

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

FORM 10-Q

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

For the quarterly period ended June 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: 001-31458

**Newcastle Investment Corp.**

(Exact name of registrant as specified in its charter)

Maryland

81-0559116

(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)798-6100

(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 S 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).

S Yes 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 S 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 S

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: 351,725,561 shares outstanding as of July 28, 2014.**

## CAUTIONARY NOTE REGARDING FORWARD LOOKING STATEMENTS

This report contains certain “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements relate to, among other things, the operating performance of our investments, the stability of our earnings, and our financing needs. 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 similar words or expressions. Forward-looking statements are based on certain assumptions, discuss future expectations, describe future plans and strategies, contain projections of results of operations or of 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:

- changes in global, national and local economic conditions, including, but not limited to, a prolonged economic slowdown and a downturn in the real estate market;
- reductions in cash flows received from our investments;
- the availability and cost of capital for future investments, particularly in a rising interest rate environment, and our ability to deploy capital accretively;
- our ability to profit from opportunistic investments, such as our investment in golf, and to mitigate the risks associated with managing operating businesses and asset classes with which we have limited experience;
- the relationship between yields on assets which are paid off and yields on assets in which such monies can be reinvested;
- changes in our asset portfolio and investment strategy as a result of a spin-off of our senior housing business or other factors;
- adverse changes in the financing markets we access affecting our ability to finance our investments;
- 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 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;
- the risks that default and recovery rates on our real estate securities and loan portfolios deteriorate compared to our underwriting estimates;
- 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, loans or real estate are temporary or not and whether circumstances bearing on the value of such assets warrant changes in carrying values;
- our dependence on our property managers and tenants in our senior housing business;
- the ability of our property managers and tenants to comply with laws, rules and regulations in the operation of our properties, to maintain and improve our properties, to deliver high quality services, to attract and retain qualified personnel and to attract residents;
- increases in costs at our senior housing properties (including, but not limited to, the costs of labor, supplies, insurance and property taxes);
- geographical concentrations with respect to the mortgage loans underlying and collateral securing certain of our debt investments, our senior housing properties and our golf properties;
- legislative/regulatory changes, including but not limited to, any modification of the terms of loans or changes in the healthcare industry;
- competition within the finance, real estate, senior housing industries, as well as other industries, such as the golf industry, in which we have and/or may pursue additional investments;
- the impact of litigation or any financial, accounting, legal or regulatory issues that may affect us or our property managers and tenants;
- our ability and willingness to maintain our qualification as a REIT;
- and
- other risks detailed from time to time below, particularly under the heading “Risk Factors,” and in our other reports filed with or furnished to the Securities and Exchange Commission (the “SEC”).

Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. The factors noted above could cause our actual results to differ significantly from those contained in any forward-looking statement.

Readers are cautioned not to place undue reliance on any of these forward-looking statements, which reflect our management’s views only as of the date of this report. We are under no duty to update any of the forward-looking statements after the date of this report to conform these statements to actual results.

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## 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 Newcastle Investment Corp. (the “Company”) or 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 prove 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>.

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.

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NEWCASTLE INVESTMENT CORP.  
FORM 10-Q

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NEWCASTLE INVESTMENT CORP. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(dollars in thousands, except share data)

