New Residential Investment Corp.
Form 10-Q
November 07, 2014

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

FORM 10-Q

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

For the quarterly period ended September 30, 2014

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: 001-35777
New Residential Investment Corp.
(Exact name of registrant as specified in its charter)

Delaware	45-3449660
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1345 Avenue of the Americas, New York, NY	10105
(Address of principal executive offices)	(Zip Code)

(212) 798-3150
(Registrant’s telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)
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 Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulations S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨
Indicate by check mark whether the registrant is a large accelerated filer, 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 x Accelerated filer ¨ Non-accelerated filer ¨ (Do not check if a smaller reporting company) 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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the last practicable date.
Common stock, $0.01 par value per share: 141,382,603 shares outstanding as of October 31, 2014.

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This report contains certain “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995, which statements involve substantial risks and uncertainties. Such forward-looking statements relate to, among other things, the operating performance of our investments, the stability of our earnings, our financing needs and the size and attractiveness of market opportunities. Forward-looking statements are generally identifiable by use of forward-looking terminology such as “may,” “will,” “should,” “potential,” “intend,” “expect,” “endeavor “seek,” “anticipate,” “estimate,” “overestimate,” “underestimate,” “believe,” “could,” “project,” “predict,” “continue” or other or expressions. Forward-looking statements are based on certain assumptions, discuss future expectations, describe future plans and strategies, contain projections of results of operations, cash flows or financial condition or state other forward-looking information. Our ability to predict results or the actual outcome of future plans or strategies is inherently uncertain. Although we believe that the expectations reflected in such forward-looking statements are based on reasonable assumptions, our actual results and performance could differ materially from those set forth in the forward-looking statements. These forward-looking statements involve risks, uncertainties and other factors that may cause our actual results in future periods to differ materially from forecasted results. Factors which could have a material adverse effect on our operations and future prospects include, but are not limited to:

- reductions in cash flows received from our investments;
- the quality and size of the investment pipeline and our ability to take advantage of investment opportunities at attractive risk-adjusted prices;
- servicer advances may not be recoverable or may take longer to recover than we expect, which could cause us to fail to achieve our targeted return on our investment in servicer advances;
- our ability to deploy capital accretively and the timing of such deployment;
- our counterparty concentration and default risks in Nationstar, Springleaf and other third-parties;
- a lack of liquidity surrounding our investments, which could impede our ability to vary our portfolio in an appropriate manner;
- the impact that risks associated with subprime mortgage loans and consumer loans, as well as deficiencies in servicing and foreclosure practices, may have on the value of our Excess MSRs, servicer advances, RMBS and consumer loan portfolios;
- the risks that default and recovery rates on our Excess MSRs, servicer advances, real estate securities, residential mortgage loans and consumer loans deteriorate compared to our underwriting estimates;
- changes in prepayment rates on the loans underlying certain of our assets, including, but not limited to, our Excess MSRs;
- the risk that projected recapture rates on the portfolios underlying our Excess MSRs are not achieved;
- the relationship between yields on assets which are paid off and yields on assets in which such monies can be reinvested;
- the relative spreads between the yield on the assets we invest in and the cost of financing;
- changes in economic conditions generally and the real estate and bond markets specifically;
- adverse changes in the financing markets we access affecting our ability to finance our investments on attractive terms, or at all;
- changing risk assessments by lenders that potentially lead to increased margin calls, not extending our repurchase agreements or other financings in accordance with their current terms or not entering into new financings with us;
- changes in interest rates and/or credit spreads, as well as the success of any hedging strategy we may undertake in relation to such changes;
- impairments in the value of the collateral underlying our investments and the relation of any such impairments to our judgments as to whether changes in the market value of our securities or loans are temporary or not and whether circumstances bearing on the value of such assets warrant changes in carrying values;
- the availability and terms of capital for future investments;
- competition within the finance and real estate industries;

- the legislative/regulatory environment, including, but not limited to, the impact of the Dodd-Frank Act, U.S. government programs intended to stabilize the economy, the federal conservatorship of Fannie Mae and Freddie Mac and legislation that permits modification of the terms of loans;

- our ability to maintain our qualification as a real estate investment trust ("REIT") for U.S. federal income tax purposes and the potentially onerous consequences that any failure to maintain such qualification would have on our business; and
- our ability to maintain our exclusion from registration under the 1940 Act and the fact that maintaining such exclusion imposes limits on our operations.

We also direct readers to other risks and uncertainties referenced in this report, including those set forth under "Risk Factors." We caution that you should not place undue reliance on any of our forward-looking statements. Further, any forward-looking statement speaks only as of the date on which it is made. New risks and uncertainties arise from time to time, and it is impossible for us to predict those events or how they may affect us. Except as required by law, we are under no obligation (and expressly disclaim any obligation) to update or alter any forward-looking statement, whether written or oral, that we may make from time to time, whether as a result of new information, future events or otherwise.

