AG Mortgage Investment Trust, Inc.
Form 10-Q
November 05, 2013

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2013

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 001-35151

AG MORTGAGE INVESTMENT TRUST, INC.

Maryland	**27-5254382**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
245 Park Avenue, 26th Floor New York, New York	**10167**
(Address of Principal Executive Offices)	(Zip Code)

(212) 692-2000
(Registrant's Telephone Number, Including Area Code)

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

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

Indicate by check mark whether the registrant is a large accelerated filed, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated filer ¨ Accelerated filer x Non-Accelerated filer ¨ Smaller reporting company ¨ (Do not check if a smaller reporting company)

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

As of November 1, 2013, there were 28,378,219 outstanding shares of common stock of AG Mortgage Investment Trust, Inc.

AG MORTGAGE INVESTMENT TRUST, INC.
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PART I

ITEM 1. FINANCIAL STATEMENTS

AG Mortgage Investment Trust, Inc. and Subsidiaries
Consolidated Balance Sheets
(Unaudited)

	September 30, 2013	December 31, 2012
Assets		
Real estate securities, at fair value:		
Agency - $2,459,557,624 and $3,536,876,135 pledged as collateral, respectively	$ 2,747,032,252	$ 3,785,867,151
Non-Agency - $620,674,314 and $529,455,020 pledged as collateral, respectively	630,034,943	568,858,645
ABS - $87,730,723 and $33,937,097 pledged as collateral, respectively	99,344,323	33,937,097
CMBS - $64,669,711 and $148,307,262 pledged as collateral, respectively	64,669,711	148,365,887
Commercial loans receivable, at fair value	30,000,000	2,500,000
Investment in affiliates	16,114,596	-
Linked transactions, net, at fair value	51,085,912	45,122,824
Cash and cash equivalents	35,089,032	149,594,782
Restricted cash	15,431,616	9,130,000
Interest receivable	12,673,519	14,242,453
Receivable on unsettled trades - $99,664,974 and $0 pledged as collateral, respectively	106,233,394	96,310,999
Receivable under reverse repurchase agreements	50,125,000	-
Derivative assets, at fair value	31,970,483	-
Other assets	853,542	454,069
Due from broker	1,383,818	884,605
Total Assets	$ 3,892,042,141	$ 4,855,268,512
Liabilities		
Repurchase agreements	$ 2,965,095,409	$ 3,911,419,818
Obligation to return securities borrowed under reverse repurchase agreements, at fair value	50,025,781	-
Payable on unsettled trades	120,099,264	84,658,035
Interest payable	2,837,294	3,204,205
Derivative liabilities, at fair value	3,477,340	36,375,947
Dividend payable	17,017,528	18,540,667
Due to affiliates	4,168,756	3,910,065
Accrued expenses	1,100,043	806,853
Taxes payable	1,373,083	1,731,141
Due to broker	19,022,027	-
Total Liabilities	3,184,216,525	4,060,646,731
Stockholders' Equity		
Preferred stock - $0.01 par value; 50,000,000 shares authorized:		
8.25% Series A Cumulative Redeemable Preferred Stock, 2,070,000 shares issued and outstanding ($51,750,000 aggregate liquidation	49,920,772	49,920,772

preference) at September 30, 2013 and December 31, 2012				
8.00% Series B Cumulative Redeemable Preferred Stock, 4,600,000 shares issued and outstanding ($115,000,000 aggregate liquidation preference) at September 30, 2013 and December 31, 2012		111,293,233		111,293,233
Common stock, par value $0.01 per share; 450,000,000 shares of common stock authorized and 28,360,046 and 26,961,936 shares issued and outstanding at September 30, 2013 and December 31, 2012, respectively		283,601		269,620
Additional paid-in capital		585,511,504		552,067,681
Retained earnings (deficit)		(39,183,494)		81,070,475
		707,825,616		794,621,781
Total Liabilities & Equity	$	3,892,042,141	$	4,855,268,512

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

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AG Mortgage Investment Trust, Inc. and Subsidiaries
Consolidated Statements of Operations
(Unaudited)