	June 30, 2014 (Unaudited)	December 31, 2013
<b>Assets</b>		
Real estate securities, available-for-sale	\$ 311,268	\$ 984,263
Real estate related and other loans, held-for-sale, net	289,112	437,530
Residential mortgage loans, held-for-investment, net	—	255,450
Residential mortgage loans, held-for-sale, net	32,083	2,185
Subprime mortgage loans subject to call option	406,217	406,217
Investments in senior housing real estate, net of accumulated depreciation	1,547,409	1,362,900
Investments in other real estate, net of accumulated depreciation	263,500	265,495
Intangibles, net of accumulated amortization	197,129	199,725
Other investments	26,123	25,468
Cash and cash equivalents	77,922	74,133
Restricted cash	3,703	5,889
Receivables and other assets	109,538	141,887
Assets of discontinued operations	—	690,746
<b>Total Assets</b>	<b>\$ 3,264,004</b>	<b>\$ 4,851,888</b>
<b>Liabilities and Equity</b>		
<b>Liabilities</b>		
CDO bonds payable	\$ 263,581	\$ 544,525
Other bonds and notes payable	82,053	230,279
Repurchase agreements	102,677	556,347
Mortgage notes payable	1,104,182	1,076,828
Credit facilities and obligations under capital leases, golf	156,578	152,498
Financing of subprime mortgage loans subject to call option	406,217	406,217
Junior subordinated notes payable	51,234	51,237
Dividends payable	36,101	36,075
Accounts payable, accrued expenses and other liabilities	269,778	276,491
Liabilities of discontinued operations	—	295,267
<b>Total Liabilities</b>	<b>\$ 2,472,401</b>	<b>\$ 3,625,764</b>
<b>Equity</b>		
Preferred stock, \$0.01 par value, 100,000,000 shares authorized, 1,347,321 shares of 9.75% Series B Cumulative Redeemable Preferred Stock, 496,000 shares of 8.05% Series C Cumulative Redeemable Preferred Stock, and 620,000 shares of 8.375% Series D Cumulative Redeemable Preferred Stock, liquidation preference \$25.00 per share, issued and outstanding as of June 30, 2014 and December 31, 2013	\$ 61,583	\$ 61,583
Common stock, \$0.01 par value, 1,000,000,000 shares authorized, 351,709,903 and 351,453,495 shares issued and outstanding, at June 30, 2014 and December 31, 2013, respectively	3,518	3,515
Additional paid-in capital	2,971,223	2,970,786
Accumulated deficit	(2,313,799)	(1,947,913)
Accumulated other comprehensive income	68,880	76,874
Total Newcastle Stockholders' Equity	791,405	1,164,845
Noncontrolling interests	198	61,279
<b>Total Equity</b>	<b>\$ 791,603</b>	<b>\$ 1,226,124</b>
<b>Total Liabilities and Equity</b>	<b>\$ 3,264,004</b>	<b>\$ 4,851,888</b>

Statement continues on the next page.

NEWCASTLE INVESTMENT CORP. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(dollars in thousands, except share data)

The following table presents certain assets of consolidated variable interest entities (“VIEs”), which are included in the Consolidated Balance Sheets above. The assets in the table below include those assets that can only be used to settle obligations of consolidated VIEs, and are in excess of those obligations. Additionally, the assets in the table below exclude intercompany balances that eliminate in consolidation.

	<b>June 30, 2014</b>	<b>December 31, 2013</b>
	<b>(Unaudited)</b>	
<b>Assets of consolidated VIEs that can only be used to settle obligations of consolidated VIEs</b>		
Real estate securities, available-for-sale	\$ 301,357	\$ 426,695
Real estate related and other loans, held-for-sale, net	289,112	437,530
Residential mortgage loans, held-for-sale, net	3,279	223,628
Subprime mortgage loans subject to call option	406,217	406,217
Investments in other real estate, net of accumulated depreciation	6,515	6,597
Other investments	19,805	19,308
Restricted cash	1,151	2,377
Receivables and other assets	3,188	3,727
<b>Total assets of consolidated VIEs that can only be used to settle obligations of consolidated VIEs</b>	<b>\$ 1,030,624</b>	<b>\$ 1,526,079</b>

The following table presents certain liabilities of consolidated VIEs, which are included in the Consolidated Balance Sheets above. The liabilities in the table below include liabilities of consolidated VIEs due to third parties only, and exclude intercompany balances that eliminate in consolidation. The liabilities also exclude amounts where creditors or beneficial interest holders have recourse to the general credit of Newcastle.

	<b>June 30, 2014</b>	<b>December 31, 2013</b>
	<b>(Unaudited)</b>	
<b>Liabilities of consolidated VIEs for which creditors or beneficial interest holders do not have recourse to the general credit of Newcastle</b>		
CDO bonds payable	\$ 263,581	\$ 544,525
Other bonds and notes payable	82,053	230,279
Financing of subprime mortgage loans subject to call option	406,217	406,217
Derivative liabilities	7,345	13,795
Accounts payable, accrued expenses and other liabilities	765	6,766
<b>Total liabilities of consolidated VIEs for which creditors or beneficial interest holders do not have recourse to the general credit of Newcastle</b>	<b>\$ 759,961</b>	<b>\$ 1,201,582</b>

See notes to consolidated financial statements.