SPECIAL NOTE REGARDING EXHIBITS

In reviewing the agreements included as exhibits to this Quarterly Report on Form 10-Q, please remember they are included to provide you with information regarding their terms and are not intended to provide any other factual or disclosure information about New Residential Investment Corp. (the “Company,” “New Residential” or “we,” “our” and “us”) the other parties to the agreements. The agreements contain representations and warranties by each of the parties to the applicable agreement. These representations and warranties have been made solely for the benefit of the other parties to the applicable agreement and:

- should not in all instances be treated as categorical statements of fact, but rather as a way of allocating the risk to one of the parties if those statements provide to be inaccurate;
- have been qualified by disclosures that were made to the other party in connection with the negotiation of the applicable agreement, which disclosures are not necessarily reflected in the agreement;
- may apply standards of materiality in a way that is different from what may be viewed as material to you or other investors; and
- were made only as of the date of the applicable agreement or such other date or dates as may be specified in the agreement and are subject to more recent developments.

Accordingly, these representations and warranties may not describe the actual state of affairs as of the date they were made or at any other time. Additional information about the Company may be found elsewhere in this Quarterly Report on Form 10-Q and the Company’s other public filings, which are available without charge through the SEC’s website at http://www.sec.gov. See “Business – Corporate Governance and Internet Address; Where Readers Can Find Additional Information.”

The Company acknowledges that, notwithstanding the inclusion of the foregoing cautionary statements, it is responsible for considering whether additional specific disclosures of material information regarding material contractual provisions are required to make the statements in this report not misleading.

NEW RESIDENTIAL INVESTMENT CORP.
FORM 10-Q

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

NEW RESIDENTIAL INVESTMENT CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(dollars in thousands, except share data)

	September 30, 2014 (Unaudited)	December 31, 2013
Assets		
Investments in:		
Excess mortgage servicing rights, at fair value	$409,236	$324,151
Excess mortgage servicing rights, equity method investees, at fair value	342,538	352,766
Servicer advances, at fair value	3,214,113	2,665,551
Real estate securities, available-for-sale	2,079,712	1,973,189
Residential mortgage loans, held-for-investment	629,398	33,539
Residential mortgage loans, held-for-sale	492,399	—
Consumer loans, equity method investees	264,039	215,062
Cash and cash equivalents	187,601	271,994
Restricted cash	29,962	33,338
Real estate owned	52,740	—
Derivative assets	28,686	35,926
Other assets	42,977	53,142
	$7,773,401	$5,958,658
Liabilities and Equity		
Liabilities		
Repurchase agreements	$2,738,349	$1,620,711
Notes payable	2,847,251	2,488,618
Trades payable	213,050	246,931
Due to affiliates	35,141	19,169
Dividends payable	49,484	63,297
Deferred tax liability	22,485	—
Accrued expenses and other liabilities	11,780	6,857
	5,917,540	4,445,583
Commitments and Contingencies		
Equity		
Common Stock, $0.01 par value, 2,000,000,000 shares authorized, 141,382,603 and 126,598,987 issued and outstanding at September 30, 2014 and December 31, 2013, respectively	1,414	1,266
Additional paid-in capital	1,330,090	1,158,384
Retained earnings	237,284	102,986
Accumulated other comprehensive income, net of tax	6,628	3,214
Total New Residential stockholders’ equity	1,575,416	1,265,850
Noncontrolling interests in equity of consolidated subsidiaries	280,445	247,225

Total Equity	1,855,861	1,513,075
	$7,773,401	$5,958,658

See notes to condensed consolidated financial statements.

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NEW RESIDENTIAL INVESTMENT CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)
(dollars in thousands, except share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Interest income	$97,587	$ 21,885	$261,733	$ 61,075
Interest expense	33,307	3,443	108,816	6,993
Net Interest Income	64,280	18,442	152,917	54,082
Impairment				
Other-than-temporary impairment ("OTTI") on securities	—	—	943	3,756
Valuation provision on loans	1,134	—	1,591	—
	1,134	—	2,534	3,756
Net interest income after impairment	63,146	18,442	150,383	50,326
Other Income				
Change in fair value of investments in excess mortgage servicing rights	28,566	208	40,670	43,899
Change in fair value of investments in excess mortgage servicing rights, equity method investees	31,833	20,645	50,950	41,741
Change in fair value of investments in servicer advances	22,948	—	105,825	—
Earnings from investments in consumer loans, equity method investees	22,490	24,129	60,185	60,293
Gain on settlement of investments	938	11,213	57,834	11,271
Other income	15,289	—	19,539	—
	122,064	56,195	335,003	157,204
Operating Expenses				
General and administrative expenses	7,499	2,449	14,886	5,640
Management fee allocated by Newcastle	—	—	—	4,134
Management fee to affiliate	5,124	4,484	14,525	6,747
Incentive compensation to affiliate	10,910	4,470	33,111	5,348
Loan servicing expense	1,778	89	2,210	219
	25,311	11,492	64,732	22,088
Income (Loss) Before Income Taxes	159,899	63,145	420,654	185,442
Income tax expense	7,801	—	29,483	—
Net Income (Loss)	$152,098	$ 63,145	$391,171	$ 185,442
Noncontrolling Interests in Income (Loss) of Consolidated Subsidiaries	$25,726	$ —	$92,524	$ —
Net Income (Loss) Attributable to Common Stockholders	$126,372	$ 63,145	$298,647	$ 185,442

