297,657	(12,573)	) 1,285,084	2.66 %	2.49 %	
Non-Agency RMBS	—	—	—	—	—	—	—	—	
Non-Agency MBS IO, fair value option	—	—	—	—	—	—	—	—	
Total Non-Agency RMBS	—	—	—	—	—	—	—	—	
Multi-Family MBS	—	—	—	—	—	—	—	—	
Multi-Family MBS PO	7,500	(1,714)	) —	5,786	(44)	) 5,742	—	6.86 %	
Multi-Family MBS PO, fair value option	—	—	—	—	—	—	—	—	
Total Multi-Family MBS	7,500	(1,714)	) —	5,786	(44)	) 5,742	—	6.86 %	
Total/Weighted Average (GAAP)	\$1,281,829	\$21,614	\$	—\$1,303,443	\$(12,617)	) \$1,290,826	2.65 %	2.51 %	



## Non-GAAP Adjustments

	Principal Balance	Unamortized Premium (Discount)	Designated Credit Reserve	Amortized Cost	Unrealized Gain/(Loss)	Fair Value	Net Weighted Average Average Yield <sup>(2)</sup> Coupon <sup>(1)</sup>		
\$ in thousands									
Agency RMBS									
15 year fixed-rate	\$—	\$ —	\$	—\$ —	\$ —	\$ —	—	—	—
Hybrid RMBS	—	—	—	—	—	—	—	—	—
Total Agency RMBS	—	—	—	—	—	—	—	—	—
Non-Agency RMBS	4,345	(1,086 )	—	3,259	45	3,304	3.73 %	4.97 %	
Non-Agency MBS IO, fair value option	122,267	—	—	7,805	(6,709 )	1,096	0.37 %	5.72 %	
Total Non-Agency RMBS	126,612	(1,086 )	—	11,064	(6,664 )	4,400	0.48 %	5.50 %	
Multi-Family MBS	8,197	(2,689 )	—	5,508	1,911	7,419	3.80 %	5.66 %	
Multi-Family MBS PO	—	—	—	—	—	—	—	—	
Multi-Family MBS PO, fair value option	21,940	—	—	10,483	3,793	14,276	—	—	
Total Multi-Family MBS	30,137	(2,689 )	—	15,991	5,704	21,695	1.03 %	1.95 %	
Total/Weighted Average (non-GAAP)	\$156,749	\$ (3,775 )	\$	—\$ 27,055	\$ (960 )	\$ 26,095	0.59 %	3.40 %	

## Non-GAAP Basis

	Principal Balance	Unamortized Premium (Discount)	Designated Credit Reserve	Amortized Cost	Unrealized Gain/(Loss)	Fair Value	Net Weighted Average Coupon <sup>(1)</sup>	Average Yield <sup>(2)</sup>
\$ in thousands								
Agency RMBS								
15 year fixed-rate	\$842	\$20	\$	—\$862	\$(16 )	\$846	2.50 %	1.83 %
Hybrid RMBS	1,273,487	23,308	—	1,296,795	(12,557 )	1,284,238	2.66 %	2.49 %
Total Agency RMBS	1,274,329	23,328	—	1,297,657	(12,573 )	1,285,084	2.66 %	2.49 %
Non-Agency RMBS	4,345	(1,086 )	—	3,259	45	3,304	3.73 %	4.97 %
Non-Agency MBS IO, fair value option	122,267	—	—	7,805	(6,709 )	1,096	0.37 %	5.72 %
Total Non-Agency RMBS	126,612	(1,086 )	—	11,064	(6,664 )	4,400	0.48 %	5.50 %
Multi-Family MBS	8,197	(2,689 )	—	5,508	1,911	7,419	3.80 %	5.66 %
Multi-Family MBS PO	7,500	(1,714 )	—	5,786	(44 )	5,742	—	6.86 %
Multi-Family MBS PO, fair value option	21,940	—	—	10,483	3,793	14,276	—	—
Total Multi-Family MBS	37,637	(4,403 )	—	21,777	5,660	27,437	0.83 %	3.26 %
Total/Weighted Average (non-GAAP)	\$1,438,578	\$17,839	\$	—\$1,330,498	\$(13,577 )	\$1,316,921	2.42 %	2.53 %

(1) Weighted average coupon is presented net of servicing and other fees.

(2) Average yield incorporates future prepayment assumptions as discussed in Note 2 to our consolidated financial statements.

December 31, 2016

GAAP Basis

	Principal Balance	Unamortized Premium (Discount)	Designated Credit Reserve	Amortized Cost	Unrealized Gain/(Loss)	Fair Value	Net Weighted Average Coupon <sup>(1)</sup>	Average Yield <sup>(2)</sup>
\$ in thousands								
Agency RMBS								
15 year fixed-rate	\$1,458	\$34	\$—	\$1,492	\$(29)	\$1,463	2.50 %	1.89 %
Hybrid RMBS	777,761	16,403	—	794,164	(5,437)	788,727	2.51 %	2.12 %
Total Agency RMBS	779,219	16,437	—	795,656	(5,466)	790,190	2.51 %	2.12 %
Non-Agency RMBS	4,394	(370)	(1,930)	2,094	235	2,329	0.93 %	11.68 %
Non-Agency MBS IO, fair value option	509,109	—	—	14,712	(9,448)	5,264	0.32 %	11.03 %
Total Non-Agency RMBS	513,503	(370)	(1,930)	16,806	(9,213)	7,593	0.32 %	11.11 %
Multi-Family MBS	—	—	—	—	—	—	—	—
Multi-Family MBS PO	100,908	(26,160)	—	74,748	(1,601)	73,147	—	6.77 %
Multi-Family MBS PO, fair value option	—	—	—	—	—	—	—	—
Total Multi-Family MBS	100,908	(26,160)	—	74,748	(1,601)	73,147	—	6.77 %
Residential Mortgage Loans	2,850	—	—	2,867	(18)	2,849	4.06 %	4.03 %
Total/Weighted Average (GAAP)	\$1,396,480	\$(10,093)	\$(1,930)	\$890,077	\$(16,298)	\$873,779	1.53 %	2.69 %

## Non-GAAP Adjustments

	Principal Balance	Unamortized Premium (Discount)	Designated Credit Reserve	Amortized Cost	Unrealized Gain/(Loss)	Fair Value	Net Weighted Average Average Yield <sup>(2)</sup> Coupon <sup>(1)</sup>		
\$ in thousands									
Agency RMBS									
15 year fixed-rate	\$—	\$ —	\$	—\$—	\$ —	\$ —	—		—
Hybrid RMBS	—	—	—	—	—	—	—		—
Total Agency RMBS	—	—	—	—	—	—	—		—
Non-Agency RMBS	4,345	(1,086	) —	3,259	25	3,284	3.75	%	5.00 %
Non-Agency MBS IO, fair value option	157,629	—	—	7,805	(5,897	) 1,908	0.39	%	7.92 %
Total Non-Agency RMBS	161,974	(1,086	) —	11,064	(5,872	) 5,192	0.48	%	7.06 %
Multi-Family MBS	8,197	(2,690	) —	5,508	906	6,414	3.01	%	4.47 %
Multi-Family MBS PO	—	—	—	—	—	—	—		—
Multi-Family MBS PO, fair value option	21,940	—	—	10,483	1,445	11,928	—		—
Total Multi-Family MBS	30,137	(2,690	) —	15,991	2,351	18,342	0.82	%	1.54 %
Residential Mortgage Loans	—	—	—	—	—	—	—		—
Total/Weighted Average (non-GAAP)	\$192,111	\$ (3,776	) \$	—\$27,055	\$ (3,521	) \$23,534	0.52	%	3.80 %

## Non-GAAP Basis

	Principal Balance	Unamortized Premium (Discount)	Designated Credit Reserve	Amortized Cost	Unrealized Gain/ (Loss)	Fair Value	Net Weighted Average Average Yield <sup>(2)</sup> Coupon <sup>(1)</sup>		
\$ in thousands									
Agency RMBS									
15 year fixed-rate	\$1,458	\$34	\$—	\$1,492	\$(29)	\$1,463	2.50 %	1.89 %	
Hybrid RMBS	777,761	16,403	—	794,164	(5,437)	788,727	2.51 %	2.12 %	
Total Agency RMBS	779,219	16,437	—	795,656	(5,466)	790,190	2.51 %	2.12 %	
Non-Agency RMBS	8,739	(1,456)	(1,930)	5,353	260	5,613	2.33 %	7.62 %	
Non-Agency MBS IO, fair value option	666,738	—	—	22,517	(15,345)	7,172	0.34 %	9.95 %	
Total Non-Agency RMBS	675,477	(1,456)	(1,930)	27,870	(15,085)	12,785	0.36 %	9.50 %	
Multi-Family MBS	8,197	(2,690)	—	5,508	906	6,414	3.01 %	4.47 %	
Multi-Family MBS PO	100,908	(26,160)	—	74,748	(1,601)	73,147	—	6.77 %	
Multi-Family MBS PO, fair value option	21,940	—	—	10,483	1,445	11,928	—	—	
Total Multi-Family MBS	131,045	(28,850)	—	90,739	750	91,489	0.19 %	5.85 %	
Residential Mortgage Loans	2,850	—	—	2,867	(18)	2,849	4.06 %	4.03 %	
Total/Weighted Average (non-GAAP)	\$1,588,591	\$(13,869)	\$(1,930)	\$917,132	\$(19,819)	\$897,313	1.41 %	2.72 %	

(1)Weighted average coupon is presented net of servicing and other fees.

(2)Average yield incorporates future prepayment assumptions as discussed in Note 2 to our consolidated financial statements.

For financial statement reporting purposes, GAAP requires us to consolidate the assets and liabilities of three Multi-Family MBS and prime jumbo residential mortgage securitization trusts. Accordingly, the measures in the foregoing tables and charts prepared on a GAAP basis at December 31, 2017 do not include our net investments in the three Multi-Family MBS and prime jumbo residential mortgage securitization trusts. However, our maximum exposure to loss from consolidation of the three trusts is \$27.1 million as of December 31, 2017. Similarly, the tables and charts prepared on a GAAP basis at December 31, 2016 do not include our net investments in three Multi-Family MBS and prime jumbo residential mortgage loan securitization trusts; our maximum exposure to loss from consolidation of the three trusts was \$24.7 million at December 31, 2016. We therefore have also presented certain information that includes our net investments in the Multi-Family MBS and prime jumbo residential mortgage securitization trusts. This information constitutes non-GAAP financial measures within the meaning of Item 10(e) of Regulation S-K, as promulgated by the SEC. We believe that this non-GAAP information enhances the ability of investors to analyze our MBS portfolio and the performance of our Non-Agency RMBS and Multi-Family MBS in the same way that we assess our MBS portfolio and such assets. While we believe the non-GAAP information included in this report provides supplemental information to assist investors in analyzing that portion of our portfolio composed of Non-Agency RMBS and Multi-Family MBS, these measures are not in accordance with GAAP, and they should not be considered a substitute for, or superior to, our financial information calculated in accordance with GAAP. Our

GAAP financial results and the reconciliations from these results should be carefully evaluated.

The following table summarizes certain characteristics of our MBS investment portfolio on a non-GAAP combined basis (including our net investments in consolidated Multi-Family MBS and residential loan securitization trusts), at fair value, according to their estimated weighted average life classifications as of December 31, 2017 and December 31, 2016, respectively:

	December 31, 2017 Fair Value	December 31, 2016 Fair Value
Greater than one year and less than five years	1,209,914,656	418,701,976
Greater than or equal to five years	107,005,869	475,761,570
Total	\$1,316,920,525	\$894,463,546

The increase in shorter maturity assets is due to the continued redeployment of capital out of credit assets and into Agency hybrid-ARM securities.

**Variances between GAAP and tax income.** Due to the potential timing differences in the recognition of GAAP net income compared to REIT taxable income on our investments, our net income and the unamortized amount of purchase discounts and premiums calculated in accordance with GAAP may differ significantly from such amounts calculated for purposes of determining our REIT taxable income. In accordance with GAAP, a portion of the purchase discounts on our Non-Agency RMBS are allocated to a Credit Reserve and, as such, are not expected to be accreted into interest income. Accordingly, potential timing differences arise with respect to the accretion of market discount into income for tax purposes as compared to GAAP.

**Financing and other liabilities.** We enter into repurchase agreements to finance the majority of our Agency and Non-Agency RMBS and Multi-Family MBS. These agreements are secured by our Agency and Non-Agency RMBS and Multi-Family MBS and bear interest at rates that have historically moved in

close relationship to the London Interbank Offer Rate, or LIBOR. As of December 31, 2017, we had entered into repurchase agreements totaling \$1,234.5 million, on a GAAP and non-GAAP basis.

The following tables summarize the average balance, the end of period balance and the maximum balance at month-end of our repurchase agreements for the period from January 1, 2017 to December 31, 2017 and the period January 1, 2016 to December 31, 2016 on a GAAP and non-GAAP basis:

Period ended December 31, 2017	Repurchase Agreements for Available-for-Sale Securities		
	Period Average Balance	End of Period Balance	Maximum Balance at Month-End During the Period
GAAP and non-GAAP basis			
Period from January 1, 2017 to December 31, 2017	\$1,078,248,126	1,234,522,000	1,248,217,000

Period ended December 31, 2016	Repurchase Agreements for Available-for-Sale Securities		
	Period Average Balance	End of Period Balance	Maximum Balance at Month-End During the Period
GAAP and non-GAAP basis			
Period from January 1, 2016 to December 31, 2016	\$624,238,314	804,811,000	804,811,000

As of December 31, 2016, we had closed all of our warehouse facilities that were structured as repurchase agreements secured by prime jumbo loans. As addressed under "Overview" above, we will for the foreseeable future no longer aggregate prime jumbo mortgage loans, and do not intend to maintain financing capacity to do so.

The following table summarizes the average balance, the end of period balance and the maximum balance at month-end of our repurchase agreements for Mortgage loans held-for-sale for the period from January 1, 2016 to December 31, 2016 on both a GAAP and non-GAAP basis:

Period ended December 31, 2016	Repurchase Agreements for Mortgage Loans Held-for-Sale Securities		
	Period Average Balance	End of Period Balance	Maximum Balance at Month-End During the Period
GAAP and non-GAAP basis			
Period from January 1, 2016 to December 31, 2016	\$7,917,213	—	16,250,254

Hedging instruments. Subject to maintaining our qualification as a REIT, we generally hedge as much of our interest rate risk as we deem prudent in light of market conditions. No assurance can be given that our hedging activities will have the desired beneficial impact on our results of operations or financial condition, and as the result of heightened volatility in financial markets, the results of our hedging activities during 2017 and 2016 did not always have such desired beneficial impact.

Interest rate hedging may continue to fail to protect or could adversely affect us because, among other things:

- our investment policies do not contain specific requirements as to the percentages or amount of interest rate risk that we are required to hedge;
- available interest rate hedging may not correspond directly with the interest rate risk for which protection is sought;
- the duration of the hedge may not match the duration of the related liability;

the party owing money in the hedging transaction may default on its obligation to pay;  
the credit quality of the party owing money on the hedge may be downgraded to such an extent that it impairs our  
ability to sell or assign our side of the hedging transaction;  
the value of derivatives used for hedging may be adjusted from time to time in accordance with accounting rules to  
reflect changes in fair value. Downward adjustments or mark-to-market losses would reduce our stockholders' equity;  
and  
changes to our investment or risk management strategy may cause us to reduce the amount of our interest rate hedges  
at times of greater market volatility, which may in turn cause us to realize losses on such hedges.

The following tables summarize our hedging activity as of December 31, 2017 and December 31, 2016:  
December 31, 2017

Expiration Year	Contracts	Notional	Fair Value
Eurodollar Futures Contracts (Short Positions)			
2018	2,740	\$2,740,000,000	\$1,714,500
2019	2,740	2,740,000,000	1,906,838
2020	2,740	2,740,000,000	1,238,650
2021	2,865	2,865,000,000	663,588
2022	3,270	3,270,000,000	(173,963 )
Total	14,355	\$14,355,000,000 <sup>(1)</sup>	\$5,349,613



December 31, 2016

Expiration Year	Contracts	Notional	Fair Value
Eurodollar Futures Contracts (Short Positions)			
2017	3,201	\$3,201,000,000	\$1,124,563
2018	2,941	2,941,000,000	2,737,863
2019	1,611	1,611,000,000	1,911,775
2020	1,583	1,583,000,000	1,491,450
2021	1,165	1,165,000,000	788,162
Total	10,501	\$10,501,000,000	\$8,053,813

The \$14,355,000,000 total notional amount of Eurodollar futures contracts as of December 31, 2017 represents the accumulation of Eurodollar futures contracts that mature on a quarterly basis between March 2018 and December 2022. The maximum notional outstanding for settlement within any single future quarterly period did not exceed \$825,000,000 as of December 31, 2017.

#### Stockholders' Equity and Book Value Per Share

As of December 31, 2017, our stockholders' equity was \$145.8 million comprised of \$37.2 million of preferred equity and \$108.6 million of common equity, and our book value per common share was \$4.91 on a basic and fully diluted basis. Our stockholders' equity increased by \$3.3 million compared to our stockholders' equity as of December 31, 2016, while book value per common share declined by 18.2% from the previous year-end amount of \$6.00. However, the increase in share count from 17,539,258 at December 31, 2016, to 22,143,758 at December 31, 2017, resulting from the June 16, 2017 follow-on equity raise, represents an increase of approximately 26.3%; as a result, book value per share is not directly comparable between the two periods. Unrealized gains and losses on AFS securities (except those related to Non-Agency RMBS IOs) are reflected in stockholders' equity rather than in our consolidated statement of operations as a component of other comprehensive income, or OCI. The decrease in stockholders' equity was the result of a combination of factors, which are further described in Results of Operations below. These factors included increased financing costs which contracted net interest margin; wider spreads on Agency hybrid-ARM securities relative to 15-year collateral, contributing to realized and unrealized losses on our investment portfolio and the aforementioned issuance of additional common stock at a price below book value, contributing to a dilution in book value per share.

#### Critical Accounting Policies and Estimates

Our financial statements are prepared in accordance with GAAP. These accounting principles may require us to make some complex and subjective decisions and assessments. Our most critical accounting policies involve decisions, assessments and estimates that could affect our reported assets and liabilities, as well as our reported revenues and expenses. Actual results could differ from these estimates. All of our estimates upon which our financial statements are based are based upon information available to us at the time of making the estimate. For a discussion of our critical accounting policies, see "Notes to Consolidated Financial Statements" beginning on page F-9 of this report.

#### Capital Allocation

The following tables set forth our allocated capital by investment type at December 31, 2017 and December 31, 2016:

Non-GAAP Basis December 31, 2017

Agency MBS	Multi-Family	Non-Agency	Residential	Unrestricted	Total
------------	--------------	------------	-------------	--------------	-------

Edgar Filing: Five Oaks Investment Corp. - Form 10-K

		MBS <sup>(1)</sup>	RMBS <sup>(1)</sup>	Loans <sup>(2)</sup>	Cash <sup>(3)</sup>		
Market Value	\$1,285,083,648	\$27,437,098	\$4,399,779	\$3,977,804	\$34,347,339	\$1,355,245,668	
Repurchase Agreements	(1,228,349,000 )	(3,618,000 )	(2,555,000 )	—	—	(1,234,522,000 )	
Hedges	5,349,613	—	—	—	—	5,349,613	
Other(4)	9,972,992	(3,286 )	47,841	—	(451,351 )	9,566,196	
Restricted Cash and Due to Broker	10,151,800	—	—	—	—	10,151,800	
Equity Allocated	\$82,209,053	\$23,815,812	\$1,892,620	\$3,977,804	\$33,895,988	\$145,791,277	
% Equity	56.4	% 16.4	% 1.3	% 2.7	% 23.2	% 100.0	%

Non-GAAP Basis	December 31, 2016					
	Agency MBS	Multi-Family MBS <sup>(1)</sup>	Non-Agency RMBS <sup>(1)</sup>	Residential Loans <sup>(2)</sup>	Unrestricted Cash <sup>(3)</sup>	Total
Market Value	\$790,190,232	\$91,488,606	\$12,784,707	\$7,473,260	\$27,534,374	\$929,471,179
Repurchase Agreements	(755,221,000 )	(42,277,000 )	(7,313,000 )	—	—	(804,811,000 )
Hedges	7,050,943	1,002,870	—	—	—	8,053,813
Other <sup>(4)</sup>	5,811,542	(66,141 )	191,955	14,293	(2,309,320 )	3,642,329
Restricted Cash and Due to Broker	5,586,893	440,686	82,965	—	—	6,110,544
Equity Allocated	\$53,418,610	\$50,589,021	\$5,746,627	\$7,487,553	\$25,225,054	\$142,466,865
% Equity	37.5	% 35.5	% 4.0	% 5.3	% 17.7	% 100.0

1. Includes the fair value of our net investments in the FREMF 2011-K13, FREMF 2012-KF01 and CSMC 2014-OAK1 Trusts.

2. Includes MSRs with a fair value of \$3,977,804 and \$4,623,725, respectively.

3. Includes cash and cash equivalents.

4. Includes interest receivable, prepaid and other assets, interest payable, dividend payable and accrued expenses and other liabilities.

This information constitutes non-GAAP financial measures within the meaning of Item 10(e) of Regulation S-K, as promulgated by the SEC. We believe that this non-GAAP information enhances the ability of investors to better understand the capital necessary to support each income-earning asset category, and thus our ability to generate operating earnings. While we believe the non-GAAP information included in this report provides supplemental information to assist investors in analyzing our portfolio, these measures are not in accordance with GAAP, and they should not be considered a substitute for, or superior to, our financial information calculated in accordance with GAAP.

## Results of Operations

As of December 31, 2017, we continued to consolidate the assets and liabilities of two Multi-Family MBS securitization trusts, the FREMF 2011-K13 Trust, and the FREMF 2012-KF01 Trust, and one prime jumbo residential mortgage securitization trust, CSMC 2014-OAK1. Our results of operations, and in particular the gross amount of interest income and interest expense reported, were impacted in part by the reduced principal balances of these consolidated securitization trusts, due to amortization of the loans underlying the trusts. In addition, for the years ended December 31, 2017 and December 31, 2016, both interest income on residential loans held in securitization trusts and interest expense on residential securitized debt obligations were reduced relative to the prior year period due to de-consolidation of the JPMMT 2014-OAK4 trust during the period ended December 31, 2016. Consequently, our results of operations for the periods ended December 31, 2017 and December 31, 2016 are not directly comparable to the period ended December 31, 2015. Dividends declared per share of common stock in 2016 included an amount of \$1.33 per share paid as a one-time deficiency dividend in December 2016.

The table below presents certain information from our Statement of Operations for the twelve months ended December 31, 2017, December 31, 2016 and December 31, 2015:

Edgar Filing: Five Oaks Investment Corp. - Form 10-K

	Year Ended December 31,		
	2017	2016	2015
Revenues:			
Interest income:			
Available-for-sale securities	\$29,521,893	\$23,475,765	\$24,298,156
Mortgage loans held-for-sale	72,160	430,986	2,097,702
Multi-family loans held in securitization trusts	54,271,017	58,587,780	68,016,595
Residential loans held in securitization trusts	5,103,853	10,585,191	19,986,204
Cash and cash equivalents	164,413	41,994	16,351
Interest expense:			
Repurchase agreements - available-for-sale securities	(13,493,197 )	(6,237,777 )	(6,467,312 )
Repurchase agreements - mortgage loans held-for-sale	—	(237,807 )	(1,323,892 )
Multi-family securitized debt obligations	(51,440,694 )	(54,940,386 )	(62,157,176 )
Residential securitized debt obligations	(4,059,894 )	(8,117,402 )	(13,156,912 )
Net interest income	20,139,551	23,588,344	31,309,716
Other-than-temporary impairments			
(Increase) decrease in credit reserves	—	(541,342 )	(745,492 )
Additional other-than-temporary credit impairment losses	—	(183,790 )	(2,890,939 )
Total impairment losses recognized in earnings	—	(725,132 )	(3,636,431 )
Other income:			
Realized gain (loss) on sale of investments, net	(14,054,164 )	(7,216,137 )	(533,832 )
Change in unrealized gain (loss) on fair value option securities	9,448,270	(4,683,410 )	(1,041,649 )
Realized gain (loss) on derivative contracts, net	2,219,719	(3,089,001 )	(12,024,730 )
Change in unrealized gain (loss) on derivative contracts, net	(2,704,413 )	5,495,463	4,909,858
Realized gain (loss) on mortgage loans held-for-sale, net	(221,620 )	94,187	1,216,314
Change in unrealized gain (loss) on mortgage loans held-for-sale	17,727	(151,023 )	(197,179 )
Change in unrealized gain (loss) on mortgage servicing rights	(487,856 )	(827,864 )	(671,957 )
Change in unrealized gain (loss) on multi-family loans held in securitization trusts	3,353,365	(5,219,530 )	6,097,000
Change in unrealized gain (loss) on residential loans held in securitization trusts	(961,100 )	404,720	(8,153,474 )
Other interest expense	(152,322 )	(1,860,000 )	—
Servicing income	922,094	932,424	211,878
Other income	46,262	32,276	85,726
Total other income (loss)	(2,574,038 )	(16,087,895 )	(10,102,045 )
Expenses:			
Management fee	2,215,050	2,472,353	2,774,432
General and administrative expenses	5,454,786	5,867,851	6,660,934
Operating expenses reimbursable to Manager	4,127,549	4,747,275	4,980,348
Other operating expenses	855,582	1,480,341	2,448,439
Compensation expense	205,585	197,452	256,608
Total expenses	12,858,552	14,765,272	17,120,761
Net income (loss)	4,706,961	(7,989,955 )	450,479
Dividends to preferred stockholders	(3,522,036 )	(3,522,036 )	(3,522,036 )
Net income (loss) attributable to common stockholders	\$1,184,925	\$(11,511,991)	\$(3,071,557 )
Earnings (loss) per share:			
Net income (loss) attributable to common stockholders (basic and diluted)	\$1,184,925	\$(11,511,991)	\$(3,071,557 )

## Edgar Filing: Five Oaks Investment Corp. - Form 10-K

Weighted average number of shares of common stock outstanding	20,048,128	14,641,701	14,721,074
Basic and diluted income (loss) per share	\$0.06	\$(0.79)	) \$(0.21)
Dividends declared per share of common stock	\$0.60	\$2.04	\$1.35

Comparison of the Year Ended December 31, 2017 to the Year Ended December 31, 2016

### Net Income Summary

For the year ended December 31, 2017, our net gain attributable to common stockholders was \$1,184,925 or \$0.06 basic and diluted net income per average share, compared with a net loss of \$11,511,991 or \$0.79 basic and diluted net loss per share, for the year ended December 31, 2016. The principal drivers of this

net gain variance are a decrease in total other income (loss) from \$16,087,895 for the year ended December 31, 2016 to \$2,574,038 for the year ended December 31, 2017, a decrease in total expenses from \$14,765,272 in 2016 to \$12,858,552 in 2017 and a decrease in impairment charges from \$725,132 in 2016 to \$0 in 2017, which in aggregate more than offset the year-over-year decrease in net interest income from \$23,588,344 for the year ended December 31, 2016 to \$20,139,551 for the year ended December 31, 2017.

#### Interest Income and Interest Expense

An important source of income is net interest income. For the years ended December 31, 2017 and December 31, 2016, our interest income was \$89,133,336 and \$93,121,716, respectively. Our interest expense was \$68,993,785 and \$69,533,372, respectively, for the years ended December 31, 2017 and December 31, 2016. The year-over year decrease in interest income was primarily the result of the reduced principal balances of the consolidated multi-family and residential mortgage loan securitization trusts. The year-over-year decrease in interest expense was impacted by the effect of the reduced principal balances of the consolidated multi-family and residential mortgage loan securitization trusts which served to offset the impact of higher funding costs as a result of multiple interest rate hikes throughout 2017.

#### Net Interest Income

For the years ended December 31, 2017 and December 31, 2016, our net interest income was \$20,139,551 and \$23,588,344, respectively, with the decrease primarily reflecting the increased funding costs and reduced balances of the consolidated trusts noted above.

#### Other Income (Loss)

For the year ended December 31, 2017, our other income (loss) represented a loss of \$2,574,038, which primarily reflects the impact of three interest rate hikes enacted by the Federal Reserve and a one-time other interest expense provision, in turn generating net realized losses on sales of investments \$14,054,164, net unrealized losses of \$2,704,413 on interest rate hedges, net realized losses on mortgage loans of \$221,620 and net unrealized losses on mortgage servicing rights of \$487,856. Additionally, we incurred net unrealized losses on residential mortgage loans held in the CSMC 2014-OAK1 Trust of \$961,100. We also incurred a \$152,322 other interest expense related to the deficiency dividend payment. These losses in aggregate more than offset net unrealized gain on fair value option securities of \$9,448,270, net realized gain on interest rate hedges of \$2,219,719, net unrealized gain on multi-family loans held in the 2011-K13 and 2012-KF01 Trusts of \$3,353,365, net unrealized gain on mortgage loans of \$17,727, net mortgage servicing income of \$922,094 and net other income of \$46,262. As noted earlier, unrealized gains on AFS securities, which typically offset unrealized losses on interest rate hedges, are a component of other comprehensive income, or OCI, and as such are reflected in stockholders' equity rather than in our consolidated statements of operations.

For the year ended December 31, 2016, our other income (loss) represented a loss of \$16,087,895, which primarily reflected the impact of volatile interest rates, particularly in the first half of the year and the post-presidential election period, investment sales related to reduction in credit assets, Re-REMIC transactions effected during the year and a one-time other interest expense provision, in turn generating net realized losses on sales of investments \$7,216,137, net realized losses of \$3,089,001 on interest rate hedges, net unrealized losses on fair value option securities of \$4,683,410 and net unrealized losses on mortgage servicing rights of \$827,864. Additionally, we incurred net unrealized losses on multi-family loans held in the 2011-K13 and 2012-KF01 Trusts of \$5,219,530 and net unrealized losses on mortgage loans of \$151,023. We also incurred a \$1,860,000 other interest expense related to the deficiency dividend payment. These losses in aggregate more than offset net unrealized gains on interest rate hedges of \$5,495,463, net unrealized gain on residential mortgage loans held in the JPMMT 2014-OAK4 and CSMC

2014-OAK1 Trusts of \$404,720, net realized gain on mortgage loans of \$94,187, net mortgage servicing income of \$932,424 and net other income of \$32,276. As noted earlier, unrealized gains on AFS securities, which typically offset unrealized losses on interest rate hedges, are a component of other comprehensive income, or OCI, and as such are reflected in stockholders' equity rather than in our consolidated statements of operations.

#### Expenses

In connection with our consolidation of the consolidated trusts, we are required to include the expenses of the trusts in our consolidated statement of operations, although we are not actually responsible for the payment of these trust expenses.

We incurred management fees of \$2,215,050 for the year ended December 31, 2017 representing amounts payable to our Manager under our management agreement. We also incurred operating expense of \$10,643,502, of which \$4,127,549 was payable to our Manager and \$6,515,953 was payable directly by us.

For the year ended December 31, 2016, we incurred management fees of \$2,472,353 representing amounts payable to our Manager under our management agreement. We also incurred operating expense of \$12,292,919, of which \$4,747,275 was payable to our Manager and \$7,545,644 was payable directly by us.

Our general and administrative expenses represent the cost of legal, accounting, auditing and consulting services and declined as a result of reduced expenses attributable to the consolidated trusts during both the years ended December 31, 2017 and December 31, 2016 at \$5,454,786 and \$5,867,851, respectively.

#### Other-Than-Temporary Impairment (OTTI)

We review each of our securities on a quarterly basis to determine if an OTTI charge is necessary. For the year ended December 31, 2017 we did not recognize any OTTI losses. For the year ended December 31, 2016 we recognized \$725,132 in OTTI losses. The lack of recognition of OTTI during the year ended December 31, 2017 reflected the sale of certain legacy Non-Agency RMBS, all of which had been sold at year end December 31, 2016. For further information about evaluating AFS securities for other-than-temporary impairments, refer to Note 2 – Summary of Significant Policies of the notes to our consolidated financial statements.

#### Net Income (Loss) and Return on Equity

Our net gain attributable to common stockholders was \$1,184,925 for the year ended December 31, 2017, after accounting for preferred stock dividends of \$3,522,036, representing an annualized gain of 0.55% on average stockholders' equity of \$215,358,032. As noted earlier, unrealized net gains or losses on AFS securities are not reflected in our statement of operations, but are instead a component of OCI. For the year ended December 31, 2017, our comprehensive loss attributable to common stockholders was \$4,600,929 which included \$5,785,854 in total OCI. This represents an annualized loss of 2.14% on average stockholders' equity.

For the year ended year December 31, 2016, our net loss attributable to common stockholders was \$11,511,991, after accounting for preferred stock dividends of \$3,522,036, representing an annualized loss of 6.08% on average stockholders' equity of \$189,211,689. As noted earlier, unrealized gains or losses on AFS securities (except Non-Agency RMBS IOs) are not reflected in our statements of operations, but are instead a component of OCI. For the year ended December 31, 2016, our comprehensive loss attributable to common stockholders was \$20,384,850 which included \$8,872,859 in total other comprehensive loss. This represents an annualized loss of 10.77% on average stockholders' equity.

#### Comparison of the Year Ended December 31, 2016 to the Year Ended December 31, 2015

##### Net Income Summary

For the year ended December 31, 2016, our net loss attributable to common stockholders was \$11,511,991 or \$0.79 basic and diluted net loss per average share, compared with a net loss of \$3,071,557 or \$0.21 basic and diluted net loss per share, for the year ended December 31, 2015. The principal drivers of this net loss variance are a decrease in net interest income from \$31,309,716 for the year ended December 31, 2015 to \$23,588,344 for the year ended December 31, 2016, an increase in total other income (loss) from \$10,102,045 in 2015 to \$16,087,895 in 2016, which in aggregate more than offset the year-over-year decrease in total expenses from \$17,120,761 in 2015 to \$14,765,272 in 2016 and a decrease in impairment charges from \$3,636,431 in 2015 to \$725,132 in 2016.

##### Interest Income and Interest Expense

An important source of income is net interest income. For the years ended December 31, 2016 and December 31, 2015, our interest income was \$93,121,716 and \$114,415,008, respectively. Our interest expense was \$69,533,372 and \$83,105,292, respectively, for the years ended December 31, 2016 and December 31, 2015. The year-over year decrease in interest income and interest expense was primarily a result of the reduced principal balances of the consolidated multi-family and residential mortgage loan securitization trusts.

##### Net Interest Income

For the years ended December 31, 2016 and December 31, 2015, our net interest income was \$23,588,344 and \$31,309,716, respectively, with the decrease primarily reflecting the reduced balances of the consolidated trusts noted above.