NEWCASTLE INVESTMENT CORP. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

(dollars in thousands, except share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Interest income	\$ 29,893	\$ 62,824	\$ 76,345	\$ 124,156
Interest expense	33,905	21,998	69,760	44,708
Net interest income (expense)	(4,012)	40,826	6,585	79,448
<b>Impairment/(Reversal)</b>				
Valuation allowance (reversal) on loans	1,526	(709)	2,772	1,525
Other-than-temporary impairment on securities	—	3,430	—	4,405
Portion of other-than-temporary impairment on securities recognized in other comprehensive income (loss), net of the reversal of other comprehensive loss into net income (loss)	—	480	—	44
Total impairment (reversal)	1,526	3,201	2,772	5,974
Net interest income (expense) after impairment/reversal	(5,538)	37,625	3,813	73,474
<b>Operating Revenues</b>				
Rental income	54,594	11,721	107,484	23,195
Care and ancillary income	5,666	2,292	11,127	4,318
Golf course operations	51,131	—	91,520	—
Sales of food and beverages - golf	19,923	—	33,462	—
Other golf revenue	12,332	—	21,682	—
Total operating revenues	143,646	14,013	265,275	27,513
<b>Other Income</b>				
Gain on settlement of investments, net	40,403	5,066	42,735	5,063
Gain (loss) on extinguishment of debt	(3,410)	—	(3,410)	1,206
Other income, net	4,692	3,024	18,166	7,591
Total other income	41,685	8,090	57,491	13,860
<b>Expenses</b>				
Loan and security servicing expense	408	1,021	1,265	2,055
Property operating expenses	24,280	8,409	48,084	16,772
Operating expenses - golf	65,178	—	123,516	—
Cost of sales - golf	8,807	—	14,763	—
General and administrative expense	9,633	9,938	18,845	14,151
Management fee to affiliate	7,475	8,148	15,512	17,713
Depreciation and amortization	31,031	4,070	61,390	8,149
Total expenses	146,812	31,586	283,375	58,840
Income from continuing operations before income tax	32,981	28,142	43,204	56,007
Income tax expense	540	—	835	—
Income from continuing operations	32,441	28,142	42,369	56,007
Income (loss) from discontinued operations, net of tax	(46)	25,581	(5,351)	35,729
<b>Net Income</b>	<b>32,395</b>	<b>53,723</b>	<b>37,018</b>	<b>91,736</b>
Preferred dividends	(1,395)	(1,395)	(2,790)	(2,790)
Net loss attributable to noncontrolling interests	29	—	690	—
<b>Income Applicable to Common Stockholders</b>	<b>\$ 31,029</b>	<b>\$ 52,328</b>	<b>\$ 34,918</b>	<b>\$ 88,946</b>

Continued on next page.

NEWCASTLE INVESTMENT CORP. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

(dollars in thousands, except share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
<b>Income Per Share of Common Stock</b>				
Basic	\$ 0.09	\$ 0.20	\$ 0.10	\$ 0.36
Diluted	\$ 0.09	\$ 0.20	\$ 0.10	\$ 0.35
<b>Income from continuing operations per share of common stock, after preferred dividends and noncontrolling interests</b>				
Basic	\$ 0.09	\$ 0.10	\$ 0.11	\$ 0.22
Diluted	\$ 0.09	\$ 0.10	\$ 0.11	\$ 0.21
<b>Income (loss) from discontinued operations per share of common stock</b>				
Basic	\$ —	\$ 0.10	\$ (0.02)	\$ 0.14
Diluted	\$ —	\$ 0.10	\$ (0.02)	\$ 0.14
<b>Weighted Average Number of Shares of Common Stock Outstanding</b>				
Basic	351,598,001	259,228,343	351,526,147	247,249,101
Diluted	362,860,506	265,396,219	362,963,068	252,807,613
<b>Dividends Declared per Share of Common Stock</b>	\$ 0.10	\$ 0.17	\$ 0.20	\$ 0.39

See notes to consolidated financial statements.

NEWCASTLE INVESTMENT CORP. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)

(dollars in thousands, except share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Net income	\$ 32,395	\$ 53,723	\$ 37,018	\$ 91,736
Other comprehensive income (loss):				
Net unrealized gain on securities	3,889	9,823	8,477	39,277
Reclassification of net realized (gain) loss on securities into earnings	(15,698)	(707)	(18,032)	(168)
Net unrecognized gain and pension prior service cost (discontinued operations)	—	—	9	—
Net unrealized gain on derivatives designated as cash flow hedges	583	1,771	1,786	3,612
Reclassification of net realized (gain) loss on derivatives designated as cash flow hedges into earnings	246	(1)	233	(1)
Other comprehensive income	(10,980)	10,886	(7,527)	42,720
Total comprehensive income	\$ 21,415	\$ 64,609	\$ 29,491	\$ 134,456
Comprehensive income attributable to Newcastle stockholders' equity	\$ 21,444	\$ 64,609	\$ 30,181	\$ 134,456
Comprehensive loss attributable to noncontrolling interests	\$ (29)	\$ —	\$ (690)	\$ —

See notes to consolidated financial statements.