Net Income Per Share of Common Stock

Basic	$0.89	$0.50	$2.22	$1.47
Diluted	$0.88	$0.49	$2.16	$1.45
Weighted Average Number of Shares of Common Stock Outstanding				
Basic	141,211,580	126,536,394	134,814,020	126,520,766
Diluted	144,166,601	129,944,643	137,972,639	128,274,974
Dividends Declared per Share of Common Stock	$0.35	$0.35	$1.20	$0.49

See notes to condensed consolidated financial statements.

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NEW RESIDENTIAL INVESTMENT CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)
(dollars in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Comprehensive income (loss), net of tax				
Net income (loss)	$152,098	$63,145	$391,171	$185,442
Other comprehensive income (loss)				
Net unrealized gain (loss) on securities	1,308	7,687	67,915	7,677
Reclassification of net realized (gain) loss on securities into earnings	(3,668)	(11,213)	(64,501)	(7,515)
	(2,360)	(3,526)	3,414	162
Total comprehensive income (loss)	$149,738	$59,619	$394,585	$185,604
Comprehensive income (loss) attributable to noncontrolling interests	$25,726	$—	$92,524	$—
Comprehensive income (loss) attributable to common stockholders	$124,012	$59,619	$302,061	$185,604

See notes to condensed consolidated financial statements.

NEW RESIDENTIAL INVESTMENT CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY (UNAUDITED)
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2014
(dollars in thousands, except share data)

	Common Stock							
	Shares	Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total New Residential Stockholders' Equity	Noncontrolling Interests in Equity of Consolidated Subsidiaries	Total Equity
Equity - December 31, 2013	126,598,987	$1,266	$1,158,384	$102,986	$ 3,214	$1,265,850	$ 247,225	$1,513,075
Dividends declared	—	—	—	(164,349)	—	(164,349)	—	(164,349)
Capital contributions	—	—	—	—	—	—	142,082	142,082
Capital distributions	—	—	—	—	—	—	(200,368)	(200,368)
Issuance of common stock	14,375,000	144	169,761	—	—	169,905	—	169,905
Option exercise	383,536	4	599	—	—	603	—	603
Dilution impact of distributions from consolidated subsidiaries	—	—	1,018	—	—	1,018	(1,018)	—
Director share grant	25,080	—	328	—	—	328	—	328
Comprehensive income (loss) (net of tax)								
Net income (loss)	—	—	—	298,647	—	298,647	92,524	391,171
Net unrealized gain (loss) on securities	—	—	—	—	67,915	67,915	—	67,915
Reclassification of net realized (gain) loss on securities into earnings	—	—	—	—	(64,501)	(64,501)	—	(64,501)
Total comprehensive income (loss)	—	—	—	—	—	302,061	92,524	394,585
Equity - September 30, 2014	141,382,603	$1,414	$1,330,090	$237,284	$ 6,628	$1,575,416	$ 280,445	$1,855,861

See notes to condensed consolidated financial statements.

NEW RESIDENTIAL INVESTMENT CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
(dollars in thousands)

	Nine Months Ended September 30,	
	2014	2013
Cash Flows From Operating Activities		
Net income (loss)	$391,171	$185,442
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Change in fair value of investments in excess mortgage servicing rights	(40,670)	(43,899)
Change in fair value of investments in excess mortgage servicer rights, equity method investees	(50,950)	(41,741)
Change in fair value of investments in servicer advances	(105,825)	—
Earnings from consumer loan equity method investees	(60,185)	(60,293)
Change in fair value of investments in derivative assets	(2,355)	—
Accretion and other amortization	(213,945)	(40,156)
(Gain) / loss on settlement of investments (net)	(57,834)	(11,271)
(Gain) / loss on transfer of loans to REO	(11,861)	—
(Gain) / loss on mortgage servicing rights recapture agreement	(323)	—
Other-than-temporary impairment (“OTTI”)	943	3,756
Valuation provision on loans	1,591	—
Non-cash directors’ compensation	328	—
Deferred tax provision	22,485	—
Changes in:		
Restricted cash	3,376	—
Other assets	(8,961)	(7,145)
Due to affiliates	15,972	1,973
Accrued expenses and other liabilities	4,665	1,752
Reduction of liability deemed as capital contribution by Newcastle	—	11,515
Other operating cash flows:		
Interest received from excess mortgage servicing rights	38,548	12,399
Interest received from servicer advance investments	91,829	—
Interest received from residential mortgage loans, held-for-investment	5,536	2,432
Distributions of earnings from excess mortgage servicing rights, equity method investees	34,680	23,659
Distributions of earnings from consumer loan equity method investees	10,599	60,293
Cash proceeds from investments, in excess of interest income	—	41,435
Net cash proceeds deemed as capital distributions to Newcastle	—	(35,571)
Net cash provided by (used in) operating activities	68,814	104,580
Cash Flows From Investing Activities		
Acquisition of investments in excess mortgage servicing rights	(75,206)	(46,421)
Acquisition of investments in excess mortgage servicing rights, equity method investees	—	(226,837)
Purchase of servicer advance investments	(5,569,238)	—
Purchase of Agency RMBS	(1,229,580)	(292,980)