##### Other Income (Loss)

For the year ended December 31, 2016, our other income (loss) represented a loss of \$16,087,895, which primarily reflected the impact of volatile interest rates, particularly in the first half of the year and the post-presidential election period, investment sales related to reduction in credit assets, Re-REMIC transactions effected during the year and a one-time other interest expense provision, in turn generating net realized losses on sales of investments \$7,216,137, net realized losses of \$3,089,001 on interest rate hedges, net unrealized losses on fair value option securities of \$4,683,410 and net unrealized losses on mortgage servicing rights of \$827,864. Additionally, we incurred net unrealized losses on multi-family loans held in the 2011-K13 and 2012-KF01 Trusts of \$5,219,530 and net unrealized losses on mortgage loans of \$151,023. We also incurred a \$1,860,000 other interest expense related to the deficiency dividend payment. These losses in aggregate more than offset net unrealized gains on interest rate hedges of \$5,495,463, net unrealized gain on residential mortgage loans held in the JPMMT 2014-OAK4 and CSMC 2014-OAK1 Trusts of \$404,720, net realized gain on mortgage loans of \$94,187, net mortgage servicing income of \$932,424 and net other income of \$32,276. As noted earlier, unrealized gains on AFS securities, which typically offset unrealized losses on interest rate hedges, are a component of other comprehensive income, or OCI, and as such are



reflected in stockholders' equity rather than in our consolidated statements of operations.

For the year ended December 31, 2015, our other income represented a loss of \$10,102,045 which primarily reflects the impact of volatile interest rates throughout the year, in turn generating net realized losses of \$12,024,730 on interest rate hedges, and net unrealized loss on mortgage servicing rights of \$671,957. Additionally, net unrealized losses on residential mortgage loans held in the JPMMT 2014-OAK4 and CSMC 2014-OAK1 Trusts were \$8,153,474, net realized losses on sales of investments of \$533,832, unrealized losses on fair value option securities of \$1,041,649 and net unrealized losses on mortgage loans of \$197,179. These losses in aggregate more than offset unrealized gain on multi-family loans held in the 2011-K13 and 2012-KF01 Trusts of \$6,097,000, net realized gain on mortgage loans of \$1,216,314, net unrealized gains on interest hedges of \$4,909,858, net mortgage servicing income of \$211,878 and net other income of \$85,726. As noted above, unrealized gains or losses on AFS securities (except Non-Agency RMBS IOs), which typically offset unrealized gains or losses on interest rate hedges, are a component of OCI and as such are reflected in stockholders' equity rather than in our consolidated statement of operations.

### Expenses

In connection with our consolidation of the consolidated trusts, we are required to include the expenses of the trusts in our consolidated statement of operations, although we are not actually responsible for the payment of these trust expenses.

We incurred management fees of \$2,472,353 for the year ended December 31, 2016 representing amounts payable to our Manager under our management agreement. We also incurred operating expense of \$12,292,919, of which \$4,747,275 was payable to our Manager and \$7,545,644 was payable directly by us.

For the year ended December 31, 2015, we incurred management fees of \$2,774,432 representing amounts payable to our Manager under our management agreement. We also incurred operating expense of \$14,346,329, of which \$4,980,348 was payable to our Manager and \$9,365,981 was payable directly by us.

Our general and administrative expenses represent the cost of legal, accounting, auditing and consulting services and declined as a result of reduced expenses attributable to the consolidated trusts during both the years ended December 31, 2016 and December 31, 2015 at \$5,867,851 and \$6,660,934, respectively.

### Other-Than-Temporary Impairment

We review each of our securities on a quarterly basis to determine if an OTTI charge is necessary. For the year ended December 31, 2016 we recognized \$725,132 in OTTI losses. For the year ended December 31, 2015 we recognized \$3,636,431 in OTTI losses. The increase in OTTI during the year ended December 31, 2016 reflected an increase in the Company's credit loss expectations on certain legacy Non-Agency RMBS, all of which had been sold at year end. For further information about evaluating AFS securities for other-than-temporary impairments, refer to Note 2 – Summary of Significant Policies of the notes to our consolidated financial statements.

## Net Income (Loss) and Return on Equity

Our net loss attributable to common stockholders was \$11,511,991 for the year ended December 31, 2016, after accounting for preferred stock dividends of \$3,522,036, representing an annualized loss of 6.08% on average stockholders' equity of \$189,211,689. As noted earlier, unrealized net gains or losses on AFS securities are not reflected in our statement of operations, but are instead a component of OCI. For the year ended December 31, 2016, our comprehensive loss attributable to common stockholders was \$20,384,850 which included \$8,872,859 in total OCI. This represents an annualized loss of 10.77% on average stockholders' equity.

For the year ended year December 31, 2015, our net loss attributable to common stockholders was \$3,071,557, after accounting for preferred stock dividends of \$3,522,036, representing an annualized loss of 1.62% on average stockholders' equity of \$189,709,805. As noted earlier, unrealized gains or losses on AFS securities (except Non-Agency RMBS IOs) are not reflected in our statements of operations, but are instead a component of OCI. For the year ended December 31, 2015, our comprehensive loss attributable to common stockholders was \$10,675,679 which included \$7,604,122 in total other comprehensive loss. This represents an annualized loss of 5.63% on average stockholders' equity.

## Liquidity and Capital Resources

Liquidity is a measurement of our ability to meet potential cash requirements, including ongoing commitments to pay dividends, fund investments, comply with margin requirements, and repay borrowings and other general business needs. Our primary sources of funds for liquidity consist of net cash provided by operating activities, cash from repurchase agreements, and other financing arrangements including potential issuance of common or preferred stock. We currently finance Agency and Non-Agency RMBS and Multi-Family MBS primarily through the use of repurchase agreements.

Our target assets, excluding those such as Multi-Family MBS that are structured as principal only securities, generate ongoing liquidity through principal and interest payments. In addition, as part of our overall investment and risk management strategies, we may from time to time sell certain assets and these sales are generally expected to provide additional liquidity. Certain of our assets such as Multi-Family MBS and residential mortgage loans may be subject to longer trade timelines, and as a result, market conditions could significantly and adversely affect the liquidity of our assets.

In addition, if we are required to liquidate all or a portion of our portfolio quickly, we may realize significantly less than the value at which we previously recorded our assets. Assets that are illiquid are more difficult to finance, and to the extent that we use leverage to finance assets that become illiquid, we may lose that leverage or have it reduced. Assets tend to become less liquid during times of financial stress, which is often the time that liquidity is most needed. As a result, our ability to sell assets or vary our portfolio in response to changes in economic and other conditions may be limited by liquidity constraints, which could adversely affect our results of operations and financial condition.

As noted earlier, our defensive approach includes our efforts to emphasize liquidity, both to meet margin calls (as discussed below) and to be able to better absorb the effects on our financing from potential exits of certain of our repo counterparties from the securities trading and/or financing business.

We intend to continue to maintain a level of liquidity in relation to our assets that enables us to meet reasonably anticipated margin calls but that also allows us to be substantially invested in Agency RMBS and Multi-Family MBS. We may misjudge the appropriate amount of our liquidity by maintaining excessive liquidity, which would lower our investment returns, or by maintaining insufficient liquidity, which would force us to liquidate assets into unfavorable market conditions and harm our operating results. As of December 31, 2017, we had unrestricted cash and cash

equivalents of \$34.3 million available to meet margin calls on our repurchase agreements and derivative instruments, compared to \$27.5 million as of December 31, 2016.

As of December 31, 2017, net proceeds from repurchase agreements related to available-for-sale securities totaled \$1,234.5 million, on a GAAP and non-GAAP basis, with a weighted-average borrowing rate of 1.56%, on a GAAP and non-GAAP basis, which we used to finance our Agency RMBS, Non-Agency RMBS and Multi-Family MBS. As of December 31, 2017, we had an overall debt-to-equity ratio of 8.5:1 on a GAAP and non-GAAP basis, compared to 5.6:1 as of December 31, 2016. The increase is due primarily to the deployment of the June 2017 follow-on equity offering proceeds and portfolio reallocation in favor of Agency RMBS described earlier. The repurchase obligations mature and reinvest every 30 to 360 days. See "Contractual Obligations and Commitments" below. We expect to continue to borrow funds in the form of repurchase agreements. As of December 31, 2017, for our available-for-sale securities we had established repurchase borrowing arrangements with various investment banking firms and other lenders and had outstanding borrowings with 14 of these lenders totaling \$1,234.5 million, on a GAAP and non-GAAP basis.

Under our repurchase agreements we may be required to pledge additional assets to our repurchase agreement counterparties (lenders) in the event that the estimated fair value of the existing pledged collateral under such agreements declines and such lenders demand additional collateral, which may take the form of additional securities or cash. We are subject to various financial covenants under our borrowing agreements and derivative contracts, which include minimum net worth and/or profitability requirements, maximum debt-to-equity ratios and minimum market capitalization requirements. As of December 31, 2017, we were in compliance with all of our financial covenants in, and were not in default under any of, such agreements and contracts. Generally, our borrowing agreements contain a financing rate, term and trigger levels for margin calls and haircuts depending on the types of collateral and the counterparties involved. If the estimated fair value of the investment securities increases due to changes in market interest rates or market factors, lenders may release collateral back to us. Specifically, margin calls may result from a decline in the value of the investments securing our borrowing agreements, prepayments on the residential mortgages securing our MBS investments and from changes in the estimated fair value of such investments generally due to principal reduction of such investments from scheduled amortization and resulting from changes in market interest rates and other market factors. Counterparties also may choose to increase haircuts based on credit evaluations of us and/or the performance of the bonds in question. Across all of our borrowing facilities, the haircuts range from a low of 5% to a high of 40%, and the weighted average haircut was 5.2% as of December 31, 2017. Declines in the value of our securities or loan portfolio can trigger margin calls by our lenders under our borrowing agreements. Should prepayment speeds on the residential mortgages underlying our MBS investments or market interest rates increase, margin calls on our borrowing agreements could result, causing an adverse change in our liquidity position.

If the decline in market value of our securities collateralizing our borrowing facilities, or the combination of declining market value of our pledged securities and increasing haircuts, were to exceed the amount of our available liquidity, we would have to sell assets and may not realize sufficient proceeds to repay the amounts we owe to our lenders. However, as our liquidity decreased, we would attempt to de-leverage in an effort to avoid such a situation. In the period ended December 31, 2017, we did experience certain margin calls, generally the result of either principal paydowns on, or decreased market prices of, our MBS investments, and all such margin calls were promptly met. In general, periods of heightened market volatility will result in more frequent changes in the prices of MBS investments, and thus increased frequency of margin calls.

Upon repayment of each borrowing under a borrowing agreement, we may use the collateral immediately for borrowing under a new borrowing agreement. We have not at the present time entered into any other commitment agreements under which the lender would be required to enter into new borrowing agreements during a specified period of time.

As of December 31, 2017, we consolidated the assets and liabilities of two Multi-Family MBS securitization trusts, the FREMF 2011-K13 Trust, and the FREMF 2012-KF01 Trust, and one prime jumbo residential mortgage securitization trust, CSMC 2014-OAK1. The assets of the trusts are restricted and can only be used to fulfill their respective obligations. Accordingly, the obligations of the trusts, which we classify as Multi-Family securitized debt obligations and residential securitized debt obligations, do not have any recourse to us as the consolidator of the trusts. As of December 31, 2017, the fair value of these non-recourse liabilities aggregated to \$1,223,623,061 and they are excluded from discussion and analysis of our leverage.

#### Forward-Looking Statements Regarding Liquidity

Based upon our current portfolio, leverage rate and available borrowing arrangements, we believe that the net proceeds of our prior equity sales combined with cash flow from operations and available borrowing capacity, will be sufficient to enable us to meet anticipated short-term (one year or less) liquidity requirements to fund our investment activities, pay fees under our management agreement, fund our distributions to stockholders and for other general corporate expenses.

Our ability to meet our long-term (greater than one year) liquidity and capital resource requirements will be subject to obtaining additional debt financing and equity capital. We may increase our capital resources by obtaining long-term credit facilities or making additional public or private offerings of equity or debt securities, possibly including classes of preferred stock, common stock and senior or subordinated notes. Such financing will depend on market conditions for capital raises and for the investment of any proceeds. If we are unable to renew, replace or expand our sources of financing on substantially similar terms, it may have an adverse effect on our business and results of operations.

To maintain our qualification as a REIT, we generally must distribute annually at least 90% of our "REIT taxable income" (determined without regard to the deduction for dividends paid and excluding net capital gain). These distribution requirements limit our ability to retain earnings and thereby replenish or increase capital for operations.

#### Contractual Obligations and Commitments

We entered into a contractual arrangement with our prior manager when we commenced operations on May 16, 2012. We entered into a new contractual arrangement with our new manager on January 18, 2018. Our Manager is entitled to receive a management fee and the reimbursement of certain expenses. Because our management agreement provides that our Manager is responsible for managing our affairs, our executive officers, who are employees of our Manager and not our employees, will not receive cash compensation from us for serving as our executive officers. We have no employees.

The Five Oaks Investment Corp. Manager Equity Plan, or the Manager Equity Plan, includes provisions for grants of restricted common stock and other equity based awards to our Manager and to our independent directors, consultants or officers whom we may directly employ in the future. In turn, our Manager will grant such awards to its employees, officers (including our current officers), members, directors or consultants. Grants to our Manager will be allocated firstly to non-member employees and officers of our Manager, and then the balance of the grants to members (including our officers) proportionally based on each member's respective ownership of our Manager. The grants to be made to our Manager and then by our Manager pursuant to such are intended to provide customary incentive compensation to those persons employed by our Manager on whose performance we rely (including our officers). The

total number of shares that may be granted subject to awards under the Manager Equity Plan will be equal to an aggregate of 3.0% of the total number of issued and outstanding shares of our common stock (on a fully diluted basis) at the time of each award (other than any shares issued or subject to awards made pursuant to the Manager Equity Plan). No grants were made under the Manager Equity Plan during the period January 1, 2017 to December 31, 2017.

The following table summarizes our contractual obligations for borrowings under repurchase agreements at December 31, 2017:

#### GAAP and non GAAP

\$ in thousands	Payments Due by Period				
	Total	Less Than 1 Year	1 - 3 Years	3 - 5 Years	More Than 5 Years
Repurchase agreements related to available-for-sale securities	\$ 1,234,522	1,234,522	—	—	—
Total contractual obligations <sup>(1)</sup>	\$ 1,234,522	1,234,522	—	—	—

We exclude multi-family securitized debt obligations, residential securitized debt obligations and related interest expense from the contractual obligations disclosed in the table above as this debt is non-recourse to us, is not cross-collateralized and must be satisfied exclusively from the proceeds of the respective multi-family mortgage loans or residential mortgage loans and related assets held in the securitization trusts.

In addition, we enter into certain contracts that contain a variety of indemnification obligations, principally with our Manager, brokers and counterparties to repurchase agreements. The maximum potential future payment amount we could be required to pay under these indemnification obligations is unlimited. We have not incurred any costs to defend lawsuits or settle claims related to these indemnification obligations. As a result, the estimated fair value of these agreements is minimal. Accordingly, we recorded no liabilities for these agreements as of December 31, 2017.

#### Off-Balance Sheet Arrangements

As of December 31, 2017, we did not maintain any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance, or special purpose or variable interest entities, established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. Further, as of December 31, 2017, we had not guaranteed any obligations of unconsolidated entities or entered into any commitment or intent to provide funding to any such entities.

In connection with the provision of seller eligibility and backstop guarantee services provided to MAXEX, we account for the related noncontingent liability at its fair value on our consolidated balance sheet as a liability; as of December 31, 2017, the amount of the liability recorded was \$222,518. The maximum potential amount of future payments that we could be required to make under the outstanding backstop guarantees was \$629,278,629. In accordance with ASC 450, Contingencies, any contingent liability must be recognized when its payment becomes probable and reasonably estimable; as of December 31, 2017, no such contingent liability was required to be recognized.

#### Distributions

We intend to make regular quarterly distributions to holders of our common stock. U.S. federal income tax law generally requires that a REIT distribute annually at least 90% of its "REIT taxable income" (determined without regard to the deduction for dividends paid and excluding net capital gain) and that it pay tax at regular corporate rates to the extent that it annually distributes less than 100% of its "REIT taxable income." We generally intend to make regular monthly distributions to holders of our preferred stock and quarterly distributions to holders of our common stock in an amount equal to all or substantially all of our taxable income. Although FOAC no longer aggregates and securitizes residential mortgages, it continues to generate taxable income from MSRs and other mortgage-related activities. This taxable income will be subject to regular corporate income taxes. We generally anticipate the retention of profits generated and taxed at FOAC. Before we make any distribution on our common stock, whether for U.S. federal income tax purposes or otherwise, we must first meet both our operating requirements and debt service on our repurchase agreements, other debt payable and on our Series A Preferred Stock. If cash available for distribution to our stockholders is less than our taxable income, we could be required to sell assets or borrow funds to make cash distributions, or we may make a portion of the required distribution in the form of a taxable stock distribution or distribution of debt securities.

We intend to announce quarterly dividends for our common stock in arrears and continue to announce monthly dividends in advance for our preferred stock. If substantially all of our taxable income has not been paid by the close of any calendar year, we intend to declare a special dividend prior to the end of such calendar year, to achieve this result. On March 16, 2018, we announced that our board of directors declared monthly cash dividend rates for the second quarter of 2018 of \$0.0200 per share of common stock.

#### Inflation

Virtually all of our assets and liabilities will be interest rate sensitive in nature. As a result, interest rates and other factors influence our performance far more so than does inflation. Changes in interest rates do not necessarily correlate with inflation rates or changes in inflation rates. Our financial statements are prepared in accordance with GAAP, and our distributions will be determined by our board of directors consistent with our obligation to distribute to our stockholders at least 90% of our "REIT taxable income" (determined without regard to the deduction for dividends paid and excluding net capital gain) on an annual basis in order to maintain our REIT qualification; in each case, our activities and balance sheet are measured with reference to historical cost and/or fair market value without considering inflation. Given the financial nature of substantially all of the Company's assets and liabilities, and the very low level of inflation, the Company does not believe inflation has had a material impact on the Company's results of operations during the last three years.

#### ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS

We seek to manage our risks related to the credit quality of our assets, interest rates, liquidity, prepayment speeds and market value while providing an opportunity to stockholders to realize attractive risk-adjusted returns through

ownership of our common stock. Although we do not seek to avoid risk completely, we believe that risk can be quantified from historical experience and we seek to manage our risk levels in order to earn sufficient compensation to justify the risks we undertake and to maintain capital levels consistent with taking such risks.

To reduce the risks to our portfolio, we employ portfolio-wide and security-specific risk measurement and management processes in our daily operations. Our Manager's risk management tools include software and services licensed or purchased from third parties, in addition to proprietary software and analytical methods developed by our Manager. These tools have not fully protected us from market risks, and there can be no assurance that they will do so in the future.

While changes in the fair value of our Agency RMBS are generally not credit-related, changes in the fair value of our Non-Agency RMBS and Multi-Family MBS, including our net investments in consolidated Multi-Family MBS and residential loan securitization trusts, may reflect both market and interest rate conditions as well as credit risk. In evaluating our asset/liability management and Non-Agency RMBS and Multi-Family MBS credit performance, our Manager considers the credit characteristics underlying our Non-Agency RMBS and Multi-Family MBS, including our net investments in consolidated Multi-Family MBS and residential loan securitization trusts. The following table presents certain information about our Agency RMBS, Non-Agency RMBS and Multi-Family MBS (including our net investments in consolidated Multi-Family MBS and residential loan securitization trusts) as of December 31, 2017 on a combined non-GAAP basis. Information presented with respect to weighted average loan to value, weighted average FICO scores and other information is aggregated based on information reported at the time of mortgage origination and therefore does not reflect changes to home values or borrower characteristics since the mortgage origination.

	December 31, 2017		
	Non-Agency RMBS <sup>(1)</sup>	Multi-Family MBS <sup>(2)</sup>	Agency RMBS
Portfolio Characteristics:			
Number of Securities	4	3	58
Carrying Value/ Estimated Fair Value	\$4,399,779	\$27,437,098	\$1,285,083,648
Amortized Cost	\$11,063,922	\$21,777,512	\$1,297,656,350
Current Par Value	\$126,612,386	\$37,637,548	\$1,274,329,317
Carrying Value to Current Par	3.5	% 72.9	% 100.8
Amortized Cost to Current Par	8.7	% 57.9	% 101.8
Net Weighted Average Coupon	0.48	% 0.83	% 2.66
3 Month CPR <sup>(3)</sup>	11.1	NA	9.0

#### Non-Agency RMBS Characteristics

	December 31, 2017 <sup>(1)</sup>	
Collateral Attributes:	Prime Jumbo New Issue	
Weighted Average Loan Age (months)	44	
Weighted Average Original Loan-to-Value	61.0	%
Weighted Average Original FICO <sup>(4)</sup>	771	
Weighted Average Loan Size	784.3	
Current Performance:		
60+ Day Delinquencies	0.7	%
Average Credit Enhancement <sup>(5)</sup>	21.4	%

	December 31, 2017 <sup>(1)</sup>		
Coupon Type	Carrying Value	% of Non-Agency RMBS	
Fixed Rate	\$4,399,779	100.0	%
Collateral Type			
Prime	\$4,399,779	100.0	%
Loan Origination Year			
Post-2011	\$4,399,779	100.0	%

1. Includes our net investment in the CSMC 2014-OAK1 Trust at December 31, 2017 on a combined, non-GAAP basis.

2. Includes our net investment in the 2011-K13 and 2012-KF01 Trusts at December 31, 2017 on a combined, non-GAAP basis.

3. Three - month CPR is reflective of the prepayment speed on the underlying securitization; however, CPR is not necessarily indicative of the proceeds received on our investments. Proceeds received on our RMBS depend on the location of our RMBS within the payments structure of each underlying security.

4. FICO represents a mortgage industry accepted credit score of a borrower, which was developed by Fair Isaac Corporation.

5. Average credit enhancement remaining on our Non-Agency RMBS portfolio, which is the average amount of protection available to absorb future credit losses due to defaults on the underlying collateral.

The following table presents the rating of our Non-Agency RMBS at December 31, 2017, including our net investments in consolidated and residential loan securitization trusts, on a combined non-GAAP basis. The rating indicates the opinion of the rating agency as to the creditworthiness of the investment, indicating the obligor's ability to meet its full financial commitment on the obligation. A rating of "NR" is assigned when major rating agencies do not provide any rating for such security.

	December 31, 2017 <sup>(1)</sup>		
	% of		
Current Rating <sup>(6)</sup>	Fair Value	Non-Agency RMBS	
Rated AAA	\$1,095,627	24.9	%
Not Rated	\$3,304,152	75.1	%



6. Reported based on the lowest rating issued by a rating agency, if more than one rating is issued on the security at the date presented.

The mortgages securing our Non-Agency RMBS are collateralized by properties located within many geographic regions across the United States. The following table presents the five largest geographic concentrations of the mortgages collateralizing our Non-Agency RMBS, including our net investments in consolidated residential loan securitization trusts, at December 31, 2017 on a combined, non-GAAP basis:

December 31, 2017 <sup>(1)</sup>			
% of			
Property Location	Fair Value	Non-Agency	
		RMBS	
California	\$1,649,612	37.5	%
Washington	\$675,954	15.4	%
Massachusetts	\$376,827	8.6	%
Florida	\$277,627	6.3	%
Tennessee	\$192,021	4.4	%

Our Multi-Family MBS investments are primarily Freddie Mac Multifamily K Certificates backed by pools of multifamily mortgage loans or re-REMICs of underlying Freddie Mac Multifamily K Certificates. These certificates are not guaranteed by Freddie Mac and therefore, repayment is based solely on the performance of the underlying pool of loans. These loans have prepayment lock-out provisions which reduce the risk of early repayment of our investment.

The following table presents the rating of our Multi-Family MBS at December 31, 2017, including our net investment in the 2011-K13 and 2012-KF01 Trusts, on a combined non-GAAP basis. The rating indicates the opinion of the rating agency as to the creditworthiness of the investment, indicating the obligor's ability to meet its full financial commitment on the obligation.

December 31, 2017 <sup>(1)</sup>			
		% of	
Current Rating	Fair Value	Multi-Family MBS	
Rated BB-	\$5,742,000	20.9	%
Not Rated	\$21,695,098	79.1	%

The following table presents the weighted average life breakdown of our MBS investment portfolio at December 31, 2017, on a combined, non-GAAP basis:

Weighted Average Life Breakdown	Carrying Value
Greater than one year and less than five years	\$1,209,914,656
Greater than or equal to five years	\$107,005,869

#### Interest rate risk

Interest rates are highly sensitive to many factors, including fiscal and monetary policies and domestic and international economic and political considerations, as well as other factors beyond our control. We are subject to interest rate risk in connection with our assets and related financing obligations. Subject to maintaining our qualification as a REIT, we engage in a variety of interest rate management techniques that seek to mitigate the influence of interest rate changes on the values of our assets.

Subject to maintaining our qualification as a REIT, we utilize derivative financial instruments, including interest rate swaps, swaptions, TBAs and futures, to hedge the interest rate and related market risks associated with our portfolio. We seek to hedge interest rate risk with respect to both the fixed income nature of our assets and the financing of our portfolio. In hedging interest rates with respect to our fixed income assets, we seek to reduce the risk of losses on the value of our investments that may result from changes in interest rates in the broader markets. In utilizing interest rate hedges with respect to our financing, we seek to improve risk-adjusted returns and, where possible, to obtain a favorable spread between the yield on our assets and the cost of our financing. We rely on our Manager's expertise to manage these risks on our behalf.

#### Interest rate effect on net interest income

Our operating results depend in large part on differences between the income earned on our assets and our cost of borrowing and hedging activities. The costs associated with our borrowings are generally based on prevailing market interest rates. During a period of rising interest rates, our borrowing costs generally will increase while the yields earned on our existing portfolio of leveraged fixed-rate MBS will remain static. Moreover, interest rates may rise at a faster pace than the yields earned on our leveraged adjustable-rate and hybrid MBS. Both of these factors could result

in a decline in our net interest spread and net interest margin. The severity of any such decline would depend on our asset/liability composition at the time, as well as the magnitude and duration of the interest rate increase. Further, an increase in short-term interest rates could also have a negative impact on the market value of our target assets. If any of these events happen, we could experience a decrease in net income or incur a net loss during these periods, which could adversely affect our liquidity and results of operations.

Our hedging techniques are partly based on assumed levels of prepayments of our target assets. If prepayments are slower or faster than assumed, the life of the investment will be longer or shorter, which would reduce the effectiveness of any hedging strategies we may use and may cause losses on such transactions. Hedging strategies involving the use of derivative securities are highly complex and may produce volatile returns.

We acquire adjustable-rate and hybrid MBS. These are assets in which some of the underlying mortgages are typically subject to periodic and lifetime interest rate caps and floors, which may limit the amount by which the security's interest yield may change during any given period. However, our borrowing costs pursuant to our financing agreements are not subject to similar restrictions. Therefore, in a period of increasing interest rates, interest rate costs on our borrowings could increase without limitation, while the interest-rate yields on our adjustable-rate and hybrid MBS could effectively be limited by caps. This issue will be magnified to the extent we acquire adjustable-rate and hybrid MBS that are not based on mortgages that are fully indexed. In addition, adjustable-rate and hybrid MBS may be subject to periodic payment caps that result in some portion of the interest being deferred and added to the principal outstanding. If this happens, we could receive less cash income on such assets than we would need to pay for interest costs on our related borrowings. These factors could lower our net interest income or cause a net loss during periods of rising interest rates, which would harm our financial condition, cash flows and results of operations.

#### Interest rate mismatch risk

We fund the majority of our adjustable-rate and hybrid MBS assets with borrowings that are based on LIBOR, while the interest rates on these assets may be indexed to other index rates, such as the one-year Constant Maturity Treasury index, the Monthly Treasury Average index or the 11th District Cost of Funds Index. Accordingly, any increase in LIBOR relative to these indices may result in an increase in our borrowing costs that is not matched by a corresponding increase in the interest earnings on these assets. Any such interest rate index mismatch could adversely affect our profitability, which may negatively impact distributions to our stockholders. To mitigate interest rate mismatches, we utilize the hedging strategies discussed above.

Our analysis of risks is based on our Manager's experience, estimates, models and assumptions. These analyses rely on models that utilize estimates of fair value and interest rate sensitivity. Actual economic conditions or implementation of decisions by our Manager may produce results that differ significantly from the estimates and assumptions used in our models.

We use a variety of recognized industry models, as well as proprietary models, to perform sensitivity analyses, which are derived from primary assumptions for prepayment rates, discount rates and credit losses. The primary assumption used in this model is implied market volatility of interest rates. The information presented in the following interest sensitivity tables projects the potential impact of sudden parallel changes in interest rates on our financial results and financial condition over the next 12 months, based on our interest sensitive financial instruments at December 31, 2017.

December 31, 2017

Change in Interest rates	Percentage Change in Projected Net Interest Income <sup>(1)</sup>	Percentage Change in Projected Portfolio Value <sup>(2)</sup>
+1.00 %	-84.72 %	-0.57 %
+0.50 %	-42.36 %	-0.20 %
-0.50 %	+42.36 %	-0.13 %
-1.00 %	+84.72 %	-0.64 %

(1) Includes underlying interest income and interest expense associated with our net investment in the 2011-K13 and 2012-KF01 Trusts.

(2) Agency RMBS and Multi-Family MBS only. Includes the fair value of our net investment in the FREMF 2011-K13 and 2012-KF01 Trusts.

The interest rate sensitivity table quantifies the potential changes in net interest income and portfolio value, which includes the value of our derivatives, should interest rates immediately change. The interest rate sensitivity table presents the estimated impact of interest rates instantaneously rising 50 and 100 basis points and falling 50 and 100 basis points. The cash flows associated with our portfolio of MBS for each rate change are calculated based on assumptions, including prepayment speeds, yield on future acquisitions, slope of the yield curve and size of the portfolio. Assumptions are made on the interest rate sensitive liabilities, which are assumed to relate to repurchase agreements, including anticipated interest rates, collateral requirements as a percent of the repurchase agreement, amount and term of borrowing.

The MBS securities, at fair value, included in the foregoing interest rate sensitivity table under "Percentage Change in Projected Portfolio Value" were limited to Agency RMBS and Multi-Family MBS, including the fair value of our net investment in the 2011-K13 and 2012-KF01 Trusts.

Due to the significantly discounted prices and underlying credit risks of our Non-Agency RMBS, we believe our Non-Agency RMBS valuations are inherently de-sensitized to changes in interest rates. As such, we cannot project the impact to these financial instruments and have excluded these RMBS from the interest rate sensitivity analysis. However, these Non-Agency RMBS have been included in the "Percentage Change in Projected Net Interest Income" analysis.

Certain assumptions have been made in connection with the calculation of the information set forth in the foregoing interest rate sensitivity table and, as such, there can be no assurance that assumed events will occur or that other events will not occur that would affect the outcomes. The base interest rate scenario assumes interest rates at December 31, 2017. The analysis utilizes assumptions and estimates based on the judgment and experience of our Manager's team. Furthermore, while we generally expect to retain such assets and the associated interest rate risk to maturity, future purchases and sales of assets could materially change our interest rate risk profile.

The change in annualized net interest income does not include any benefit or detriment from faster or slower prepayment rates on our Agency RMBS, Non-Agency RMBS and Multi-Family MBS. We anticipate that faster prepayment speeds in lower interest rate scenarios will generate lower realized yields on premium Agency RMBS and

higher realized yields on discount Agency and Non-Agency RMBS. Similarly, we anticipate that slower prepayment speeds in higher interest rate scenarios will generate higher realized yields on premium Agency RMBS and lower realized yields on discount Agency and Non-Agency RMBS. Although we have sought to construct our portfolio to limit the effect of changes in prepayment speeds, there can be no assurance this will actually occur, and the realized yield of our portfolio may be significantly different than we anticipate in changing interest rate scenarios.

Given the low interest rates at December 31, 2017, we applied a floor of 0% for all anticipated interest rates included in our assumptions. Because of this floor, we anticipate that any hypothetical interest rate shock decrease would have a limited positive impact on our funding costs; however, because prepayments speeds are unaffected by this floor, we expect that any increase in our prepayment speeds (occurring as a result of any interest rate decrease or otherwise) could result in an acceleration of our premium amortization on Agency RMBS and accretion of discount on our Agency and Non-Agency RMBS. As a result, because this floor limits the positive impact of any interest rate decrease on our funding costs, hypothetical interest rate decreases could cause the fair value of our financial instruments and our net interest income to decline.

The information set forth in the interest rate sensitivity table and all related disclosures constitutes forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act. Actual results could differ significantly from those estimated in the foregoing interest rate sensitivity table.

#### Prepayment risk

Prepayment risk is the risk that principal will be repaid at a different rate than anticipated. As we receive prepayments of principal on our assets, premiums paid on such assets will be amortized against interest income. In general, an increase in prepayment rates will accelerate the amortization of purchase premiums, thereby reducing the interest income earned on the assets. Conversely, discounts on such assets are accreted into interest income. In general, an increase in prepayment rates will accelerate the accretion of purchase discounts, thereby increasing the interest income earned on the assets.

Normally, we believe that we will be able to reinvest proceeds from scheduled principal payments and prepayments at acceptable yields; however, no assurances can be given that, should significant prepayments occur, market conditions would be such that acceptable investments could be identified and the proceeds timely reinvested.

#### Extension risk

We compute the projected weighted-average life of our investments based upon assumptions regarding the rate at which the borrowers will prepay the underlying mortgages. In general, when a fixed-rate or hybrid adjustable-rate security is acquired with borrowings, we may, but are not required to, enter into an interest rate swap agreement or other hedging instrument that effectively fixes our borrowing costs for a period close to the anticipated average life of the fixed-rate portion of the related assets. This strategy is designed to protect us from rising interest rates, because the borrowing costs are fixed for the duration of the fixed-rate portion of the related target asset.

However, if prepayment rates decrease in a rising interest rate environment, then the life of the fixed-rate portion of the related assets could extend beyond the term of the swap agreement or other hedging instrument. This could have a negative impact on our results from operations, as borrowing costs would no longer be fixed after the end of the hedging instrument, while the income earned on the fixed-rate or hybrid adjustable-rate assets would remain fixed. This situation could also cause the market value of our fixed-rate or hybrid adjustable-rate assets to decline, with little or no offsetting gain from the related hedging transactions. In extreme situations, we could be forced to sell assets to maintain adequate liquidity, which could cause us to incur losses.

#### Market risk

**Market value risk.** Our AFS securities are reflected at their estimated fair value, with the difference between amortized cost and estimated fair value reflected in accumulated other comprehensive income. The estimated fair value of these securities fluctuates primarily due to changes in interest rates, market valuation of credit risks and other factors. Generally, in a rising interest rate environment, we would expect the fair value of these securities to decrease; conversely, in a decreasing interest rate environment, we would expect the fair value of these securities to increase. As market volatility increases or liquidity decreases, the fair value of our assets may be adversely impacted.

The sensitivity analysis table presented in "Interest rate mismatch risk" sets forth the estimated impact of an instantaneous parallel shift in the yield curve, up and down 50 and 100 basis points, on the market value of our interest rate-sensitive investments and net interest income, at December 31, 2017, assuming a static portfolio. When evaluating the impact of changes in interest rates, prepayment assumptions and principal reinvestment rates are adjusted based on our Manager's expectations. The analysis presented utilized assumptions, models and estimates of our Manager based on the judgment and experience of our Manager's team.