NEWCASTLE INVESTMENT CORP. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF EQUITY (Unaudited)

FOR THE SIX MONTHS ENDED JUNE 30, 2014

(dollars in thousands, except share data)

	Newcastle Stockholders							Total Newcastle Stockholders' Equity	Noncontrolling Interests	Total Equity (Deficit)
	Preferred Stock		Common Stock		Additional Paid- in Capital	Accumulated Deficit	Accumulated Other Comp. Income (Loss)			
	Shares	Amount	Shares	Amount						
<b>Equity - December 31, 2013</b>	2,463,321	\$ 61,583	351,453,495	\$ 3,515	\$ 2,970,786	\$ (1,947,913)	\$ 76,874	\$ 1,164,845	\$ 61,279	\$ 1,226,124
Dividends declared	—	—	—	—	—	(73,105)	—	(73,105)	—	(73,105)
Issuance of common stock (options and directors)	—	—	256,408	3	437	—	—	440	—	440
Spin-off of New Media	—	—	—	—	—	(330,489)	(467)	(330,956)	(60,391)	(391,347)
Comprehensive income (loss)										
Net income (loss)	—	—	—	—	—	37,708	—	37,708	(690)	37,018
Other comprehensive income	—	—	—	—	—	—	(7,527)	(7,527)	—	(7,527)
Total comprehensive income (loss)								30,181	(690)	29,491
<b>Equity - June 30, 2014</b>	<u>2,463,321</u>	<u>\$ 61,583</u>	<u>351,709,903</u>	<u>\$ 3,518</u>	<u>\$ 2,971,223</u>	<u>\$ (2,313,799)</u>	<u>\$ 68,880</u>	<u>\$ 791,405</u>	<u>\$ 198</u>	<u>\$ 791,603</u>

See notes to consolidated financial statements

NEWCASTLE INVESTMENT CORP. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

(dollars in thousands, except share data)

	Six Months Ended June 30,	
	2014	2013
<b>Cash Flows From Operating Activities</b>		
Net income	\$ 37,018	\$ 91,736
Adjustments to reconcile net income to net cash provided by operating activities (inclusive of amounts related to discontinued operations):		
Depreciation and amortization	65,986	8,149
Accretion of discount and other amortization	(10,074)	(22,426)
Interest income in CDOs redirected for reinvestment or CDO bond paydown	(949)	(817)
Interest income on investments accrued to principal balance	(11,274)	(12,673)
Interest expense on debt accrued to principal balance	220	219
Non-cash directors' compensation	200	275
Valuation allowance on loans	2,772	1,525
Other-than-temporary impairment on securities	—	4,449
Change in fair value of investments in excess mortgage servicing rights	—	(3,894)
Change in fair value of investments in equity method investees	—	(19,170)
Straight-lining of rental income	(12,138)	—
Equity in earnings from equity method investments	(289)	—
Distributions of earnings from equity method investees	—	1,069
(Gain)/loss on settlement of investments (net)	(42,735)	(5,063)
Unrealized gain on non-hedge derivatives and hedge ineffectiveness	(16,862)	(5,409)
(Gain)/loss on extinguishment of debt	3,410	(1,206)
Change in:		
Restricted cash	2,890	3,036
Receivables and other assets	6,572	580
Accounts payable, accrued expenses and other liabilities	(8,523)	367
Payment of deferred interest	—	(648)
Deferred interest received	—	5,125
Net cash provided by operating activities	16,224	45,224
<b>Cash Flows From Investing Activities</b>		
Principal repayments from repurchased CDO debt	26,567	75,903
Principal repayments from CDO securities	12,997	1,781
Principal repayments from non-Agency RMBS	119	25,178
Return of investments in excess mortgage servicing rights	—	15,803
Principal repayments from loans and non-CDO securities (excluding non-Agency RMBS)	33,234	146,401
Principal repayment from security accounted for as a linked transaction	116,806	—
Purchase of real estate securities	—	(1,034,234)
Purchase of securities accounted for as linked transactions	—	(103,140)
Purchase of real estate related and other loans	—	(174,234)
Proceeds from sale of investments	763,336	37,905
Acquisition of investments in real estate	(227,535)	—
Additions to investments in real estate	(9,662)	(834)
Contributions to equity method investees	—	(386,502)
Distributions of capital from equity method investees	—	12,134
Deposits paid on investments	(650)	(5,520)
Net cash provided by (used in) investing activities	715,212	(1,389,359)