	Three Months Ended September 30, 2013	Three Months Ended September 30, 2012	Nine Months Ended September 30, 2013	Nine Months Ended September 30, 2012
Net Interest Income				
Interest income	$ 33,278,284	$ 28,285,116	$ 114,163,747	$ 60,164,752
Interest expense	5,584,419	4,228,610	19,749,592	8,506,041
	27,693,865	24,056,506	94,414,155	51,658,711
Other Income				
Net realized gain/(loss)	(45,247,890)	4,105,323	(116,489,235)	14,087,123
Gain on linked transactions, net	2,060,270	6,688,111	6,558,879	13,492,268
Realized loss on periodic interest settlements of interest rate swaps, net	(9,123,233)	(2,471,590)	(21,205,353)	(6,061,954)
Unrealized gain/(loss) on real estate securities and loans, net	40,136,126	45,917,570	(60,668,593)	78,755,229
Unrealized gain/(loss) on derivative and other instruments, net	(5,779,945)	(13,371,486)	67,348,314	(26,793,133)
	(17,954,672)	40,867,928	(124,455,988)	73,479,533
Expenses				
Management fee to affiliate	2,523,547	1,657,701	8,195,890	3,903,378
Other operating expenses	2,819,431	1,653,547	7,780,385	3,227,786
Equity based compensation to affiliate	55,105	120,612	186,983	312,712
Excise tax	373,083	272,195	1,391,942	605,773
	5,771,166	3,704,055	17,555,200	8,049,649
Income/(loss) before provision for income taxes and equity in earnings from affiliate	3,968,027	61,220,379	(47,597,033)	117,088,595
Provision for income taxes	(122,979)	-	(2,778,758)	-
Equity in earnings from affiliate	2,155,471	-	1,911,830	-
Net Income/(Loss)	6,000,519	61,220,379	(48,463,961)	117,088,595
Dividends on preferred stock	3,367,354	790,100	10,102,062	790,100
Net Income/(Loss) Available to Common Stockholders	$ 2,633,165	$ 60,430,279	$ (58,566,023)	$ 116,298,495
Earnings/(Loss) Per Share of Common Stock				
Basic	$ 0.09	$ 3.13	$ (2.10)	$ 7.07
Diluted	$ 0.09	$ 3.10	$ (2.10)	$ 7.07
Weighted Average Number of Shares of Common Stock Outstanding				

Basic	28,359,937	19,336,154	27,906,946	16,439,100
Diluted	28,359,943	19,462,984	27,906,946	16,449,450
Dividends Declared per Share of Common Stock	$ 0.60	$ 0.77	$ 2.20	$ 2.17

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

AG Mortgage Investment Trust, Inc. and Subsidiaries
Consolidated Statements of Stockholders' Equity
(Unaudited)

	Common Stock Shares	Amount	8.25 % Series A Cumulative Redeemable Preferred Stock	8.00 % Series B Cumulative Redeemable Preferred Stock	Additional Paid-in Capital	Retained Earnings/(Deficit)	Total
Balance at January 1, 2012	10,009,958	$100,100	$-	$-	$198,228,694	$7,955,126	$206,283,920
Net proceeds from issuance of common stock	12,857,056	128,570	-	-	259,574,984	-	259,703,554
Net proceeds from issuance of preferred stock	-	-	49,919,633	111,302,268	-	-	161,221,901
Grant of restricted stock and amortization of equity based compensation	16,466	165	-	-	368,715	-	368,880
Common dividends declared	-	-	-	-	-	(39,666,700)	(39,666,700)
Preferred Series A dividends declared	-	-	-	-	-	(521,847)	(521,847)
Preferred Series B dividends declared	-	-	-	-	-	-	-
Net income	-	-	-	-	-	117,088,595	117,088,595
Balance at September 30, 2012	22,883,480	$228,835	$49,919,633	$111,302,268	$458,172,393	$84,855,174	$704,478,303
Balance at January 1, 2013	26,961,936	$269,620	$49,920,772	$111,293,233	$552,067,681	$81,070,475	$794,621,781
Net proceeds from issuance of common stock	1,381,739	13,817	-	-	33,162,471	-	33,176,288
	16,371	164	-	-	281,352	-	281,516

Grant of restricted stock and amortization of equity based compensation							
Common dividends declared	-	-	-	-	-	(61,687,946)	(61,687,946)
Preferred Series A dividends declared	-	-	-	-	-	(3,202,062)	(3,202,062)
Preferred Series B dividends declared	-	-	-	-	-	(6,900,000)	(6,900,000)
Net loss	-	-	-	-	-	(48,463,961)	(48,463,961)
Balance at September 30, 2013	28,360,046	$283,601	$49,920,772	$111,293,233	$585,511,504	$(39,183,494)	$707,825,616

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

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AG Mortgage Investment Trust, Inc. and Subsidiaries
Consolidated Statements of Cash Flows
(Unaudited)