**Real estate risk.** MBS, residential and multi-family property values are subject to volatility and may be adversely affected by a number of factors, including national, regional and local economic conditions; local real estate conditions (such as an oversupply of housing); changes or continued weakness in specific industry segments; construction quality, age and design; demographic factors; and retroactive changes to building or similar codes. Decreases in property values reduce the value of the collateral for mortgage loans and the potential proceeds available to borrowers to repay the loans, which could cause us to suffer losses on our Non-Agency RMBS and Multi-Family MBS investments.

#### Liquidity risk

Our liquidity risk is principally associated with our financing of long-maturity assets with short-term borrowings in the form of repurchase agreements. Although the interest rate adjustments of these assets and liabilities fall within the guidelines established by our operating policies, maturities are not required to be, nor are they, matched.

Should the value of our assets pledged as collateral suddenly decrease, margin calls relating to our repurchase agreements could increase, causing an adverse change in our liquidity position. Additionally, if one or more of our repurchase agreement counterparties chose not to provide on-going funding, our ability to finance would decline or exist at possibly less advantageous terms. As such, we cannot assure that we will always be able to roll over our

repurchase agreements. See "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations-Liquidity and Capital Resources" for further information about our liquidity and capital resource management.

#### Credit risk

We believe that our investment strategy will generally keep our risk of credit losses low to moderate. However, we retain the risk of potential credit losses on all of the loans underlying our Non-Agency RMBS and Multi-Family MBS. With respect to our Non-Agency RMBS that are senior in the credit structure, credit support contained in RMBS deal structures provides a level of protection from losses. We seek to manage the remaining credit risk through our pre-acquisition due diligence process and by factoring assumed credit losses into the purchase prices we pay for Non-Agency RMBS. In addition, with respect to any particular target asset, our Manager's investment team evaluates relative valuation, supply and demand trends, shape of yield curves, prepayment rates, delinquency and default rates, recovery of various sectors and vintage of collateral. In particular, the evaluation process involves modeling under various different scenarios the future cash flows expected to be generated by a specific security based on the current and projected delinquency and default status of the portfolio, and expected recoveries derived primarily from LTV metrics, relative to the purchase price of the RMBS. At purchase, our Manager estimates the proportion of the discount that we do not expect to recover and incorporates it into our Manager's expected yield and accretion calculations. As part of our Non-Agency RMBS surveillance process, our Manager tracks and compares each security's actual performance over time to the performance expected at the time of purchase or, if our Manager has modified its original purchase assumptions, to its revised performance expectations. To the extent that actual performance of our Non-Agency RMBS deviates materially from our Manager's expected performance parameters, our Manager may revise its performance expectations, such that the amount of purchase discount designated as credit discount may be increased or decreased over time. At times, we may enter into credit default swaps or other derivative instruments in an attempt to manage our credit risk. Nevertheless, unanticipated credit losses could adversely affect our operating results. With respect to our Multi-Family MBS, to date we have purchased subordinated tranches in, or backed by, multi-family securitizations sponsored by Freddie Mac that in certain cases represent the most junior tranche in the capital structure. Our pre-acquisition due diligence process involves an analysis of the multi-family loan portfolio underlying the relevant security, in order to determine the adequacy of available credit enhancement and/or the purchase price discount to absorb potential credit losses on the portfolio.

#### Risk Management

To the extent consistent with maintaining our REIT qualification, we will seek to manage risk exposure to protect our investment portfolio against the effects of major interest rate changes. We may generally seek to manage this risk by:

- relying on our Manager's investment selection process;
- monitoring and adjusting, if necessary, the reset index and interest rate related to Agency and Non-Agency RMBS and other mortgage-related investments and our financings;

attempting to structure our financing agreements to have a range of different maturities, terms, amortizations and interest rate adjustment periods; using hedging instruments, primarily Eurodollar futures, but also interest rate swap agreements, options, interest rate cap agreements, floors and forward sales to adjust the interest rate sensitivity of Agency RMBS and other mortgage-related investments and our borrowings; and actively managing, on an aggregate basis, the interest rate indices, interest rate adjustment periods and gross reset margins of Agency RMBS and other mortgage-related investments and the interest rate indices and adjustment periods of our financings. In executing on our current risk management strategy, we have entered into futures transactions.

## ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The Report of Independent Registered Public Accounting Firm, the Company's consolidated financial statements and notes to the Company's consolidated financial statements appear in a separate section of this Form 10-K (beginning on Page F-2 following Part IV). The index to the Company's consolidated financial statements appears on Page F-1.

## ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

## ITEM 9A. CONTROLS AND PROCEDURES

### Evaluation of Disclosure Controls and Procedures

Our management is responsible for establishing and maintaining disclosure controls and procedures (as defined in Rules 13a-15(e) or 15d-15(e)) under the Securities Exchange Act of 1934, as amended, or Exchange Act, that are designed to ensure that information we are required to disclose in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include controls and procedures designed to ensure that information required to be disclosed by us in the reports we file or submit under the Exchange Act is accumulated and communicated to our management, including our principal executive officer and principal financial officer, to allow timely decisions regarding required disclosure.

Under the supervision and with the participation of management, including our principal executive officer and principal financial officer, we carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to paragraph (b) of Exchange Act Rules 13a-15 or 15d-15 as of December 31, 2017. Based upon our evaluation, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures were not effective as of December 31, 2017 as a result of the material weaknesses described below.

### Management's Annual Report on Internal Control Over Financial Reporting

Our management is also responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Exchange Act Rules 13a-15(f) and 15d-15(f) as a process designed by, or under the supervision of, our principal executive and principal financial officers and effected by our Board, management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles (GAAP) and includes those policies and procedures that:



pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of our assets;  
provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and  
provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

Under the supervision of our Audit Committee and with the participation of management, including our principal executive officer and principal financial officer, we evaluated the effectiveness, as of December 31, 2017, of our internal control over financial reporting. In making this assessment, management used the criteria set forth in the “Internal Control-Integrated Framework” (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO Framework). Based on its evaluation under the COSO Framework, our management has concluded that our internal control over financial reporting was not effective as of December 31, 2017 as a consequence of the material weaknesses described below.

As previously discussed in our 2016 10-K, in connection with our determination of an inability to offset net gains realized on certain hedging transactions in 2013 for federal income tax purposes with net capital losses realized in 2013 on the sale of certain securities, during the quarter ended September 30, 2016, management and our Audit Committee identified a material weakness in our internal control over financial reporting. A “material weakness” is a deficiency, or a combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis. The material weakness consisted of a failure to ensure adequate timely technical review of the position proposed and analysis undertaken by our nationally recognized tax-consulting specialist and taken by us in calculating our REIT taxable income for 2013. As a result, we declared on November 9, 2016, and paid on December 27, 2016, a deficiency dividend to reduce our 2013 undistributed taxable income, as adjusted, and satisfy the REIT distribution requirements. We also recorded a charge of \$1.86 million in the third quarter of 2016 for interest charges expected to be payable to the IRS following the payment of the dividend. The material weakness did not impact any prior period GAAP financial statements, and thus did not result in any misstatements of our annual audited or interim financial statements. Nonetheless, when taken together with the material weakness described below, management and our Audit Committee have concluded that additional remediation measures described below continue to be necessary to enhance our control environment.

In connection with the preparation of our financial statements for inclusion in our 2015 10-K we identified a material weakness in our internal control over financial reporting. Such material weakness did not result in any misstatements in our audited consolidated financial statements included in our 2015 10-K, but did require adjustments during the 2015 annual audit with respect to net income (loss) attributable to common stockholders, total other comprehensive income,

and basic and diluted income (loss) per share in our preliminary 2015 consolidated financial statements, and required the restatement of the unaudited condensed consolidated financial statements for the periods ended June 30, 2015 and September 30, 2015, originally included in our Quarterly Reports on Form 10-Q for the second and third quarters of 2015, respectively.

The material weakness consisted of a failure of our control over the critical timely review of account balances to determine whether the appropriate accounting policy and methodology had been applied, which in turn resulted in the incorrect reporting of unrealized losses on two Non-Agency RMBS IOs for which we had elected the fair value option at the inception of each transaction. Such losses were incorrectly reported through other comprehensive income (OCI) instead of through our statements of operations for each of the quarter and year-to-date periods ended June 30, 2015 and September 30, 2015, respectively. The first IO was acquired in the Oaks Mortgage Trust Series 2015-1 transaction completed in April 2015, and the second IO was acquired in the Oaks Mortgage Trust Series 2015-2 transaction completed in November 2015. In connection with the preparation of our third quarter financial statements for the period ended September 30, 2017, we identified a further instance of a failure of our internal control over the depth and timeliness of review of account balances, specifically relating to the asset and liability balances of securitizations that we consolidate in our financial statements. A discrepancy between the liability balance reported in a consolidation workbook required an adjustment to the asset and liability balances during the preparation of our consolidated balance sheet for the period ended September 30, 2017. While the adjustment did not impact our stockholders' equity or our net income, if uncorrected, such a discrepancy could cause our reported total asset and total liability balances be inaccurate, possibly by material amounts.

This Annual Report on Form 10-K does not include an attestation report of our independent registered public accounting firm regarding our internal control over financial reporting. As an emerging growth company, we are not currently required to obtain such attestation report.

#### Remedial Action

To remediate the material weakness in our internal control over financial reporting related to our REIT taxable income for 2013 noted above, we have implemented certain changes to the design of our internal controls. Specifically, for any REIT tax matters that we have not previously addressed, we are now required to obtain a written technical review and conclusion from a nationally recognized accounting firm or law firm, which must be presented to and approved by our Audit Committee prior to our adoption of the related conclusion.

To remediate the material weakness in our internal control over financial reporting related to timely review of account balances (and consequent deficiencies in our disclosure controls and procedures), we have continued to implement certain changes to the design of our internal controls. Specifically, we previously contracted with a nationally recognized accounting systems and services provider to provide us with a more robust accounting system that has improved the effectiveness of correct accounting treatment for transactions that we enter into. Implementation of the new system was completed effective January 1, 2017, and we have substantially completed the process, with the assistance of an experienced financial reporting consultant, of formalizing enhanced written policies and procedures appropriate to the design and operation of controls and procedures applicable to the new system. We began the testing of controls during the fourth quarter, and also enhanced the timeliness and strengthened the review process in respect of consolidated trust account balances to ensure that the related control operated at the level of precision necessary to effectively and timely identify, investigate and resolve any discrepancies.

We believe the actions described above will be sufficient to remediate the identified material weaknesses and strengthen our internal control over financial reporting, as well as our disclosure controls and procedures. However, while we believe meaningful progress has been made, and the new and enhanced systems and controls are now fully operational, we may determine to take additional measures to address our control deficiencies or to modify the

remediation plans described above. The identified material weakness in our internal control over financial reporting will not be considered remediated until the new controls have been in operation for a sufficient period of time, tested and concluded by management to be designed and operating effectively. We intend that such remediation will be complete by December 31, 2018, but we cannot currently ascertain whether additional actions will be required, or the costs therefor.

#### Changes in Internal Control Over Financial Reporting

Except as described above, there have been no changes in our internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Exchange Act Rule 13a-15 or 15d-15 that occurred during our most recently completed fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

#### ITEM 9B. OTHER INFORMATION.

The following discussion supplements and updates the discussions (the "Prior Discussion") contained in our prospectus dated January 17, 2017 under the heading "U.S. Federal Income Tax Considerations" and prospectus supplement dated October 13, 2017 under the heading "Supplemental U.S. Federal Income Tax Considerations" and supersedes the Prior Discussions to the extent the discussion below is inconsistent with the Prior Discussions. The Prior Discussions and the discussion below (collectively referred to as the "Tax Discussion") are subject to the qualifications set forth therein and below. The tax treatment of security holders will vary depending upon the holder's particular situation, and the Tax Discussion addresses only holders that hold securities as a capital asset and does not deal with all aspects of taxation that may be relevant to particular holders in light of their personal investment or tax circumstances. The Tax Discussion also does not deal with all aspects of taxation that may be relevant to certain types of holders to which special provisions of the federal income tax laws apply, including:

dealers in securities or currencies;

traders in securities that elect to use a mark-to-market method of accounting for their securities holdings;

banks and other financial institutions;

tax-exempt organizations;

certain insurance companies;

persons liable for the alternative minimum tax;

persons that hold securities as a hedge against interest rate or currency risks or as part of a straddle or conversion transaction;

non-U.S. individuals and foreign corporations; and

holders whose functional currency is not the U.S. dollar.

The statements in the Tax Discussion are based on the Code, its legislative history, current and proposed regulations under the Code, published rulings and court decisions. This summary describes the provisions of these sources of law only as they are currently in effect. All of these sources of law may change at any time, and any change in the law may apply retroactively. We cannot assure you that new laws, interpretations of law or court decisions, any of which may take effect retroactively, will not cause any statement in this discussion to be inaccurate.

As supplemented and updated by this summary, and by the discussion in any applicable prospectus supplement, investors should review the discussion in the prospectus under the heading “Federal Income Tax Considerations” for a more detailed summary of the federal income tax consequences of the purchase, ownership, and disposition of our securities and our election to be subject to federal income tax as a REIT.

**PROSPECTIVE INVESTORS SHOULD CONSULT THEIR TAX ADVISORS REGARDING THE U.S. FEDERAL, STATE, LOCAL, FOREIGN AND OTHER TAX CONSEQUENCES OF THE ACQUISITION, OWNERSHIP, AND DISPOSITION OF OUR SECURITIES.**

#### Enactment of Tax Act

On December 22, 2017, the Tax Cut and Jobs Act, which we refer to as the "Tax Act", was enacted. The Tax Act makes major changes to the Code, including a number of provisions of the Code that may affect the taxation of REITs and the holders of their securities. The most significant of these provisions are described below. The individual and collective impact of these changes on REITs and their security holders is uncertain and may not become evident for some period of time. Prospective investors should consult their tax advisors regarding the implications of the Tax Act on their investment.

#### Revised Individual Tax Rates and Deductions

The Tax Act adjusted the tax brackets and reduced the top federal income tax rate for individuals from 39.6% to 37%. In addition, numerous deductions were eliminated or limited, including the deduction for state and local taxes being limited to \$10,000 per year. These individual income tax changes are generally effective beginning in 2018, but without further legislation, they will sunset after 2025.

#### Pass-Through Business Income Tax Rate Lowered through Deduction

Under the Tax Act, individuals, trusts, and estates generally may deduct 20% of “qualified business income” (generally, domestic trade or business income other than certain investment items) of a partnership, S corporation, or sole proprietorship. In addition, “qualified REIT dividends” (i.e., REIT dividends other than capital gain dividends and portions of REIT dividends designated as qualified dividend income eligible for capital gain tax rates) and certain other income items are eligible for the deduction. The deduction, however, is subject to complex limitations to its availability. As with the other individual income tax changes, the provisions related to the deduction are effective beginning in 2018, but without further legislation, they will sunset after 2025.

#### Graduated Corporate Tax Rates Replaced With Single Rate Elimination of Corporate Alternative Minimum Tax

The Tax Act eliminated graduated corporate income tax rates with a minimum rate of 35% and replaced them with a single corporate income tax rate of 21% and reduced the dividends received deduction for certain corporate subsidiaries. The 21% rate may also apply to our net income for any taxable period in which we fail to qualify as a

REIT. The Tax Act also permanently eliminated the corporate alternative minimum tax. These provisions are effective beginning in 2018.

#### Net Operating Loss Modifications

The Tax Act limited the net operating loss (“NOL”) deduction to 80% of taxable income (before the deduction). The Tax Act also generally eliminated NOL carrybacks for individuals and non-REIT corporations (NOL carrybacks did not apply to REITs under prior law) but allows indefinite NOL carryforwards. The new NOL rules apply beginning in 2018.

#### Limitations on Interest Deductibility

The Tax Act limits the net interest expense deduction of a business to 30% of the sum of adjusted taxable income, business interest, and certain other amounts. The Tax Act allows a real property trade or business to elect out of such limitation so long as it uses the alternative depreciation system which lengthens the depreciation recovery period with respect to certain property. The limitation with respect to the net interest expense deduction applies beginning in 2018.

#### Withholding Rate Reduced

The Tax Act reduced the highest rate of withholding with respect to distributions to non-U.S. holders that are treated as attributable to gains from the sale or exchange of U.S. real property interests from 35% to 21%. These provisions are effective beginning in 2018.

#### Potential Acceleration of Income Recognition

The Tax Act may require us to, in certain situations, include certain amounts in income no later than such amounts are reflected on certain of our financial statements. The application of this rule may require us to accrue income earlier than otherwise described in the prospectus. This provision is applicable to tax years beginning after December 31, 2017, but will apply only to taxable years beginning after December 31, 2018 with respect to income from a debt instrument issued with original issue discount.

## PART III

## ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

## Information About Directors

Set forth below is information regarding the current members of our board of directors. The biographical information concerning such directors has been furnished by them to the Company. Age and other information are as of March 1, 2018. There are no family relationships between any director and executive officer.

Name	Age	Position Held with Us	Director Since
James C. Hunt	47	Chairman of the Board	2018
David Oston	59	Chief Financial Officer, Secretary, Treasurer and Director	2012
Neil A. Cummins <sup>(1)</sup>	63	Independent Director	2013
William A. Houlihan <sup>(1)</sup>	62	Independent Director	2013
Walter C. Keenan <sup>(1)</sup>	50	Independent Director	2015

(1)Currently a member of the audit committee, compensation committee and nominating and corporate governance committee. Mr. Houlihan is the chair of our audit committee. Mr. Keenan is the chair of our compensation committee. Mr. Cummins is chair of our nominating and corporate governance committee.

## Board Qualifications

The nominating and corporate governance committee is responsible for reviewing with our board of directors, on an annual basis, the appropriate characteristics, skills and experience required for our board of directors as a whole and its individual members. While the nominating and corporate governance committee has established no minimum eligibility requirements for candidates to serve on our board of directors, in performing its duties, the nominating and corporate governance committee considers any criteria it deems appropriate, including but not limited to the following criteria:

- personal and professional integrity, ethics and values;
- experience in corporate management, such as serving as an officer or former officer of a publicly held company, and a general understanding of marketing, finance and other elements relevant to the success of a publicly-traded company in today's business environment;
- experience in our industry and with relevant social policy concerns;
- experience as a board member of another publicly held company;
- academic expertise in an area of our operations; and
- practical and mature business judgment, including ability to make independent analytical inquiries.

Each director must also possess fundamental qualities of intelligence, honesty, good judgment, high ethics and standards of integrity, fairness and responsibility. The nominating and corporate governance committee may, in its discretion, consider diversity in identifying nominees for directors. Our board of directors evaluates each individual in the context of the board of directors as a whole, with the objective of assembling a group that can best represent stockholder interests through the exercise of sound judgment using its diversity of experience in these various areas. Directors must be willing to devote sufficient time to carrying out their duties and responsibilities effectively, and should be committed to serve on our board of directors for an extended period of time.

We believe that the members of our board of directors represent a desirable mix of backgrounds, skills and experiences, and they all share the personal attributes of effective directors described above. Included in the

biographical information set forth below are some of the specific experiences and skills of our directors that led the board to conclude that, in light of our business and structure, such individuals should serve as members of the board.

#### Biographical Information — Directors

James C. ("Chris") Hunt joined our Board in January 2018 and serves as our Chairman. Mr. Hunt has 25 years of experience in real estate, real estate finance and corporate governance and management. He currently serves as the CEO and President of Hunt Companies, Inc. and has been a member of the Hunt Companies Inc. Board of Directors since 2001. In addition, he serves as CEO and is on the Board of Directors of various subsidiaries and affiliates of Hunt Companies Inc. Mr. Hunt also oversees Hunt's private market real estate development and acquisition activities, which includes market rate residential properties and mixed-use retail developments. Mr. Hunt is responsible for establishing relationships with development and financial partners. Mr. Hunt began his career at Hunt in 1993 as Project Developer for Hunt's construction division, was later appointed Vice President, Executive Vice President and subsequently President. Mr. Hunt received a B.A. in Economics and an MBA from the University of Texas, Austin.

As a consequence of 25 years' experience in real estate, real estate finance and corporate governance and management, Mr. Hunt is well qualified to provide valuable advice to our board of directors in many important areas.

David Oston has been our Chief Financial Officer, Treasurer, Secretary and a director since our formation in March 2012 and has been the CFO, Treasurer and Secretary of our Manager since its formation in March 2012. He has more than 30 years' experience underwriting, investing and managing financial exposures in various sectors of the credit markets. Starting in 2002 through 2008, Mr. Oston was a portfolio manager at Stanfield/Ceres with a focus on structured products and mortgages. Ceres Capital was the investment manager for Victoria. In June 2008, Ceres Capital entered Chapter 11 under the Bankruptcy Code. Mr. Oston became a Managing Director of Ivy Square in 2008, where he remained until joining our Manager in 2012. Prior to Stanfield/Ceres, Mr. Oston spent 13 years with Natexis Banques Populaires in a variety of roles, including CFO of the New York branch, where he had responsibility for portfolio and balance sheet management. Mr. Oston started his career at ANZ/Grindlays, where he spent nine years in a variety of credit-related roles, before spending another two years at Banque Bruxelles Lambert. Mr. Oston graduated with an M.A and a B.A. in Economic Geography from the University of Cambridge, in England.

As a consequence of over 30 years' experience in a wide range of financial and investment management markets, Mr. Oston is well qualified to provide valuable advice to our board of directors in many important areas.

Neil A. Cummins has been an independent director of our board of directors since the closing of our initial public offering, or IPO, in March 2013. Mr. Cummins has been active in international financial markets for over 30 years. Mr. Cummins is currently Chairman of Oak Ridge Investments LLC, a privately-owned investment manager. From 1997 to 2012, Mr. Cummins held a variety of global roles with Barclays Capital, including founding Management Committee member, Global Head of Distribution and Research, Global Head of Strategic Relationship Management and voting member of the Barclays Bank Group Credit Committee. He also served on the Board of Directors of iBoxx Limited and the International Index Company from 2003 to 2005. From 1985 to 1997, Mr. Cummins was a Managing Director of Morgan Stanley, and served on the Board of Directors of Morgan Stanley Bank Luxembourg SA and the Supervisory Board of Morgan Stanley Bank AG, Frankfurt. Prior to 1985, Mr. Cummins worked in the international financial markets, principally with Mellon Bank N.A. Mr. Cummins graduated with a B.A. in Economics from Indiana University.

As a consequence of over 30 years' experience in international financial markets, Mr. Cummins is well qualified to provide valuable advice to our board of directors in many important areas.

William A. Houlihan has been an independent director of our board of directors since the listing of our common stock on the NYSE in March 2013. Mr. Houlihan has more than 30 years of diversified financial sector and business experience.

He has served since November 2012 as a director and audit committee chairman for Max Exchange, LLC, a privately-owned residential mortgage loan trading business. He has served since 2009 as a director and financial expert on the audit committee of First Physicians Capital Group, a privately-owned healthcare investment company, which was registered with the Securities and Exchange Commission, or SEC, prior to completion of a going-private transaction in January 2015, from April 2013 to September 2014 as Non-Executive Chairman of its board of directors and since May 2013 as the chairman of its audit committee.

He served from July 2013 to July 2015 as lead independent director and chairman of the audit committee of Tiptree Financial Partners, LP, or Tiptree, a publicly traded financial services holding company; and from August 2010 to July 2013 as lead independent director and chairman of the audit committee for Care Investment Trust, a publicly traded healthcare REIT which merged with Tiptree in July 2013. From 2003 to 2010, he was a director of SNL Financial, a privately owned financial information company, and in addition, from 1998 to 2012 he was a director and shareholder of a family-owned commercial real estate investment partnership.

He served from March 2013 to February 2014 as the chief financial officer for Amalgamated Bank, a privately owned company. From 2001 through 2008, Mr. Houlihan was a private investor while he served as transitional Chief Financial Officer for several distressed financial services companies: Sixth Gear, Inc. from October 2007 to November 2008, Sedgwick Claims Management Services from August 2006 until January 2007, Metris Companies from August 2004 to January 2006, and Hudson United Bancorp from January 2001 to November 2003. From 1981 until 2000, and for short-term periods in 2004 and 2007, Mr. Houlihan worked for a number of investment banking companies, including UBS, J.P. Morgan, Keefe Bruyette & Woods, Bear Stearns and Goldman Sachs. He also held several auditing and accounting positions from June 1977 through June 1981.

Mr. Houlihan graduated with an M.B.A. in Finance from New York University Graduate School of Business, and a B.S. in Accounting from Manhattan College. In addition, he was licensed as a Certified Public Accountant, but his license is currently inactive. Since January 2017, he has served as an adjunct professor at the Feliciano School of



Business at Monclair State University.

On March 13, 2015, Mr. Houlihan settled an administrative proceeding brought by the SEC regarding his alleged failure to file on a timely basis required Schedule 13D amendments and Section 16(a) reports relating to his beneficial ownership of securities of First Physicians Capital Group, Inc., or FPCG. Mr. Houlihan is a member of the board of directors of FPCG and a greater than 10% beneficial owner of FPCG securities. In the settlement, Mr. Houlihan did not admit or deny the SEC's allegations, consented to the entry of a cease and desist order requiring him not to cause any violation of Sections 13(d)(2) and 16(a) of the Securities Exchange Act of 1934, as amended, or the Exchange Act, and agreed to pay a civil penalty of \$15,000 to the SEC.

As a consequence of Mr. Houlihan's over 30 years of pertinent experience, qualifications and skills including significant financial expertise and literacy, he is well qualified to provide significant and relevant expertise and advice to our board of directors in relation to many areas, including accounting and financial matters.

Walter C. Keenan has been an independent director of our board of directors since April 17, 2015. Mr. Keenan has over 25 years of experience in the financial services industry as an advisor, investor and executive manager. Since July 2013, he has served as Chief Executive Officer of Advantage Insurance Inc., or Advantage Insurance, a specialty insurance group serving the insurance needs of high net worth individuals and business owners worldwide. Mr. Keenan was a consultant to Advantage Insurance from July 2012 through July 2013. From October 2013 to May 2016, Mr. Keenan served as a director and audit committee chair of Republic Companies, Inc., a regional property and casualty insurance company. Prior to joining Advantage Insurance, from March 2011 to October 2011, Mr. Keenan served as Executive Chairman of Medicus Insurance Holdings, Inc., a provider of professional liability insurance to physicians, and was Chairman from July 2006 to March 2011. Before becoming an insurance industry executive, Mr. Keenan worked in private equity as President of JMP Capital, the principal investments group of JMP Group LLC (NYSE: JMP) from 2007 to 2011 and as a Principal of The Cypress Group from 2005 to 2007. Mr. Keenan's work for JMP and Cypress included strategic investments in two mortgage REIT companies. Mr. Keenan began his career at Morgan Stanley, where he worked in investment banking from 1989 to 2003. Mr. Keenan received a Bachelor of Arts degree with Honors from Southern Methodist University.

As a consequence of over 25 years' experience in financial services, Mr. Keenan is well qualified to provide valuable advice to our board of directors in many important areas.

#### Information About Executive Officers

Set forth below is information regarding our executive officers as of March 1, 2018. Each officer holds office at the pleasure of our board of directors and until their successors shall have been duly elected and qualified. There are no family relationships between any director and executive officer.

Name	Age	Position Held with Us
James P. Flynn	40	Chief Executive Officer
Michael Larsen	38	President
David Oston	59	Chief Financial Officer, Secretary, Treasurer and Director

#### Biographical Information - Executive Officers

James P. Flynn has been our Chief Executive Officer since January 2018. He has over 15 years' experience in the financial markets. Mr. Flynn currently serves as President and Chief Investment Officer of Hunt Mortgage Group, a wholly owned subsidiary of Hunt Companies, Inc., an affiliate of our Manager. Mr. Flynn joined Hunt Mortgage Group (formerly Centerline Capital Group) in 2007 and is a member of its executive management team and investment and credit committees. Prior to joining Hunt Mortgage Group, Mr. Flynn practiced law at Gibson Dunn & Crutcher LLP in its real estate practice group and prior to that Mr. Flynn was an investment banker at Lehman Brothers. Mr. Flynn received a B.S. in Finance and Accounting from the McDonough School of Business at Georgetown University, magna cum laude and JD from Columbia University Law School, Harlan Fiske Stone Scholar. Mr. Flynn is a member of the California State Bar, ULI, CREFC, MBA and NAREIM.

Michael Larsen has been our President since January 2018. He has over 15 years' experience in the financial markets. Mr. Larsen currently serves as Senior Managing Director, Chief Financial Officer and Chief Operating Officer of Hunt Mortgage Group, a wholly-owned subsidiary of the Hunt Companies, Inc., an affiliate of our Manager. Mr. Larsen joined Hunt Mortgage Group (formerly Centerline Capital Group) in 2002 and is a member of its executive management team and investment committee. Prior to joining Hunt Mortgage Group, Mr. Larsen worked in the real estate consulting and structured finance practices at Arthur Andersen. Mr. Larsen received a B.A. from the University of Pennsylvania and an MBA from Columbia University. Mr. Larsen has been a participant in the Real Estate Roundtable's TPAC and RECPAC committees and is a member of the MBA.

David Oston. See “Biographical Information — Directors” above.

#### SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE

Under federal securities laws, our executive officers, directors and any persons beneficially owning more than 10% of a registered class of our equity securities are required to report their ownership and any changes in that ownership to the SEC. These persons are also required by SEC rules and regulations to furnish us with copies of these reports.

Based solely on our review of the reports and amendments to those reports furnished to us or written representations from our directors and executive officers that these reports were not required from those persons, we believe that, during the year ended December 31, 2017, all of these filing requirements applicable to our directors, executive officers, and greater than 10% stockholders were complied with on a timely basis.

#### Code of Ethics

Concurrently with our IPO, we adopted a Code of Business Conduct and Ethics and Policy Against Insider Trading that is applicable to all of our executive officers and other personnel, including our principal executive officer, our principal financial officer, our principal accounting officer, our controller, and persons performing similar functions for the Company. The Code of Business Conduct and Ethics and Policy Against Insider Trading establishes policies and procedures that we believe promote adherence to, and the conduct of business according to, the highest ethical standards. A copy of our Code of Business Conduct and Ethics and Policy Against Insider Trading is available on the “Investors Relations” section of our website at <http://investor.fiveoaksinvestment.com/> under the Corporate Governance tab.

## Corporate Governance Guidelines

Concurrently with our IPO, we adopted a set of Corporate Governance Guidelines, which describe our corporate governance practices and policies and provide a framework for the governance of our board of directors. The nominating and corporate governance committee is responsible for overseeing these guidelines and reporting and making recommendations to our board of directors concerning corporate governance matters. From time to time, the nominating and corporate governance committee reviews our Corporate Governance Guidelines and, if necessary, recommends changes to the full board of directors. Our current Corporate Governance Guidelines are available in the “Investors Relations” section of our website at <http://investor.fiveoaksinvestment.com/> under the Corporate Governance tab.

## Audit Committee

The Company maintains a separately designated standing audit committee established in accordance with Section 3(a)(58)(A) of Securities Exchange Act of 1934, as amended, or the Exchange Act. The Audit Committee currently consists of Messrs. Cummins, Houlihan and Keenan.

## Audit Committee Financial Expert

Mr. Houlihan is the chair of our audit committee. Our board of directors has determined that Mr. Houlihan qualifies as an “audit committee financial expert” as such term is defined in Item 407(d)(5)(ii) of Regulation S-K based on his education and experience in his respective fields, and is independent under the current listing standards of the NYSE.

## ITEM 11. EXECUTIVE COMPENSATION

### Compensation Discussion and Analysis

Our Compensation Discussion and Analysis describes our compensation program, objectives and policies for our executive officers for the year ended December 31, 2017.

## Overview of Compensation Program and Philosophy

We have no employees. We are externally managed by our Manager pursuant to a management agreement between our Manager and us. Because the management agreement provides that our Manager is responsible for managing our affairs, our Manager provides us with all of the personnel required to manage our operations. As a result, our executive officers, all of whom were employees of our Manager for the year ended December 31, 2017, do not receive any cash compensation from us. Instead, we pay our Manager a management fee and our Manager uses the proceeds from the management fee, in part, to pay compensation to its officers and personnel, including our executive officers. We do not reimburse our Manager or its affiliates for the salaries and other compensation of their personnel other than our chief financial officer, general counsel and other corporate finance, tax, accounting, internal audit, legal risk management, operations, compliance and other non-investment personnel of the Manager and its affiliates who spend all or a portion of their time managing our affairs, based on the percentage of time each spends on our affairs. Our Manager makes all decisions relating to the compensation of our executive officers based on such factors as our Manager may determine are appropriate.

Our Manager utilizes compensation programs that are designed, structured and implemented to align with our long-term strategic objectives. Specifically, our Manager's compensation programs are designed to provide competitive compensation tied to strategic and financial results, differentially reward high performers, and provide an appropriate mix of cash and deferred compensation.

We did not pay any cash compensation to any of our executive officers, nor did we make any grants of plan-based awards, stock options or stock grants of any kind to them for the year ended December 31, 2017; however, we have adopted the Manager Equity Plan pursuant to which we make awards to our Manager which, in turn, grants such awards to its employees, officers, members (including our current executive officers), directors or consultants. We do not provide our executive officers with pension benefits, perquisites or other personal benefits. We do not have any employment agreements with any person and have no arrangements to make cash payments to our executive officers upon their termination from service as our officers or a change in control of the Company.

## Certain Risks Related to Compensation

As noted above, we are externally managed by our Manager pursuant to the terms of the management agreement and we do not pay our executive officers any compensation. The base fee under the management agreement is calculated based on a percentage of stockholders' equity and is payable quarterly in arrears. Calculation of the management fee is not primarily dependent upon our financial performance or the performance of our management, and thus the base management fee does not create an incentive for management to take excessive or unnecessary risks. Pursuant to the new management agreement we signed with our Manager on January 18, 2018, starting in the first full quarter commencing after the first 12-month anniversary of the signing, we are also required to pay out Manager an incentive fee of 20% of the excess of our Core Earnings (as defined in the management agreement) over a hurdle rate of 8% per annum. There is a risk that the introduction of an incentive fee can promote excessive and unnecessary risk. See risk factor entitled "The incentive fee payable to our Manager under the management agreement is payable quarterly and is based on our core earnings and, therefore, may cause our Manager to select investments in more risky assets to increase its incentive compensation," on page 24.

The initial term of the Management Agreement ends on January 18, 2021. The Management Agreement automatically renews for successive one year terms beginning January 18, 2021 and each January 18 thereafter, unless it is sooner terminated upon written notice delivered no later than 180 days prior to a renewal date by the affirmative vote of at least two-thirds (2/3) of the independent directors of the Board or by a vote of at least two-thirds of our outstanding shares of common stock, based upon a determination that (a) the Manager's performance is unsatisfactory and materially detrimental to us or (b) the compensation payable to the Manager under the Management Agreement is not

fair to us (provided that in the instance of (b), we shall not have the right to terminate the Management Agreement if the Manager agrees to continue to provide services under the Management Agreement at fees that at least two-thirds of the independent directors of the Board determine to be fair, provided further that in the instance of (b), the Manager will be afforded the opportunity to renegotiate its compensation prior to termination). We may also terminate the Management Agreement at any time, including during the initial term, without the payment of any termination fee, with at least 30 days' prior written notice from us "for cause" as described in the Management Agreement. In the event of a termination of the Manager other than a termination for cause, we are required to pay a termination fee to the Manager. The termination fee is equal to three times the sum of (a) the average annual Base Management Fee and (b) the average annual Incentive Fee, in each case, earned by the Manager during the 24-month period immediately preceding the effective date of termination, calculated as of the end of the most recently completed fiscal quarter before the effective date of termination. Our Manager may terminate the Management Agreement upon written notice delivered no later than 180 days prior to a renewal date.