Continued on next page

NEWCASTLE INVESTMENT CORP. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

(dollars in thousands, except share data)

	Six Months Ended June 30,	
	2014	2013
<b>Cash Flows From Financing Activities</b>		
Repurchases of CDO bonds payable	\$ —	\$ (9,722)
Repayments of other bonds and notes payable	(168,111)	(20,157)
Borrowings under repurchase agreements	64,925	2,004,020
Borrowings under repurchase agreements accounted for as linked transactions	5,283	59,968
Repayments of repurchase agreements	(518,595)	(1,301,819)
Repayments under repurchase agreements accounted for as linked transactions	(65,929)	—
Repayments of credit facilities, media and golf	(4,423)	—
Repayments of capital lease liabilities	(17)	—
Margin deposits under repurchase agreements	(12,277)	(152,725)
Return of margin deposits under repurchase agreements	12,277	120,225
Borrowings under mortgage notes payable	32,857	—
Repayment of mortgage notes payable	(6,272)	—
Issuance of common stock	240	962,827
Costs related to issuance of common stock	—	(1,302)
New Media and New Residential spin-offs	(23,845)	(181,582)
Common stock dividends paid	(70,290)	(93,619)
Preferred stock dividends paid	(2,790)	(2,790)
Payment of financing costs	(2,491)	(35)
Net cash provided by (used in) financing activities	(759,458)	1,383,289
<b>Net Increase in Cash and Cash Equivalents</b>	(28,022)	39,154
<b>Cash and Cash Equivalents of Continuing Operations, Beginning of Period</b>	74,133	231,898
<b>Cash and Cash Equivalents of Discontinued Operations, Beginning of Period</b>	31,811	—
<b>Cash and Cash Equivalents, End of Period</b>	\$ 77,922	\$ 271,052
<b>Supplemental Disclosure of Cash Flow Information</b>		
Cash paid during the period for income taxes	\$ 1,153	\$ —
Cash paid during the period for interest expense	\$ 39,409	\$ 25,592
<b>Supplemental Schedule of Non-Cash Investing and Financing Activities</b>		
Preferred stock dividends declared but not paid	\$ 930	\$ 930
Common stock dividends declared but not paid	\$ 35,171	\$ 43,021
<b>Reduction of Assets and Liabilities relating to the spin-off of New Media</b>		
Property, plant and equipment, net	\$ 266,385	\$ —
Goodwill and intangibles, net	\$ 271,350	\$ —
Restricted cash	\$ 6,477	\$ —
Receivables and other assets	\$ 101,940	\$ —
Credit facilities, media	\$ 177,955	\$ —
Accounts payable, accrued expenses and other liabilities	\$ 100,695	\$ —
<b>Reduction of Assets and Liabilities relating to the spin-off of New Residential</b>		
Real estate securities, available for sale	\$ —	\$ 1,647,289
Residential mortgage loans, held-for-investment, net	\$ —	\$ 35,865
Investments in excess mortgage servicing rights at fair value	\$ —	\$ 229,936
Investments in equity method investees	\$ —	\$ 392,469
Receivables and other assets	\$ —	\$ 37,844
Repurchase agreements	\$ —	\$ 1,320,360
Accounts payable, accrued expenses and other liabilities	\$ —	\$ 642

See notes to consolidated financial statements

**NEWCASTLE INVESTMENT CORP. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)**

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(dollars in tables in thousands, except share data)

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**1. GENERAL**

Newcastle Investment Corp. (and its subsidiaries, "Newcastle") is a Maryland corporation that was formed in 2002. Newcastle focuses on opportunistically investing in, and actively managing, a variety of real estate-related and other investments. Newcastle is organized and conducts its operations to qualify as a real estate investment trust ("REIT") for U.S. federal income tax purposes. As such, Newcastle 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. Newcastle's common stock is traded on the New York Stock Exchange under the symbol "NCT".

On February 13, 2014, Newcastle completed the spin-off of New Media Investment Group Inc. ("New Media"), and established New Media as a separate, publicly traded company (NYSE:NEWM). The spin-off was effected as a taxable pro rata distribution by Newcastle of all of the outstanding shares of common stock it held of New Media to Newcastle's common stockholders of record at the close of business on February 6, 2014. The distribution ratio was 0.0722 shares of New Media common stock for each share of Newcastle common stock.