	Nine Months Ended September 30, 2013	Nine Months Ended September 30, 2012
Cash Flows from Operating Activities		
Net income/(loss)	$ (48,463,961)	$ 117,088,595
Adjustments to reconcile net income/(loss) to net cash provided by operating activities:		
Net realized (gain)/loss	116,489,235	(14,087,123)
Net amortization of premium related to real estate securities	36,501,617	25,957,829
Unrealized (gains) from equity method investments	(1,286,037)	-
Unrealized (gains)/losses on linked transactions, net	3,898,885	(6,630,834)
Unrealized (gains)/losses on derivative and other instruments, net	(67,348,314)	26,793,133
Unrealized (gains)/losses on real estate securities and loans, net	60,668,593	(78,755,229)
Equity based compensation to affiliate	186,983	312,712
Equity based compensation expense	132,103	121,442
Change in operating assets/liabilities:		
Interest receivable	1,884,612	(11,644,920)
Other assets	(399,473)	(739,389)
Due from affiliates	-	104,994
Due from broker	(499,213)	-
Interest payable	3,080,028	1,925,763
Due to affiliates	258,691	1,712,360
Accrued expenses	293,190	644,013
Due to broker	-	(379,914)
Taxes payable	(358,058)	-
Net cash provided by operating activities	105,038,881	62,423,432
Cash Flows from Investing Activities		
Purchase of real estate securities	(2,679,895,866)	(3,837,629,974)
Purchase of securities underlying linked transactions	(218,804,843)	(485,212,383)
Investment in affiliates	(14,357,976)	-
Proceeds from sale of real estate securities	3,143,631,407	733,698,851
Proceeds from sale of securities underlying linked transactions	131,400,523	19,540,469
Principal repayments on real estate securities	417,502,447	195,364,056
Principal repayments on securities underlying linked transactions	68,647,086	38,127,461
Net payments made on reverse repurchase agreements	(50,133,363)	-
Net proceeds from sales of securities borrowed under reverse repurchase agreements	49,024,920	-
Purchase of commercial loans	(30,017,825)	-
Net settlement of interest rate swaps	(9,346,968)	(332,127)
Net settlement of TBAs	(374,861)	1,363,750
Restricted cash provided by (used in) investment activities	(3,908,000)	1,451,001
Net cash provided by (used in) investing activities	803,366,681	(3,333,628,896)
Cash Flows from Financing Activities		
Net proceeds from issuance of common stock	33,176,288	259,664,211
Net proceeds from issuance of preferred stock	-	161,128,492

Borrowings under repurchase agreements		20,325,114,240		15,936,148,227
Borrowings under repurchase agreements underlying linked transactions		2,899,553,903		1,753,757,081
Repayments of repurchase agreements		(21,271,438,649)		(13,243,069,017)
Repayments of repurchase agreements underlying linked transactions		(2,952,632,359)		(1,518,618,310)
Collateral received from (held by) derivative counterparty		15,211,121		(2,100,000)
Collateral received from (held by) repurchase counterparty		1,417,291		(1,443,993)
Dividends paid on common stock		(63,211,085)		(29,093,703)
Dividends paid on preferred stock		(10,102,062)		(521,847)
Net cash provided by (used in) financing activities		(1,022,911,312)		3,315,851,141
Net change in cash and cash equivalents		(114,505,750)		44,645,677
Cash and cash equivalents, Beginning of Period		149,594,782		35,851,249
Cash and cash equivalents, End of Period	$	35,089,032	$	80,496,926
Supplemental disclosure of cash flow information:				
Cash paid for interest on repurchase agreements	$	19,994,933	$	9,198,068
Cash paid for income tax	$	4,528,945	$	-
Real estate securities recorded upon unlinking of Linked Transactions	$	43,415,283	$	170,956,115
Repurchase agreements recorded upon unlinking of Linked Transactions	$	35,674,382	$	139,532,632
Supplemental disclosure of non-cash financing activities:				
Common stock dividends declared but not paid	$	17,017,528	$	17,584,168

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

AG Mortgage Investment Trust Inc. and Subsidiaries
Notes to Consolidated Financial Statements (unaudited)
September 30, 2013

1. Organization

AG Mortgage Investment Trust, Inc. (the "Company") was organized in the state of Maryland on March 1, 2011. The Company is focused on investing in, acquiring and managing a diversified portfolio of residential mortgage-backed securities, or RMBS, issued or guaranteed by a government-sponsored enterprise such as Fannie Mae or Freddie Mac, or any agency of the U.S. Government such as Ginnie Mae (collectively, "Agency RMBS"), and other real estate-related securities and financial assets, including Non-Agency RMBS, ABS, CMBS and loans (as defined below).

Non-Agency RMBS represent fixed-and floating-rate residential RMBS issued by entities or organizations other than a U.S. government-sponsored enterprise or agency of the U.S. government, including investment grade (AAA through BBB) and non investment grade classes (BB and below). The mortgage loan collateral for residential Non-Agency RMBS consists of residential mortgage loans that do not generally conform to underwriting guidelines issued by U.S. government agencies or U.S. government-sponsored entities.

Asset Backed Securities ("ABS") are securitized investments similar to the aforementioned investments except the underlying assets are diverse, not only representing real estate related assets.