#### Insider Trading Policy

We maintain an insider trading policy, which prohibits short selling, dealing in publicly traded options and hedging or monetization transactions in our securities.

#### Director Compensation

##### Executive directors

A member of our board of directors who is also an employee of our Manager or any of our or its affiliates is referred to as an executive director. David Oston is our only executive director. Executive directors do not receive cash compensation for serving on our board of directors. However, we have adopted the Manager Equity Plan pursuant to which we make awards to our Manager, which in turn, grants such awards to its employees, officers, members (including our current officers), directors or consultants. The purpose of any such grants will be to encourage their respective individual efforts toward our continued success, long-term growth and profitability and to reward and retain them.

##### Independent directors

As compensation for serving on our board of directors, each independent director receives an annual cash retainer of \$50,000, payable in arrears, and an annual retainer of 1,500 restricted shares of our common stock, granted under our Manager Equity Plan. The grants of restricted stock are generally made immediately following our annual stockholders' meeting, and vest in full on the first anniversary of the grant date, subject to continuing service on our board of directors on the vesting date. We also reimburse these independent directors for reasonable out-of-pocket expenses incurred in connection with the performance of their duties as directors, including, without limitation, travel expenses in connection with their attendance at full board of directors and committee meetings. In addition, the chair of our audit committee receives a separate annual cash retainer of \$15,000, and the chairs of our compensation committee and our nominating and corporate governance committee each receive an annual cash retainer of \$10,000, in each case in addition to the annual board service cash retainer and the grant of 1,500 restricted shares of our common stock. Independent directors may also receive retainers or meeting fees for participation on ad hoc committees formed on an as-needed basis from time to time.

Our senior management reports once a year to the full board of directors or the compensation committee regarding the status of our non-management director compensation in relation to other U.S. companies of comparable size and our competitors. Such report includes consideration of both direct and indirect forms of compensation to our non-management directors and recommends any changes in non-management director compensation. Director fees are the sole form of compensation that members of our audit committee receive from us.

#### Director Compensation for 2017

The table below sets forth the compensation paid to each individual serving as a non-executive director at any time during 2017\*.

Name	Fees Earned or Paid in Cash	Stock Awards <sup>(1)</sup>	All Other Compensation <sup>(2)</sup>	Total
Neil A. Cummins	\$ 60,000	\$ 6,495	\$ 3,750	\$70,245
William A. Houlihan	65,000	6,495	3,750	75,245
Walter C. Keenan	60,000	6,495	1,950	68,445

\* Columns for “Option Awards,” “Non-Equity Incentive Plan Compensation” and “Change in Pension Value and Nonqualified Deferred Compensation Earnings” have been omitted because they are not applicable.

(1) The amounts in this column reflect the aggregate grant date fair value of grants of restricted stock to each listed director on October 18, 2017, calculated in accordance with ASC Topic 718. Assumptions used in the calculation of these amounts are included in Note 14 to our audited financial statements for the year ended December 31, 2017. As of December 31, 2017, each of Messrs. Cummins, Houlihan and Keenan held 1,500 unvested shares of restricted stock (and Messrs. Cummins and Houlihan each held 6,000 shares of formerly restricted stock that vested prior to such date and Mr. Keenan held 3,000 shares of formerly restricted stock that vested prior to such date).

(2) The amounts in this column reflect dividends paid in 2017 on all vested and unvested shares of restricted stock held by the directors in the table.

#### COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION

During 2017, Messrs. Cummins, Houlihan and Keenan were members of our compensation committee. Each of the members of the compensation committee is (and was during his service in 2017) an independent director. No member of the compensation committee at any time during 2017 was an officer or employee of the Company or any of its subsidiaries during 2016, and no such individual was formerly an officer of the Company or any of its subsidiaries or was a party to any disclosable related person transaction involving the Company. During 2017, none of the executive officers of the Company has served on the board of directors or on the compensation committee of any other entity that has or had executive officers that served as a member of the board of directors or compensation committee of the Company.

#### COMPENSATION COMMITTEE REPORT

Our compensation committee has reviewed and discussed the Compensation Discussion and Analysis herein with management and, based on such review and discussion, has recommended to our board of directors that such Compensation Discussion and Analysis be included in this Annual Report on Form 10-K.

March 16, 2018

Compensation Committee

Neil A. Cummins  
William Houlihan  
Walter C. Keenan (Chairman)

**ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

**Securities Authorized for Issuance under Equity Compensation Plan**

The Five Oaks Investment Corp. Manager Equity Plan, or the Manager Equity Plan, includes provisions for grants of restricted common stock and other equity based awards to our Manager and to our independent directors, consultants or officers whom we may directly employ in the future, if any. In turn, our Manager grants such awards to its employees, officers (including our current officers), members, directors or consultants. The total number of shares that may be granted subject to awards under the Manager Equity Plan is equal to an aggregate of 3.0% of the total number of issued and outstanding shares of our common stock (on a fully diluted basis) at the time of each award (other than any shares issued or subject to awards made pursuant to the Manager Equity Plan).

The following information is with respect to our Manager Equity Plan as of December 31, 2017:

## Equity Compensation Plan Information

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in the first column)
Equity compensation plans approved by security holders	—	—	724,418
Equity compensation plans not approved by security holders	—	—	—
Total	—	—	724,418

## Security Ownership of Certain Beneficial Owners and Management

The following table sets forth information regarding the beneficial ownership of shares of our common stock and 8.75% Series A Cumulative Redeemable Preferred Stock, or Preferred Stock, as of March 1, 2018, by: (1) each director of the Company, (2) each executive officer of the Company, (3) all directors and executive officers of the Company as a group, and (4) all persons known by us to be beneficial owners of more than 5% of any class of our voting securities.

In accordance with SEC rules, beneficial ownership includes: all shares the investor actually owns beneficially or of record; all shares over which the investor has or shares voting or dispositive control (such as in the capacity as a general partner of an investment fund); and all shares the investor has the right to acquire within 60 days (such as shares of restricted common stock which are scheduled to vest within 60 days).

Unless otherwise indicated, all shares are owned directly, and the indicated person has sole voting and investment power. Except as indicated in the footnotes to the table below, the business address of each of the individuals listed below is the address of our principal executive office, 230 Park Avenue, 19th Floor, New York, New York 10169. None of our shares of common stock beneficially owned by any of our directors or executive officers have been pledged as security.

## Beneficial Ownership Table

Name of Beneficial Owner	Shares of Common Stock Owned	Percentage of Common Stock Owned	Shares of Preferred Stock Owned	Percentage of Preferred Stock Owned
5% Holders				
XL Investments Ltd <sup>(1)</sup>	3,330,550	14.06 %	—	—



Edgar Filing: Five Oaks Investment Corp. - Form 10-K

XL Global, Inc. <sup>(2)</sup>	10,230	*	—	—
Hunt Companies Equity Holdings LLC <sup>(3)</sup>	2,249,901	9.50	%	—
Directors and Executive Officers <sup>(4)</sup>				
James P. Flynn	—	*	—	—
James C. Hunt	—	*	—	—
Michael Larsen	—	*	—	—
David Oston	40,352	*	—	—
Neil A. Cummins	22,294	*	—	—
William A. Houlihan	40,293	*	—	—
Walter C. Keenan	11,511	*	—	—
All directors and executive officers as a group (seven persons)	114,450	0.48	%	—

\* Represents less than 1% of the shares of our common stock outstanding.

XL Investments Ltd, or XL Investments, is the record owner of 3,330,550 shares of common stock. XL Group Ltd is the ultimate parent holding company of XL Investments and indirectly owns all of the equity interests of XL Investments. XL Group Ltd is a Bermuda exempted company whose ordinary shares are listed on the NYSE. The address for XL Investments is One Bermudiana Road, Hamilton HM08, Bermuda. Pursuant to an agreement dated January 18, 2018, with affiliates of Hunt Companies, Inc., XL Investments agreed to terminate warrants to purchase 3,753,492 shares of common stock held by XL Investments.

XL Global is the record owner of 10,230 shares of common stock. XL Group Ltd is the ultimate parent holding company of XL Global and indirectly owns all of the equity interests of XL Global. XL Group Ltd. is a Bermuda exempted company whose ordinary shares are listed on the NYSE. The address for XL Global is 200 Liberty Street, 22nd Floor, New York, New York 10281.

Pursuant to the terms of a securities purchase agreement with us dated January 18, 2018, Hunt Companies Equities Holdings LLC, or Hunt CE Holdings LLC, agreed to purchase 1,539,406 shares of common stock for an aggregate purchase price of \$7,342,967. In addition, pursuant to the terms of a

share purchase agreement dated January 18, 2018, between Hunt CE Holdings LLC and XL Investments, Hunt CE Holdings LLC agreed to purchase 710,495 shares of common stock for an aggregate purchase price of \$3,389,061.

(4) Excludes David C Carroll and Kian Fui (Paul) Chong, who as of March 1, 2018, were no longer directors or officers of the Company.

## ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE

### TRANSACTIONS WITH RELATED PERSONS

#### Management Agreement

On January 18, 2018, we entered a new management agreement with HIM, which replaced the previous management agreement we had executed on May 16, 2012, with Oak Circle Capital Partners LLC, pursuant to which our Manager provides for the day-to-day management of our operations. The management agreement requires our Manager to manage our business affairs in conformity with the policies and the investment guidelines that are approved and monitored by our board of directors. All of our executive officers are employees of our Manager, or affiliates thereof. Pursuant to the prior management agreement, we paid our Manager a monthly management fee and reimbursed our prior Manager for certain expenses. For the years ended December 31, 2017 and 2016, the Company incurred management fees under the management agreement of \$2,215,050 and \$2,472,353, respectively. In addition, the Company is required to reimburse the Manager for operating expenses related to the Company incurred by the Manager, including accounting services, auditing and tax services, technology and office facilities, operations, compliance, legal and filing fees, and miscellaneous general and administrative costs, including the cost of non-investment management personnel of the Manager who spend all or a portion of their time managing the Company's affairs. For the years ended December 31, 2017 and 2016, the Company incurred reimbursable expenses of \$4,127,549 and \$4,747,275, respectively.

#### Relationship with the XL Group of Companies

XL Investments, an indirect wholly owned subsidiary of XL Group Ltd, purchased \$25.0 million of our shares of common stock in May 2012. As part of its investment in May 2012, XL Investments also agreed to make an additional investment in us of up to \$25.0 million, subject to certain conditions and over a period of time. The conditions were deemed satisfied upon the closing of our IPO, and accordingly XL Investments accelerated the timing of its investment and bought \$25.0 million of our common stock in a concurrent private placement at the IPO price, or 1,666,667 shares. Pursuant to a share purchase agreement dated January 18, 2018, XL Investment agreed to sell 710,495 shares to Hunt Companies Equities Holdings, LLC. Accordingly, as of March 1, 2018, XL Investments owned 14.06% of our common stock. Despite the reduction in the number of shares of our common stock owned by, and an agreement to terminate all of the warrants previously held by, XL Investments, it maintains a significant ownership stake in us and therefore, XL Investments will continue to have the ability to influence the outcome of matters that require a vote of our stockholders, including a change of control.

We have agreed with XL Investments that, for so long as XL Investments and any other of the XL group of companies collectively beneficially own at least 9.8% of our issued and outstanding common stock (on a fully diluted basis), XL Investments will have the right to appoint an observer to attend all board of directors' meetings but such observer will have no right to vote at any board of directors meeting. The board observer will be indemnified by us to the same extent as our directors.

Our charter prohibits, with certain exceptions, any stockholder from beneficially or constructively owning, applying certain attribution rules under the Internal Revenue Code, more than 9.8% by value or number of shares, whichever is more restrictive, of our outstanding shares of common stock, or 9.8% by value or number of shares, whichever is more

restrictive, of our outstanding capital stock. Our board of directors has granted XL Investments an exemption from the 9.8% ownership limitation.

#### Relationship with the Hunt Companies, Inc. Group of Companies

On January 18, 2018, we entered into a series of transactions with affiliates of the Hunt Companies, Inc. ("Hunt"). Having simultaneously agreed to terminate the management agreement with our prior manager, Oak Circle Capital Partners, LLC, we entered into a new management agreement with Hunt Investment Management, LLC ("HIM"), pursuant to which HIM provides for the day-to-day management of our operations. Additionally, another affiliate of Hunt purchased 1,539,406 shares of our common stock in a private placement, and purchased a further 710,495 shares of common stock from XL Investments, resulting in Hunt owning an aggregate of 9.50% of our common stock upon closing of the transaction. Hunt Mortgage Group, another affiliate of Hunt, has granted a right of first offer on certain commercial real estate or multi-family loans which are floating-rate and bridge or transitional in nature.

As a consequence of affiliates of Hunt serving as our Manager, maintaining a significant ownership stake in us, and originating loans and credit risk securities that we will purchase and hold on our balance sheet, the potential exists for conflicts of interest to arise in our relationship with Hunt. In addition, after an initial grace period of 12 months, we will be required to pay our Manager an incentive fee if our core earnings (as defined in our management agreement) exceed a hurdle rate of 8% per annum. This may encourage our Manager to take excessive risks with our investment, hedging or business strategies in order to manage our core earnings such that they will exceed the hurdle rate, and therefore that an incentive fee will be payable. Our board of director's is responsible for supervising our Manager, and ensuring that in managing our day-to-day operations, our Manager does so in a manner that appropriately addresses any potential conflicts of interest. There is no guarantee that the policies and procedures adopted by us, the terms and conditions of the Management Agreement or the policies and procedures adopted by our Manager, Hunt and their respective affiliates, will enable us to identify, adequately address or mitigate all potential conflicts of interests.

We entered into a Shareholder Agreement with Hunt Companies Equity Holdings, LLC ("HCEH") pursuant to which, the Company granted HCEH the right to designate one designee to the Company's Board. The right granted to HCEH expires at such time as HCEH's and its affiliates "beneficial ownership" of the Company's common stock as determined pursuant to Rule 13d-3 under the Exchange Act of 1934, is less than 5%.

#### Registration Rights Agreements

We have entered into a registration rights agreement with XL Investments, our Manager, Messrs. Carroll, Chong and Oston, and Darren Comisso and Thomas Flynn (executive officers of our prior Manager) pursuant to which we have agreed to register the resale of shares of common stock owned by XL Investments and its transferees, any shares of common stock owned from time to time by Messrs. Carroll, Chong, Comisso, Flynn and Oston and their transferees and any shares of common stock and warrants that we may grant to our Manager under the Manager Equity Plan, which we collectively refer to as the registrable securities. Pursuant to the registration rights agreement, XL Investments and its affiliated transferees have the right to demand that we cause their registrable securities to be

registered for resale on a registration statement. All other holders of registrable securities have the option to include their registrable securities in such registration statement and we must maintain the effectiveness of such registration statement until all the registrable securities are sold under a shelf registration statement or another registration statement, or until all the registrable securities are eligible to be sold pursuant to Rule 144 under the Securities Act of 1933, as amended, or the Securities Act, without volume limitation or other restrictions on transfer; however, XL Investments and its affiliated transferees are limited to two demand registrations. The registration rights agreement also requires us to file a “shelf registration statement” for the remaining registrable securities as soon as practicable after we become eligible to use Form S-3, and we must maintain the effectiveness of this shelf registration statement until all the registrable securities have been sold under the shelf registration statement or sold pursuant to Rule 144 under the Securities Act. On April 29, 2016, we filed a “shelf registration statement” for the registrable securities, which was declared effective by the SEC on July 20, 2016.

On January 18, 2018, we entered into an additional registration rights agreement with Hunt Companies Equity Holdings, LLC, pursuant to which we agreed to register the resale of shares of common stock owned by Hunt Companies Equity Holdings, LLC. Pursuant to the registration rights agreement, Hunt Companies Equity Holdings, LLC, and its affiliated transferees were provided with certain demand and piggyback registration rights in respect of shares of our common stock owned or subsequently acquired by them.

#### Related Party Transaction Policies

Concurrently with our IPO, our board of directors adopted a written policy regarding the approval of any “related person transaction,” which is any transaction or series of transactions in which we are or are to be a participant, the amount involved exceeds \$120,000 and a “related person” (as defined under SEC rules) has a direct or indirect material interest. Under the policy, a related person must promptly disclose to our compliance officer any related person transaction and all material facts about the transaction. Our secretary would then assess and promptly communicate that information to the compensation committee of our board of directors. Based on its consideration of all of the relevant facts and circumstances, the compensation committee will decide whether or not to approve such transaction and will generally approve only those transactions that do not create a conflict of interest. If we become aware of an existing related person transaction that has not been pre-approved under this policy, the transaction will be referred to the compensation committee, which will evaluate all options available, including ratification, revision or termination of such transaction. Our policy requires any director who may be interested in a related person transaction to recuse himself or herself from any consideration of such related person transaction.

#### Limitations on Liability and Indemnification of Officers and Directors

Our charter and bylaws provide indemnification for our directors and officers to the fullest extent permitted by Maryland law in effect from time to time, to obligate itself to indemnify and to pay or reimburse reasonable expenses in advance of final disposition of a proceeding to (1) any individual who is a present or former director or officer of ours or (2) any individual who, while a director or officer of ours and at our request, serves or has served as a director, officer, partner or trustee of another corporation, real estate investment trust, partnership, joint venture, trust, employee benefit plan or any other enterprise from and against any claim or liability to which such person may become subject or which such person may incur by reason of his or her service in such capacity. We have the power, with the approval of our board of directors, to provide such indemnification and advancement of expenses to a person who served a predecessor of ours in any of the capacities described in (1) or (2) above and to any employee or agent of ours or a predecessor of ours. However, the Maryland General Corporation Law, or MGCL, prohibits us from indemnifying a director or officer for any act or omission if:

• the act or omission of the director or officer was material to the matter giving rise to the proceeding and (i) was committed in bad faith or (ii) was the result of active and deliberate dishonesty;

the director or officer actually received an improper personal benefit in money, property or services; or in the case of any criminal proceeding, the director or officer had reasonable cause to believe that the act or omission was unlawful.

In addition, under the MGCL, we may not indemnify a director or officer in a suit by us or in our right in which the director or officer was adjudged liable to us or in a proceeding in which the director or officer was adjudged liable on the basis that a personal benefit was improperly received. However, indemnification with respect to any proceeding by us or in our right or in which the director or officer was adjudged liable on the basis that a personal benefit was improperly received shall be limited to expenses. A court may order indemnification if it determines that the director or officer is fairly and reasonably entitled to indemnification, even though the director or officer did not meet the prescribed standard of conduct or was adjudged liable on the basis that a personal benefit was improperly received.

We have entered into indemnification agreements with each of our directors and executive officers that would provide for indemnification to the maximum extent permitted by Maryland law.

The above-described limitation of liability and indemnification may be held not to be enforceable for violations of the federal securities laws of the United States.

#### Independence Determinations

Our board of directors undertakes periodic reviews of director independence. In such reviews, the board of directors considers transactions and relationships between (1) each director, entities with which such person is affiliated and/or any member of such person's immediate family, and (2) the Company and its subsidiaries and affiliates, in order to ascertain whether any such relationships or transactions are inconsistent with a determination that such person is "independent" in accordance with applicable rules and regulations of the NYSE, applicable law, and the rules and regulations of the SEC. The board of directors bases its determinations primarily on a review of the responses of such persons to questions regarding employment and compensation history, affiliations and family and other relationships between the Company, the directors, and entities with which such persons are affiliated, discussions and analyses with respect to the foregoing, and the recommendations of the nominating and corporate governance committee.

As a result of such reviews, as well as the directors' responses to the Company's questionnaire with respect to independence matters, our board of directors has affirmatively determined that all persons who served as directors of the Company during any part of the 2017 calendar year, and all current directors, were and are "independent" for purposes of Section 303A of the Listed Company Manual of the NYSE, with the exception of Mr. Carroll, the Company's Chief Executive Officer and President prior to January 18, 2018, Mr. Oston, the Company's Chief Financial Officer, Secretary and Treasurer, and Mr. Hunt, the Company's Chairman of the Board. Each individual who was a member of the Company's audit committee, compensation committee, and nominating and corporate governance committee during any part of the 2017 calendar year has been determined by our board of directors to be independent in accordance with such standards as well. In determining that each director other than Messrs. Hunt, Carroll and Oston are independent, in addition to confirming that none of the automatic disqualifications prescribed

by the NYSE are applicable to such persons, the board of directors also affirmatively determined that each such person has no direct or indirect material relationship with the Company or its subsidiaries.

As none of Messrs. Cummins, Houlihan or Keenan had or has any direct or indirect relationship with the Company or its subsidiaries, they were each deemed to be independent.

#### ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

##### FEES BILLED BY THE INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Fees and expenses paid to our principal accountant, Grant Thornton LLP, for the years ended December 31, 2017 and 2016 consisted of the following:

	Year Ended December 31, 2017	Year Ended December 31, 2016
Audit Fees <sup>(1)</sup>	\$ 806,660	\$ 622,980
Audit-Related Fees	—	—
Tax Fees	—	—
All Other Fees	—	—
Total	\$ 806,660	\$ 622,980

(1)Represents fees and expenses for professional services provided in connection with the audit of our annual financial statements and review of our quarterly financial statements, statutory audits, and advice on accounting matters directly related to the audit and audit services provided in connection with other regulatory filings.

##### PRE-APPROVAL POLICY

The audit committee charter provides that the audit committee of our board of directors shall pre-approve all audit services, audit-related tax services and other permitted services to be performed for us by our independent registered public accounting firm and the related fees. Pursuant to its charter and in compliance with rules of the SEC and PCAOB the audit committee has established a pre-approval policy and procedures that require the pre-approval of all services to be performed by the independent registered public accounting firm. The independent registered public accounting firm may be considered for other services not specifically approved as audit services or audit-related services and tax services so long as the services are not prohibited by SEC or PCAOB rules and would not otherwise impair the independence of the independent registered public accounting firm. During 2017, all of the above services were approved by the audit committee in accordance with this policy.

#### PART IV

##### Item 15. Exhibits, Financial Statements and Schedules

###### (a)Financial Statements.

	Page
Financial Statements	<u>F-1</u>
Report of Independent Registered Public Accounting Firm	<u>F-2</u>
Consolidated Balance Sheets	<u>F-3</u>

Edgar Filing: Five Oaks Investment Corp. - Form 10-K

Consolidated Statements of Operations	<u>F-4</u>
Consolidated Statements of Comprehensive Income (Loss)	<u>F-5</u>
Consolidated Statement of Stockholders' Equity	<u>F-6</u>
Consolidated Statements of Cash Flows	<u>F-7</u>
Notes to Consolidated Financial Statements	<u>F-9</u>

(b) Exhibits.

The Exhibits listed in the Exhibit Index, which appear immediately following the signature pages, are incorporated herein by reference and are filed as part of this Annual Report on Form 10-K.

(c) Schedules.

Schedule IV - Mortgage Loan on Real Estate

Schedules other than the one listed above are omitted because they are not applicable or deemed not material.





EXHIBIT INDEX

Exhibit

No.	Document
3.1	<u>Amended and Restated Articles of Incorporation of Five Oaks Investment Corp. (incorporated by reference to Exhibit 3.1 to Five Oaks Investment Corp. Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2013 (File No. 001-35845), which was filed with the Securities and Exchange Commission on May 3, 2013 (the "2013 1st Quarter 10-Q"))).</u>
3.2	<u>Articles Supplementary, designating the Series A Cumulative Redeemable Preferred Stock (Liquidation Preference \$25.00 per share) (incorporated by reference to Exhibit 3.1 to Five Oaks Investment Corp. Current Report on Form 8-K (File No. 001-35845), which was filed with the Securities and Exchange Commission on December 23, 2013).</u>
3.3	<u>Articles of Amendment, increasing the aggregate number of authorized shares of Series A Cumulative Redeemable Preferred Stock (Liquidation Preference \$25.00 per share) (incorporated by reference to Exhibit 3.2 to Five Oaks Investment Corp. Current Report on Form 8-K (File No. 001-35845), which was filed with the Securities and Exchange Commission on May 27, 2014).</u>
3.4	<u>Second Amended and Restated Bylaws of Five Oaks Investment Corp. (incorporated by reference to Exhibit 3.2 to the 2013 1st Quarter 10-Q).</u>
4.1	<u>Specimen Common Stock Certificate of Five Oaks Investment Corp. (incorporated by reference to Exhibit 4.1 to Pre-Effective Amendment No. 1 to Five Oaks Investment Corp. Registration Statement on Form S-11 (File No. 333-185570), which was filed with the Securities and Exchange Commission on January 22, 2013 ("Pre-Effective Amendment No. 1"))).</u>
4.2	<u>Specimen Certificate representing the Series A Cumulative Redeemable Preferred Stock (Liquidation Preference \$25.00 per share) (incorporated by reference to Exhibit 4.2 to Pre-Effective Amendment No. 1 to Five Oaks Investment Corp. Registration Statement on Form S-11 (File No. 333-191787), which was filed with the Securities and Exchange Commission on December 9, 2013).</u>
4.3	<u>Warrant Termination Agreement, dated as of January 18, 2018, by and between Five Oaks Investment Corp. and XL Investments Ltd. (incorporated by reference to Exhibit 4.1 to Five Oaks Investment Corp. Current Report on Form 8-K (File No. 0001-35845), which was filed with the Securities and Exchange Commission on January 18, 2018).</u>
10.1†	<u>Five Oaks Investment Corp. Manager Equity Plan (incorporated by reference to Exhibit 10.5 to Pre-Effective Amendment No. 1).</u>
10.2	<u>Trademark License Agreement, dated as of September 6, 2012, between Oak Circle Capital Partners LLC and Five Oaks Investment Corp. (incorporated by reference to Exhibit 10.6 filed with the DRS).</u>
10.3	<u>Form of Indemnification Agreement (incorporated by reference to Exhibit 10.6 to Five Oaks Investment Corp. Annual Report on Form 10-K for the year ended December 31, 2015 (File No. 001-35845), which was filed with the Securities and Exchange Commission on March 3, 2016 (the "2015 Form 10-K").</u>
10.4	

Amended and Restated Letter Agreement, dated as of January 21, 2013, between Five Oaks Investment Corp. and XL Investments Ltd, regarding the appointment of a board observer by XL Investments Ltd (incorporated by reference to Exhibit 10.8 to Pre-Effective Amendment No. 1).

10.5 Form of Master Repurchase Agreement (incorporated by reference to Exhibit 10.9 to the IPO S-11).

10.6 Master Services Agreement, dated as of June 1, 2012, by and among Five Oaks Investment Corp., Oak Circle Capital Partners LLC and Stone Coast Fund Services LLC (incorporated by reference to Exhibit 10.10 to Amendment No. 2 to Five Oaks Investment Corp. Registration Statement on Form S-11 (File No. 333-185570), which was filed with the Securities and Exchange Commission on February 21, 2013).

10.7 Master Repurchase Agreement, dated as of February 25, 2014, by and among Credit Suisse First Boston Mortgage Capital LLC as buyer, Five Oaks Acquisition Corp. as seller and Five Oaks Investment Corp. as guarantor (incorporated by reference to Exhibit 10.1 to Five Oaks Investment Corp. Current Report on Form 8-K (File No. 001-35845) filed with the Securities and Exchange Commission on February 26, 2014 (the "2014 February 8-K"))).

10.8 Guaranty, dated as of February 25, 2014, by Five Oaks Investment Corp. in favor of Credit Suisse First Boston Mortgage Capital LLC (incorporated by reference to Exhibit 10.2 to the 2014 February 8-K).

10.9 Loan and Security Agreement dated as of July 18, 2014, between Bank of America, N.A. as lender, Five Oaks Acquisition Corp. as borrower (incorporated by reference to Exhibit 10.1 to Five Oaks Investment Corp. Current Report on Form 8-K (File No. 001-35845), which was filed with the Securities and Exchange Commission on August 7, 2014 (the "2014 August 8-K"))).

- 10.10 Guaranty, dated as of July 18, 2014, by Five Oaks Investment Corp. in favor of Bank of America, N.A. (incorporated by reference to Exhibit 10.2 to the 2014 August 8-K).
- 10.11 Master Repurchase Agreement dated as of July 29, 2014, by and among Barclays Bank PLC as purchaser and agent, Five Oaks Acquisition Corp. as seller and Five Oaks Investment Corp. as guarantor (incorporated by reference to Exhibit 10.3 to the 2014 August 8-K).
- 10.12 Guaranty, dated as of July 29, 2014, by Five Oaks Investment Corp. in favor of Barclays Bank PLC (incorporated by reference to Exhibit 10.4 to the 2014 August 8-K).
- 10.13 Mortgage Loan Purchase and Servicing Agreement dated as of September 26, 2014, between Five Oaks Acquisition Corp., as seller and servicing administrator, and J.P. Morgan Mortgage Acquisition Corp., as purchaser (incorporated by reference to Exhibit 10.1 to Five Oaks Investment Corp. Current Report on Form 8-K (File No. 001-35845), which was filed with the Securities and Exchange Commission on October 15, 2014 (the “2014 October 8-K”)).
- 10.14 Assignment, Assumption and Recognition Agreement dated as of October 9, 2014, by and among J.P. Morgan Acceptance Corporation I, J.P. Morgan Mortgage Trust 2014-OAK4, J.P. Morgan Mortgage Acquisition Corp. and Five Oaks Acquisition Corp. (incorporated by reference to Exhibit 10.2 to the 2014 October 8-K).
- 10.15 Form of Mortgage Loan Purchase and Interim Servicing Agreement between Aggregator 1, as purchaser, and originator, as seller, with corresponding Form of Assignment, Assumption and Recognition Agreement among Aggregator 1, as assignor, Five Oaks Acquisition Corp. as assignee, and originator (incorporated by reference to Exhibit 10.6 to Five Oaks Investment Corp. Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2014 (File No. 001-35845), which was filed with the Securities and Exchange Commission on November 14, 2014 (the “2014 3rd Quarter 10-Q”)).
- 10.16 Form of Flow Sale and Interim Servicing Agreement between Aggregator 2, as purchaser, and originator, as seller and interim servicer, with corresponding Form of Assignment, Assumption and Recognition Agreement (Whole Loan Transfer), among Aggregator 2, as assignor, Five Oaks Acquisition Corp., as assignee, originator and servicer (incorporated by reference to Exhibit 10.7 to the 2014 3rd Quarter 10-Q).
- 10.17 Mortgage Loan Purchase and Sale Agreement, dated as of December 23, 2014, between Five Oaks Acquisition Corp. and Credit Suisse First Boston Mortgage Securities Corp. (incorporated by reference to Exhibit 10.1 to Five Oaks Investment Corp. Current Report on Form 8-K (File No. 001-35845), which was filed with the Securities and Exchange Commission on January 12, 2015 (the “2015 January 8-K”)).
- 10.18 Certificate Purchase Agreement, dated December 22, 2014, among Credit Suisse First Boston Mortgage Securities Corp., Credit Suisse Securities (USA) LLC, Wells Fargo Securities, LLC, Five Oaks Acquisition Corp. and Five Oaks Investment Corp. (incorporated by reference to Exhibit 10.2 to the 2015 January 8-K).
- 10.19 Indemnity Letter, dated December 23, 2014, among Five Oaks Investment Corp., Credit Suisse Securities (USA) LLC and Credit Suisse First Boston Mortgage Securities Corp. (incorporated by reference to Exhibit 10.3 to the 2015 January 8-K).
- 10.20 Pooling And Servicing Agreement, dated as of December 1, 2014, among Credit Suisse First Boston Mortgage Securities Corp., Christiana Trust, Select Portfolio Servicing, Inc. and Wells Fargo Bank, N.A. (incorporated by reference to Exhibit 10.4 to the 2015 January 8-K).

- 10.21 Master Repurchase Agreement, dated as of December 30, 2014, between Bank of America, N.A. and Five Oaks Acquisition Corp. (incorporated by reference to Exhibit 10.5 to the 2015 January 8-K).
- 10.22 Guaranty, dated as of December 30, 2014, by Five Oaks Investment Corp., to and for the benefit of Bank of America, N.A. (incorporated by reference to Exhibit 10.6 to the 2015 January 8-K).
- 10.23 Equity Distribution Agreement, dated as of October 13, 2017, by and between Five Oaks Investment Corp., Oak Circle Capital Partners LLC and JMP Securities LLC (incorporated by reference to Exhibit 10.1 to Five Oaks Investment Corp. Current Report on Form 8-K (File No. 001-35845) which was filed with the Securities and Exchange Commission on October 13, 2017).
- 10.24 Equity Distribution Agreement, dated as of October 13, 2017, by and between Five Oaks Investment Corp., Oak Circle Capital Partners LLC and Landenburg Thalman & Co. Inc. (incorporated by reference to Exhibit 10.2 to Five Oaks Investment Corp. Current Report on Form 8-K (File No. 001-35845) which was filed with the Securities and Exchange Commission on October 13, 2017).
- 10.25 Management Agreement, dated as of January 18, 2018, by and between Five Oaks Investment Corp. and Hunt Investment Management LLC (incorporated by reference to Exhibit 10.1 to Five Oaks Investment Corp. Current Report on Form 8-K (File No. 001-35845), which was filed with the Securities and Exchange Commission on January 18, 2018).
- 10.26 Securities Purchase Agreement, dated as of January 18, 2018, by and between Five Oaks Investment Corp. and Hunt Companies Equity Holdings, LLC (incorporated by reference to Exhibit 10.2 to Five Oaks Investment Corp. Current Report on Form 8-K (File No. 001-35845), which was filed with the Securities and Exchange Commission on January 18, 2018).

- 10.27 Registration Rights Agreement, dated as of January 18, 2018, by and between Five Oaks Investment Corp. and Hunt Companies Equity Holdings, LLC (incorporated by reference to Exhibit 10.3 to Five Oaks Investment Corp. Current Report on Form 8-K (File No. 001-35845), which was filed with the Securities and Exchange Commission on January 18, 2018).
- 10.28 Shareholder Agreement, dated as of January 18, 2018, by and between Five Oaks Investment Corp. and Hunt Companies Equity Holdings, LLC (incorporated by reference to Exhibit 10.4 to Five Oaks Investment Corp. Current Report on Form 8-K (File No. 001-35845), which was filed with the Securities and Exchange Commission on January 18, 2018).
- 10.29 Termination Agreement, dated as of January 18, 2018, by and between Five Oaks Investment Corp. and Oak Circle Capital Partners LLC (incorporated by reference to Exhibit 10.5 to Five Oaks Investment Corp. Current Report on Form 8-K (File No. 001-35845), which was filed with the Securities and Exchange Commission on January 18, 2018).
- 12.1 Computation of Ratios of Earnings to Fixed Charges.\*
- 21.1 List of Subsidiaries of Five Oaks Investment Corp.\*
- 23.1 Consent of Grant Thornton LLP \*
- 31.1 Certification Chief Executive Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.\*
- 31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002\*
- 32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.\*
- 32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.\*
- 101.INS XBRL Instance Document\*
- 101.SCH XBRL Taxonomy Extension Schema Document\*
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document\*
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document\*
- 101.LAB XBRL Taxonomy Extension Label Linkbase Document\*
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document\*

\* Filed herewith.