In December 2013, Newcastle restructured an investment in mezzanine debt issued by NGP Mezzanine, LLC ("NGP"), the indirect parent of NGP Realty Sub, L.P. ("National Golf"). National Golf owns 27 golf properties across 8 states, and leases these properties to American Golf Corporation ("American Golf"), an affiliated operating company. American Golf also leases an additional 52 golf properties and manages 11 properties, all owned by third parties. As part of the transaction, Newcastle acquired the equity of NGP and American Golf's indirect parent, AGC Mezzanine Pledge LLC ("AGC"), and therefore is consolidating these entities.

As a result, Newcastle now conducts its business through the following segments: (i) investments in senior housing properties ("senior housing"), (ii) debt investments financed with collateralized debt obligations ("CDOs"), (iii) other debt investments ("other debt"), (iv) investments in golf properties and facilities ("Golf") and (v) corporate. With respect to the CDOs and other debt investments, subject to the passing of certain periodic coverage tests, Newcastle is generally entitled to receive the net cash flows from these structures on a periodic basis.

Newcastle is party to a management agreement (the "Management Agreement") with FIG LLC (the "Manager"), a subsidiary of Fortress Investment Group LLC ("Fortress"), under which the Manager advises Newcastle on various aspects of its business and manages its day-to-day operations, subject to the supervision of Newcastle's board of directors. For its services, the Manager is entitled to an annual management fee and incentive compensation, both as defined in, and in accordance with the terms of, the Management Agreement.

Newcastle either leases senior housing properties under triple net leases or has its senior housing properties managed pursuant to property management agreements (the "Senior Housing Management Agreements") with third parties (collectively, the "Senior Housing Managers"). Currently, the Senior Housing Managers are affiliates or subsidiaries of either Holiday Acquisition Holdings LLC ("Holiday"), a portfolio company that is majority owned by private equity funds managed by an affiliate of Newcastle's Manager, or FHC Property Management LLC (together with its subsidiaries, "Blue Harbor"), an affiliate of Newcastle's Manager.

On June 16, 2014, Newcastle announced that its board of directors unanimously approved a plan to spin off its senior housing business. Newcastle intends to effect the spin-off by distributing shares of its subsidiary, New Senior Investment Group Inc. ("New Senior", NYSE: SNR). New Senior will be a publicly traded REIT that primarily targets senior housing related investments. New Senior has filed a registration statement with the SEC with respect to the planned spin-off. The spin-off is subject to certain conditions, such as the SEC declaring effective New Senior's registration statement, the filing and approval of an application to list New Senior's common stock on the NYSE and the formal declaration of the distribution by the board of directors.

Approximately 6.4 million shares of Newcastle's common stock were held by Fortress, through its affiliates, and its principals as of June 30, 2014. In addition, Fortress, through its affiliates, held options to purchase approximately 25.5 million shares of Newcastle's common stock as of June 30, 2014.

**NEWCASTLE INVESTMENT CORP. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)**

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A principal of the Manager owned or leased aircraft that Newcastle chartered from a third-party aircraft operator for business purposes in the course of operations. Newcastle paid market rates for the charters. The operators remitted a portion of these amounts to the principal. These amounts totaled less than \$0.1 million for the six months ended June 30, 2014 and 2013.

The accompanying consolidated financial statements and related notes of Newcastle 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 ("GAAP") have been condensed or omitted. In the opinion of management, all adjustments considered necessary for a fair presentation of Newcastle'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 financial statements should be read in conjunction with Newcastle's consolidated financial statements for the year ended December 31, 2013 and notes thereto included in Newcastle's Annual Report on Form 10-K filed with the SEC. Capitalized terms used herein, and not otherwise defined, are defined in Newcastle'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.

***Recently Adopted Accounting Policies***

The following accounting policies have been adopted in connection with Golf.

**REVENUE RECOGNITION**

Revenue from green fees, cart rentals, food and beverage sales, merchandise sales and other income (consisting primarily of range income, banquets, and club and other rental income) are generally recognized at the time of sale, when services are rendered and collection is reasonably assured.

Revenue from membership dues is recognized in the month earned. Membership dues received in advance are included in deferred revenues and recognized as revenue ratably over the appropriate period, which is generally twelve months or less. The monthly dues are generally structured to cover the club operating costs and membership services.