Purchase of Non-Agency RMBS	(1,148,631)	(202,484)
Purchase of residential mortgage loans, held-for-investment	(1,357,268)	—
Purchase of derivative assets	(70,027)	—
Purchase of real estate owned	(6,314)	—
Payment for settlement of derivatives	(22,643)	—
Return of investments in excess mortgage servicing rights	30,615	15,132
Return of investments in excess mortgage servicing rights, equity method investees	26,498	4,018
Principal repayments from servicing advance investments	5,188,295	—
Principal repayments from Agency RMBS	213,993	219,187
Principal repayments from Non-Agency RMBS	71,019	50,878
Principal repayments from residential mortgage loans, held-for-investment	33,235	2,400
Return of investments in consumer loan equity method investees	—	52,923
Proceeds from sale of Agency RMBS	796,392	—
Proceeds from sale of Non-Agency RMBS	1,273,191	123,130
Proceeds from settlement of derivatives	14,107	—
Proceeds from sale of residential mortgage loans	249,690	—
Proceeds from sale of real estate owned	4,140	—
Net cash provided by (used in) investing activities	(1,577,732)	(301,054)

Continued on next page.

NEW RESIDENTIAL INVESTMENT CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
(dollars in thousands)

	Nine Months Ended September 30, 2014	2013
Cash Flows From Financing Activities		
Repayments of repurchase agreements	(2,839,051)	(1,283,567)
Margin deposits under repurchase agreements and derivatives	(221,598)	(210,507)
Repayments of notes payable	(5,019,000)	—
Payment of deferred financing fees	(8,389)	(166)
Common stock dividends paid	(178,162)	(17,712)
Borrowings under repurchase agreements	3,957,212	1,425,413
Return of margin deposits under repurchase agreements and derivatives	243,658	210,158
Borrowings under notes payable	5,377,633	—
Issuance of common stock	173,201	—
Costs related to issuance of common stock	(2,693)	—
Capital contributions	—	245,058
Noncontrolling interest in equity of consolidated subsidiaries - contributions	142,082	—
Noncontrolling interest in equity of consolidated subsidiaries - distributions	(200,368)	—
Net cash provided by (used in) financing activities	1,424,525	368,677
Net Increase (Decrease) in Cash and Cash Equivalents	(84,393)	172,203
Cash and Cash Equivalents, Beginning of Period	271,994	—
Cash and Cash Equivalents, End of Period	$187,601	$172,203
Supplemental Disclosure of Cash Flow Information		
Cash paid during the period for interest	$105,937	$6,853
Cash paid during the period for income taxes	9,119	—
Supplemental Schedule of Non-Cash Investing and Financing Activities Prior to Date of Cash Contribution by Newcastle		
Cash proceeds from investments, in excess of interest income	$—	$41,435
Acquisition of real estate securities	—	242,750
Acquisition of investments in excess mortgage servicing rights, equity method investees at fair value	—	125,099
Acquisition of residential mortgage loans, held-for-investment	—	35,138
Acquisition of investments in consumer loan equity method investees	—	245,421
Borrowings under repurchase agreements	—	1,179,068
Repayments of repurchase agreements	—	3,902
Capital contributions by Newcastle	—	648,408
Contributions in-kind by Newcastle	—	1,093,684
Capital distributions to Newcastle	—	1,228,054
Supplemental Schedule of Non-Cash Investing and Financing Activities Subsequent to Date of Cash Contribution by Newcastle		

Dividends declared but not paid	$49,484	$44,308
Non-cash distribution from Consumer Loan Companies	609	—

See notes to condensed consolidated financial statements.

NEW RESIDENTIAL INVESTMENT CORP. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
September 30, 2014
(dollars in tables in thousands, except share data)

1. GENERAL

New Residential Investment Corp. (together with its subsidiaries, “New Residential”) is a Delaware corporation that was formed as a limited liability company in September 2011 for the purpose of making real estate related investments and commenced operations on December 8, 2011. On December 20, 2012, New Residential was converted to a corporation. Newcastle Investment Corp. (“Newcastle”) was the sole stockholder of New Residential until the spin-off (Note 13), which was completed on May 15, 2013. Newcastle is listed on the New York Stock Exchange (“NYSE”) under the symbol “NCT.”