Commercial Mortgage Backed Securities ("CMBS") represent investments of fixed- and floating-rate CMBS, including investment grade (AAA through BBB) and non investment grade classes (BB and below). CMBS will be secured by, or evidence an ownership interest in, a single commercial mortgage loan or a pool of commercial mortgage loans.

Collectively, the Company refers to Agency RMBS, Non-Agency RMBS, ABS and CMBS assets types as real estate securities.

Commercial Loans Receivable ("loans") are secured by an interest in commercial real estate and represent a contractual right to receive money on demand or on fixed or determinable dates.

The Company is externally managed by AG REIT Management, LLC (the "Manager"), a wholly-owned subsidiary of Angelo, Gordon & Co., L.P. ("Angelo, Gordon"), a privately-held, SEC-registered investment adviser. The Manager, pursuant to a delegation agreement dated as of June 29, 2011, has delegated to Angelo, Gordon the overall responsibility with respect to the Manager's day-to-day duties and obligations arising under the management agreement.

The Company conducts its operations to qualify and be taxed as a real estate investment trust ("REIT") under the Internal Revenue Code of 1986, as amended (the "Code").

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated.

2. Summary of Significant Accounting Policies

The accompanying unaudited consolidated financial statements and related notes have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial reporting and the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Certain prior period amounts have been reclassified to conform to the current period's presentation. In the opinion of management, all adjustments considered necessary for a fair presentation for the interim period of the Company's financial position, results of operations and cash flows have been included and are of a normal and recurring nature. The operating results presented for interim periods are not necessarily indicative of the results that may be expected for any other interim period or for the entire year.

AG Mortgage Investment Trust Inc. and Subsidiaries
Notes to Consolidated Financial Statements (unaudited)
September 30, 2013

Cash and cash equivalents

Cash is comprised of cash on deposit with financial institutions. We classify highly liquid investments with original maturities of three months or less from the date of purchase as cash equivalents. We place our cash and cash equivalents with high credit quality institutions to minimize credit risk exposure. Any cash held by the Company as collateral would be included in a due to broker line item on the consolidated balance sheet and in cash flows from financing activities on the consolidated statement of cash flows.

Restricted cash

Restricted cash includes cash pledged as collateral for clearing and executing trades, interest rate swaps and repurchase agreements. Restricted cash is carried at cost, which approximates fair value.

Offering costs

The Company incurred costs in connection with common stock offerings and issuances of preferred stock. The offering costs were paid out of the proceeds of the respective offerings. Offering costs in connection with common stock offerings have been accounted for as a reduction of additional paid-in-capital and offering costs in connection with preferred stock offerings have been accounted for as a reduction of their respective gross proceeds.

Use of estimates

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results may differ from those estimates.

Earnings/(Loss) per share

In accordance with the provisions of Accounting Standards Codification ("ASC") 260, "Earnings per Share," the Company calculates basic income/(loss) per share by dividing net income/(loss) available to common stockholders for the period by weighted-average shares of the Company's common stock outstanding for that period. Diluted income/(loss) per share takes into account the effect of dilutive instruments, such as stock options, warrants and unvested restricted stock, but uses the average share price for the period in determining the number of incremental shares that are to be added to the weighted-average number of shares outstanding.

Valuation of financial instruments

The fair value of the financial instruments that the Company records at fair value will be determined by the Manager, subject to oversight of the board of directors, and in accordance with ASC 820, "Fair Value Measurements and Disclosures." When possible, the Company determines fair value using independent data sources. ASC 820 establishes a hierarchy that prioritizes the inputs to valuation techniques giving the highest priority to readily available unadjusted quoted prices in active markets for identical assets (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements) when market prices are not readily available or reliable. The three levels of the hierarchy under ASC 820 are described below:

- Level 1 Quoted prices in active markets for identical assets or liabilities.

- Level 2 Prices determined using other significant observable inputs. These may include quoted prices for similar securities, interest rates, prepayment speeds, credit risk and others.
- Level 3 Prices determined using significant unobservable inputs. In situations where quoted prices or observable inputs are unavailable (for example, when there is little or no market activity for an investment at the end of the period), unobservable inputs may be used. Unobservable inputs reflect the Company's assumptions about the factors that market participants would use in pricing an asset or liability, and would be based on the best information available.

Transfers between levels are assumed to occur at the beginning of the reporting period.

Accounting for real estate securities

Investments in real estate securities are recorded in accordance with ASC 320. The Company has chosen to make a fair value election pursuant to ASC 825 for its real estate securities portfolio. Real estate securities are recorded at fair market value on the consolidated balance sheet and the periodic change in fair market value is recorded in current period earnings on the consolidated statement of operations as a component of "Unrealized gain/(loss) on real estate securities and loans, net."