Private country club members generally pay an advance initiation fee upon their acceptance as a member to the country club. Initiation fees at most private clubs are deposits which are generally refundable 30 years after the date of acceptance as a member. Revenue related to membership deposits is recognized over the expected life of an active membership. For membership deposits, the difference between the amount paid by the member and the present value of the refund obligation is deferred and recognized on a straight-line basis over the expected life of an active membership.

The present value of the refund obligation is recorded as a membership deposit liability in the consolidated balance sheets and accretes over the nonrefundable term (30 years) using the effective interest method. This accretion is recorded as interest expense in the consolidated statements of income.

**EXPENSE RECOGNITION**

**Operating Leases and Other Operating Expenses** - Other operating expenses for the Golf business consist primarily of equipment leases, utilities, repairs and maintenance, supplies, seed, soil and fertilizer, and marketing. Many of the golf properties and related facilities are leased under long-term operating leases. In addition to minimum payments, certain leases require payment of the excess of various percentages of gross revenue or net operating income over the minimum rental payments. The leases generally require the payment of taxes assessed against the leased property and the cost of insurance and maintenance. The majority of lease terms range from 10 to 20 years, and typically, the leases contain renewal options. Certain leases include minimum scheduled increases in rental payments at various times during the term of the lease. These scheduled rent increases are recognized on a straight-line basis over the term of the lease, resulting in an accrual, which is included in accounts payable, accrued expenses and other liabilities, for the amount by which the cumulative straight-line rent exceeds the contractual cash rent.

## CAPITAL LEASES

The Golf business leases golf carts and other equipment that are classified as capital leases. The value of capital leases is recorded as an asset on the balance sheet, along with a liability related to the associated payments. Amortization of capital lease assets is

calculated using the straight-line method over the shorter of the estimated useful lives and the initial lease terms. The cost of equipment under capital leases is included in investments in other real estate in the consolidated balance sheets. Payments under the lease are treated as reductions of the liability, with a portion being recorded as interest expense under the effective interest method.

### *Recent Accounting Pronouncements*

In April 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-08, *Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity*. ASU 2014-08 changes the criteria for reporting a discontinued operation. Under the new pronouncement, a disposal of a part of an organization that has a major effect on its operations and financial results is a discontinued operation. This update is effective for Newcastle in the first quarter of 2015. Newcastle is currently evaluating the new guidance to determine the impact it may have to its consolidated financial statements.

In May 2014, the FASB and the International Accounting Standards Board ("IASB") 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 Newcastle in the first quarter of 2017. Early application is not permitted. Entities have the option of using either a full retrospective or a modified approach to adopt the guidance in the ASU. Newcastle 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 Newcastle in the first quarter of 2015. Early application is not permitted. Disclosures are not required for comparative periods presented before the effective date. Newcastle is currently evaluating the new guidance to determine the impact 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, leases, financial instruments and hedging. Some of the proposed changes are significant and could have a material impact on Newcastle's reporting. Newcastle has not yet fully evaluated the potential impact of these proposals, but will make such an evaluation as the standards are finalized.

## 2. ACQUISITIONS

### Acquisitions of Senior Housing properties

i. Managed Properties

In January and May 2014, Newcastle completed the acquisitions of five senior housing properties in three different portfolios for an aggregate purchase price of approximately \$44.5 million plus acquisition-related costs. Each of these acquisitions was accounted for as a business combination, under which all assets acquired and liabilities assumed are recognized at their acquisition-date fair value with acquisition-related costs being expensed as incurred. For two of the properties, Newcastle has retained Holiday to manage the properties. Pursuant to the property management agreements with Holiday, Newcastle pays management fees equal to either (i) 5% of the property's effective gross income (as defined in the agreements) or (ii) 6% of the property's effective gross income (as defined in the agreements) for the first two years and 7% thereafter. For the other three properties acquired, Newcastle has retained Blue Harbor to manage the properties. Pursuant to the agreements with Blue Harbor, Newcastle pays management fees equal to 6% of the property's effective gross income (as defined in the agreements) for the first two years and 7% thereafter. In addition, Newcastle will reimburse Holiday and Blue Harbor for certain expenses, primarily the compensation expense associated with the on-site employees.

ii. Triple Net Lease Properties

On June 30, 2014, Newcastle completed the acquisition of six senior housing properties for an aggregate purchase price of approximately \$183.0 million plus acquisition-related costs. The acquisition was accounted for as a business combination, under which all assets acquired and liabilities assumed are recognized at their acquisition-date fair value with acquisition-related costs being expensed as incurred.