Following the spin-off, New Residential is an independent publicly traded real estate investment trust (“REIT”) primarily focused on investing in residential mortgage related assets. New Residential is listed on the NYSE under the symbol “NRZ.”

New Residential has elected and intends to qualify to be taxed as a REIT for U.S. federal income tax purposes. As such, New Residential will generally not be subject to U.S. federal corporate income tax on that portion of its net income that is distributed to stockholders if it distributes at least 90% of its REIT taxable income to its stockholders by prescribed dates and complies with various other requirements. See Note 17 regarding New Residential's taxable REIT subsidiaries.

New Residential has entered into a management agreement (the “Management Agreement”) with FIG LLC (the “Manager”), an affiliate of Fortress Investment Group LLC (“Fortress”), under which the Manager advises New Residential on various aspects of its business and manages its day-to-day operations, subject to the supervision of New Residential’s board of directors. For its services, the Manager is entitled to management fees and incentive compensation, both defined in, and in accordance with the terms of, the Management Agreement. The Manager also manages Newcastle and investment funds that own a majority of Nationstar Mortgage LLC (“Nationstar”), a leading residential mortgage servicer, and Springleaf Holdings, Inc. (“Springleaf”), managing member of the Consumer Loan Companies (Note 9).

As of September 30, 2014, New Residential conducted its business through the following segments: (i) investments in Excess MSRs, (ii) investments in servicer advances, (iii) investments in real estate securities, (iv) investments in real estate loans, (v) investments in consumer loans and (vi) corporate.

Approximately 2.4 million shares of New Residential’s common stock were held by Fortress, through its affiliates, and its principals as of September 30, 2014. In addition, Fortress, through its affiliates, held options to purchase approximately 9.0 million shares of New Residential’s common stock as of September 30, 2014.

The consolidated financial statements for periods prior to May 15, 2013 have been prepared on a spin-off basis from the consolidated financial statements and accounting records of Newcastle and reflect New Residential’s historical results of operations, financial position and cash flows, in accordance with U.S. GAAP. As presented in the Consolidated Statements of Cash Flows, New Residential did not have any cash balance during periods prior to April 5, 2013, which is the first date Newcastle contributed cash to New Residential. All of its cash activity occurred in Newcastle’s accounts during these periods. The consolidated financial statements for periods prior to May 15, 2013 do not necessarily reflect what New Residential’s consolidated results of operations, financial position and cash flows would have been had New Residential operated as an independent company prior to the spin-off.

Certain expenses of Newcastle, comprised primarily of a portion of its management fee, have been allocated to New Residential to the extent they were directly associated with New Residential for periods prior to the spin-off on May 15, 2013. The portion of the management fee allocated to New Residential prior to the spin-off represents the product of the management fee rate payable by Newcastle (1.5%) and New Residential's gross equity, which management believes is a reasonable method for quantifying the expense of the services provided by the employees of the Manager to New Residential. The incremental cost of certain legal, accounting and other expenses related to New Residential's operations prior to May 15, 2013 are reflected in the accompanying consolidated financial statements. New Residential and Newcastle do not share any expenses following the spin-off.

The accompanying condensed consolidated financial statements and related notes of New Residential have been prepared in accordance with accounting principles generally accepted in the United States for interim financial reporting and the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, certain information and footnote disclosures normally included in financial statements prepared under U.S. generally accepted accounting principles have been condensed or omitted. In the opinion of management, all adjustments considered necessary for a fair presentation of New Residential’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. These consolidated financial statements should be read in conjunction with New Residential’s consolidated financial statements for the year ended December 31, 2013 and notes thereto included in New Residential’s Annual Report on Form 10-K filed with the Securities and Exchange Commission. Capitalized terms used herein, and not otherwise defined, are defined in New Residential’s consolidated financial statements for the year ended December 31, 2013.

Certain prior period amounts have been reclassified to conform to the current period's presentation. In addition, New Residential completed a one-for-two reverse stock split in October 2014 (Notes 13 and 18). The impact of this reverse stock split has been retroactively applied to all periods presented.

Recently Adopted Accounting Policies

Purchased Credit-Impaired ("PCI") Loans

New Residential evaluates the credit quality of its loans, as of the acquisition date, for evidence of credit quality deterioration. Loans with evidence of credit deterioration since their origination, and where it is probable that New Residential will not collect all contractually required principal and interest payments, are PCI loans. At acquisition, New Residential aggregates PCI loans into pools based on common risk characteristics and loans aggregated into pools are accounted for as if each pool were a single loan with a single composite interest rate and an aggregate expectation of cash flows.

The excess of the total cash flows (both principal and interest) expected to be collected over the carrying value of the PCI loans is referred to as the accretable yield. This amount is not reported on New Residential’s Condensed Consolidated Balance Sheets but is accreted into interest income at a level rate of return over the remaining estimated life of the pool of loans.