AG Mortgage Investment Trust Inc. and Subsidiaries
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These investments generally meet the requirements to be classified as available for sale under ASC 320-10-25, “Debt and Equity Securities,” which requires the securities to be carried at fair value on the consolidated balance sheet with changes in fair value charged to other comprehensive income, a component of Stockholders’ Equity. Electing the fair value option allows the Company to record changes in fair value in the statement of operations, which, in management’s view, more appropriately reflects the results of operations for a particular reporting period as all securities activities will be recorded in a similar manner.

We evaluate securities for other-than-temporary impairment ("OTTI") on at least a quarterly basis, and more frequently when economic or market conditions warrant such evaluation. The determination of whether a security is other-than-temporarily impaired involves judgments and assumptions based on subjective and objective factors. When the fair value of an investment security is less than its amortized cost at the balance sheet date, the security is considered impaired, and the impairment is designated as either “temporary” or “other-than-temporary.”

When an investment security is impaired, an OTTI is considered to have occurred if (i) we intend to sell the security (i.e. a decision has been made as of the reporting date) or (ii) it is more likely than not that we will be required to sell the security before recovery of its amortized cost basis. If we intend to sell the security or if it is more likely than not that we will be required to sell the investment security before recovery of its amortized cost basis, the entire amount of the impairment loss, if any, is recognized in earnings as a realized loss and the cost basis of the security is adjusted to its fair value. For securities accounted for under ASC 325-40, “Beneficial Interests in Securitized Financial Assets,” an OTTI is deemed to have occurred when there is an adverse change in the expected cash flows to be received and the fair value of the security is less than its carrying amount. In determining whether an adverse change in cash flows occurred, the present value of the remaining cash flows, as estimated at the initial transaction date (or the last date previously revised), is compared to the present value of the expected cash flows at the current reporting date. The estimated cash flows reflect those a “market participant” would use and are discounted at a rate equal to the current yield used to accrete interest income. Any resulting OTTI adjustments are reflected in the net realized gain/(loss) line item on the consolidated statement of operations.

Increases in interest income may be recognized on a security that an OTTI charge was taken, if the performance of such security subsequently improves. The determination as to whether an OTTI exists is subjective, given that such determination is based on information available at the time of assessment as well as the Company’s estimate of the future performance and cash flow projections for the individual security. As a result, the timing and amount of an OTTI constitutes an accounting estimate that may change materially over time.

Securities in an unrealized loss position at September 30, 2013 are not considered other than temporarily impaired as the Company has the ability and intent to hold the securities to maturity or for a period of time sufficient for a forecasted market price recovery up to or above the cost of the investment, and the Company is not required to sell the security for regulatory or other reasons. See Note 3 for a summary of OTTI charges recorded.

Sales of securities

Sales of securities are driven by the Manager’s portfolio management process. The Manager seeks to mitigate risks including those associated with prepayments and will opportunistically rotate the portfolio into securities with more favorable attributes. Strategies may also be employed to manage net capital gains, which need to be distributed for tax purposes.

Realized gains or losses on sales of securities and derivatives, inclusive of linked transactions are included in the net realized gain/(loss) line item on the consolidated statement of operations. The cost of positions sold is calculated using a FIFO basis. Realized gains and losses are recorded in earnings at the time of disposition.

Accounting for loans

Investments in mortgage loans are recorded in accordance with ASC 310. The Company has chosen to make a fair value election pursuant to ASC 825 for its loan portfolio. Loans are recorded at fair market value on the consolidated balance sheet and any periodic change in fair market value will be recorded in current period earnings on the consolidated statement of operations as a component of "Unrealized gain/(loss) on real estate securities and loans, net."

AG Mortgage Investment Trust Inc. and Subsidiaries
Notes to Consolidated Financial Statements (unaudited)
September 30, 2013

The Company amortizes or accretes any premium or discount over the life of the related loan utilizing the effective interest method. On at least a quarterly basis, the Company evaluates the collectability of both interest and principal of each loan, if circumstances warrant, to determine whether they are impaired. A loan is impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the existing contractual terms. When a loan is impaired, the amount of the loss accrual is calculated and recorded accordingly. Income recognition is suspended for loans at the earlier of the date at which payments become 90-days past due or when, in the opinion of management, a full recovery of income and principal becomes doubtful. When the ultimate collectability of the principal of an impaired loan is in doubt, all payments are applied to principal under the cost recovery method. When the ultimate collectability of the principal of an impaired loan is not in doubt, contractual interest is recorded as interest income when received, under the cash basis method until an accrual is resumed when the loan becomes contractually current and performance is demonstrated to be resumed. A loan is written off when it is no longer realizable and/or legally discharged.

Investment in affiliates

The Company's unconsolidated ownership interests in affiliates are generally accounted for using the equity method. The underlying entities have chosen to make a fair value election pursuant to ASC 825; as such the Company will treat its investment in affiliates consistently with this election. The investment in affiliates is recorded at fair market value on the consolidated balance sheet and periodic changes in fair market value will be recorded in current period earnings on the consolidated statement of operation as a component of "Equity in earnings from affiliate." Capital contributions, distributions and profits and losses of such entities are allocated in accordance with the terms of the applicable agreements.