†Management contract or compensatory plan or arrangement.



Item 16. Form 10-K Summary

None.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

FIVE OAKS INVESTMENT CORP.

March 16, 2018 /s/ James C. Hunt  
James C. Hunt  
Chairman of the Board

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ James C. Hunt James C. Hunt	Chairman of the Board	March 16, 2018
/s/ David Oston David Oston	Chief Financial Officer, Treasurer, Secretary and Director (Principal Financial Officer and Principal Accounting Officer)	March 16, 2018
/s/ Neil A. Cummins Neil A. Cummins	Director	March 16, 2018
/s/ William Houlihan William Houlihan	Director	March 16, 2018
/s/ Walter C. Keenan Walter C. Keenan	Director	March 16, 2018

Contents

	Page
Financial Statements	
<u>Report of Independent Registered Public Accounting Firm</u>	<u>F-2</u>
<u>Consolidated Balance Sheets as of December 31, 2017 and December 31, 2016</u>	<u>F-3</u>
<u>Consolidated Statements of Operations for the years ended December 31, 2017, December 31, 2016 and December 31, 2015</u>	<u>F-4</u>
<u>Consolidated Statements of Comprehensive Income (Loss) for the years ended December 31, 2017, December 31, 2016 and December 31, 2015</u>	<u>F-5</u>
<u>Consolidated Statement of Stockholders' Equity for the years ended December 31, 2017, December 31, 2016 and December 31, 2015</u>	<u>F-6</u>
<u>Consolidated Statements of Cash Flows for the years ended December 31, 2017, December 31, 2016 and December 31, 2015</u>	<u>F-7</u>
<u>Notes to Audited Consolidated Financial Statements</u>	<u>F-9</u>

F-1

---



Report of Independent Registered Public Accounting Firm

Board of Directors and Shareholders of  
Five Oaks Investment Corp.

Opinion on the financial statements

We have audited the accompanying consolidated balance sheets of Five Oaks Investment Corp. (a Maryland corporation) and subsidiaries (the “Company”) as of December 31, 2017 and 2016, the related consolidated statements of operations, comprehensive income (loss), changes in stockholders’ equity, and cash flows for each of the three years in the period ended December 31, 2017, and the related notes and schedule (collectively referred to as the “financial statements”). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2017 and 2016, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2017, in conformity with accounting principles generally accepted in the United States of America.

Basis for opinion

These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on the Company’s financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (“PCAOB”) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ GRANT THORNTON LLP

We have served as the Company's auditor since 2012.

New York, New York  
March 16, 2018

FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES  
Consolidated Balance Sheets

	12/31/2017 <sup>(1)</sup>	12/31/2016 <sup>(1)</sup>
<b>ASSETS</b>		
Available-for-sale securities, at fair value (includes pledged securities of \$1,295,225,428 and \$876,121,505 for December 31, 2017 and December 31, 2016, respectively)	\$1,290,825,648	\$870,929,601
Mortgage loans held-for-sale, at fair value	—	2,849,536
Multi-family loans held in securitization trusts, at fair value	1,130,874,274	1,222,905,433
Residential loans held in securitization trusts, at fair value	119,756,455	141,126,720
Mortgage servicing rights, at fair value	2,963,861	3,440,809
Cash and cash equivalents	34,347,339	27,534,374
Restricted cash	11,275,263	10,355,222
Deferred offering costs	179,382	96,489
Accrued interest receivable	8,852,036	7,619,717
Investment related receivable	7,461,128	3,914,458
Derivative assets, at fair value	5,349,613	8,053,813
Other assets	656,117	775,031
<b>Total assets</b>	<b>\$2,612,541,116</b>	<b>\$2,299,601,203</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>LIABILITIES:</b>		
Repurchase agreements:		
Available-for-sale securities	\$1,234,522,000	\$804,811,000
Multi-family securitized debt obligations	1,109,204,743	1,204,583,678
Residential securitized debt obligations	114,418,318	134,846,348
Accrued interest payable	6,194,464	5,467,916
Dividends payable	39,132	39,132
Deferred income	222,518	203,743
Due to broker	1,123,463	4,244,678
Fees and expenses payable to Manager	752,000	880,000
Other accounts payable and accrued expenses	273,201	2,057,843
<b>Total liabilities</b>	<b>2,466,749,839</b>	<b>2,157,134,338</b>
<b>COMMITMENTS AND CONTINGENCIES (NOTE 15)</b>		
<b>STOCKHOLDERS' EQUITY:</b>		
Preferred Stock: par value \$0.01 per share; 50,000,000 shares authorized, 8.75% Series A cumulative redeemable, \$25 liquidation preference, 1,610,000 and 1,610,000 issued and outstanding at December 31, 2017 and December 31, 2016, respectively	37,156,972	37,156,972
Common Stock: par value \$0.01 per share; 450,000,000 shares authorized, 22,143,758 and 17,539,258 shares issued and outstanding, at December 31, 2017 and December 31, 2016, respectively	221,393	175,348
Additional paid-in capital	224,048,169	204,264,868
Accumulated other comprehensive income (loss)	(15,054,484)	(9,268,630)

Edgar Filing: Five Oaks Investment Corp. - Form 10-K

Cumulative distributions to stockholders	(104,650,235 )	(89,224,194 )
Accumulated earnings (deficit)	4,069,462	(637,499 )
Total stockholders' equity	145,791,277	142,466,865
Total liabilities and stockholders' equity	\$2,612,541,116	\$2,299,601,203

Our consolidated balance sheets include assets and liabilities of consolidated variable interest entities (“VIE's) as the Company is the primary beneficiary of these VIEs. As of December 31, 2017 and December 31, 2016, assets of consolidated VIEs totaled \$1,255,404,335 and \$1,369,120,941, respectively, and the liabilities of consolidated VIEs totaled \$1,228,295,517 and \$1,344,404,080, respectively

See Notes 6 and 7 for further discussion

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

F-3

---

## FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

## Consolidated Statements of Operations

	Year Ended December 31, 2017	Year Ended December 31, 2016	Year Ended December 31, 2015
Revenues:			
Interest income:			
Available-for-sale securities	\$ 29,521,893	\$ 23,475,765	\$ 24,298,156
Mortgage loans held-for-sale	72,160	430,986	2,097,702
Multi-family loans held in securitization trusts	54,271,017	58,587,780	68,016,595
Residential loans held in securitization trusts	5,103,853	10,585,191	19,986,204
Cash and cash equivalents	164,413	41,994	16,351
Interest expense:			
Repurchase agreements - available-for-sale securities	(13,493,197 )	(6,237,777 )	(6,467,312 )
Repurchase agreements - mortgage loans held-for-sale	—	(237,807 )	(1,323,892 )
Multi-family securitized debt obligations	(51,440,694 )	(54,940,386 )	(62,157,176 )
Residential securitized debt obligations	(4,059,894 )	(8,117,402 )	(13,156,912 )
Net interest income	20,139,551	23,588,344	31,309,716
Other-than-temporary impairments			
(Increase) decrease in credit reserves	—	(541,342 )	(745,492 )
Additional other-than-temporary credit impairment losses	—	(183,790 )	(2,890,939 )
Total impairment losses recognized in earnings	—	(725,132 )	(3,636,431 )
Other income:			
Realized gain (loss) on sale of investments, net	(14,054,164 )	(7,216,137 )	(533,832 )
Change in unrealized gain (loss) on fair value option securities	9,448,270	(4,683,410 )	(1,041,649 )
Realized gain (loss) on derivative contracts, net	2,219,719	(3,089,001 )	(12,024,730 )
Change in unrealized gain (loss) on derivative contracts, net	(2,704,413 )	5,495,463	4,909,858
Realized gain (loss) on mortgage loans held-for-sale, net	(221,620 )	94,187	1,216,314
Change in unrealized gain (loss) on mortgage loans held-for-sale	17,727	(151,023 )	(197,179 )
Change in unrealized gain (loss) on mortgage servicing rights	(487,856 )	(827,864 )	(671,957 )
Change in unrealized gain (loss) on multi-family loans held in securitization trusts	3,353,365	(5,219,530 )	6,097,000
Change in unrealized gain (loss) on residential loans held in securitization trusts	(961,100 )	404,720	(8,153,474 )
Other interest expense	(152,322 )	(1,860,000 )	—
Servicing income	922,094	932,424	211,878
Other income	46,262	32,276	85,726
Total other income (loss)	(2,574,038 )	(16,087,895 )	(10,102,045 )
Expenses:			
Management fee	2,215,050	2,472,353	2,774,432
General and administrative expenses	5,454,786	5,867,851	6,660,934
Operating expenses reimbursable to Manager	4,127,549	4,747,275	4,980,348
Other operating expenses	855,582	1,480,341	2,448,439
Compensation expense	205,585	197,452	256,608
Total expenses	12,858,552	14,765,272	17,120,761
Net income (loss)	4,706,961	(7,989,955 )	450,479
Dividends to preferred stockholders	(3,522,036 )	(3,522,036 )	(3,522,036 )
Net income (loss) attributable to common stockholders	\$ 1,184,925	\$ (11,511,991 )	\$ (3,071,557 )

Edgar Filing: Five Oaks Investment Corp. - Form 10-K

Earnings (loss) per share:

Net income (loss) attributable to common stockholders (basic and diluted)	\$ 1,184,925	\$(11,511,991)	\$(3,071,557 )
Weighted average number of shares of common stock outstanding	20,048,128	14,641,701	14,721,074
Basic and diluted income (loss) per share	\$ 0.06	\$(0.79 )	\$(0.21 )
Dividends declared per weighted average share of common stock	\$ 0.60	\$ 2.04	\$ 1.35

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

F-4

---

# FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

## Consolidated Statements of Comprehensive Income (Loss)

	Year Ended December 31, 2017	Year Ended December 31, 2016	Year Ended December 31, 2015
Net income (loss)	4,706,961	\$(7,989,955)	\$450,479
Other comprehensive income (loss):			
Increase (decrease) in net unrealized gain (loss) on available-for-sale securities, net	(13,268,331)	(3,824,461)	(14,776,266)
Reclassification adjustment for net gain (loss) included in net income (loss)	7,482,477	(5,589,740)	1,969,108
Reclassification adjustment for other-than-temporary impairments included in net income (loss)	—	541,342	745,492
Reclassification cumulative adjustment for Linked Transactions	—	—	4,457,544
Total other comprehensive income (loss)	(5,785,854)	(8,872,859)	(7,604,122)
Less: Dividends to preferred stockholders	(3,522,036)	(3,522,036)	(3,522,036)
Comprehensive income (loss) attributable to common stockholders	(4,600,929)	\$(20,384,850)	\$(10,675,679)

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

F-5

## FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

## Consolidated Statements of Stockholders' Equity

	Preferred Stock		Common Stock		Additional	Accumulated	Cumulative	Accu
	Shares	Par Value	Shares	Par Value	Paid in Capital	Other Comprehensive Income (Loss)	Distributions to Stockholders	Earni (Defi
Balance at January 1, 2015	1,610,000	\$37,156,972	14,718,750	\$146,953	\$189,332,874	\$7,208,351	\$(32,406,541 )	\$11,3
Issuance of common stock, net	—	—	14,000	140	(140 )	—	—	—
Cost of issuing common stock	—	—	—	—	—	—	—	—
Issuance of preferred stock, net	—	—	—	—	—	—	—	—
Redemption of preferred stock, net	—	—	—	—	—	—	—	—
Purchase of treasury stock, net	—	—	(68,356 )	(684 )	(358,307 )	—	—	—
Restricted stock compensation expense	—	—	(8,000 )	—	63,275	—	—	—
Net income (loss)	—	—	—	—	—	—	—	450,4
Increase (decrease) in net unrealized gain on available-for-sale securities, net	—	—	—	—	—	(14,776,266 )	—	—
Reclassification adjustment for net gain (loss) included in net income	—	—	—	—	—	1,969,108	—	—
Reclassification cumulative adjustments for Linked Transactions	—	—	—	—	—	4,457,544	—	(4,45
Reclassification adjustment for other-than-temporary impairments included in net income	—	—	—	—	—	745,492	—	—
Common dividends declared	—	—	—	—	—	—	(19,874,663 )	—
Preferred dividends declared	—	—	—	—	—	—	(3,522,036 )	—
Balance at December 31, 2015	1,610,000	\$37,156,972	14,656,394	\$146,409	\$189,037,702	\$(395,771 )	\$(55,803,240 )	\$7,35
	1,610,000	\$37,156,972	14,656,394	\$146,409	\$189,037,702	\$(395,771 )	\$(55,803,240 )	\$7,35

Edgar Filing: Five Oaks Investment Corp. - Form 10-K

Balance at January 1, 2016									
Issuance of common stock, net	—	—	2,952,364	29,524	15,477,118	—	(15,506,642	)	—
Cost of issuing common stock	—	—	—	—	(2,757	)	—		—
Issuance of preferred stock, net	—	—	—	—	—	—	—		—
Redemption of preferred stock, net	—	—	—	—	—	—	—		—
Purchase of treasury stock, net	—	—	(58,500	) (585	) (282,980	)	—		—
Restricted stock compensation expense	—	—	(11,000	)	—	35,785	—	—	—
Net income (loss)	—	—	—	—	—	—	—		(7,98
Increase (decrease) in net unrealized gain on available-for-sale securities, net	—	—	—	—	—	(3,824,461	)	—	—
Reclassification adjustment for net gain (loss) included in net income	—	—	—	—	—	(5,589,740	)	—	—
Reclassification adjustment for other-than-temporary impairments included in net income	—	—	—	—	—	541,342	—		—
Common dividends declared	—	—	—	—	—	—	(14,392,276	)	—
Preferred dividends declared	—	—	—	—	—	—	(3,522,036	)	—
Balance at December 31, 2016	1,610,000	\$37,156,972	17,539,258	\$175,348	\$204,264,868	\$(9,268,630	) \$(89,224,194	)	\$(63
Balance at January 1, 2017	1,610,000	\$37,156,972	17,539,258	\$175,348	\$204,264,868	\$(9,268,630	) \$(89,224,194	)	\$(63
Issuance of common stock, net	—	—	4,604,500	46,045	21,140,820	—	—		—
Cost of issuing common stock	—	—	—	—	(1,351,239	)	—		—
Issuance of preferred stock, net	—	—	—	—	—	—	—		—
Redemption of preferred stock, net	—	—	—	—	—	—	—		—
Purchase of treasury stock, net	—	—	—	—	—	—	—		—
Restricted stock compensation expense	—	—	—	—	(6,280	)	—		—



Edgar Filing: Five Oaks Investment Corp. - Form 10-K

Net income (loss)	—	—	—	—	—	—	—	4,706
Increase (decrease) in net unrealized gain on available-for-sale securities, net	—	—	—	—	—	(13,268,331 )	—	—
Reclassification adjustment for net gain (loss) included in net income (loss)	—	—	—	—	—	7,482,477	—	—
Reclassification adjustment for other-than-temporary impairments included in net income (loss)	—	—	—	—	—	—	—	—
Common dividends declared	—	—	—	—	—	—	(11,904,005 )	—
Preferred dividends declared	—	—	—	—	—	—	(3,522,036 )	—
Balance at December 31, 2017	1,610,000	\$37,156,972	22,143,758	\$221,393	\$224,048,169	\$(15,054,484)	\$(104,650,235)	\$4,000,000

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

FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES  
Consolidated Statements of Cash Flows

	Year Ended December 31, 2017	Year Ended December 31, 2016	Year Ended December 31, 2015
Cash flows from operating activities:			
Net income (loss)	\$ 4,706,961	\$ (7,989,955 )	\$ 450,479
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Other-than-temporary impairment charges	—	725,132	3,636,431
Amortization/accretion of available-for-sale securities premiums and discounts, net	(1,475,701 )	(6,751,667 )	(13,210,849 )
Realized (gain) loss on sale of investments, net	14,054,164	7,216,137	533,832
Realized (gain) loss on derivative contracts, net	(2,219,719 )	3,089,001	12,024,730
Realized (gain) loss on mortgage loans held-for-sale	221,620	(94,187 )	(1,216,314 )
Unrealized (gain) loss on fair value option securities	(9,448,270 )	4,683,410	1,041,649
Unrealized (gain) loss on derivative contracts	2,704,413	(5,495,463 )	(4,909,858 )
Unrealized (gain) loss on mortgage loans held-for-sale	(17,727 )	151,023	197,179
Unrealized (gain) loss on mortgage servicing rights	487,856	827,864	671,957
Unrealized (gain) loss on multi-family loans held in securitization trusts	(3,353,365 )	5,219,530	(6,097,000 )
Unrealized (gain) loss on residential loans held in securitization trusts	961,100	(404,720 )	8,153,474
Restricted stock compensation expense	(6,280 )	35,785	63,275
Net change in:			
Accrued interest receivable	(1,547,501 )	(707,019 )	1,204,188
Deferred offering costs	(82,893 )	(96,489 )	945,661
Other assets	118,914	(218,541 )	(484,891 )
Accrued interest payable	1,028,149	119,993	(693,848 )
Deferred income	18,775	203,743	—
Fees and expenses payable to Manager	(128,000 )	37,097	(219,097 )
Other accounts payable and accrued expenses	(1,784,642 )	1,790,336	(27,522 )
Net cash provided by operating activities	4,237,854	2,341,010	2,063,476
Cash flows from investing activities:			
Purchase of available-for-sale securities	(1,060,558,013 )	(585,984,081 )	(241,590,864 )
Purchase of mortgage loans held-for-sale	—	(14,772,535 )	(502,308,627 )
Purchase of mortgage servicing rights	(10,910 )	—	(4,940,630 )
Purchase of FHLBI stock	—	—	(2,403,000 )
Proceeds from sales of available-for-sale securities	495,030,356	263,153,843	333,672,932
Proceeds from mortgage loans held-for-sale	2,098,010	22,490,929	531,673,280
Proceeds from FHLBI stock	—	2,403,000	—
Net proceeds from (payments for) derivative contracts	2,219,506	(3,089,001 )	(11,940,730 )
Principal payments from available-for-sale securities	136,715,868	96,655,967	70,476,212
Principal payments from mortgage loans held-for-sale	547,635	275,636	15,432,462
Investment related receivable	(3,546,670 )	(2,323,115 )	—
Due to broker	(3,121,215 )	4,244,678	—
Net cash (used in) provided by investing activities	(430,625,433 )	(216,944,679 )	188,071,035
Cash flows from financing activities:			

Edgar Filing: Five Oaks Investment Corp. - Form 10-K

Proceeds from issuance of common stock	19,835,626	15,503,885	—
Purchase of treasury stock	—	(283,565 )	(358,991 )
Dividends paid on common stock	(11,904,005 )	(29,898,918 )	(19,874,663 )
Dividends paid on preferred stock	(3,522,036 )	(3,522,036 )	(3,522,036 )
Proceeds from repurchase agreements - available-for-sale securities	14,224,216,000	7,940,492,000	5,951,792,999
Proceeds from repurchase agreements - mortgage loans held-for-sale	—	16,405,081	66,937,322
Proceeds from FHLBI advances	—	—	155,497,000
Payments for FHLBI advances	—	(49,697,000 )	(105,800,000)
Principal repayments of repurchase agreements - available-for-sale securities	(13,794,505,000)	(7,644,912,000)	(6,136,468,999)

F-7

---

Principal repayments of repurchase agreements - mortgage loans held-for-sale	—	(25,909,538	) (107,696,717 )
Net cash (used in) provided by financing activities	434,120,585	218,177,909	(199,494,085 )
Net increase (decrease) in cash, cash equivalents and restricted cash	7,733,006	3,574,240	(9,359,574 )
Cash, cash equivalents and restricted cash, beginning of period	37,889,596	34,315,356	43,674,930
Cash, cash equivalents and restricted cash, end of period	\$45,622,602	\$37,889,596	\$34,315,356
Supplemental disclosure of cash flow information			
Cash paid for interest	\$14,477,370	\$6,355,591	\$8,554,565
Non-cash investing and financing activities information			
Dividends declared but not paid at end of period	\$39,132	\$39,132	\$39,132
Net change in unrealized gain (loss) on available-for-sale securities	\$(5,785,854	) \$(8,872,859	) \$(7,604,122 )
Consolidation of multi-family loans held in securitization trusts	\$1,135,251,880	\$1,227,523,075	\$1,455,155,339
Consolidation of residential loans held in securitization trusts	\$120,152,455	\$141,597,866	\$413,327,217
Consolidation of multi-family securitized debt obligations	\$1,113,556,782	\$1,209,181,035	\$1,369,124,789
Consolidation of residential securitized debt obligations	\$114,738,735	\$135,223,045	\$381,791,476
MBS securities recorded upon adoption of revised accounting standard for repurchase agreement financing	\$—	\$—	\$210,238,658
Repurchase agreements recorded upon adoption of revised accounting standard for repurchase agreement financing	\$—	\$—	\$149,293,000

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

FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2017

NOTE 1 – ORGANIZATION AND BUSINESS OPERATIONS

Five Oaks Investment Corp. (the “Company”) is a Maryland corporation focused primarily on investing in, financing and managing residential mortgage-backed securities (“RMBS”), multi-family mortgage backed securities (“Multi-Family MBS”, and together with RMBS, “MBS”), mortgage servicing rights and other mortgage-related investments. With effect from January 18, 2018 the Company is externally managed by Hunt Investment Management, LLC (the “Manager”), an asset management firm incorporated in Delaware who replaced the prior manager, Oak Circle Capital Partners LLC (“Oak Circle”). The Company’s common stock is listed on the NYSE under the symbol “OAKS” and our Series A Preferred Stock is traded on the NYSE under the symbol “OAKS-PRA.”

The Company was incorporated on March 28, 2012 and commenced operations on May 16, 2012. The Company began trading as a publicly traded company on March 22, 2013.

The Company has elected to be taxed as a real estate investment trust (“REIT”) and to comply with Sections 856 through 859 of the Internal Revenue Code of 1986, as amended, the (“Code”). Accordingly, the Company generally will not be subject to U.S. federal income tax to the extent of its distributions to stockholders and as long as certain asset, income and share ownership tests are met. The Company invests in Agency RMBS, which are RMBS for which the principal and interest payments are guaranteed by a U.S. Government agency such as the Government National Mortgage Association or a U.S. Government-sponsored entity such as the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation. The Company also invests in Non-Agency RMBS, which are RMBS that are not guaranteed by a U.S. Government agency or a U.S. Government-sponsored entity. Additionally, the Company invests in Multi-Family MBS, which are MBS for which the principal and interest may be sponsored by a U.S. Government agency such as the Government National Mortgage Association or a U.S. Government-sponsored entity such as the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation, or may not be sponsored by a U.S. Government agency or a U.S. Government-sponsored entity. The Company also invests in mortgage servicing rights, may also invest in other mortgage-related investments and historically has invested in residential mortgage loans.

On June 10, 2013, the Company established Five Oaks Acquisition Corp. (“FOAC”) as a wholly owned taxable REIT subsidiary (“TRS”), for the acquisition and disposition of residential mortgage loans and certain other loan-related activities. The Company consolidates this subsidiary under generally accepted accounting principles in the United States of America (“GAAP”).

On April 30, 2014, the Company established Five Oaks Insurance LLC (“FOI”) as a wholly owned subsidiary. FOI was dissolved on July 18, 2016. The Company previously consolidated this subsidiary under GAAP.

In September 2014, and October 2014, respectively, the Company acquired first loss tranches issued or backed by two Freddie Mac-sponsored Multi-Family MBS K series securitizations (the “FREM F 2011-K13 Trust” and the “FREM F 2012-KF01 Trust”). The Company determined that each of the trusts was a variable interest entity (“VIE”) and that in each case the Company remains the primary beneficiary, and accordingly consolidated the assets and liabilities of the trusts into the Company’s financial statements in accordance with GAAP. On April 21, 2016, and April 26, 2016, respectively, the Company completed two re-securitization transactions (the “Re-REMIC transactions”). The Company consolidates the assets and liabilities of the newly established trusts, in each case based upon the Company’s purchase of first-loss securities of the Re-REMIC transactions. Accordingly, the Company has determined that it remains the primary beneficiary of the underlying trusts and continues to consolidate the assets and liabilities of each underlying

trust.

In October 2014, and December 2014, respectively, the Company also acquired first loss and subordinated tranches issued by two residential mortgage-backed securitizations (the “JPMMT 2014-OAK4 Trust” and the “CSMC 2014-OAK1 Trust”). During the second quarter of 2016, the Company sold the first loss and subordinated tranches issued by the JPMMT 2014-OAK4 Trust, and as a result, having determined that it is no longer the primary beneficiary of the trust, and the Company no longer consolidates the assets and liabilities of that trust. The Company determined that CSMC 2014-OAK1 Trust was a VIE and that the Company continues to be the primary beneficiary, and accordingly consolidates the assets and liabilities of the trust into the Company’s financial statements in accordance with GAAP.

On March 23, 2015, the Company established Oaks Funding LLC as a wholly owned subsidiary of FOAC, to fulfill certain functions as depositor in respect of residential mortgage loan securitization transactions. The Company consolidates this subsidiary under GAAP.

On April 20, 2016, the Company established Oaks Funding II LLC as a wholly owned subsidiary of FOAC, to fulfill certain functions as depositor in respect of certain Re-REMIC transactions. The Company consolidates this subsidiary under GAAP.

On April 20, 2016, the Company established Oaks Holding I LLC as a wholly owned subsidiary to hold certain investment securities. The Company consolidates this subsidiary under GAAP.

## NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Basis of Presentation

These financial statements have been prepared in accordance with U.S. GAAP and are expressed in United States dollars.

The consolidated financial statements of the Company include the accounts of its subsidiaries.

### Reclassification

Certain prior year amounts have been reclassified to conform to current year presentation.

### Principles of Consolidation

The accompanying consolidated financial statements of the Company include the accounts of the Company and all its subsidiaries which are majority-owned, controlled by the Company or a variable interest entity where the Company is the primary beneficiary. All significant intercompany transactions have been eliminated on consolidation.

F-9

---

FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2017

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

VIEs

An entity is referred to as a VIE if it lacks one or more of the following characteristics: (1) sufficient equity at risk to finance its activities without additional subordinated financial support provided by any parties, including the equity holders; (2) as a group the holders of the equity investment at risk have (a) the power, through voting rights or similar rights, to direct the activities of a legal entity that most significantly impacts the entity's economic performance, (b) the obligation to absorb the expected losses of the legal entity and (c) the right to receive the expected residual returns of the legal entity; and (3) the voting rights of these investors are proportional to their obligations to absorb the expected losses of the entity, their rights to receive the expected returns of their equity, or both, and whether substantially all of the entity's activities involve or are conducted on behalf of an investor that has disproportionately fewer voting rights. An investment that lacks one or more of the above three characteristics is considered to be a VIE. The Company reassesses its initial evaluation of an entity as a VIE based upon changes in the facts and circumstances pertaining to the VIE.

VIEs are required to be consolidated by their primary beneficiary. The primary beneficiary of a VIE is determined to be the party that has both the power to direct the activities that most significantly impact the VIE's economic performance and the obligation to absorb losses of, or the right to receive benefits from, the VIE that could potentially be significant to the VIE. This determination may involve complex and subjective analyses. In general, the obligation to absorb losses is a function of holding a majority of the first loss tranche, while the ability to direct the activities that most significantly impact the VIEs economic performance will be determined based upon the rights associated with acting as the directing certificate holder, or equivalent, in a given transaction. The Company is required to reconsider its evaluation of whether to consolidate a VIE each reporting period based upon changes in the facts and circumstances pertaining to the VIE.

The Company has evaluated its Non-Agency RMBS and Multi-Family MBS investments to determine if each represents a variable interest in a VIE. The Company monitors these investments and analyzes them for potential consolidation. The Company's real estate securities investments represent variable interests in VIEs. At December 31, 2017, the Company determined that it continues to be the primary beneficiary of two Multi-Family MBS transactions (FREM 2011-K13 and FREMF 2012-KF01), and one residential mortgage loan transaction (CSMC 2014-OAK1), in each case based on its power to direct the trust's activities and its obligations to absorb losses derived from the ownership of the first-loss tranches. In the case of the FREMF 2011-K13 and the FREMF 2012-KF01 trusts, the Company determined that it is the primary beneficiary of certain intermediate trusts that have the power to direct the activities and the obligations to absorb losses of the underlying trusts. Accordingly, the Company consolidated the assets, liabilities, income and expenses of each of the underlying trusts, and has elected the fair value option in respect of the assets and liabilities of each trust. However, the Company's maximum exposure to loss from consolidated trusts was \$27,108,818 and \$24,716,861, respectively, at December 31, 2017, and December 31, 2016. At December 31, 2017 and December 31, 2016, with the exception of the above transactions, the maximum exposure of the Company to VIEs was limited to the fair value of its investment in Non-Agency RMBS and Multi-Family MBS as disclosed in Note 4 (Non-Agency RMBS \$0 and \$7,592,802 respectively, and Multi-Family MBS \$5,742,000 and \$73,146,566, respectively).

GAAP also requires us to consider whether securitizations we sponsor and other transfers of financial assets should be treated as sales or financings. During the year ended December 31, 2015, the Company transferred residential mortgage loans with an aggregate unpaid principal balance of \$518,455,163 to Oaks Mortgage Trust Series 2015-1

and Oaks Mortgage Trust 2015-2, and accounted for these transfers as sales for financial reporting purposes, in accordance with Accounting Standards Codification (“ASC”) 860. The Company also determined that it was not the primary beneficiary of these VIEs because it lacked the power to direct the activities that will have the most significant economic impact on the entities, all of these securities were sold in January 2017. The Company’s analysis incorporates the considerations applicable to Consolidation (Topic 810). The Company’s determination involves complex and subjective analysis resulting from the various legal and structural aspects of each transaction. This analysis has focused in particular on ASC 810-10-25-38C and 25-38D, along with ASC 810-10-25-38G and ASC 810-10-15-13A and 15-13B. The Company’s maximum exposure to loss from these VIEs was limited to the fair value of its investments in Non-Agency RMBS issued by the two VIEs, with an aggregate fair value of \$0 at December 31, 2017 (December 31, 2016: \$4,413,403). This amount is included in Available-for-sale (“AFS”) securities on the Company’s consolidated balance sheet. The Company is party to customary and standard repurchase obligations in respect of loans that it has sold to the two VIEs to the extent they have breached standard representations and warranties, but is not a party to arrangements to provide financial support to the VIEs that the Company believes could expose it to additional loss.

#### Use of Estimates

The financial statements have been prepared on the accrual basis of accounting in accordance with GAAP. The preparation of financial statements in conformity with GAAP requires the Company to make a number of significant estimates. These include estimates of fair value of certain assets and liabilities, amount and timing of credit losses, prepayment rates, and other estimates that affect the reported amounts of certain assets and liabilities as of the date of the financial statements and the reported amounts of certain revenues and expenses during the reported period. It is likely that changes in these estimates (e.g. valuation changes due to supply and demand, credit performance, prepayments, interest rates, or other reasons) will occur in the near term. The Company’s estimates are inherently subjective in nature and actual results could differ from its estimates and the differences may be material.

#### Cash and Cash Equivalents

Cash and cash equivalents include cash held in bank accounts on an overnight basis and other short term deposit accounts with banks having original maturities of 90 days or less. The Company maintains its cash and cash equivalents in highly rated financial institutions, and at times these balances exceed insurable amounts.

Restricted cash represents the Company’s cash held by counterparties as collateral against the Company’s securities, derivatives and/or repurchase agreements. Cash held by counterparties as collateral is not available to the Company for general corporate purposes, but may be applied against amounts due to securities, derivatives or repurchase counterparties or returned to the Company when the collateral requirements are exceeded or, at the maturity of the derivative or repurchase agreement.

The following table provides a reconciliation of cash, cash equivalents and restricted cash reported within the consolidated balance sheet that sum to the total of the same amounts shown in the statement of cash flows.



FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2017

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

	December 31, 2017	December 31, 2016	December 31, 2015
Cash and cash equivalents	\$ 34,347,339	\$ 27,534,374	\$ 26,140,718
Restricted cash	11,275,263	10,355,222	8,174,638
Total cash, cash equivalents and restricted cash	\$ 45,622,602	\$ 37,889,596	\$ 34,315,356

Deferred Income

Certain service revenues received in the period are recorded as a liability in the Company's consolidated balance sheets in the line item "Deferred income", for subsequent recognition as income in the Company's consolidated statements of operations.

Deferred Offering Costs

In accordance with ASC Subtopic 505-10, the direct costs incurred to issue shares classified as equity, such as legal and accounting fees, should be deducted from the related proceeds and the net amount recorded as stockholders' equity. Accordingly, payments made by the Company in respect of such costs related to the issuance of shares are recorded as an asset in the accompanying consolidated balance sheets in the line item "Deferred offering costs", for subsequent deduction from the related proceeds upon closing of the offering.

To the extent that certain costs, in particular legal fees, are known to have been accrued but have not yet been invoiced and paid, they are included in "Other accounts payable and accrued expenses" on the accompanying consolidated balance sheets.

Available-for-Sale Securities, at Fair Value

Revenue Recognition, Premium Amortization, and Discount Accretion

Interest income on the Company's AFS securities portfolio, with the exception of Non-Agency RMBS IOs (as further described below), is accrued based on the actual coupon rate and the outstanding principal balance of such securities. The Company recognizes interest income using the effective interest method for all AFS securities. As such, premiums and discounts are amortized or accreted into interest income over the lives of the securities in accordance with ASC 310-20, "Nonrefundable Fees and Other Costs", ASC 320-10, "Investments Debt and Equity Securities" or ASC 325-40, "Beneficial Interests in Securitized Financial Assets", as applicable. Total interest income is recorded in the "Interest Income" line item on the consolidated statements of operations.

On at least a quarterly basis for securities accounted for under ASC 320-10 and ASC 310-20 (generally Agency RMBS), prepayments of the underlying collateral must be estimated, which directly affect the speed at which the Company amortizes such securities. If actual and anticipated cash flows differ from previous estimates; the Company recognizes a "catch-up" adjustment in the current period to the amortization of premiums for the impact of the cumulative change in the effective yield through the reporting date.

Similarly, the Company also reassesses the cash flows on at least a quarterly basis for securities accounted for under ASC 325-40 and ASC 310-30 (generally Non-Agency RMBS and Multi-Family MBS). In estimating these cash flows, there are a number of assumptions that are subject to uncertainties and contingencies. These include the rate

and timing of principal and interest receipts (including assumptions of prepayments, repurchases, defaults and liquidations), the pass-through or coupon rate and interest rate fluctuations. In addition, interest payment shortfalls due to delinquencies on the underlying mortgage loans have to be judgmentally estimated. Differences between previously estimated cash flows and current actual and anticipated cash flows are recognized prospectively through an adjustment of the yield over the remaining life of the security based on the current amortized cost of the investment as adjusted for credit impairment, if any.