On a quarterly basis, New Residential estimates the total cash flows expected to be collected over the remaining life of each pool. Probable decreases in expected cash flows trigger the recognition of impairment. Impairments are recognized through the valuation provision for loans and an increase in the allowance for loan losses. Probable and significant increases in expected cash flows would first reverse any previously recorded allowance for loan losses with any remaining increases recognized prospectively as a yield adjustment over the remaining estimated life of the pool of loans.

The excess of the total contractual cash flows over the cash flows expected to be collected is referred to as the nonaccretable difference. This amount is not reported on New Residential's Condensed Consolidated Balance Sheets and represents an estimate of the amount of principal and interest that will not be collected.

The liquidation of PCI loans, which may include sales of loans, receipt of payment in full by the borrower, or foreclosure, results in removal of the loans from the underlying PCI pool. When the amount of the liquidation proceeds, if any, is less than the unpaid principal balance of the loan, the difference is first applied against the PCI pool’s nonaccretable difference. When the nonaccretable difference for a particular loan pool has been fully depleted, any excess of the unpaid principal balance of the loan over the liquidation proceeds is written off against the PCI pool’s allowance for loan losses.

Loans Held-for-Sale

Loans acquired with the intent to sell are classified as held-for-sale. Loans held-for-sale are measured at the lower of cost or fair value, with valuation changes recorded in other income. Purchase price discounts or premiums are deferred in a contra loan account until the related loan is sold. The deferred discounts or premiums are an adjustment to the basis of the loan and are included in the quarterly determination of the lower of cost or fair value adjustments and/or the gain or loss recognized at the time of sale.

Real Estate Owned ("REO")

REO assets are those individual properties where New Residential receives the property in satisfaction of a debt (e.g., by taking legal title or physical possession). New Residential measures REO assets at the lower of cost or fair value, with valuation changes recorded in other income. See Note 12 for further details on the fair value measurement of REO.

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Reclassification of Loans upon Foreclosure

In January 2014, the FASB issued ASU 2014-04, Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure. The standard clarifies the timing of when a creditor is considered to have taken physical possession of residential real estate collateral for a consumer mortgage loan, resulting in the reclassification of the loan receivable to REO. A creditor has taken physical possession of the property when either (1) the creditor obtains legal title through foreclosure, or (2) the borrower transfers all interests in the property to the creditor via a deed in lieu of foreclosure or a similar legal agreement. The standard also requires disclosure of the amount of foreclosed residential real estate property held by the creditor and the recorded investment in residential real estate mortgage loans that are in process of foreclosure. New Residential has included this disclosure through an early adoption of this guidance with prospective application. New Residential's adoption of this guidance did not have an impact on its consolidated financial statements as this guidance was consistent with its prior practice. See Note 8 for the new disclosure.

Classification of Government-Guaranteed Loans upon Foreclosure

In August 2014, the FASB issued ASU No. 2014-14, Receivables - Troubled Debt Restructurings by Creditors (Subtopic 310-40): Classification of Certain Government-Guaranteed Mortgage Loans upon Foreclosure (a consensus of the FASB Emerging Issues Task Force). The standard provides guidance on how to classify and measure certain government-guaranteed mortgage loans upon foreclosure. A mortgage loan is to be derecognized and a separate other receivable is to be recognized upon foreclosure in the amount of the loan balance (principal and interest) expected to be recovered from the guarantor if (1) the loan has a government guarantee that is not separable from the loan before foreclosure, (2) at the time of foreclosure, the creditor has the intent to convey the real estate property to the guarantor and make a claim on the guarantee, and the creditor has the ability to recover under that claim, and 3) at the time of foreclosure, any amount of the claim that is determined on the basis of the fair value of the real estate is fixed. The ASU is effective in the first quarter of 2015 and early adoption is permitted.

New Residential has adopted ASU No. 2014-14 as of September 30, 2014, as it relates to the reverse mortgage portfolio. This portfolio is comprised primarily of U.S. Department of Housing and Urban Development (HUD)-guaranteed reverse mortgage loans.

Upon foreclosure of a reverse mortgage loan, New Residential receives the real estate property in satisfaction of the loan and intends to dispose of the property for the best possible economic value. To the extent the liquidation proceeds are less than the unpaid principal balance (UPB) of the loan, New Residential submits a claim to HUD for the lesser of the remaining UPB or the pre-determined HUD claim amount. New Residential's exposure to market risk while the foreclosed property is in its possession is limited to the extent the HUD claim amount is unlikely to cover any shortfall in property disposal proceeds.

After adoption of ASU No. 2014-14, upon foreclosure of a guaranteed reverse mortgage loan, New Residential records a separate other receivable for the expected liquidation proceeds, comprised of both the property disposal proceeds and the maximum HUD claim amount.

New Residential has used the modified retrospective transition method of adoption, that resulted in no cumulative-effect adjustment as of the beginning of the current fiscal year.