Investment consolidation

For each investment made, the Company evaluates the underlying entity that issued the securities acquired or to which the Company makes a loan to determine the appropriate accounting. A similar analysis will be performed for each entity with which the Company enters into an agreement for management, servicing or related services. In performing the analysis, the Company will refer to guidance in ASC 810-10, "Consolidation." In situations where the Company is the transferor of financial assets, the Company will refer to the guidance in ASC 860-10, "Transfers and Servicing."

In variable interest entities ("VIEs"), an entity is subject to consolidation under ASC 810-10 if the equity investors either do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support, are unable to direct the entity's activities or are not exposed to the entity's losses or entitled to its residual returns. VIEs within the scope of ASC 810-10 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 of a VIE that most significantly impact the VIE's economic performance and the obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE. This determination can sometimes involve complex and subjective analyses. Further, ASC 810-10 also requires ongoing assessments of whether an enterprise is the primary beneficiary of a VIE. In accordance with ASC 810-10, all transferees, including variable interest entities, must be evaluated for consolidation. If the Company were to treat securitizations as sales in the future, the Company will analyze the transactions under the guidelines of ASC 810-10 for consolidation. All VIEs in which the Company has participated are non-recourse to the Company.

The Company may periodically enter into transactions in which it sells assets. Upon a transfer of financial assets, the Company will sometimes retain or acquire senior or subordinated interests in the related assets. Pursuant to ASC

860-10, a determination must be made as to whether a transferor has surrendered control over transferred financial assets. That determination must consider the transferor's continuing involvement in the transferred financial asset, including all arrangements or agreements made contemporaneously with, or in contemplation of, the transfer, even if they were not entered into at the time of the transfer. The financial components approach under ASC 860-10 limits the circumstances in which a financial asset, or portion of a financial asset, should be derecognized when the transferor has not transferred the entire original financial asset to an entity that is not consolidated with the transferor in the financial statements being presented and/or when the transferor has continuing involvement with the transferred financial asset. It defines the term "participating interest" to establish specific conditions for reporting a transfer of a portion of a financial asset as a sale.

Under ASC 860-10, after a transfer of financial assets that meets the criteria for treatment as a sale legal isolation, ability of transferee to pledge or exchange the transferred assets without constraint and transferred control an entity recognizes the financial and servicing assets it acquired or retained and the liabilities it has incurred, derecognizes financial assets it has sold and derecognizes liabilities when extinguished. The transferor would then determine the gain or loss on sale of financial assets by allocating the carrying value of the underlying mortgage between securities or loans sold and the interests retained based on their fair values. The gain or loss on sale is the difference between the cash proceeds from the sale and the amount allocated to the securities or loans sold. When a transfer of financial assets does not qualify for sale accounting, ASC 860-10 requires the transfer to be accounted for as a secured borrowing with a pledge of collateral.

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From time to time, the Company may securitize mortgage loans it holds if such financing is available. These transactions will be recorded in accordance with ASC 860-10 and will be accounted for as either a "sale" and the loans will be removed from the balance sheet or as a "financing" and will be classified as "real estate securities" on the consolidated balance sheet, depending upon the structure of the securitization transaction. ASC 860-10 is a complex standard that may require the Company to exercise significant judgment in determining whether a transaction should be recorded as a "sale" or a "financing."

Interest income recognition

Interest income on the Company's real estate securities portfolio is accrued based on the actual coupon rate and the outstanding principal balance of such securities. The Company has elected to record interest in accordance with ASC 835-30-35-2 using the effective interest method for all securities accounted for under the fair value option (ASC 825). 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 will flow though the interest income line item on the Consolidated Statement 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 we amortize such securities. If actual and anticipated cash flows differ from previous estimates, we recognize 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, we also reassess the cash flows on at least a quarterly basis for securities accounted for under ASC 325-40 (generally Non-Agency RMBS, ABS, CMBS and interest only securities). In estimating these cash flows, there are a number of assumptions that will be 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.

Interest income on the Company's loan portfolio is accrued based on the actual coupon rate and the outstanding principal balance of such loans. The Company has elected to record interest in accordance with ASC 835-30-35-2 using the effective interest method for all loans accounted for under the fair value option (ASC 825). Any amortization will be reflected as an adjustment to interest income in the consolidated statements of operations.

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 will apply 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 (loans) 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 generally should be recognized prospectively through adjustment of the loan's yield over its remaining life. Decreases in cash flows expected to be collected should be recognized as impairment.

The Company's accrual of interest, discount and premium for U.S. federal and other tax purposes differs from the financial accounting treatment of these items as described above.