For investments purchased with evidence of deterioration of credit quality for which it is probable, at acquisition, that the Company will be unable to collect all contractually required payments receivable, the Company applies the provisions of ASC 310-30, "Loans and Debt Securities Acquired with Deteriorated Credit Quality." ASC 310-30 addresses accounting for differences between contractual cash flows and cash flows expected to be collected from an investor's initial investment in loans or debt securities acquired in a transfer if those differences are attributable, at least in part, to credit quality. ASC 310-30 limits the yield that may be accreted (accretable yield) to the excess of the investor's estimate of undiscounted expected principal, interest and other cash flows (cash flows expected at acquisition to be collected) over the investor's initial investment in the loan. ASC 310-30 requires that the excess of contractual cash flows over cash flows expected to be collected (nonaccretable difference) not be recognized as an adjustment of yield, loss accrual or valuation allowance.

Subsequent increases in cash flows expected to be collected are generally recognized prospectively through adjustment of the investment's yield over its remaining life. Decreases in cash flows expected to be collected are recognized as impairment to the extent that such decreases are due, at least in part, to an increase in credit loss expectations ("credit impairment"). To the extent that decreases in cash flows expected to be collected are the result of factors other than credit impairment, for example a change in rate of prepayments, such changes are generally recognized prospectively through adjustment of the investment's yield over its remaining life.

The Company's accrual of interest, discount and premium for U.S. federal and other tax purposes is likely to differ from the financial accounting treatment of these items as described above.

Gains and losses from the sale of AFS securities are recorded as realized gains (losses) within realized gain (loss) on sale of investments, net in the Company's consolidated statements of operations. Upon the sale of a security, the Company will determine the cost of the security and the amount of unrealized gains or losses to reclassify out of accumulated other comprehensive income (loss) into earnings based on the specific identification method. Unrealized gains and losses on the Company's AFS securities are recorded as unrealized gain (loss) on available-for-sale securities, net in the Company's consolidated statements of comprehensive income (loss).

FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2017

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Impairment

The Company evaluates its MBS, on a quarterly basis, to assess whether a decline in the fair value of an AFS security below the Company's amortized cost basis is an other-than-temporary impairment ("OTTI"). The presence of OTTI is based upon a fair value decline below a security's amortized cost basis and a corresponding adverse change in expected cash flows due to credit related factors as well as non-credit factors, such as changes in interest rates and market spreads. Impairment is considered other-than-temporary if an entity (i) intends to sell the security, (ii) will more likely than not be required to sell the security before it recovers in value or (iii) does not expect to recover the security's amortized cost basis, even if the entity does not intend to sell the security. Under these scenarios, the impairment is other-than-temporary and the full amount of impairment should be recognized currently in earnings and the cost basis of the investment security is adjusted. However, if an entity does not intend to sell the impaired debt security and it is more likely than not that it will not be required to sell before recovery, OTTI should be recognized to the extent that a decrease in future cash flows expected to be collected is due, at least in part, to an increase in credit impairment. A decrease in future cash flows due to factors other than credit, for example a change in the rate of prepayments, is considered a non-credit impairment. The full amount of the difference between the security's previous and new cost basis resulting from credit impairment is recognized currently in earnings, and the difference between the new amortized cost basis and the cash flows expected to be collected is accreted as interest income in accordance with the effective interest method. Decreases in cash flows expected to be collected resulting from non-credit impairment are generally recognized prospectively through adjustment of the investment's yield over its remaining life.

Mortgage Loans Held-for-Sale, at Fair Value

Mortgage loans held-for-sale are reported at fair value as a result of a fair value option election. See Note 3 - Fair Value Measurements for details on fair value measurement. Mortgage loans are classified as held-for-sale based upon the Company's intent to sell them in the secondary whole loan market.

Interest income on mortgage loans held-for-sale is recognized at the loan coupon rate. Interest income recognition is suspended when mortgage loans are placed on non-accrual status. The accrual of interest on loans is discontinued when, in management's opinion, the interest is considered non-collectible, and in all cases when payment becomes greater than 90 days past due. Loans return to accrual status when principal and interest become current and are anticipated to be fully collectible.

Multi-Family and Residential Mortgage Loans Held in Securitization Trusts

Multi-family and residential mortgage loans held in consolidated securitization trusts are comprised of multi-family mortgage loans held in the FREMF 2011-K13 Trust and the FREMF 2012-KF01 Trust, and residential mortgage loans held in the CSMC 2014-OAK1 Trust, as of December 31, 2017. Based on a number of factors, the Company determined that it was the primary beneficiary of the VIEs underlying the trusts, met the criteria for consolidation and, accordingly, has consolidated the three trusts, including their assets, liabilities, income and expenses in its financial statements. The Company has elected the fair value option on each of the assets and liabilities held within the trusts. See Note 3 - Fair Value Measurement below for additional detail. As the result of the Company's determination that it is not the primary beneficiary of JPMMT 2014-OAK4 Trust it does not consolidate this trust.

Interest income on multi-family and residential mortgage loans held in securitization trusts is recognized at the loan coupon rate. Interest income recognition is suspended when mortgage loans are placed on non-accrual status. The

accrual of interest on loans is discontinued when, in management's opinion, the interest is considered non-collectible, and in all cases when payment becomes greater than 90 days past due. Loans return to accrual status when principal and interest become current and are anticipated to be fully collectible.

#### Mortgage Servicing Rights and Excess Servicing Rights, at Fair Value

Mortgage servicing rights ("MSRs") are associated with residential mortgage loans that the Company has historically purchased and subsequently sold or securitized. MSRs are held and managed at the Company's TRS. As the owner of MSRs, the Company is entitled to receive a portion of the interest payments from the associated residential mortgage loan, and is obligated to service directly or through a subservicer, the associated loan. MSRs are reported at fair value as a result of a fair value option election. See Note 3 - Fair Value Measurement below for additional detail.

Residential mortgage loans for which the Company owns the MSRs are directly serviced by one or more sub-servicers retained by the Company, since the Company does not directly service any residential mortgage loans.

MSR income is recognized at the contractually agreed rate, net of the costs of sub-servicers retained by the Company. If a sub-servicer with which the Company contracts were to default, an evaluation of MSR assets for impairment would be undertaken at that time.

To the extent that the Company determines it is the primary beneficiary of a residential mortgage loan securitization trust into which it has sold loans, any associated MSRs are eliminated on the consolidation of the trust. The trust is contractually obligated to pay a portion of the interest payments from the associated residential mortgage loans for the direct servicing of the loans, and after deduction of sub-servicing fees payable to contracted sub-servicers, the net amount, excess servicing rights, represents a liability of the trust. See Note 3 - Fair Value Measurement below for additional detail.

#### Non-Agency RMBS IOs, at Fair Value

Non-Agency RMBS IOs that the Company owns are associated with residential mortgage loan securitizations that the Company has previously sponsored, and are reported at fair value as a result of a fair value option election. See Note 3 - Fair Value Measurements for details on fair value measurement. Interest income on IOs is recognized at the contractually agreed rate, and changes in fair value are recognized in the Company's consolidated statement of operations.

#### Repurchase Agreements

The Company finances the acquisition of certain of its mortgage-backed securities through the use of repurchase agreements. The repurchase agreements are generally short-term debt, which expire within one year. Borrowings under repurchase agreements generally bear interest rates at a specified margin over LIBOR and are generally uncommitted. In accordance with ASC 860 "Transfers and Servicing" the Company accounts for the repurchase agreements as collateralized financing transactions and they are carried at their contractual amounts, as specified in the respective agreements. The contractual amounts approximate fair value due to their short-term nature.

FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2017

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Residential Loan Warehouse Facilities

The Company previously financed the acquisition of certain of its residential mortgage loans through the use of short-term, uncommitted residential loan warehouse facilities, which were structured as repurchase agreements. The Company accounted for outstandings under these facilities as collateralized financing transactions which were carried at their contractual amounts, and approximated fair value due to their short-term nature.

Secured Loans

In February 2015, the Company's wholly owned subsidiary, FOI, became a member of the Federal Home Loan Bank of Indianapolis ("FHLBI"). As a member of FHLBI, FOI borrowed funds from FHLBI in the form of secured advances ("FHLB advances"). FHLB advances were treated as secured financing transactions and were carried at their contractual amounts. In connection with FHLB advances, FOI was required to purchase FHLBI stock, which was recorded on the Company's consolidated balance sheet as an asset. All FHLB stock was redeemed and all FHLB advances were paid during 2016.

Multi-Family and Residential Securitized Debt Obligations

Multi-family and residential securitized debt obligations represent third-party liabilities of the FREMF 2011-K13 Trust, FREMF 2012-KF01 Trust and CSMC 2014-OAK1 Trust, and excludes liabilities of the trust acquired by the Company that are eliminated on consolidation. The third-party obligations of each trust do not have any recourse to the Company as the consolidator of each trust.

Backstop Guarantees

The Company, through FOAC and in return for fees, provides seller eligibility and backup guarantee services in respect of residential mortgage loans that are traded through one or more loan exchanges operated by MAXEX LLC ("MAXEX"). See Note 14 and Note 15 for additional information regarding MAXEX. To the extent that a loan seller approved by FOAC fails to honor its obligations to repurchase one or more loans based on an arbitration finding that such seller has breached its representations and warranties, FOAC provides a backstop guarantee of the repurchase obligation. The Company has evaluated its backstop guarantees pursuant to ASC 460, Guarantees, and has determined them to be performance guarantees, for which ASC 460 contains initial recognition and measurement requirements, and related disclosure requirements. FOAC is obligated in two respects: (i) a noncontingent liability, which represents FOAC's obligation to stand ready to perform under the terms of the guarantee in the event that the specified triggering event(s) occur; and (ii) the contingent liability, which represents FOAC's obligation to make future payments if those triggering events occur. FOAC recognizes the noncontingent liability at the inception of the guarantee at the fair value, which is the fee received or receivable, and is recorded on the Company's consolidated balance sheet as a liability in the line item "Deferred income." The Company amortizes these fees into income on a straight-line basis over five years, based on an assumed constant prepayment rate of 15% for residential mortgage loans and other observable data. The Company's contingent liability is accounted for pursuant to ASC 450, Contingencies, pursuant to which the contingent liability must be recognized when its payment becomes probable and reasonably estimable.

Common Stock

At December 31, 2017, and December 31, 2016, the Company was authorized to issue up to 450,000,000 shares of common stock, par value \$0.01 per share, with such designations, voting and other rights and preferences as may be determined from time to time by the Company's Board of Directors. The Company had 22,143,758 shares of common stock issued and outstanding at December 31, 2017 and 17,539,258 at December 31, 2016.

#### Stock Repurchase Program

On December 15, 2015, the Company's Board of Directors authorized a stock repurchase program ("Repurchase Program"), to repurchase up to \$10 million of the Company's outstanding common stock. Subject to applicable securities laws, repurchase of common stock under the Repurchase Program may be made at times and in amounts as the Company deems appropriate, using available cash resources. Shares of common stock repurchased by the Company under the Repurchase Program, if any, will be canceled and, until reissued by the Company, will be deemed to be authorized but unissued shares of common stock. The Repurchase Program may be suspended or discontinued by the Company at any time and without prior notice. As of December 31, 2016, the Company had repurchased 126,856 shares of common stock at a weighted average price of \$5.09. There has been no activity in 2017. As of December 31, 2017, \$9.4 million of common stock remained authorized for future repurchases under the Repurchase Program.

#### Preferred Stock

At December 31, 2017, and December 31, 2016, the Company was authorized to issue up to 50,000,000 share of preferred stock, par value \$0.01 per share, with such designations, voting and other rights and preferences as may be determined from time to time by the Company's Board. The Company had 1,610,000 shares of preferred stock issued and outstanding at both December 31, 2017 and December 31, 2016.

#### Income Taxes

The Company has elected to be taxed as a REIT under the Code for U.S. federal income tax purposes, commencing with the Company's short taxable period ended December 31, 2012. So long as the Company qualifies as a REIT, with the exception of our taxable REIT subsidiaries, the Company generally will not be subject to U.S. federal income taxes on its taxable income to the extent it annually distributes at least 90% of its net taxable income to stockholders and maintains its qualification as a REIT.

In addition to the Company's election to be taxed as a REIT, the Company complies with Sections 856 through 860 of the Code. Accordingly, the Company generally will not be subject to U.S. federal income tax to the extent of its distributions to stockholders and as long as certain asset, income and share ownership tests are met. To maintain its qualification as a REIT, the Company must distribute at least 90% of its REIT taxable income to its stockholders and meet certain other requirements. The Company may also be subject to certain state, local and franchise taxes. Under certain circumstances, federal income and excise taxes may be due on its undistributed taxable income. If the Company were to fail to meet these requirements, it would be subject to U.S. federal income tax, which

FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2017

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

could have a material adverse impact on its results of operations and amounts available for distributions to its stockholders. The Company believes it will meet all of the criteria to maintain the Company's REIT qualification for the applicable periods, but there can be no assurance that these criteria will continue to be met in subsequent periods.

The Company assesses its tax positions for all open tax years and determines whether the Company has any material unrecognized liabilities in accordance with ASC 740, Income Taxes. The Company records these liabilities to the extent the Company deems them more likely than not to be incurred. The Company's accounting policy with respect to interest and penalties is to classify these amounts as other interest expense. As further described in Note 19, the Company declared and paid in the fourth quarter of 2016 a deficiency dividend relating to a determination of an inability to offset certain net gains on hedging transactions in 2013 against net capital losses on the sale of certain mortgage-backed securities. In connection with this declaration, during the first quarter of 2017, the Company paid an amount of \$2.01 million for interest charges to the IRS. The Company previously provisioned \$1.86 million in the third quarter of 2016 in the Company's consolidated balance sheets in the line item "Other accounts payable and accrued expenses"; the remaining balance of \$0.15 million was expensed in the first quarter of 2017, which is included in "Other interest expense" in the Company's consolidated statements of operations. The first quarter 2017 payment of \$2.01 million is included in "cash paid for interest" in the Company's consolidated statements of cash flows.

The Tax Cuts and Jobs Act was enacted in December 2017 and is generally effective tax years beginning after 2017. This new legislation has no material adverse effect on the Company's business and contains several potentially favorable provisions.

Certain activities of the Company are conducted through a TRS and therefore are taxed as a standalone U.S. C-Corporation. Accordingly, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

If a TRS generates net income, the TRS can declare dividends to the Company which will be included in its taxable income and necessitate a distribution to its stockholders. Conversely, if the Company retains earnings at a TRS level, no distribution is required and the Company can increase book equity of the consolidated entity.

Earnings per Share

The Company calculates basic and diluted earnings per share by dividing net income attributable to common stockholders for the period by the weighted-average shares of the Company's common stock outstanding for that period. Diluted earnings per share takes into account the effect of dilutive instruments, such as warrants, stock options, and unvested restricted stock, but use the average share price for the period in determining the number of incremental shares that are to be added to the weighted-average number of shares outstanding. See Note 17 for details of the computation of basic and diluted earnings per share.

Stock-Based Compensation

The Company is required to recognize compensation costs relating to stock-based payment transactions in the financial statements. The Company accounts for share-based compensation issued to its Manager and non-management directors using the fair value based methodology prescribed by ASC 505, Equity (“ASC 505”), or ASC 718, Share-Based Payment (“ASC 718”), as appropriate. Compensation cost related to restricted common stock issued to the Manager is initially measured at estimated fair value at the grant date, and is remeasured on subsequent dates to the extent the awards are unvested. Additionally, compensation cost related to restricted common stock issued to the non-management directors is measured at its estimated fair value at the grant date and amortized and expensed over the vesting period. See Note 14 for details of stock-based awards issuable under the Manager Equity Plan.

#### Comprehensive Income (Loss) Attributable to Common Stockholders

Comprehensive income (loss) is comprised of net income (loss), as presented in the consolidated statement of comprehensive income (loss), adjusted for changes in unrealized gain or loss on AFS securities (excluding Non-Agency RMBS IOs), reclassification adjustments for net gain (loss) and other-than-temporary impairments included in net income (loss) and dividends paid to preferred stockholders.

#### Recently Issued and/or Adopted Accounting Standards

##### Revenue from Contracts with Customers

In May 2014, the Financial Accounting Standards Board, or FASB, issued ASU No. 2014-09, which is a comprehensive revenue recognition standard that supersedes virtually all existing revenue guidance under GAAP. ASU 2014-09 also creates a new topic in the Codification, Topic 606 (“ASC 606”). In addition to superseding and replacing nearly all existing GAAP revenue recognition guidance, including industry-specific guidance, ASC 606 does the following: (1) established a new control-based revenue recognition model; (2) changes the basis for deciding when revenue is recognized over time or at a point in time; (3) provides new and more detailed guidance on specific aspects of revenue recognition; and (4) expands and improves disclosures about revenue. As a result of the issuance of ASU No. 2015-14 in August 2015, deferring the effective date of ASU No. 2014-09 by one year, the ASU is effective for annual periods, and interim periods within those annual periods, beginning on or after December 15, 2017, with early adoption prohibited.

In May 2016, the FASB issued ASU 2016-11, “Revenue Recognition (Topic 605) and Derivatives and Hedging (Topic 815): Rescission of SEC Guidance Because of Accounting Standards Updates 2014-09 and 2014-16 Pursuant to Staff Announcements at the March 3, 2016 EITF Meeting.” The amendments make targeted improvements to clarify the principal versus agent assessment and are intended to make the guidance more operable and lead to more consistent application. The amendments in this update are effective immediately.

ASC 606 applies to all contracts with customers with exceptions for financial instruments and other contractual rights or obligations that are within the scope of other ASC Topics. Exclusions from the scope of ASC 606 include interest income related to the following: investment securities available for sale (subject to ASC 320, Investments - Debt and Equity Securities or ASC 325, Investments - Other); residential mortgage loans and multi-family loans (subject to either ASC



FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2017

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

310, Receivables or ASC 825, Financial Instruments); and derivative assets and derivative liabilities (subject to ASC 815, Derivatives and Hedging). The Company evaluated the applicability of this ASU with respect to its investment portfolio, considering the scope exceptions listed above, and has determined that the adoption of this ASU will not have a material impact on the Company's financial condition or results of operations as the substantial majority of the Company's revenue is generated by financial instruments and other contractual rights and obligations that are not within the scope of ASC 606.

Recognition and Measurement of Financial Assets and Financial Liabilities

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

Stock Compensation

In March 2016, the FASB issued ASU 2016-09, effective January 1, 2017, which simplifies several aspects of the accounting for employee share-based payment transactions for both public and nonpublic entities. The areas for simplifications in the update involve several aspects of the accounting for share-based payment transactions, including income tax consequences, classifications of awards as either equity or liabilities, and classification on the statement of cash flows. The Company has determined this ASU will not have a material impact on the Company's financial condition or results of operations.

Credit Losses

In June 2016, the FASB issued ASU 2016-13 which is a comprehensive amendment of credit losses on financial instruments. Currently GAAP requires an "incurred loss" methodology for recognizing credit losses that delays recognition until it is probable a loss has been incurred. The standard's core principle is that an entity replaces the "incurred loss" impairment methodology in current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. For public business entities that are SEC filers, the amendment in this update are effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The Company continues to assess the impact of this guidance.

Classification of Certain Cash Receipts and Cash Payments

In August 2016, the FASB issued ASU 2016-15, which amends ASC Topic 230, Statement of Cash Flows ("ASC 230"), to reduce diversity in how certain transactions are classified in the statement of cash flows. The ASU is effective for public business entities for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. The Company has determined this ASU will not have a material impact on the Company's financial condition or results of operations.

Interests Held through Related Parties That Are under Common Control

In October 2016, the FASB issued ASU 2016-17, to amend the consolidation guidance on how a reporting entity that is the single decision maker of a VIE should treat indirect interests in the entity held through related parties that are under common control with the reporting entity when determining whether it is the primary beneficiary of that VIE. The ASU is effective for public business entities for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. The Company has determined this ASU has not had a material impact on the Company's financial condition or results of operations.

#### Restricted Cash

In November 2016, the FASB issued ASU 2016-18, which amends ASC Topic 230, Statement of Cash Flows, to reduce diversity in how entities present restricted cash and restricted cash equivalents in the statement of cash flows. The amendments in ASU 2016-18 require restricted cash and restricted cash equivalents to be included with cash and cash equivalents when reconciling the beginning-of-period and of end-of-period total amounts shown on the statement of cash flows. The ASU is effective for public business entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017. Early application is permitted, provided that all of the amendments are adopted in the same period. The amendments of this ASU should generally be applied using a retrospective transition method to each period presented. The Company adopted the ASU beginning with the first quarter of 2017. The prior period consolidated statement of cash flows has been retrospectively adjusted to conform to this presentation.

#### NOTE 3 - FAIR VALUE MEASUREMENTS

The Company discloses the fair value of its financial instruments according to a fair value hierarchy (Levels 1, 2 and 3, as defined). In accordance with GAAP, the Company is required to provide enhanced disclosures regarding instruments in the Level 3 category (which require significant management judgment), including a separate reconciliation of the beginning and ending balances for each major category of assets and liabilities. Additionally, GAAP permits entities to choose to measure many financial instruments and certain other items at fair value (the "fair value option"), and the election of such choice is irrevocable. Unrealized gains and losses on items for which the fair value option has been elected are irrevocably recognized in earnings at each subsequent reporting date.

#### Available-for-sale Securities

The Company currently invests in Agency RMBS, Multi-Family MBS and Non-Agency RMBS.

#### Designation

The Company classifies its MBS securities as AFS investments. Although the Company generally intends to hold most of its investment securities until maturity, it may, from time to time, sell any of its investment securities as part of the overall management of its portfolio. All assets classified as AFS, except Non-Agency RMBS IOs, are reported at estimated fair value, with unrealized gains and losses, excluding other than temporary impairments, included in accumulated

FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2017

NOTE 3 – FAIR VALUE MEASUREMENTS (Continued)

other comprehensive income, a separate component of shareholders' equity. As the result of a fair value election, unrealized gains and losses on Non-Agency RMBS IOs are recorded in the Company's consolidated statement of operations.

Determination of MBS Fair Value

The Company determines the fair values for the Agency RMBS, Multi-Family MBS and Non-Agency RMBS in its portfolio based on obtaining a valuation for each Agency RMBS, Multi-Family MBS and Non-Agency RMBS from third-party pricing services, and may also obtain dealer quotes, as described below. The third-party pricing services use common market pricing methods that may include pricing models that may incorporate such factors as coupons, prepayment speeds, spread to the Treasury curves and interest rate swap curves, duration, periodic and life caps and credit enhancement, as applicable. The dealers incorporate common market pricing methods, including a spread measurement to the Treasury curve or interest rate swap curve as well as underlying characteristics of the particular security, including coupon, periodic and life caps, collateral type, rate reset period and seasoning or age of the security, as applicable.

The Company obtains pricing data from a primary third-party pricing service for each Agency RMBS, Multi-Family MBS and Non-Agency RMBS. If other available market data indicates that the pricing data from the primary third-party service is materially inaccurate, or pricing data is unavailable from the primary third-party pricing service, the Company undertakes a review of other available prices and takes additional steps to determine fair value. In all cases, the Company validates its understanding of methodology and assumptions underlying the fair value used. The Company determines that the pricing data from the primary third-party service is materially inaccurate if it is not materially representative of where a specific security can be traded in the normal course of business. In making such determination, the Company follows a series of steps, including review of collateral marks from margin departments of repurchase agreement counterparties, utilization of bid list, inventory list and extensive unofficial market color, review of other third-party pricing service data and a yield analysis of each Multi-Family MBS and Non-Agency RMBS based on the pricing data from the primary third-party pricing service and the Company's cash flow assumptions.

The Company reviews all pricing of Agency and Non-Agency RMBS and Multi-Family MBS used to ensure that current market conditions are properly represented. This review includes, but is not limited to, comparisons of similar market transactions or alternative third-party pricing services, dealer quotes and comparisons to a pricing model. Values obtained from the third-party pricing service for similar instruments are classified as Level 2 securities if the pricing methods used are consistent with the Level 2 definition. If quoted prices for a security are not reasonably available from the pricing service, but dealer quotes are, the Company classifies the security as a Level 2 security. If neither is available, the Company determines the fair value based on characteristics of the security that are received from the issuer and based on available market information received from dealers and classifies it as a Level 3 security.

Mortgage Loans Held-for-Sale

Designation

The Company classified its residential mortgage loans as held-for-sale ("HFS") investments.

The Company elected the fair value option for residential mortgage loans it acquired and classified as HFS. The fair value option was elected to help mitigate earnings volatility by better matching the asset accounting with any related hedges. The Company's policy is to record separately interest income on these fair value elected loans. Additionally, upfront costs related to these loans are not deferred or capitalized. Fair value adjustments are reported in unrealized gain (loss) on mortgage loans held-for-sale on the consolidated statements of operations. The fair value option is irrevocable once the loan is acquired.

#### Determination of Mortgage Loan Fair Value

The Company determines the fair values of the mortgage loans in its portfolio from third-party pricing services. The third-party pricing services use common market pricing methods which may include pricing models that may incorporate such factors as coupons, prepayment speeds, spread to the Treasury curves and interest rate swap curves, duration, periodic and life caps, as applicable. In addition, the third-party pricing services benchmark their pricing models against observable pricing levels being quoted by a range of market participants active in the purchase and sale of residential mortgage loans.

The Company obtains pricing data from a primary third-party pricing service for each mortgage loan. If other available market data indicates that the pricing data from the primary third-party service is materially inaccurate, or pricing data is unavailable from the primary third-party pricing service, the Company undertakes a review of other available prices and takes additional steps to determine fair value. In all cases, the Company validates its understanding of methodology and assumptions underlying the fair value used. The Company determines that the pricing data from the primary third-party service is materially inaccurate if it is not materially representative of the price at which a specific loan can be traded in the normal course of business.

The Company reviews all pricing of mortgage loans used to ensure that current market conditions are properly represented. This review includes, but is not limited to, comparisons of similar market transactions or alternative third-party pricing services, dealer quotes and comparisons to a pricing model. Values obtained from the third-party pricing service for similar instruments are classified as Level 2 assets if the pricing methods used are consistent with the Level 2 definition. If quoted prices for a loan are not reasonably available from the pricing service, but alternative quotes are, the Company classifies the loan as a Level 2 asset. If neither is available, the Company determines the fair value based on characteristics of the loan and based on other available market information and classifies it as a Level 3 asset.

#### MSRs and Excess Servicing Rights

##### Designation

MSRs are associated with residential mortgage loans that the Company has purchased and subsequently sold or securitized, and are typically acquired directly from loan originators and recognized at the time that loans have been transferred to a third party or a securitization, in each case providing such transfer has met the GAAP criteria for sale. The Company retains the rights to service certain loans that it has sold or securitized, but employs one or more sub-servicers to perform the servicing activities.

FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2017

NOTE 3 – FAIR VALUE MEASUREMENTS (Continued)

To the extent that the Company determines it is the primary beneficiary of a residential mortgage loan securitization trust into which it has sold loans, any associated MSR's are eliminated on the consolidation of the trust. The trust is contractually obligated to pay a portion of the interest payments from the associated residential mortgage loans for the direct servicing of the loans, and after deduction of sub-servicing fees payable to contracted sub-servicers, the net amount, excess servicing rights, represents a liability of the trust. Upon consolidation of the trust, the fair value of the excess servicing rights is equal to the related MSR's held at the Company's TRS.

The Company has elected the fair value option in respect of MSR's and excess servicing rights.

Determination of Fair Value

The Company determines the fair value of its MSR's and excess servicing rights from third-party pricing services. The third-party pricing services use common market pricing methods that include market discount rates, prepayment speeds of serviced loans, the market cost of servicing, and observed market pricing for MSR purchase and sale transactions. Changes in the fair value of MSR's occur primarily as a result of the collection and realization of expected cash flows, as well as changes in valuation inputs and assumptions.

The Company obtains MSR pricing data from a primary third-party pricing service, and validates its understanding of methodology and assumptions underlying the fair value used. Fair values are estimated based on applying inputs to generate the net present value of estimated net servicing income, and as a consequence of the fact that these discounted cash flow models utilize certain significant unobservable inputs and observable MSR purchase and sale transactions are relatively infrequent, the Company classifies MSR's as a Level 3 asset.

See Note 12 for a further presentation on MSR's.

Multi-Family Mortgage Loans Held in Securitization Trusts and Multi-Family Securitized Debt Obligations

Designation

Multi-family mortgage loans held in consolidated securitization trusts are comprised of multi-family mortgage loans held in the FREMF 2011-K13 Trust and the FREMF 2012-KF01 Trust as of December 31, 2017. Based on a number of factors, the Company determined that it was the primary beneficiary of the VIEs underlying the trusts, met the criteria for consolidation and, accordingly, has consolidated the FREMF 2011-K13 Trust and the FREMF 2012-KF01 Trust, including their assets, liabilities, income and expenses in its financial statements. The Company has elected the fair value option on each of the assets and liabilities held within these trusts.

Determination of Fair Value

In accordance with ASU 2014-13, the Company has elected the fair value option in respect of the assets and liabilities of the FREMF 2011-K13 Trust and the FREMF 2012-KF01 Trust. The trusts are "static", that is no reinvestment is permitted and there is very limited active management of the underlying assets. Under the ASU, the Company is required to determine whether the fair value of the financial assets or the fair value of the financial liabilities of each of the trusts is more observable, but in either case, the methodology results in the fair value of the assets of each of the

trusts being equal to the fair value of their liabilities. The Company has determined that the fair value of the liabilities of each of the trusts is more observable, since in all cases prices for the liabilities are available from the primary third-party pricing service utilized for Multi-Family MBS, while the individual assets of each of the trusts are inherently incapable of precise measurement given their illiquid nature and the limitations on available information related to these assets. Given that the Company's methodology for valuing the assets of the trusts is an aggregate value derived from the fair value of the trust liabilities, the Company has determined that the valuation of the trust assets in their entirety should be classified as Level 2 valuations.

#### Residential Mortgage Loans Held in Securitization Trusts and Residential Securitized Debt Obligations

##### Designation

Residential mortgage loans held in consolidated securitization trusts are comprised of residential mortgage loans held in the CSMC 2014-OAK1 Trust as of December 31, 2017. Based on a number of factors, the Company determined that it was the primary beneficiary of the VIE underlying the trust, met the criteria for consolidation and, accordingly, has consolidated the CSMC 2014-OAK1 Trust including its assets, liabilities, income and expenses in its financial statements. The Company has elected the fair value option on each of the assets and liabilities held within the trust. As the result of the Company's determination that it is not the primary beneficiary of JPMMT 2014-OAK4 Trust, Oaks Mortgage Trust Series 2015-1 and 2015-2, it does not consolidate these trusts.

##### Determination of Fair Value

In accordance with ASU 2014-13, the Company has elected the fair value option in respect of the assets and liabilities of the CSMC 2014-OAK1 Trust. The trust is "static", that is no reinvestment is permitted and there is very limited active management of the underlying assets. Under the ASU, the Company is required to determine whether the fair value of the financial assets or the fair value of the financial liabilities of the trust is more observable, but in either case, the methodology results in the fair value of the assets of the trust being equal to the fair value of its liabilities. The Company has determined that the fair value of the liabilities of the trust is more observable, since in all cases prices for the liabilities are available from the primary third-party pricing service utilized for Non-Agency RMBS, with the exception of the excess servicing rights, which are available from an alternative third-party pricing service. While the individual assets of the trust, i.e. the underlying residential mortgage loans, are capable of being priced, the Company has determined that the pricing of the liabilities is more easily and readily determined. Given that the Company's methodology for valuing the assets of the trust is an aggregate value derived from the fair value of the trust's liabilities, the Company has determined that the valuation of the trust assets in their entirety should be classified as Level 2 valuations.

##### Accounting for Derivative Financial Instruments

FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2017

NOTE 3 – FAIR VALUE MEASUREMENTS (Continued)

In accordance with FASB guidance ASC 815 “Derivatives and Hedging”, all derivative financial instruments, whether designated for hedging relationships or not, are recorded at fair value on the consolidated balance sheet as assets or liabilities. The Company obtains valuation information for each derivative financial instrument from the related derivative counterparty. If other available market data indicates that the valuation information from the counterparty is materially inaccurate, or pricing data is unavailable from the counterparty, the Company shall undertake a review of other available valuation information, including third party pricing services and/or dealers, and shall take additional steps to determine fair value. The Company reviews all valuations of derivative financial instruments used to ensure that current market conditions are properly represented. This review includes, but is not limited to, comparisons of similar market transactions or alternative third-party pricing services, dealer quotes and comparisons to a pricing model. Values based on quoted prices for similar instruments in active markets, including exchange-traded instruments, are classified as Level 1 valuations. Values obtained from the derivative counterparty, the third-party pricing service or dealers, as appropriate, for similar instruments are classified as Level 2 valuations if the pricing methods used are consistent with the Level 2 definition. If none of these sources is available, the Company determines the fair value based on characteristics of the instrument and based on available market information received from dealers and classifies it as a Level 3 valuation.

At the inception of a derivative contract, the Company determines whether or not the instrument will be part of a qualifying hedge accounting relationship. Due to the volatility of the credit markets and difficulty in effectively matching pricing or cash flows, the Company has elected to treat all current derivative contracts as trading instruments. The changes in fair value of derivatives accounted for as trading instruments are reported in the consolidated statement of operations as unrealized gain (loss) on derivative contracts, net.

The Company enters into interest rate derivative contracts for a variety of reasons, including minimizing significant fluctuations in earnings or market values on certain assets or liabilities that may be caused by changes in interest rates. The Company may, at times, enter into various forward contracts, including short securities, Agency to-be-announced securities (“TBAs”), options, futures, swaps and caps. Due to the nature of these instruments, they may be in a receivable/asset position or a payable/liability position at the end of an accounting period. Amounts payable to, and receivable from, the same party under contracts may be offset as long as the following conditions are met: (a) each of the two parties owes the other determinable amounts; (b) the reporting party has the right to offset the amount owed with the amount owed by the other party; (c) the reporting party intends to offset; and (d) the right of offset is enforceable by law. If the aforementioned conditions are not met, amounts payable to and receivable from are presented by the Company on a gross basis in the consolidated balance sheet.

Other Financial Instruments

The carrying value of short term instruments, including cash and cash equivalents, receivables and repurchase agreements whose term is less than twelve months, generally approximates fair value due to the short term nature of the instruments.