Recent Accounting Pronouncements

In May 2014, the FASB issued ASU 2014-09, Revenues from Contracts with Customers (Topic 606). The standard's core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. In doing so, companies will need to use more judgment and make more estimates than under today's guidance. These may include identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. The ASU is effective for New Residential in the first quarter of 2017. Early adoption is not permitted. Entities have the option of using either a full retrospective or a modified approach to adopt the guidance in the ASU. New Residential is currently evaluating the new guidance to determine the impact it may have on its consolidated financial statements.

In June 2014, the FASB issued ASU No. 2014-11, Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures. The standard changes the accounting for repurchase-to-maturity transactions and linked repurchase financing transactions to secured borrowing accounting. The ASU also expands disclosure requirements related to certain transfers of financial assets that are accounted for as sales and certain transfers accounted for as secured borrowings. The ASU is effective for New Residential in the first quarter of 2015. Early adoption is not permitted. Disclosures are not required for comparative periods presented before the effective date. New Residential is currently evaluating the new guidance to determine the impact it may have on its consolidated financial statements.

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In August 2014, the FASB issued ASU No. 2014-15, Presentation of Financial Statements - Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. The standard provides guidance on management's responsibility to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern by requiring management to assess an entity's ability to continue as a going concern by incorporating and expanding on certain principles that are currently in U.S. auditing standards. The ASU is effective for New Residential for the annual period ending on December 31, 2016. Early adoption is permitted. New Residential is currently evaluating the new guidance to determine the impact that it may have on its consolidated financial statements.

The FASB has recently issued or discussed a number of proposed standards on such topics as consolidation, financial statement presentation, financial instruments and hedging. Some of the proposed changes are significant and could have a material impact on New Residential's reporting. New Residential has not yet fully evaluated the potential impact of these proposals, but will make such an evaluation as the standards are finalized.

2. OTHER INCOME, ASSETS AND LIABILITIES

Other income is comprised of the following:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Gain (loss) on derivative instruments	$4,799	$—	$2,355	$—
Gain (loss) on transfer of loans to REO	5,167	—	11,861	—
Fee earned on deal termination	5,000	—	5,000	—
Other income	323	—	323	—
	$15,289	$—	$19,539	$—

Gain on settlement of investments is comprised of the following:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Gain on sale of real estate securities, net	$3,668	$11,213	$65,444	$11,271
Gain (loss) on sale of derivatives	(2,403)	—	(6,186)	—
Gain (loss) on liquidated residential mortgage loans, held-for-investment	782	—	782	—
Gain (loss) on sale of REO	(159)	—	(801)	—
Other gains (losses)	(950)	—	(1,405)	—
	$938	$11,213	$57,834	$11,271

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Other assets and liabilities are comprised of the following:

	Other Assets			Accrued Expenses and Other Liabilities	
	September 30, 2014	December 31, 2013		September 30, 2014	December 31, 2013
Margin receivable, net	$17,220	$40,132	Interest payable	$246	$4,010
Interest and other receivables	8,530	7,548	Accounts payable	10,586	2,829
Deferred financing costs, net[(A)]	5,487	4,773	Derivative liability	345	18
Other assets	11,740	689	Current taxes payable	584	—
	$42,977	$53,142	Other liabilities	19	—
				$11,780	$6,857

(A) Deferred financing costs is net of accumulated amortization of $8,443 and $768 as of September 30, 2014 and December 31, 2013, respectively.

As reflected on the Condensed Consolidated Statements of Cash Flows, accretion and other amortization is comprised of the following:

	Nine Months Ended September 30,	
	2014	2013
Accretion of servicer advance interest income	$153,790	$—
Accretion of excess mortgage servicing rights income	37,703	30,541
Accretion of net discount on securities and loans[(A)]	30,127	9,644
Amortization of deferred financing costs	(7,675)	(29)
	$213,945	$40,156

(A) Includes accretion of the accretable yield on PCI loans.

3. SEGMENT REPORTING

New Residential conducts its business through the following segments: (i) investments in Excess MSRs, (ii) investments in servicer advances, (iii) investments in real estate securities, (iv) investments in real estate loans, (v) investments in consumer loans, and (vi) corporate. The corporate segment consists primarily of (i) general and administrative expenses, (ii) the allocation of management fees by Newcastle until the spin-off on May 15, 2013, (iii) the management fees and incentive compensation owed to the Manager by New Residential following the spin-off, (iv) corporate cash and related interest income, and (v) the secured corporate loan and related interest expense.