Repurchase agreements

The Company finances the acquisition of certain assets within its portfolio through the use of repurchase agreements. Repurchase agreements are treated as collateralized financing transactions and are carried at primarily their contractual amounts, including accrued interest, as specified in the respective agreements. The carrying amount of the Company's repurchase agreements approximates fair value as the debt is short-term in nature.

The Company pledges certain securities as collateral under repurchase agreements with financial institutions, the terms and conditions of which are negotiated on a transaction-by-transaction basis. The amounts available to be borrowed are dependent upon the fair value of the securities pledged as collateral, which fluctuates with changes in interest rates, type of security and liquidity conditions within the banking, mortgage finance and real estate industries. In response to declines in fair value of pledged securities, lenders may require the Company to post additional collateral or pay down borrowings to re-establish agreed upon collateral requirements, referred to as margin calls. As of September 30, 2013 and December 31, 2012, the Company has met all margin call requirements.

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In instances where the Company acquires assets through repurchase agreements with the same counterparty from whom the assets were purchased, the Company evaluates such transactions in accordance with ASC 860-10. This standard requires the initial transfer of a financial asset and repurchase financing that are entered into contemporaneously with, or in contemplation of, one another to be considered linked unless all of the criteria found in ASC 860-10 are met at the inception of the transaction. If the transaction meets all of the conditions, the initial transfer shall be accounted for separately from the repurchase financing, and the Company will record the assets and the related financing on a gross basis on its balance sheet with the corresponding interest income and interest expense in the statements of operations. If the transaction is determined to be linked, the Company will record the initial transfer and repurchase financing on a net basis and record a forward commitment to purchase assets as a derivative instrument with changes in market value being recorded on the consolidated statement of operations. Such forward commitments are recorded at fair value with subsequent changes in fair value recognized in income. The Company refers to these transactions as Linked Transactions. When or if a transaction is no longer considered to be linked, the real estate security and related repurchase financing will be reported on a gross basis. The unlinking of a transaction causes a realized event in which the fair value of the real estate security as of the date of unlinking will become the cost basis of the real estate security. The difference between the fair value on the unlinking date and the existing cost basis of the security will be the realized gain or loss. Recognition of effective yield for such security will be calculated prospectively using the new cost basis.

Accounting for derivative financial instruments

The Company may enter into derivative contracts, including interest rate swaps and interest rate caps, as a means of mitigating its interest rate risk. The Company uses interest rate derivative instruments primarily to mitigate interest rate risk rather than to enhance returns. The Company accounts for derivative financial instruments in accordance with ASC 815-10, “Derivatives and Hedging.” ASC 815-10 requires an entity to recognize all derivatives as either assets or liabilities on the balance sheet and to measure those instruments at fair value. Additionally, the fair value adjustments will affect either other comprehensive income in stockholders’ equity until the hedged item is recognized in earnings or net income depending on whether the derivative instrument is designated and qualifies as a hedge for accounting purposes and, if so, the nature of the hedging activity. As of September 30, 2013 and December 31, 2012, the Company did not have any interest rate derivatives designated as hedges. All derivatives have been recorded at fair value in accordance with ASC 820-10, with corresponding changes in value recognized in the consolidated statement of operations.

When derivative contracts are executed with the same counterparty for bilateral collateral arrangements, or the same Central Clearing Counterparty (“CCP”) and Futures Commission Merchants (“FCM”) under central clearing, the value of the derivative contracts is reported on a net-by-counterparty or net by CCP/FCM basis, as applicable on the balance sheet, where a legal right of off-set exists under an enforceable netting agreement. As a result, the net exposure to counterparties or CCP/FCM is reported as either an asset or liability on the consolidated balance sheet.

To-be-announced securities

A to-be-announced security (“TBA”) is a futures contract for the purchase or sale of Agency RMBS at a predetermined price, face amount, issuer, coupon and stated maturity on an agreed-upon future date. The specific Agency RMBS delivered into or received from the contract upon the settlement date, published each month by the Securities Industry and Financial Markets Association, are not known at the time of the transaction. TBAs are exempt from ASC 815 and are accounted for under ASC 320 if there is no other way to purchase or sell that security, if delivery or receipt of that security and settlement will occur within the shortest period possible for that type of security and if it is probable at inception and throughout the term of the individual contract that physical delivery or receipt of the security will occur (referred to as the "regular-way" exception). Unrealized gains and losses associated with TBA contracts not subject to the regular-way exception or not designated as hedging instruments are recognized in the consolidated statement of operations in the line item "unrealized gain/(loss) on derivative and other instruments, net."