NOTE 4 – AVAILABLE-FOR-SALE SECURITIES

Edgar Filing: Five Oaks Investment Corp. - Form 10-K

The following table presents the Company's AFS investment securities by collateral type at fair value as of December 31, 2017 and December 31, 2016:

	December 31, 2017	December 31, 2016
Mortgage-backed securities:		
Agency		
Federal Home Loan Mortgage Corporation	\$530,640,091	\$326,958,046
Federal National Mortgage Association	754,443,557	463,232,187
Non-Agency	—	7,592,802
Multi-Family	5,742,000	73,146,566
Total mortgage-backed securities	\$1,290,825,648	\$870,929,601

The following tables present the amortized cost and fair value of the Company's AFS investment securities by collateral type as of December 31, 2017 and December 31, 2016:

	December 31, 2017			
	Agency	Non-Agency	Multi-Family	Total
Face Value	\$1,274,329,317	\$ —	\$7,500,000	\$1,281,829,317
Unamortized premium	23,818,687	—	—	23,818,687
Unamortized discount	—	—	—	—
Designated credit reserve and OTTI (2)	—	—	—	—
Net, unamortized	(491,020 )	—	(1,713,542 )	(2,204,562 )
Amortized Cost	1,297,656,984	—	5,786,458	1,303,443,442
Gross unrealized gain	751,458	—	—	751,458
Gross unrealized (loss)	(13,324,794 )	—	(44,458 )	(13,369,252 )
Fair Value	\$1,285,083,648	\$ —	\$5,742,000	\$1,290,825,648



## FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2017

## NOTE 4 – AVAILABLE-FOR-SALE SECURITIES (Continued)

	December 31, 2016			
	Agency	Non-Agency <sup>(1)</sup>	Multi - Family	Total
Face Value	\$779,219,115	\$ 4,393,771	\$ 100,907,815	\$884,520,701
Unamortized premium	17,748,138	—	—	17,748,138
Unamortized discount	—	—	—	—
Designated credit reserve and OTTI <sup>(2)</sup>	—	(1,929,833 )	—	(1,929,833 )
Net, unamortized	(1,311,292 )	(369,887 )	(26,160,083 )	(27,841,262 )
Amortized Cost	795,655,961	2,094,051	74,747,732	872,497,744
Gross unrealized gain	2,663,975	234,647	509,519	3,408,141
Gross unrealized (loss)	(8,129,703 )	—	(2,110,685 )	(10,240,388 )
Fair Value	\$790,190,233	\$ 2,328,698	\$73,146,566	\$865,665,497

(1) Non-Agency AFS does not include interest-only securities with a notional amount of \$509,109,248, book value of \$14,712,374 unrealized loss of \$9,448,271 and a fair value of \$5,264,104 at December 31, 2016.

(2) Discount designated as Credit Reserve is generally not expected to be accreted into interest income. Amounts disclosed reflect Credit Reserve of \$0 and \$1,929,833 and at December 31, 2017 and December 31, 2016.

At December 31, 2017, the Company did not intend to sell any of its MBS that were in an unrealized loss position, and it is “more likely than not” that the Company will not be required to sell these MBS before recovery of their amortized cost basis, which may be at their maturity.

The Company did not recognize any credit-related OTTI losses through earnings during the year ended December 31, 2017. As of December 31, 2016, the Company recognized credit-related losses of \$0.73 million on one Non-Agency RMBS for the year then ended.

Non-Agency RMBS on which OTTI is recognized have experienced, or are expected to experience, credit-related adverse cash flow changes, or credit impairment. The Company’s estimate of cash flows for its Non-Agency RMBS is based on its review of the underlying mortgage loans securing these RMBS. The Company considers information available about the structure of the securitization, including structural credit enhancement, if any, and the past and expected future performance of underlying mortgage loans, including timing of expected future cash flows, prepayment rates, default rates, loss severities, delinquency rates, percentage of non-performing loans, FICO scores at loan origination, year of origination, loan-to-value ratios, geographic concentrations, as well as Rating Agency reports, general market assessments, and dialogue with market participants. Significant judgment is used in both the Company’s analysis of the expected cash flows for its Non-Agency RMBS and any determination of OTTI that is the result, at least in part, of credit impairment.

The following table present the composition of OTTI charges recorded by the Company for the years ended December 31, 2017, 2016, and 2015:

	Year Ended December 31,		
	2017	2016	2015
Cumulative credit loss at beginning of period	\$(3,074,728)	\$(3,636,431)	—

## Additions:

Initial (increase) in credit reserves	—	(541,342	) (745,492	)
Subsequent (increase) in credit reserves	—	—	—	
Initial additional other-than-temporary credit impairment losses	—	(183,790	) (2,890,939)	
Subsequent additional other-than-temporary credit impairment losses	—	—	—	
Reductions:				
For securities sold decrease in credit reserves	—	1,286,835	—	
For securities sold decrease in other-than-temporary impairment	—	—	—	
Cumulative credit (loss) at end of period		\$(3,074,728)	\$(3,074,728)	(3,636,431)

The Company did not record any unrealized losses on legacy Non-Agency RMBS during the years ended December 31, 2017 and December 31, 2016, however, the Company did incur unrealized losses of \$1.8 million during the year ended December 31, 2015.

The following table presents the components comprising the carrying value of AFS securities not deemed to be other than temporarily impaired by length of time the securities had an unrealized loss position as of December 31, 2017, and December 31, 2016. At December 31, 2017 the Company held 59 AFS securities, of which 49 were in an unrealized loss position for less than twelve consecutive months and five were in an unrealized loss for more than twelve months. All of these securities were either Agency RMBS or Multi-Family MBS. As such, credit-related adverse cash flow changes are not applicable and consequently no OTTI is recognized. At December 31, 2016, the Company held 46 AFS securities, of which 31 were in an unrealized loss position for less than twelve consecutive months and five were in an unrealized loss position for more than twelve months.

# FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2017

### NOTE 4 – AVAILABLE-FOR-SALE SECURITIES (Continued)

	Less than 12 months		Greater than 12 months		Total	
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
December 31, 2017	\$1,084,010,586	\$(11,135,736)	\$95,024,791	\$(2,233,516)	\$1,179,035,377	\$(13,369,252)
December 31, 2016	\$619,414,077	\$(8,129,704)	\$45,879,433	\$(2,110,684)	\$665,293,510	\$(10,240,388)

To the extent the Company determines there are likely to be decreases in cash flows expected to be collected, and as a result of non-credit impairment, such changes are generally recognized prospectively through adjustment of the security's yield over its remaining life.

The following table presents a summary of the Company's net realized gain (loss) from the sale of AFS securities, inclusive of securities previously booked as linked, for the years ended December 2017, December 2016, and December 2015.

	December 31, 2017	December 31, 2016	December 31, 2015
AFS securities sold, at cost	\$509,084,520	\$268,849,640	\$267,741,325
AFS principal payments, at cost	—	98,166,335	70,836,624
Proceeds from AFS securities sold	495,030,356	263,143,871	267,567,905
Proceeds from AFS principal payments	—	96,655,967	70,476,212
Net realized gain (loss) on sale of AFS securities	\$(14,054,164)	\$(7,216,137)	\$(533,832)

The following tables present the fair value of AFS investment securities by rate type as of December 31, 2017 and December 31, 2016:

	December 31, 2017			
	Agency	Non-Agency	Multi-Family	Total
Adjustable rate	\$1,284,237,670	\$—	\$—	\$1,284,237,670
Fixed rate	845,978	—	5,742,000	6,587,978
Total	\$1,285,083,648	\$—	\$5,742,000	\$1,290,825,648

	December 31, 2016			
	Agency	Non-Agency	Multi-Family	Total
Adjustable rate	\$788,727,476	\$7,592,802	\$—	\$796,320,278
Fixed rate	1,462,757	—	73,146,566	74,609,323
Total	\$790,190,233	\$7,592,802	\$73,146,566	\$870,929,601

The following tables present the fair value of AFS investment securities by maturity date as December 31, 2017 and December 31, 2016:

	December 31, 2017	December 31, 2016
Less than one year	\$—	\$—
Greater than one year and less than five years	1,187,909,353	399,872,894
Greater than or equal to five years	102,916,295	471,056,707
Total	\$1,290,825,648	\$870,929,601

As described in Note 2, when the Company purchases a credit-sensitive AFS security at a significant discount to its face value, the Company generally does not amortize into income a significant portion of this discount that the Company is entitled to earn because it does not expect to collect it due to the inherent credit risk of the security. The Company may also record an OTTI for a portion of its investment in the security to the extent the Company believes that the amortized cost will exceed the present value of expected future cash flows. The amount of principal that the Company does not amortize into income is designated as an off balance sheet credit reserve on the security, with unamortized net discounts or premiums amortized into income over time to the extent realizable.

Actual maturities of AFS securities are affected by the contractual lives of the associated mortgage collateral, periodic payments of principal, and prepayments of principal. Therefore, actual maturities of available-for-sale securities are generally shorter than stated contractual maturities. Stated contractual maturities are generally greater than ten years.

The following tables present the changes for the year ended December 31, 2017 and the year ended December 31, 2016 of the unamortized net discount and designated credit reserves on the Company's MBS.

## FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2017

## NOTE 4 – AVAILABLE-FOR-SALE SECURITIES (Continued)

	December 31, 2017		
	Designated credit reserve	Unamortized net discount	Total
Beginning Balance as of January 1, 2017	\$(1,929,833)	\$(27,841,262)	\$(29,771,095)
Acquisitions	—	—	—
Dispositions	1,929,833	22,685,756	24,615,589
Accretion of net discount	—	2,950,944	2,950,944
Realized gain on paydowns	—	—	—
Realized credit losses	—	—	—
Addition to credit reserves	—	—	—
Release of credit reserves	—	—	—
Ending Balance at December 31, 2017	\$—	\$(2,204,562 )	\$(2,204,562 )

	December 31, 2016		
	Designated credit reserve	Unamortized net discount	Total
Beginning Balance as of January 1, 2016	\$(8,891,565)	\$(57,280,275)	\$(66,171,840)
Acquisitions	—	—	—
Dispositions	4,893,913	21,637,637	26,531,550
Accretion of net discount	—	6,703,365	6,703,365
Realized gain on paydowns	—	325,709	325,709
Realized credit losses	3,023,911	(183,790 )	2,840,121
Addition to credit reserves	(1,021,433 )	1,021,433	—
Release of credit reserves	65,341	(65,341 )	—
Ending Balance at December 31, 2016	\$(1,929,833)	\$(27,841,262)	\$(29,771,095)

Gains and losses from the sale of AFS securities are recorded within realized gain (loss) on sale of investments, net in the Company's consolidated statements of operations.

Unrealized gains and losses on the Company's AFS securities except Non-Agency RMBS IOs are recorded as unrealized gain (loss) on available-for-sale securities, net in the Company's consolidated statement of comprehensive income (loss). For the years ended December 31, 2017, December 31, 2016 and December 31, 2015 the Company had unrealized gains (losses) on AFS securities of (\$5,785,854), (8,872,859) and (\$7,604,122), respectively.

The following tables present components of interest income on the Company's AFS securities for the years December 31, 2017, December 31, 2016, December 31, 2015:

	Year Ended December 31, 2017		
	Coupon interest	Net (premium amortization)/ discount accretion	Interest income
Agency	\$28,003,938	\$(654,970 )	\$27,348,968

Edgar Filing: Five Oaks Investment Corp. - Form 10-K

Non-Agency	42,254	9,946	52,200
Multi-Family	—	2,120,725	2,120,725
Total	\$28,046,192	\$1,475,701	\$29,521,893

F-21

---

## FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2017

## NOTE 4 – AVAILABLE-FOR-SALE SECURITIES (Continued)

	Year Ended December 31, 2016		
	Coupon interest	Net (premium amortization)/ discount accretion	Interest income
Agency	\$ 13,138,828	\$ 341,020	\$ 13,479,848
Non-Agency	2,579,344	1,343,594	3,922,938
Multi-Family	1,006,106	5,066,873	6,072,979
Total	\$ 16,724,278	\$ 6,751,487	\$ 23,475,765

	Year Ended December 31, 2015		
	Coupon interest	Net (premium amortization)/ discount accretion	Interest income
Agency	\$ 7,286,166	\$ 241,550	\$ 7,527,716
Non-Agency	2,357,814	7,653,839	10,011,653
Multi-Family	1,443,326	5,315,461	6,758,787
Total	\$ 11,087,306	\$ 13,210,850	\$ 24,298,156

## NOTE 5 – MORTGAGE LOANS HELD-FOR-SALE, at FAIR VALUE

Mortgage loans held-for-sale consists of residential mortgage loans carried at fair value as a result of the fair value option. The following table presents the carrying value of the Company's mortgage loans held-for-sale as of December 31, 2017 and December 31, 2016:

	December 31, December 31,	
	2017	2016
Unpaid principal balance \$	—	\$ 2,867,263
Fair value adjustment —	(17,727)	)
Carrying value \$	—	\$ 2,849,536

The geographic concentrations of credit risk exceeding 5% of the total loan balances related to the mortgage loans held-for-sale as of December 31, 2017 and December 31, 2016 are as follows:

	December 31, December 31,	
	2017	2016
Texas	—	56.0 %
Kentucky	—	24.4 %
North Carolina	—	19.6 %





# FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2017

### NOTE 6 – THE FREMF TRUSTS

The Company has elected the fair value option on the assets and liabilities of the FREMF 2011-K13 Trust and the FREMF 2012-KF01 Trust, which requires that changes in valuations of the trusts be reflected in the Company's statements of operations. The Company's net investment in the trusts is limited to the Multi-Family MBS comprised of first loss PO securities and IO securities acquired by the Company in 2014 with an aggregate net carrying value of \$21,695,098 at December 31, 2017 and \$18,342,040 at December 31, 2016.

The consolidated balance sheets of the FREMF trusts at December 31, 2017 and December 31, 2016 are set out below:

Balance Sheets	December 31, 2017	December 31, 2016
Assets		
Multi-family mortgage loans held in securitization trusts	\$ 1,130,874,274	\$ 1,222,905,433
Receivables	4,377,606	4,617,642
Total assets	\$ 1,135,251,880	\$ 1,227,523,075
Liabilities and Equity		
Multi-family securitized debt obligations	\$ 1,109,204,743	\$ 1,204,583,678
Payables	4,352,039	4,597,357
	\$ 1,113,556,782	\$ 1,209,181,035
Equity	21,695,098	18,342,040
Total liabilities and equity	\$ 1,135,251,880	\$ 1,227,523,075

The multi-family mortgage loans held in securitization trusts had an unpaid principal balance of \$1,078,622,737 at December 31, 2017 and \$1,147,753,367 at December 31, 2016. The multi-family securitized debt obligations had an unpaid principal balance of \$1,078,622,737 at December 31, 2017 and \$1,147,753,367 at December 31, 2016.

The consolidated statements of operations of the FREMF trusts for the years ended December 31, 2017, December 31, 2016 and December 31, 2015 are set out below:

Statements of Operations	December 31, 2017	December 31, 2016	December 31, 2015
Interest income	\$ 54,271,017	\$ 58,587,780	\$ 68,016,595
Interest expense	51,440,694	54,940,386	62,157,176
Net interest income	\$ 2,830,323	\$ 3,647,394	\$ 5,859,419
General and administrative fees	(2,551,296 )	(2,711,189 )	(3,249,208 )
Unrealized gain (loss) on multi-family loans held in securitization trusts	3,353,365	(5,219,530 )	6,097,000
Net income (loss)	\$ 3,632,392	\$ (4,283,325 )	\$ 8,707,211

The geographic concentrations of credit risk exceeding 5% of the total loan balances related to the FREMF trusts as of December 31, 2017 and December 31, 2016 are as follows:

December 31, 2017	December 31, 2016
New York 16.5 %	Texas 17.9 %
Texas 14.2 %	New York 15.7 %
Washington 8.7 %	Washington 8.4 %

Colorado	7.8 %	Colorado	7.5 %
Georgia	5.7 %	Georgia	5.5 %

#### NOTE 7 – RESIDENTIAL MORTGAGE LOAN SECURITIZATION TRUSTS

The Company has elected the fair value option on the assets and liabilities of the CSMC 2014-OAK1 Trust, which requires that changes in valuations of the trust be reflected in the Company's statements of operations. The Company's net investment in the trust is limited to the Non-Agency RMBS comprised of subordinated and first loss securities, IO securities and excess servicing rights acquired by the Company in 2014 with an aggregate net carrying value of \$5,413,720 at December 31, 2017 and \$6,374,821 at December 31, 2016. The Company previously consolidated the assets and liabilities of the JPMMT 2014-OAK4 Trust, but based on the sale of subordinated and first loss securities during the second quarter of 2016, has determined that it is no longer the primary beneficiary of the trust, and accordingly no longer consolidates the assets and liabilities of this trust.

The consolidated balance sheets of the residential mortgage loan securitization trusts at December 31, 2017 and December 31, 2016 are set out below:

F-23

---

## FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2017

## NOTE 7 – RESIDENTIAL MORTGAGE LOAN SECURITIZATION TRUSTS (continued)

Balance Sheets	December 31, 2017	December 31, 2016
Assets		
Residential mortgage loans held in securitization trusts	\$ 119,756,455	\$ 141,126,720
Receivables	396,000	471,146
Total assets	\$ 120,152,455	\$ 141,597,866
Liabilities and Equity		
Residential securitized debt obligations	\$ 114,418,318	\$ 134,846,348
Payables	320,417	376,697
	\$ 114,738,735	\$ 135,223,045
Equity	5,413,720	6,374,821
Total liabilities and equity	\$ 120,152,455	\$ 141,597,866

The residential mortgage loans held in securitization trusts had an unpaid principal balance of \$118,884,113 at December 31, 2017 and \$140,690,705 at December 31, 2016. The residential mortgage loan securitized debt obligations had an unpaid principal balance of \$118,884,113 at December 31, 2017 and \$140,690,705 at December 31, 2016. As of March 31, 2016, the most recent quarterly reporting date prior to deconsolidation of the JPMMT 2014-OAK4 Trust, the residential mortgage loans held in the trust and the residential securitized debt obligations issued by the trust both had an unpaid principal balance of \$202,911,543.

The consolidated statements of operations of the residential mortgage loan securitization trusts for the years ended December 31, 2017, December 31, 2016 and December 31, 2015 are set out below:

Statements of Operations	December 31, 2017	December 31, 2016	December 31, 2015
Interest income	\$ 5,103,853	\$ 10,585,191	\$ 19,986,204
Interest expense	4,059,894	8,117,402	13,156,912
Net interest income	\$ 1,043,959	\$ 2,467,789	\$ 6,829,292
General and administrative fees	(44,976 )	(266,957 )	(635,547 )
Unrealized gain (loss) on residential mortgage loans held in securitization trusts	(961,100 )	404,720	(8,153,474 )
Net income (loss)	\$ 37,883	\$ 2,605,552	\$ (1,959,729 )

The geographic concentrations of credit risk exceeding 5% of the total loan balances related to the residential mortgage loan securitization trusts as at December 31, 2017 and December 31, 2016 are as follows:

	December 31, 2017		December 31, 2016	
California	37.0	%	37.6	%
Washington	15.3	%	15.4	%
Massachusetts	8.1	%	8.4	%
Florida	6.4	%	5.7	%

NOTE 8 – USE OF SPECIAL PURPOSE ENTITIES AND VARIABLE INTEREST ENTITIES

A Special Purpose Entity (“SPE”) is an entity designed to fulfill a specific limited purpose of the company that organized it, and a SPE is frequently used for the purpose of securitizing, or re-securitizing, financial assets. SPEs are typically structured as pass through entities that receive principal and interest on the underlying collateral and distribute those payments to certificate holders. As a consequence of their purpose and design, SPEs are typically VIEs.

As further discussed in Notes 2, 6 and 7, the Company has evaluated its investments in Multi-Family MBS and Non-Agency RMBS and has determined that they are VIEs. The Company has then undertaken an analysis of whether it is the primary beneficiary of any of these VIEs, and has determined that it is the primary beneficiary of the FREMF 2011-K13 Trust, FREMF 2012-KF01 Trust and CSMC 2014-OAK1 Trust. Accordingly, the Company consolidated the assets, liabilities, income and expenses of these trusts in its financial statements as of and for the periods ending December 31, 2017, December 31, 2016 and December 31, 2015. However, the assets of each of the trusts are restricted, and can only be used to fulfill the obligations of the respective trusts. Additionally, the obligations of each of the trusts do not have any recourse to the Company as the consolidator of the trusts. The Company has elected the fair value option in respect of the assets and liabilities of the trusts.

For the Company’s remaining Multi-Family and Non-Agency MBS investments that are VIEs, the Company has determined that it is not the primary beneficiary, and accordingly these investments are accounted for as further described in Notes 2, 6 and 7. As further described in Note 2, GAAP also requires the Company to consider whether securitizations the Company sponsors and other transfers of financial assets should be treated as sales or financings. During the year ended December 31, 2015, the Company transferred residential mortgage loans to Oaks Mortgage Trust Series 2015-1 and Oaks Mortgage Trust 2015-2, and accounted for these transfers as sales for financial reporting purposes, in accordance with ASC 860. The Company also determined that it was not the primary

# FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2016

### NOTE 8 – USE OF SPECIAL PURPOSE ENTITIES AND VARIABLE INTEREST ENTITIES (continued)

beneficiary of these VIEs because it lacked the power to direct the activities that will have the most significant economic impact on the entities. The Company no longer has an exposure to loss from these VIEs as they were sold during the first quarter of 2017.

### NOTE 9 – RESTRICTED CASH AND DUE TO BROKER

As of December 31, 2017, the Company is required to maintain certain cash balances with counterparties for broker activity and collateral for the Company's repurchase agreements in non-interest bearing accounts.

The following table presents the Company's restricted cash balances as of December 31, 2017 and December 31, 2016:

	December 31, 2017	December 31, 2016
Restricted cash balance held by:		
Broker counterparties for derivatives trading	\$(1,123,463 )	\$(4,244,678 )
Repurchase counterparties as restricted collateral	11,275,263	10,355,222
Total	\$10,151,800	\$6,110,544

### NOTE 10 – BORROWINGS

#### Repurchase Agreements

The Company has entered into repurchase agreements at December 31, 2017 to finance its portfolio of investments. The repurchase agreements bear interest at a contractually agreed rate. The repurchase obligations mature and typically reinvest every 30 days to one year and have a weighted average aggregate interest rate of 1.56% at December 31, 2017. Repurchase agreements are accounted for as secured borrowings since the Company maintains effective control of the financed assets. The following table summarizes certain characteristics of the Company's repurchase agreements at December 31, 2017 and December 31, 2016:

	December 31, 2017			December 31, 2016		
	Amount outstanding	Weighted average interest rate	Market value of collateral held	Amount outstanding	Weighted average interest rate	Market value of collateral held
Agency	\$1,228,349,000	1.55 %	\$1,285,083,649	\$755,221,000	0.97 %	\$790,190,232
Non-Agency	2,555,000	3.38 %	4,399,779	7,313,000	2.39 %	12,784,707
Multi-Family	3,618,000	3.16 %	5,742,000	42,277,000	2.52 %	73,146,566
Total	\$1,234,522,000	1.56 %	\$1,295,225,428	\$804,811,000	1.07 %	\$876,121,505

At December 31, 2017 and December 31, 2016, the repurchase agreements had the following remaining maturities:

	December 31, 2017	December 31, 2016
< or equal to 30 days	\$1,175,407,000	\$737,823,000

Edgar Filing: Five Oaks Investment Corp. - Form 10-K

31 to 60 days	56,560,000	19,897,000
61 to 90 days	2,555,000	47,091,000
Total	\$1,234,522,000	\$804,811,000

Under the repurchase agreements, the respective lender retains the right to mark the underlying collateral to fair value. A reduction in the value of pledged assets would require the Company to provide additional collateral or fund margin calls. In addition, the repurchase agreements are subject to certain financial covenants, the most restrictive of these covenants requires that, on the last day of any fiscal quarter, our total stockholders' equity shall not be less than the greater of (1) \$75,000,000 or (2) 50% of the highest stockholders' equity on the last day of the preceding eight fiscal quarters. The Company was in compliance with these covenants as of December 31, 2017 and December 31, 2016.

The following tables summarize certain characteristics of the Company's repurchase agreements at December 31, 2017 and December 31, 2016:

Repurchase Agreement Counterparties	December 31, 2017				Market Value of collateral held
	Amount Outstanding	Percent of total amount outstanding		Weighted average days to maturity	
North America	\$939,438,000	76.10	%	13	\$985,672,703
Asia <sup>(1)</sup>	292,529,000	23.70	%	14	305,152,946
Europe <sup>(1)</sup>	2,555,000	0.20	%	78	4,399,779
Total	\$1,234,522,000	100.00	%	13	\$1,295,225,428

(1) Counterparties domiciled in Europe and Asia, or their U.S. subsidiaries.

# FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2017

## NOTE 10 – BORROWINGS (Continued)

Repurchase Agreement Counterparties	December 31, 2016		Weighted average days to maturity	Market Value of collateral held
	Amount Outstanding	Percent of total amount outstanding		
Wells Fargo Securities	\$33,666,000	4.18 %	8	57,627,433
Other North America	703,788,000	87.46 %	16	742,690,286
Asia <sup>(1)</sup>	62,733,000	7.79 %	14	66,198,478
Europe <sup>(1)</sup>	4,624,000	0.57 %	44	9,605,308
Total	\$804,811,000	100.00 %	16	\$876,121,505

(1)Counterparties domiciled in Europe and Asia, or their U.S. subsidiaries.

## NOTE 11 – DERIVATIVE INSTRUMENTS HEDGING AND NON-HEDGING ACTIVITIES

The Company enters into a variety of derivative instruments in connection with its risk management activities. The Company's primary objective for executing these derivatives and non-derivative instruments is to mitigate the Company's economic exposure to future events that are outside its control. The Company's derivative financial instruments are utilized principally to manage market risk and cash flow volatility associated with interest rate risk (including associated prepayment risk) related to certain assets and liabilities. As part of its risk management activities, the Company may, at times, enter into various forward contracts, including short securities, Agency to-be-announced securities, or TBAs, options, futures, swaps, swaptions and caps. In executing on the Company's current risk management strategy, the Company has entered into interest rate swaps, swaption agreements, TBA's and futures contracts. Amounts receivable and payable under interest rate swap agreements are accounted for as unrealized gain (loss) on derivative contracts, net in the consolidated statement of operations. Premiums on swaptions are amortized on a straight line basis between trade date and expiration date and are recognized in the consolidated statement of operations as a realized loss on derivative contracts.

The following summarizes the Company's significant asset and liability derivatives, the risk exposure for these derivatives and the Company's risk management activities used to mitigate certain of these risks. While the Company uses derivative instruments to achieve the Company's risk management activities, it is possible that these instruments will not effectively mitigate all or a substantial portion of the Company's market rate risk. In addition, the Company might elect, at times, not to enter into certain hedging arrangements in order to maintain compliance with REIT requirements.

### Balance Sheet Presentation

The following tables present the gross fair value and notional amounts of the Company's derivative financial instruments as of December 31, 2017 and December 31, 2016.

December 31, 2017				
Derivative Assets		Derivative Liabilities		
Contracts	Fair value	Notional	Contracts	Notional

				Fair value	
Eurodollar Futures	14,355	5,349,613	14,355,000,000	—	—
Total	14,355	\$5,349,613	14,355,000,000	—	\$ —

December 31, 2016

Derivative Assets			Derivative Liabilities		
	Contract	Fair value	Notional	Contract	Fair value
Eurodollar Futures	10,501	8,053,813	10,501,000,000	—	—
Total	10,501	\$8,053,813	10,501,000,000	—	\$ —

#### Offsetting of Financial Assets and Liabilities

The Company's repurchase agreements are governed by underlying agreements that provide for a right of setoff in the event of default of either counterparty to the agreement. The Company also has in place with its counterparties ISDA Master Agreements ("Master Agreements") for its derivative contracts. In accordance with the Master Agreements with each counterparty, if on any date amounts would otherwise be payable in the same currency and in respect of the same transaction by each party to the other, then, on such date, each party's obligation to make payment of any such amount will be automatically satisfied and discharged and, if the aggregate amount that would otherwise have been payable by one party exceeds the aggregate amount that would otherwise have been payable by the other party, is replaced by an obligation upon the party by whom the larger aggregate amount would have been payable to pay to the other party the excess of the larger aggregate amount over the smaller aggregate amount. The Company has pledged financial collateral as restricted cash to its counterparties for its derivative contracts and repurchase agreements. See Note 2 for specific details on the terms of restricted cash with counterparties and Note 9 for the amounts of restricted cash outstanding.



## FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2017

## NOTE 11 – DERIVATIVE INSTRUMENTS HEDGING AND NON-HEDGING ACTIVITIES (Continued)

Under GAAP, if the Company has a valid right of setoff, it may offset the related asset and liability and report the net amount. The Company presents repurchase agreements subject to Master Agreements or similar agreements on a gross basis, and derivative assets and liabilities subject to such arrangements on a net basis, based on derivative type and counterparty, in its consolidated balance sheets. Separately, the company presents cash collateral subject to such arrangements on a net basis, based on counterparty, in its consolidated balance sheets. However, the Company does not offset financial assets and liabilities with the associated cash collateral on its consolidated balance sheets.

The below tables provide a reconciliation of these assets and liabilities that are subject to Master Agreements or similar agreements and can be potentially offset on the Company's consolidated balance sheets as of December 31, 2017 and December 31, 2016:

December 31, 2017					
Description of	Gross amounts of recognized assets	Gross amounts offset in the Balance Sheet	Net amounts of assets presented in the Balance Sheet	Gross amounts not offset in the Balance Sheet	
				Financial instruments	Net amount
				Cash collateral (Received)/ Pledged	
Futures	\$5,349,613	\$	—\$5,349,613	\$ —	—\$5,349,613
Total	\$5,349,613	\$	—\$5,349,613	\$ —	—\$5,349,613

December 31, 2016					
Description of	Gross amounts of recognized assets	Gross amounts offset in the Balance Sheet	Net amounts of assets presented in the Balance Sheet	Gross amounts not offset in the Balance Sheet	
				Financial instruments	Net amount
				Cash collateral (Received)/ Pledged	
Futures	\$8,053,813	\$	—\$8,053,813	\$ —	—\$8,053,813
Total	\$8,053,813	\$	—\$8,053,813	\$ —	—\$8,053,813

December 31, 2017

Gross amounts not offset

Edgar Filing: Five Oaks Investment Corp. - Form 10-K

Description	Gross amounts of recognized liabilities	Gross amounts offset in the Balance Sheet		Net amounts of liabilities presented in the Balance Sheet		Cash collateral (received)/Pledged		Net amount
		in the Balance Sheet	of liabilities presented in the Balance Sheet	Financial instruments	Cash collateral (received)/Pledged	Net amount		
Repurchase agreements	\$(1,234,522,000)	\$	—	\$(1,234,522,000)	\$	—	\$	—\$(1,234,522,000)
Total	\$(1,234,522,000)	\$	—	\$(1,234,522,000)	\$	—	\$	—\$(1,234,522,000)
December 31, 2016								

Description	Gross amounts of recognized liabilities	Gross amounts offset in the Balance Sheet		Net amounts of liabilities presented in the Balance Sheet		Cash collateral (received)/Pledged		Net amount
		in the Balance Sheet	of liabilities presented in the Balance Sheet	Financial instruments	Cash collateral (received)/Pledged	Net amount		
Repurchase agreements	\$(804,811,000)	\$	—	\$(804,811,000)	\$	—	\$	—\$(804,811,000)
Total	\$(804,811,000)	\$	—	\$(804,811,000)	\$	—	\$	—\$(804,811,000)

#### Income Statement Presentation

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

The following table summarizes the underlying hedged risks and the amount of gains and losses on derivative instruments reported net in the consolidated statement of operations as realized gain (loss) on derivative contracts, net and unrealized gain (loss) on derivative contracts, net for the years ended December 31, 2017, December 31, 2016, and December 31, 2015:

## FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2017

## NOTE 11 – DERIVATIVE INSTRUMENTS HEDGING AND NON-HEDGING ACTIVITIES (Continued)

Year Ended December 31, 2017			
Primary underlying risk	Amount of realized gain (loss)	Amount of unrealized appreciation (depreciation)	Total
Interest rate:			
Futures	2,219,719	(2,704,413 )	(484,694 )
Total	\$2,219,719	\$ (2,704,413 )	\$ (484,694)
Year Ended December 31, 2016			
Primary underlying risk	Amount of realized gain (loss)	Amount of unrealized appreciation (depreciation)	Total
Interest rate:			
Futures	(3,089,001 )	5,495,463	2,406,462
Total	\$(3,089,001)	\$ 5,495,463	\$2,406,462
Year Ended December 31, 2015			
Primary underlying risk	Amount of realized gain (loss)	Amount of unrealized appreciation (depreciation)	Total
Interest rate:			
Interest rate swaps <sup>(1)</sup>	\$(7,047,875 )	\$ 1,755,108	\$(5,292,767)
Swaptions	(84,000 )	62,450	(21,550 )
Futures	(4,892,855 )	3,092,300	(1,800,555 )
Total	\$(12,024,730)	\$ 4,909,858	\$(7,114,872)

(1) In the year ended December 31, 2015, net swap interest expense totaled \$2,216,417 comprised of \$2,719,563 in interest expense paid (included in realized gain (loss)) and \$503,146 in accrued interest income (included in unrealized gain (loss)).

## NOTE 12 - MSRs

As of December 31, 2017, the Company retained the servicing rights associated with an aggregate principal balance of \$338,167,569 of residential mortgage loans that the Company had previously transferred to three residential mortgage loan securitization trusts. The Company's MSRs are held and managed at the Company's TRS, and the Company employs one or more licensed sub-servicers to perform the related servicing activities. To the extent that the Company determines it is the primary beneficiary of a residential mortgage loan securitization trust into which it has sold loans, any associated MSRs are eliminated on the consolidation of the trust. The trust is contractually obligated to pay a portion of the interest payments from the associated residential mortgage loans for the direct servicing of the loans, and after deduction of sub-servicing fees payable to contracted sub-servicers, the net amount, excess servicing rights, represents a liability of the trust. Upon consolidation of the trust, the fair value of the excess servicing rights is equal to the related MSRs held at the Company's TRS. As a result of the Company's determination that it is not the primary

beneficiary of OAKS Mortgage Trust 2015-1 and OAKS Mortgage Trust 2015-2, it does not consolidate these trusts, and as a consequence, MSR associated with these trusts are recorded on the Company's consolidated balance sheet at December 31, 2017. In addition, the Company previously consolidated the assets and liabilities of the JPMMT 2014-OAK4 Trust, but based on the sale of subordinated and first loss securities during the second quarter of 2016, determined that it is no longer the primary beneficiary of the trust, and accordingly no longer consolidates its assets and liabilities. As a consequence, MSR associated with this trust are now recorded on the Company's consolidated balance sheet at December 31, 2017.

The following table presents the Company's MSR activity as of the years ended December 31, 2017 and December 31, 2016:

	December 31, 2017	December 31, 2016
Balance at beginning of year	\$3,440,809	\$4,268,673
MSRs retained from sales to securitizations	10,910	—
MSRs related to deconsolidation of securitization trust	—	364,163
Changes in fair value due to:		
Changes in valuation inputs or assumptions used in valuation model	39,688	(102,855 )
Other changes to fair value <sup>(1)</sup>	(527,546 )	(1,089,172 )
Balance at end of period	\$2,963,861	\$3,440,809
Loans associated with MSRs <sup>(2)</sup>	\$338,167,569	\$397,925,409
MSR values as percent of loans <sup>(3)</sup>	0.88	% 0.86 %

(1) Amounts represent changes due to realization of expected cash flows

(2) Amounts represent the principal balance of loans associated with MSRs outstanding at December 31, 2017 and December 31, 2016, respectively

# FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2017

### NOTE 12 – MSR<sub>s</sub> (continued)

- (3) Amounts represent the carrying value of MSR<sub>s</sub> at December 31, 2017 and December 31, 2016, respectively divided by the outstanding balance of the loans associated with these MSR<sub>s</sub>

The following table presents the components of servicing income recorded on the Company’s statements of operations for the years ended December 31, 2017, December 31, 2016 and December 31, 2015:

	Year Ended December 31, 2017	Year Ended December 31, 2016	Year Ended December 31, 2015
Servicing income, net	\$ 922,094	\$ 932,425	\$ 211,878
Income from MSR <sub>s</sub> , net	\$ 922,094	\$ 932,425	\$ 211,878

### NOTE 13 – FINANCIAL INSTRUMENTS

GAAP defines fair value and provides a consistent framework for measuring fair value under GAAP. ASC 820 “Fair Value Measurement” expands fair value financial statement disclosure requirements. ASC 820 does not require any new fair value measurements and only applies to accounting pronouncements that already require or permit fair value measures, except for standards that relate to share-based payments.