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Summary financial data on New Residential's segments is given below, together with a reconciliation to the same data for New Residential as a whole:

	Servicing Related Assets		Residential Securities and Loans				
	Excess MSRs	Servicer Advances	Real Estate Securities	Real Estate Loans	Consumer Loans	Corporate	Total
Three Months Ended September 30, 2014							
Interest income	$12,914	$50,967	$11,179	$22,526	$—	$1	$97,587
Interest expense	3	25,157	1,932	5,065	1,149	1	33,307
Net interest income (expense)	12,911	25,810	9,247	17,461	(1,149)	—	64,280
Impairment	—	—	—	1,134	—	—	1,134
Other income	60,722	22,948	955	14,950	22,490	(1)	122,064
Operating expenses	103	4,796	169	3,163	632	16,448	25,311
Income (Loss) Before Income Taxes	73,530	43,962	10,033	28,114	20,709	(16,449)	159,899
Income tax expense	—	7,403	—	306	92	—	7,801
Net Income (Loss)	$73,530	$36,559	$10,033	$27,808	$20,617	$(16,449)	$152,098
Noncontrolling interests in income (loss) of consolidated subsidiaries	$—	$25,726	$—	$—	$—	$—	$25,726
Net income (loss) attributable to common stockholders	$73,530	$10,833	$10,033	$27,808	$20,617	$(16,449)	$126,372

	Servicing Related Assets		Residential Securities and Loans				
	Excess MSRs	Servicer Advances	Real Estate Securities	Real Estate Loans	Consumer Loans	Corporate	Total
Nine Months Ended September 30, 2014							
Interest income	$37,703	$153,790	$41,939	$28,300	$—	$1	$261,733
Interest expense	1,294	86,885	9,513	6,454	4,170	500	108,816
Net interest income (expense)	36,409	66,905	32,426	21,846	(4,170)	(499)	152,917
Impairment	—	—	943	1,591	—	—	2,534
Other income	91,943	105,657	59,410	17,808	60,185	—	335,003
Operating expenses	488	5,815	800	4,140	745	52,744	64,732
Income (Loss) Before Income Taxes	127,864	166,747	90,093	33,923	55,270	(53,243)	420,654
Income tax expense	—	29,085	—	306	92	—	29,483
Net Income (Loss)	$127,864	$137,662	$90,093	$33,617	$55,178	$(53,243)	$391,171
Noncontrolling interests in income (loss) of consolidated subsidiaries	$—	$92,524	$—	$—	$—	$—	$92,524

Net income (loss) attributable to common stockholders	$127,864	$45,138	$90,093	$33,617	$55,178	$(53,243)	$298,647

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	Servicing Related Assets		Residential Securities and Loans				
	Excess MSRs	Servicer Advances	Real Estate Securities	Real Estate Loans	Consumer Loans	Corporate	Total
September 30, 2014							
Investments	$751,774	$3,214,113	$2,079,712	$1,121,797	$264,039	$—	$7,431,435
Cash and cash equivalents	—	88,770	13,273	2,889	9,766	72,903	187,601
Restricted cash	—	29,962	—	—	—	—	29,962
Derivative assets	—	—	1,115	27,571	—	—	28,686
Other assets	1,122	7,768	22,879	62,695	609	644	95,717
Total assets	$752,896	$3,340,613	$2,116,979	$1,214,952	$274,414	$73,547	$7,773,401
Debt	$—	$2,824,007	$1,725,737	$910,856	$125,000	$—	$5,585,600
Other liabilities	1,715	27,557	214,018	4,973	1,132	82,545	331,940
Total liabilities	1,715	2,851,564	1,939,755	915,829	126,132	82,545	5,917,540
Total equity	751,181	489,049	177,224	299,123	148,282	(8,998)	1,855,861
Noncontrolling interests in equity of consolidated subsidiaries	—	280,445	—	—	—	—	280,445
Total New Residential stockholders' equity	$751,181	$208,604	$177,224	$299,123	$148,282	$(8,998)	$1,575,416
Investments in equity method investees	$342,538	$—	$—	$—	$264,039	$—	$606,577

	Servicing Related Assets		Residential Securities and Loans				
	Excess MSRs	Servicer Advances	Real Estate Securities	Real Estate Loans	Consumer Loans	Corporate	Total
Three Months Ended September 30, 2013							
Interest income	$9,761	$—	$11,437	$683	$—	$4	$21,885
Interest expense	—	—	3,443	—	—	—	3,443
Net interest income (expense)	9,761	—	7,994	683	—	4	18,442
Impairment	—	—	—	—	—	—	—
Other income	20,853	—	11,213	—	24,129	—	56,195
Operating expenses	82	—	10	94	1	11,305	11,492
Income (Loss) Before Income Taxes	30,532	—	19,197	589	24,128	(11,301)	63,145
Income tax expense	—	—	—	—	—	—	—
Net Income (Loss)	$30,532	$—	$19,197	$589	$24,128	$(11,301)	$63,145
Noncontrolling interests in income (loss) of consolidated subsidiaries	$—	$—	$—	$—	$—	$—	$—
Net income (loss) attributable to common stockholders	$30,532	$—	$19,197	$589	$24,128	$(11,301)	$63,145

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Servicing Related Assets		Residential Securities and Loans
Excess MSRs	Servicer Advances	Real Estate Securities