Short positions in U.S. Treasury securities through reverse repurchase agreements

The Company may sell short U.S. Treasury securities contracts to help mitigate the potential impact of changes in interest rates. The Company may borrow securities to cover short sales of U.S. Treasury securities under reverse repurchase agreements, which are accounted for as borrowing transactions, and the Company recognizes an obligation to return the borrowed securities at fair value on its consolidated balance sheet based on the value of the underlying borrowed securities as of the reporting date. Realized and unrealized gains and losses associated with purchases and short sales of U.S. Treasury securities are recognized in "net realized gain/(loss)", and "unrealized gain/(loss) on derivative and other instruments, net", respectively, on our consolidated statements of operations.

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Manager compensation

The management agreement provides for payment to the Manager of a management fee. The management fee is accrued and expensed during the period for which it is calculated and earned. For a more detailed discussion on the fees payable under the management agreement, see Note 10.

Income taxes

The Company conducts its operations to qualify and be taxed as a REIT. Accordingly, the Company will generally not be subject to federal or state corporate income tax to the extent that the Company makes qualifying distributions to its stockholders, and provided that it satisfies on a continuing basis, through actual investment and operating results, the REIT requirements including certain asset, income, distribution and stock ownership tests. If the Company fails to qualify as a REIT, and does not qualify for certain statutory relief provisions, it will be subject to U.S. federal, state and local income taxes and may be precluded from qualifying as a REIT for the four taxable years following the year in which the Company fails to qualify as a REIT.

The dividends paid deduction of a REIT for qualifying dividends to its stockholders is computed using the Company's taxable income as opposed to net income reported under GAAP in the financial statements. Taxable income, generally, will differ from net income reported on the financial statements because the determination of taxable income is based on tax provisions and not financial accounting principles.

The Company has elected to treat AG MIT II, LLC, AG MITT RMAT 2013, LLC and AG MITT RMAT 2013 II, LLC as taxable REIT subsidiaries, ("TRS") and may elect to treat other subsidiaries at TRSs. In general, a TRS may hold assets and engage in activities that the Company cannot hold or engage in directly and generally may engage in any real estate or non-real estate-related business. While a TRS will generate net income, a TRS can declare dividends to the Company which will be included in the Company's taxable income and necessitate a distribution to stockholders. Conversely, if we retain earnings at the TRS level, no distribution is required and the Company can increase book equity of the consolidated entity. A TRS is subject to federal, state and local corporate income taxes.

The Company's financial results are generally not expected to reflect provisions for current or deferred income taxes, except for any activities conducted through one or more TRSs that are subject to corporate income taxation. The Company believes that it will operate in a manner that will allow it to qualify for taxation as a REIT. As a result of the Company's expected REIT qualification, it does not generally expect to pay federal or state corporate income tax. Many of the REIT requirements, however, are highly technical and complex. If the Company were to fail to meet the REIT requirements, it would be subject to federal income taxes and applicable state and local taxes. During the three and nine months ended September 30, 2013 the Company recognized an income tax provision of $0.1 million and $2.8 million, respectively, related to the income and sale of investments held within AG MITT RMAT 2013, LLC and AG MITT RMAT 2013 II, LLC.

As a REIT, if the Company fails to distribute in any calendar year at least the sum of (i) 85% of its ordinary income for such year, (ii) 95% of its capital gain net income for such year, and (iii) any undistributed taxable income from the prior year, the Company would be subject to a non-deductible 4% excise tax on the excess of such required distribution over the sum of (i) the amounts actually distributed and (ii) the amounts of income retained and on which the Company has paid corporate income tax.

The Company evaluates uncertain income tax positions, if any, in accordance with ASC Topic 740, "Income Taxes". The Company classifies interest and penalties, if any, related to unrecognized tax benefits as a component of provision for income taxes. See Note 9 for further details.

Stock-based compensation

The Company applies the provisions of ASC 718, "Compensation Stock Compensation" with regard to its equity incentive plans. ASC 718 covers a wide range of share-based compensation arrangements including stock options, restricted stock plans, performance-based awards, stock appreciation rights and employee stock purchase plans. ASC 718 requires that compensation cost relating to stock-based payment transactions be recognized in financial statements. The cost is measured based on the fair value of the equity or liability instruments issued.

Compensation cost related to restricted common shares issued to the Company's directors is measured at its estimated fair value at the grant date, and is amortized and expensed over the vesting period on a straight-line basis. Compensation cost related to restricted common shares 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. The Company has elected to use the straight-line method to amortize compensation expense for the restricted common shares granted to the Manager.

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Recent accounting pronouncements

In December 2011, the FASB issued Accounting Standards Updated 2011-11, "Disclosures about Offsetting Assets and Liabilities" (ASU 2011-11). ASU 2011-11 amends Topic 210 to require additional disclosure information about offsetting and related arrangements. Entities will be required to disclose both gross information and net information about both instruments and transactions eligible for offset in the statement of financial position and