Valuation techniques are based on observable and unobservable inputs. Observable inputs reflect readily obtainable data from independent sources, while unobservable inputs reflect the Company’s market assumptions. The three levels are defined as follows:

Level 1 Inputs – Quoted prices for identical instruments in active markets.

Level 2 Inputs – Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable.

Level 3 Inputs – Instruments with primarily unobservable value drivers.

The following tables summarize the valuation of the Company’s assets and liabilities at fair value within the fair value hierarchy levels as of December 31, 2017 and December 31, 2016:

	December 31, 2017			Balance as of December 31, 2017
	Quoted prices in active markets for identical assets Level 1	Significant other observable inputs Level 2	Unobservable inputs Level 3	
Assets:				
Residential mortgage-backed securities (a)	\$—	\$ 1,290,825,648	\$ —	\$ 1,290,825,648
Residential mortgage loans	—	—	—	—
Multi-Family mortgage loans held in securitization trusts	—	1,130,874,274	—	1,130,874,274

Edgar Filing: Five Oaks Investment Corp. - Form 10-K

Residential mortgage loans held in securitization trusts	—	119,756,455	—	119,756,455
Mortgage servicing rights	—	—	2,963,861	2,963,861
Futures	5,349,613	—	—	5,349,613
Total	\$5,349,613	\$2,541,456,377	\$ 2,963,861	\$2,549,769,851
Liabilities:				
Multi-family securitized debt obligations	\$—	\$(1,109,204,743)	\$ —	\$(1,109,204,743)
Residential securitized debt obligations	—	(114,418,318 )	—	(114,418,318 )
Total	\$—	\$(1,223,623,061)	\$ —	\$(1,223,623,061)

F-29

---

## FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2017

## NOTE 13 – FINANCIAL INSTRUMENTS (continued)

	December 31, 2016			Balance as of
	Quoted prices in active markets for identical assets Level 1	Significant other observable inputs Level 2	Unobservable inputs Level 3	December 31, 2016
Assets:				
Residential mortgage-backed securities (a)	\$—	\$870,929,601	\$—	\$870,929,601
Residential mortgage loans	—	2,849,536	—	2,849,536
Multi-Family mortgage loans held in securitization trusts	—	1,222,905,433	—	1,222,905,433
Residential mortgage loans held in securitization trusts	—	141,126,720	—	141,126,720
Mortgage servicing rights	—	—	3,440,809	3,440,809
Futures	8,053,813	—	—	8,053,813
Total	\$8,053,813	\$2,237,811,290	\$3,440,809	\$2,249,305,912
Liabilities:				
Multi-family securitized debt obligations	\$—	\$(1,204,583,678)	\$—	\$(1,204,583,678)
Residential securitized debt obligations	—	(134,846,348)	—	(134,846,348)
Total	\$—	\$(1,339,430,026)	\$—	\$(1,339,430,026)

(a) For more detail about the fair value of the Company's MBS, see Note 3 and Note 4.

During the years ended December 31, 2017 and December 31, 2016, the Company did not have any transfers between any of the levels of the fair value hierarchy. Transfers between levels are deemed to take place on the last day of the reporting period in which the transfer takes place.

As of December 31, 2017 and December 31, 2016, the Company had \$2,963,861 and \$3,440,809, respectively, in Level 3 assets. The Company's Level 3 assets are comprised of MSRs. Accordingly, for more detail about Level 3 assets, also see Note 12.

The following table provides quantitative information about the significant unobservable inputs used in the fair value measurement of the Company's MSRs classified as Level 3 fair value assets at December 31, 2017 and December 31, 2016:

As of December 31, 2017

Valuation Technique	Unobservable Input	Range	Weighted Average
Discounted cash flow	Constant prepayment rate	8.0 - 25.4%	12.8 %
	Discount rate	12.0	% 12.0 %

As of December 31, 2016

Valuation Technique	Unobservable Input	Range	Weighted Average
Discounted cash flow	Constant prepayment rate	8.0 - 26.5%	13.7 %
	Discount rate	12.0	% 12.0 %

## NOTE 14 – RELATED PARTY TRANSACTIONS

## Management Fee

The Company is externally managed and advised by the Manager. Pursuant to the terms of the management agreement in effect for the year ended December 31, 2017, the Company paid the Manager a management fee equal to 1.5% per annum, calculated and payable monthly in arrears. For purposes of calculating the management fee, the Company's stockholders' equity means the sum of the net proceeds from all issuances of the Company's equity securities since inception (allocated on a pro rata daily basis for such issuances during the fiscal quarter of any such issuance), plus the Company's retained earnings at the end of the most recently completed calendar quarter (without taking into account any non-cash equity compensation expense incurred in current or prior periods), less any amount that the Company pays for repurchases of the Company's common stock since inception, and excluding any unrealized gains, losses or other items that do not affect realized net income (regardless of whether such items are included in other comprehensive income or loss, or in net income). This amount is adjusted to exclude one-time events pursuant to changes in GAAP and certain non-cash items after discussions between the Manager and the Company's independent directors and approval by a majority of the Company's independent directors. To the extent asset impairment reduces the Company's retained earnings at the end of any completed calendar quarter, it will reduce the management fee for such quarter. The Company's stockholders' equity for the purposes of calculating the management fee could be greater than the amount of stockholders' equity shown on the financial statements. The initial term of the management agreement expired on May 16, 2014, but there have continued to be automatic, one-year renewals at the end of the initial term and each year thereafter. On January 18, 2018 the management agreement in effect for the year ended December 31, 2017 was terminated, and a new agreement with Hunt Investment Management, LLC became effective. Pursuant to the terms of the new management contract, we are required to pay our Manager an annual base management fee of 1.50% of Stockholders' Equity (as defined in the management agreement), payable quarterly (0.375% per quarter) in arrears. The definition of stockholders' equity in the new management agreement



FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2017

NOTE 14 – RELATED PARTY TRANSACTIONS (Continued)

is materially unchanged from the definition in our prior management agreement. Additionally, starting in the first full calendar quarter following January 18, 2019, we are also required to pay our Manager a quarterly incentive fee equal to 20% of the excess of Core Earnings (as defined in the management agreement) over a hurdle rate of 8% per annum.

On June 7, 2017, the Company's prior Manager agreed to waive a portion equal to 0.75% of its 1.50% management fee on the net proceeds of the June 16, 2017 common stock offering, beginning with the payment due for the month of June 2017. The net amount of management fee waived through the period ended December 31, 2017 is \$79,415.

For the year ended December 31, 2017, the Company incurred management fees of \$2,215,050 (2016: \$2,472,353; 2015: \$2,774,432), included in Management Fee in the consolidated statement of operations, of which \$182,000 (2016: \$400,000) was accrued but had not been paid, included in fees and expenses payable to Manager in the consolidated balance sheets.

Expense Reimbursement

Pursuant to the management agreement, the Company is required to reimburse the Manager for operating expenses related to the Company incurred by the Manager, including accounting services, auditing and tax services, technology and office facilities, operations, compliance, legal and filing fees, and miscellaneous general and administrative costs, including the cost of non-investment management personnel of the Manager who spend all or a portion of their time managing the Company's affairs.

On August 7, 2017, we received a commitment letter ("the Commitment Letter") from Oak Circle. The Commitment Letter provided that in furtherance of dialogues between our Board of Directors and Oak Circle to seek additional economies in the expenses for which Oak Circle may seek reimbursement from us pursuant to our Management Agreement, pursuant to the Commitment Letter Oak Circle represents, covenants and commits to us in respect of the 12-month period commencing October 1, 2017, Oak Circle will not seek reimbursement for, and we shall not be obligated to reimburse Oak Circle, for any non-investment management professional compensation-related expenses pursuant to Section 8(a) of the Management Agreement in excess of \$2,000,000 unless otherwise agreed upon by our Board of Directors. On January 18, 2018 the management agreement in effect for the year ended December 31, 2017 was terminated, and a new agreement with Hunt Investment Management, LLC became effective. Pursuant to the terms of the new management agreement, our Manager has agreed upon certain limitations on manager expense reimbursement from us.

For the year ended December 31, 2017, the Company incurred reimbursable expenses of \$4,127,549 (2016: \$4,747,275; 2015: \$4,980,348) included in operating expenses reimbursable to Manager in the consolidated statement of operations, of which \$570,000 (2016: \$480,000) was accrued but had not yet been paid, included in fees and expenses payable to Manager in the consolidated balance sheets.

Fulfillment and Securitization Fees

During 2015, the Company's Manager accrued fees pursuant to Section 8(b) of the management agreement in addition to the Management Fee for services rendered in connection to FOAC's aggregation of loans and subsequent contribution of these and certain other loans into the OAKS 2015-1 Trust and OAKS 2015-2 Trust. All of the invoices for such fees were approved by the Company's Audit Committee pursuant to the Company's related party transaction policies. There were no fees accrued during 2017 (2016: \$0; 2015: \$200,000) and no fees payable at December 31,

2017 (2016: \$0).

### Manager Equity Plan

The Company has adopted a Manager Equity Plan under which the Company may compensate the Manager and the Company's independent directors or consultants, or officers whom it may employ in the future. In turn, the Manager, in its sole discretion, grants such awards to its directors, officers, employees or consultants. The Company will be able to issue under the Manager Equity Plan up to 3.0% of the total number of issued and outstanding shares of common stock (on a fully diluted basis) at the time of each award.

Stock based compensation arrangements may include incentive stock options and non-qualified stock options, stock appreciation rights, restricted stock, restricted stock units, unrestricted stock awards and other awards based on the Company's common stock.

The following table summarizes the activity related to restricted common stock for the years December 31, 2017 and 2016:

	Year Ended December 31,			
	2017		2016	
	Shares	Weighted Average Grant Date Fair Market Value	Shares	Weighted Average Grant Date Fair Market Value
Outstanding Unvested Shares at Beginning of Period	4,500	\$ 5.97	15,500	\$ 12.79
Granted	4,500	4.33	4,500	5.97
Vested	(4,500)	5.97	(15,500)	12.79
Outstanding Unvested Shares at End of Period	4,500	\$ 4.33	4,500	\$ 5.97

For the year ended December 31, 2017, the Company recognized compensation expense related to restricted common stock of \$20,585 (2016: \$35,785; 2015: \$63,275). The Company has unrecognized compensation expense of \$15,535 as of December 31, 2017 (2016: \$16,634; 2015: \$46,405) for unvested shares of restricted common stock. As of December 31, 2017, the weighted average period for which the unrecognized compensation expense will be recognized is 9.7 months.

FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2017

NOTE 14 – RELATED PARTY TRANSACTIONS (Continued)

MAXEX LLC

The Company's lead independent director is also an independent director of an entity, MAXEX LLC ("MAXEX"), with which the Company has a commercial business relationship. The objective of MAXEX, together with its subsidiaries, is to create a whole loan mortgage trading platform which encompasses a centralized counterparty with a standardized purchase and sale contract and an independent dispute resolution process. As of December 31, 2016, the Company had sold \$22.5 million of residential mortgage loans to a third party buyer that were effected through MAXEX, for which the Company did not receive compensation other than receipt of loan sale proceeds from the third party; the Company has sold an additional \$2.1 million in loans through MAXEX in 2017. For the year ended December 31, 2017, the Company has received \$64,976 (2016: 209,088) in fees, net of \$15,156 (2016: 44,354) in marketing services fees paid to MAXEX, relating to its provision to MAXEX of seller eligibility review and backstop services. These fees are recorded on the Company's consolidated balance sheet as a liability in the line item "Deferred Income". See Note 15 for additional disclosure relating to the backstop services.

NOTE 15 – GUARANTEES

The Company, through FOAC, is party to customary and standard loan repurchase obligations in respect of residential mortgage loans that it has sold into securitizations or to third parties, to the extent it is determined that there has been a breach of standard seller representations and warranties in respect of such loans. To date, the Company has not been required to repurchase any loan due to a claim of breached seller reps and warranties.

In July 2016, the Company announced that it would no longer aggregate and securitize residential mortgage loans; however, given FOAC's extensive experience understanding and analyzing seller representation and warranty risk, the Company has sought to capitalize on its infrastructure and knowledge to become the provider of seller eligibility review and backstop services to MAXEX. See Note 14 for a further description of MAXEX. MAXEX's wholly owned clearinghouse subsidiary, Central Clearing and Settlement LLC ("CCAS") functions as the central counterparty with which buyers and sellers transact, and acts as the buyer's counterparty for each transaction. Pursuant to a Master Agreement dated June 15, 2016, as amended August 29, 2016 and January 30, 2017, among MAXEX, CCAS and FOAC, FOAC provides seller eligibility review services under which it reviews, approves and monitors sellers that are to sell loans via CCAS. Once approved, and having signed the standardized loan sale contract, the seller then sells loan(s) to CCAS, and CCAS simultaneously sells loan(s) to the buyer on substantially the same terms including representations and warranties. To the extent that a seller approved by FOAC fails to honor its obligation to repurchase a loan based on an arbitration finding that it breached its representations and warranties, FOAC is obligated to backstop the seller's repurchase obligation. The term of the backstop guarantee is the earlier of the contractual maturity of the underlying mortgage, or its earlier repayment in full; however, the incidence of claims for breaches of representations and warranties over time is considered unlikely to occur more than five years from the sale of a mortgage.

The maximum potential amount of future payments that the Company could be required to make under the outstanding backstop guarantees, which represents the outstanding balance of all underlying mortgage loans sold by approved sellers to CCAS, was estimated to be \$629,278,629 as of December 31, 2017 and \$469,015,145 as of December 31, 2016. Amounts payable in excess of the outstanding principal of the related mortgage, for example any premium paid by the loan buyer or costs associated with collecting mortgage payments, are not currently estimable. Amounts that may become payable under the backstop guarantee are normally recoverable from the related seller, as

well as from any payments received on (or from the sale of property securing) the mortgage loan repurchased. Pursuant to the Master Agreement, FOAC is required to maintain minimum available liquidity equal to the greater of (i) \$5.0 million or (ii) 0.10% of the aggregate unpaid principal balance of loans backstopped by FOAC, either directly or through a credit support agreement acceptable by MAXEX. As of December 31, 2017, the Company was not aware of any circumstances expected to lead to the triggering of a backstop guarantee obligation. The Company assessed its backstop guarantee obligation as of December 31, 2017 in accordance with ASC 460, "Guarantees", and the carrying value of the liability was the unamortized portion of fees receivable in respect of the issuance of the guarantees. See Note 2 for more information on the Company's accounting policy with respect to guarantee fees receivable.

In addition, the Company enters into certain contracts that contain a variety of indemnification obligations, principally with the Manager, brokers and counterparties to repurchase agreements. The maximum potential future payment amount the Company could be required to pay under these indemnification obligations is unlimited. The Company has not incurred any costs to defend lawsuits or settle claims related to these indemnification obligations. As a result, the estimated fair value of these agreements is minimal. Accordingly, the Company recorded no liabilities for these agreements as of December 31, 2017.

## NOTE 16 – STOCKHOLDERS' EQUITY

### Ownership and Warrants

As a result of the May 2012 and March 2013 private offerings of common stock to XL Investments Ltd, an indirectly wholly owned subsidiary of XL Group Ltd, XL Investments Ltd owns a significant minority investment in the Company. Pursuant to the terms of the May 2012 private offering, the Company agreed to issue to XL Investments Ltd warrants to purchase the Company's common stock. The warrants were subsequently issued, effective as of September 29, 2012, and entitled XL Investments Ltd, commencing on July 25, 2013 (120 days following the closing of the Company's IPO) to purchase an aggregate of 3,125,000 shares of the Company's common stock at a per share exercise price equal to 105% of the \$15.00 IPO price, or \$15.75. Pursuant to the terms of the warrants and as a result of the deficiency dividend paid on December 27, 2016, the exercise price of the warrants was adjusted to \$13.11 per share of common stock, and the number of shares of common stock purchasable upon exercise of the warrants increased to 3,753,492. XL Global, Inc., a subsidiary of XL Group Ltd, holds a minority stake in the prior manager, Oak Circle. Pursuant to an agreement dated January 18, 2018, with affiliates of Hunt Companies, Inc., XL Investments agreed to terminate warrants to purchase 3,753,492 shares of common stock held by XL Investments.

### Common Stock

The Company has 450,000,000 authorized shares of common stock, par value \$0.01 per share, with 22,143,758 and 17,539,258 shares issued and outstanding as of December 31, 2017 and December 31, 2016, respectively.

On December 27, 2016 the Company paid a deficiency dividend in the amount of \$19,384,684, representing \$1.33 for each common share, payable in a combination of cash and stock with an aggregate payment of 20% of the deficiency dividend, or \$3,878,042, in cash and 80% of the deficiency dividend, or \$15,506,642, in stock. Pursuant to this deficiency dividend, the Company issued 2,936,864 shares of common stock for \$5.28 per share.

## FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2017

## NOTE 16 – STOCKHOLDERS' EQUITY (continued)

On June 16, 2017, the Company issued 4,600,000 shares of common stock, including the concurrent exercise of the underwriters' overallotment option, for \$4.60 per share. Net estimated proceeds to the Company were \$19.8 million.

## Stock Repurchase Program

On December 15, 2015, the Company's board of directors authorized a stock repurchase program (or the "Repurchase Program"), to repurchase up to \$10 million of the Company's outstanding common stock. Shares of the Company's common stock may be purchased in the open market, including through block purchases, or through privately negotiated transactions, or pursuant to any trading plan that may be adopted in accordance with Rule 10b 18(b)(1) of the Securities Exchange Act of 1934, as amended. The timing, manner, price and amount of any repurchases will be determined at the Company's discretion and the program may be suspended, terminated or modified at any time for any reason. Among other factors, the Company intends to only consider repurchasing shares of the Company's common stock when the purchase price is less than the Company's estimate of the Company's current net asset value per common share. Shares of common stock repurchased by the Company under the Repurchase Program, if any, will be canceled and, until reissued by the Company, will be deemed to be authorized but unissued shares of the Company's common stock. Through December 31, 2016, the Company had repurchased 126,856 shares of common stock at a weighted average share price of \$5.09. No share repurchases were made during the year ended December 31, 2017. As of December 31, 2017, \$9.4 million of common stock remained authorized for future share repurchase under the Repurchase Program.

## Preferred Stock

The Company has 50,000,000 authorized shares of preferred stock, par value \$0.01 per share, with 1,610,000 shares of 8.75% Series A Cumulative Redeemable Preferred Stock ("Series A Preferred Stock"), and liquidation preference of \$25.00 per share, issued and outstanding as of both December 31, 2017 and December 31, 2016. The Series A Preferred Stock is entitled to receive a dividend rate of 8.75% per year on the \$25 liquidation preference and is senior to the common stock with respect to distributions upon liquidation, dissolution or winding up. The Company declares quarterly and pays monthly dividends on the shares of the Series A Preferred Stock, in arrears, on the 27th day of each month to holders of record at the close of business on the 15th day of each month. No dividends may be paid on the Company's common stock unless full cumulative dividends have been paid on the preferred stock. The Company has paid full cumulative dividends on its preferred stock on a monthly basis since it was first issued in December 2013.

## Distributions to stockholders

For the 2017 taxable year to date, the Company has declared dividends to common stockholders totaling \$11,904,005, or \$0.60 per share. The following table presents cash dividends declared by the Company on its common stock for the year ended December 31, 2017:

Declaration Date	Record Date	Payment Date	Dividend Amount	Cash Dividend Per Weighted Average Share
December 27, 2016	January 17, 2017	January 30, 2017	\$876,963	\$0.04374
December 27, 2016	February 15, 2017	February 27, 2017	\$876,963	\$0.04374

Edgar Filing: Five Oaks Investment Corp. - Form 10-K

December 27, 2016	March 15, 2017	March 30, 2017	\$876,963	\$0.04374
March 16, 2017	April 17, 2017	April 27, 2017	\$876,963	\$0.04374
March 16, 2017	May 15, 2017	May 30, 2017	\$876,963	\$0.04374
March 16, 2017	June 15, 2017	June 29, 2017	\$876,963	\$0.04374
June 14, 2017	July 17, 2017	July 28, 2017	\$1,106,963	\$0.05522
June 14, 2017	August 15, 2017	August 30, 2017	\$1,106,963	\$0.05522
June 14, 2017	September 15, 2017	September 28, 2017	\$1,106,963	\$0.05522
September 15, 2017	October 16, 2017	October 30, 2017	\$1,106,963	\$0.05522
September 15, 2017	November 15, 2017	November 29, 2017	\$1,107,188	\$0.05523
September 15, 2017	December 15, 2017	December 28, 2017	\$1,107,188	\$0.05523

The following table presents cash dividends declared by the Company on its Series A Preferred Stock for the year ended December 31, 2017:

F-33

---

## FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2017

## NOTE 16 – STOCKHOLDERS' EQUITY (continued)

Declaration Date	Record Date	Payment Date	Dividend Amount	Cash Dividend Per Weighted Average Share
December 27, 2016	January 17, 2017	January 27, 2017	\$293,503	\$0.18230
December 27, 2016	February 15, 2017	February 27, 2017	\$293,503	\$0.18230
December 27, 2016	March 15, 2017	March 27, 2017	\$293,503	\$0.18230
March 16, 2017	April 17, 2017	April 27, 2017	\$293,503	\$0.18230
March 16, 2017	May 15, 2017	May 30, 2017	\$293,503	\$0.18230
March 16, 2017	June 15, 2017	June 27, 2017	\$293,503	\$0.18230
June 14, 2017	July 17, 2017	July 27, 2017	\$293,503	\$0.18230
June 14, 2017	August 15, 2017	August 28, 2017	\$293,503	\$0.18230
June 14, 2017	September 15, 2017	September 27, 2017	\$293,503	\$0.18230
September 15, 2017	October 16, 2017	October 27, 2017	\$293,503	\$0.18230
September 15, 2017	November 15, 2017	November 27, 2017	\$293,503	\$0.18230
September 15, 2017	December 15, 2017	December 27, 2017	\$293,503	\$0.18230

## NOTE 17 – EARNINGS PER SHARE

In accordance with ASC 260, outstanding instruments that contain rights to non-forfeitable dividends are considered participating securities. The Company is required to apply the two-class method or the treasury stock method of computing basic and diluted earnings per share when there are participating securities outstanding. The Company has determined that outstanding unvested restricted shares issued under the Manager Equity Plan are participating securities, and they are therefore included in the computation of basic and diluted earnings per share. The following tables provide additional disclosure regarding the computation for the years ended December 31, 2017, December 31, 2016 and December 31, 2015:

	Year Ended December 31, 2017		Year Ended December 31, 2016		Year Ended December 31, 2015	
Net income (loss)		\$4,706,961		\$(7,989,955)		\$450,479
Less dividends paid:						
Common stock	\$11,904,005		\$29,898,918		\$19,874,663	
Preferred stock	3,522,036		3,522,036		3,522,036	
		15,426,041		33,420,954		23,396,699
Undistributed earnings		\$(10,719,080)		\$(41,410,909)		\$(22,946,220)
	Unvested Share-Based Payment Awards	Common Stock	Unvested Share-Based Payment Awards	Common Stock	Unvested Share-Based Payment Awards	Common Stock
Distributed earnings	\$ 0.60	\$ 0.60	\$ 2.04	\$ 2.04	\$ 1.35	\$ 1.35
Undistributed earnings (deficit)	(0.54 )	(0.54 )	(2.83 )	(2.83 )	(1.56 )	(1.56 )
Total	\$ 0.06	\$ 0.06	\$ (0.79 )	\$ (0.79 )	\$ (0.21 )	\$ (0.21 )

No adjustment was required for the calculation of diluted earnings per share for the warrants described in Note 16 because the warrants' exercise price is greater than the average market price of the common shares for the period, and thereby anti-dilutive.

#### NOTE 18 – SEGMENT REPORTING

The Company invests in a portfolio comprised of MBS, residential mortgage loans, and other mortgage-related investments, and operates as a single reporting segment.

#### NOTE 19 – INCOME TAXES

Certain activities of the Company are conducted through a TRS, FOAC, which is therefore subject to tax as a corporation. Pursuant to ASC 740, deferred tax assets are reduced by a valuation allowance if, based on the weight of available evidence, it is more likely than not (a likelihood of more than 50%) that some portion or all of the deferred tax assets will not be realized.

#### Impacts of Tax Reform:

On December 22, 2017, the Tax Cut and Jobs Act (H.R. 1) (the "Tax Act") was signed into law. The Tax Act contains significant changes to corporate taxation, including the reduction of the corporate income tax rate to 21%. We have substantially completed our assessment of the effects of the Tax Act and we are able to



# FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2017

### NOTE 19 – INCOME TAXES (continued)

determine reasonable estimates for the impacts of the items specified below. We continue to monitor and analyze the application of the “tax act” to our business and continue to assess our provision for income taxes as future guidance is issued.

The key aspects of the Tax Act on our financial statements for the year ended December 31, 2017 were; (1) The federal statutory tax rate was reduced to 21%. In prior years, the Company valued its deferred tax asset at 34%. The related re-measurement of the deferred tax asset resulted in a reduction of \$364,000. This amount is fully offset by a corresponding reduction to the valuation allowance as discussed in the paragraph below, (2) Taxpayers that have existing AMT credit from previously paid AMT tax will be allowed to offset their regular tax liability for any future taxable year. Additionally, the AMT credit will be refundable for any taxable year beginning after December 31, 2017 and before January 1, 2022 in an amount equal to 50% of the excess of the AMT credit for the taxable year over the amount of the credit allowable for the year against regular tax liability. In tax year 2021, 100% of any remaining excess AMT credit will be refunded. As a result, the valuation allowance attributable to prior years AMT credit in the amount of \$12,000 is released and AMT credit accrued for the current year is recognized in the deferred tax asset.

The following table reconciles the Company’s TRS GAAP net income (loss) to taxable income (in thousands):

	Year Ended December 31,		
	2017	2016	2015
	(in	(in	(in
	thousands)	thousands)	thousands)
GAAP consolidated net income (loss) attributable to Five Oaks Investment Corp	4,707	(7,990	) 450
GAAP net loss (income) from REIT operations	(4,645)	6,654	(1,826 )
GAAP net income (loss) of taxable subsidiary	62	(1,336	) (1,376 )
Capitalized transaction fees	(41	) (41	) (41 )
Unrealized gain (loss)	639	1,964	2,041
Deferred income	19	204	—
Tax income (loss) of taxable subsidiary before utilization of net operating losses	679	791	624
Utilizations of net operating losses	(679	) (791	) (624 )
Net tax income of taxable subsidiaries	—	—	—

The following is a reconciliation of the statutory federal and state tax rates to the effective rates, for the years ended December 31, 2017, 2016 and 2015:

	Year Ended December 31,		
	2017	2016	2015
	(in	(in	(in
	thousands)	thousands)	thousands)
U.S. Federal Statutory Income Tax	1,601	(2,717	) 153
State Taxes	1	(53	) (54 )
REIT Income not subject to federal income tax	(1,579)	2,263	(621 )
Tax affect of U.S. corporate rate change	364	—	—
Valuation Allowance	(406	) 507	522
Total income tax provision (benefit)	(19	) —	—
Effective income tax rate	0.41	% —	% — %

The TRS has a deferred tax asset (liability), comprised of the following (in thousands):

	As of December 31, 2017	As of December 31, 2016
Accumulated net operating losses of TRS	337	758
Unrealized gain (loss)	251	127
Capitalized transaction costs	122	196
Deferred income	57	77
AMT Credit	19	12
Deferred tax asset	786	1,170
Valuation allowance	(767)	(1,170)
Net non-current deferred tax asset (liability)	19	—

F-35

---

FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2017

NOTE 19 – INCOME TAXES (continued)

We have provided a valuation allowance against our deferred tax asset, that results in no deferred asset at December 31, 2017, and 2016 except for refundable AMT credits as discussed above. The Company recorded a 100% valuation allowance related to the TRS net deferred tax asset because we believe it is more likely than not that the deferred tax asset will not be fully realized. The valuation allowance decreased by \$403,000 as a result of the decrease in statutory tax rates as discussed above. The realization of the deferred tax asset associated with net operating losses is dependent on projections of future taxable income, for which there is uncertainty when considering historic results and the nature of the business. Accordingly, no provision or benefit (current or deferred tax expense) for income taxes is reflected in the accompanying financial statements. At December 31, 2017, and 2016 the TRS had net operating loss carryforwards for federal income tax purposes of \$1.3 million and \$2.0 million, which are available to offset future taxable income and begin expiring in 2034. For state purposes, the Company is in the process of determining filing requirements, but anticipates materially all prior losses to be recognized.

The Company files income tax returns with the U.S. federal government and various states. The Company is subject to examinations for the prior three years. The Company has assessed its tax positions for all open years and concluded there are no material uncertain tax positions.

The Company declared and paid in the fourth quarter of 2016 a deficiency dividend relating to a determination of an inability to offset certain net gains on hedging transactions in 2013 against net capital losses on the sale of certain mortgage-backed securities. In connection with this declaration, the Company provisioned an amount of \$1.86 million in 2016 for interest charges expected to be paid to the IRS following the payment of the dividend. On March 8, 2017, the Company paid an amount of \$2.01 million to the IRS for interest charges related to the 2016 fourth quarter deficiency dividend. The amount paid exceeded the provision of \$1.86 million taken in 2016 due to timing of the payment and accordingly the Company recorded additional interest expense of \$0.15 million, which is included in "Other interest expense" in the Company's consolidated statements of operations. The first quarter 2017 payment of \$2.01 million is included in "cash paid for interest" in the Company's consolidated statements of cash flows.

NOTE 20 – SUBSEQUENT EVENT

On January 18, 2018, we announced a new strategic direction, and the entry into a new external management agreement with Hunt Investment Management, LLC, an affiliate of the Hunt Companies, Inc. ("Hunt") and the concurrent mutual termination of our management agreement with Oak Circle. Management by Hunt is expected to provide Five Oaks with a new strategic direction through the reallocation of capital into new investment opportunities focused in the commercial real estate mortgage space and direct access to Hunt's significant pipeline of transitional floating-rate multi-family and commercial real estate loans. Hunt and its affiliates have extensive experience in the origination, servicing, risk management and financing of this asset class and the floating-rate nature of the loans should reduce or eliminate the need for complex interest-rate hedging. The new management agreement is expected to better align our interests with those of our new manager through an incentive fee arrangement and agreed upon certain limitations on manager expense reimbursements from us. Pursuant to the terms of the termination agreement between Five Oaks and Oak Circle, the termination of the prior management agreement did not trigger, and Oak Circle was not paid, a termination fee by us. Hunt separately agreed to pay Oak Circle a negotiated payment in connection with the termination agreement.

In connection with the transaction, an affiliate of Hunt purchased 1,539,406 shares of our common stock in a private placement by, at a purchase price of \$4.77 per share resulting in an aggregate capital raise of \$7,342,967. In addition, an affiliate of Hunt also purchased 710,495 Five Oaks shares from our largest shareholder, XL Investments Ltd. ("XL

Investments"), for the same price per share. The purchase price per share represents a 56.9% premium over the Five Oaks common share price as of the closing on January 17, 2018. In connection with the acquisition of shares from XL Investments, XL Investments agreed to terminate all of its currently held Five Oaks warrants. After completion of these share purchases, Hunt and its affiliates own approximately 9.5% of Five Oaks outstanding common shares. Also in connection with the transaction, and is further described in Sections 10 hereof and in our Current Report on Form 8-K filed with the Securities and Exchange Commission on January 18, 2018, David Carroll resigned as a director, Chairman and CEO of the Company and the Five Oaks board appointed James C. ("Chris") Hunt as a director and Chairman of the board and named James P. Flynn as CEO of Five Oaks and Michael P. Larsen President of Five Oaks.

On March 16, 2018, we announced a change to the frequency of any dividends for our common stock. From and after the third quarter of 2018, dividends, if any, on our common stock will be paid on a quarterly basis, a change from previously being paid on a monthly basis. Dividends, if any, on our preferred stock will continue to be paid on a monthly basis.

#### NOTE 21 – QUARTERLY FINANCIAL DATA

The following table presents a comparative breakdown of our unaudited summary quarterly financial data for the immediately preceding eight quarters.

## FIVE OAKS INVESTMENT CORP. AND SUBSIDIARIES

## Notes to Consolidated Financial Statements

December 31, 2017

## NOTE 21 – QUARTERLY FINANCIAL DATA (continued)

	2017 Quarter Ended			
	March 31	June 30	September 30	December 31
Total interest income	\$22,191	\$ 21,595	\$ 22,627	\$ 22,720
Total interest expense	(16,408 )	(16,767 )	(17,881 )	(17,938 )
Net interest income	5,784	4,828	4,746	4,782
Other-than-temporary impairment	—	—	—	—
Other income (loss)	201	(3,989 )	(5,949 )	7,164
Total expenses	3,615	3,135	3,053	3,055
Net income (loss)	2,369	(2,297 )	(4,256 )	8,891
Net income (loss) attributable to common shareholders (basic and diluted)	1,489	(3,167 )	(5,137 )	8,000
Earnings (loss) per share:				
Net income (loss) attributable to common shareholders (basic and diluted)	1,489	(3,167 )	(5,137 )	8,000
Weighted average number of shares of common stock outstanding:	17,539,258	18,297,500	22,139,258	22,142,926
Basic and diluted income (loss) per share	0.08	(0.17 )	(0.23 )	0.36
	2016 Quarter Ended			
	March 31	June 30	September 30	December 31
Total interest income	\$24,617	\$ 23,610	\$ 22,733	\$ 22,162
Total interest expense	(18,857 )	(17,837 )	(16,580 )	(16,259 )
Net interest income	5,760	5,772	6,153	5,903
Other-than-temporary impairment	(21 )	(146 )	(558 )	—
Other income (loss)	(18,275 )	(5,838 )	(908 )	8,932
Total expenses	4,412	3,864	3,191	3,298
Net income (loss)	(16,948 )	(4,076 )	1,496	11,538
Net income (loss) attributable to common shareholders (basic and diluted)	(17,828 )	(4,947 )	616	10,647
Earnings (loss) per share:				
Net income (loss) attributable to common shareholders (basic and diluted)	(17,828 )	(4,947 )	616	10,647
Weighted average number of shares of common stock outstanding:	14,605,515	14,597,894	14,600,193	14,762,006
Basic and diluted income (loss) per share	(1.22 )	(0.34 )	0.04	0.72

Schedule IV – Mortgage Loans on  
Real Estate

Reconciliation

Beginning Balance	2,849,981
Additions during period	
Mortgage loans purchased	—
Other	—
Deductions during period	
Mortgage loans sold	(2,302,342)
Amortization	(547,639 )
Ending Balance	—

F-38