On June 30, 2014, Newcastle also entered into a triple net lease of these properties with a third party (the "June 2014 Master Tenant"). The lease has a 15-year term with two five-year renewal options and first-year rent equal to approximately \$14.2 million with annual increases during each of the following three years of 3.75% and up to 2.5% thereafter. Under the lease, the June 2014 Master Tenant is responsible for (i) operating the properties and bearing the related costs, including maintenance, utilities, taxes, insurance, repairs and capital improvements, and (ii) complying with the terms of the mortgage financing documents.

As part of the June 2014 Master Tenant lease, Newcastle committed to making available \$6.5 million immediately for capital improvements and other repairs in the properties under the lease agreement and also agreed to make available to the June 2014 Master Tenant an additional \$9.0 million at certain intervals during the lease period to be used for further capital improvements. Upon funding the capital improvements, Newcastle will be entitled to a rent increase.

NEWCASTLE INVESTMENT CORP. AND SUBSIDIARIES

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The following table summarizes the allocation of the purchase price to the fair value of identifiable assets acquired and liabilities assumed in connection with the acquisition, in accordance with the acquisition method of accounting:

	Three months ended March 31, 2014 Acquisitions	Three months ended June 30, 2014 Acquisitions(A)		Total
	Managed Properties	Managed Properties	Triple Net Lease Properties	
<u>Allocation of Purchase Price</u>				
Investments in Real Estate	\$ 20,630	\$ 13,785	\$ 167,828	\$ 202,243
Resident Lease Intangibles	2,370	3,361	16,828	22,559
Other Intangibles	—	4,847	—	4,847
Other Liabilities, net of other Assets	(200)	(288)	(1,625)	(2,113)
Total purchase price	\$ 22,800	\$ 21,705	\$ 183,031	\$ 227,536
Mortgage Notes Payable (B)	(17,250)	(15,607)	—	(32,857)
Net assets acquired	\$ 5,550	\$ 6,098	\$ 183,031	\$ 194,679
Total acquisition related costs (C)	\$ 368	\$ 573	\$ 792	\$ 1,733

(A) The values assigned above are not yet finalized as Newcastle is in the process of identifying all acquired intangibles and gathering market and other information with which to determine the fair values of the real estate property and intangible assets acquired. Therefore the purchase price allocations set forth above are preliminary and are subject to change. The final determination of fair values for these assets may result in different allocations among the various asset classes from those set forth above and any such differences could be material.

(B) See Note 10.

(C) Acquisition-related costs are expensed as incurred and included within general and administrative expense on the consolidated statements of income.

NEWCASTLE INVESTMENT CORP. AND SUBSIDIARIES

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**3. SPIN-OFF OF NEW RESIDENTIAL AND NEW MEDIA**

On May 15, 2013, Newcastle completed the spin-off of New Residential from Newcastle.

On February 13, 2014, Newcastle completed the spin-off of New Media from Newcastle.

The following table presents the carrying value of the assets and liabilities of New Media, immediately preceding the February 13, 2014 spin-off.

<b>Assets</b>	
Property, plant and equipment, net	\$ 266,385
Intangibles, net	144,664
Goodwill	126,686
Cash and cash equivalents	23,845
Restricted cash	6,477
Receivables and other assets	101,940
<b>Total Assets</b>	<b>\$ 669,997</b>
<b>Liabilities</b>	
Credit facilities - media	\$ 177,955
Accounts payable, accrued expenses and other liabilities	100,695
<b>Total Liabilities</b>	<b>\$ 278,650</b>
<b>Net Assets</b>	<b>\$ 391,347</b>

As a result of the May 15, 2013 spin-off and the February 13, 2014 spin-off, for all periods presented, the assets, liabilities and results of operations of those components of Newcastle's operations that (i) were part of the spin-off, and (ii) represent operations in which Newcastle has no significant continuing involvement, are presented separately in discontinued operations in Newcastle's consolidated financial statements.

NEWCASTLE INVESTMENT CORP. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

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(dollars in tables in thousands, except share data)

Results from discontinued operations related to New Media and New Residential were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Interest Income	\$ —	\$ 5,060	\$ —	\$ 15,095
Interest Expense	—	—	2,096	—
Net interest income (loss)	—	5,060	(2,096)	15,095
Media income	—	—	68,213	—
Other income (loss)	—	(2)	—	(2)
Change in fair value of investments in excess mortgage servicing rights	—	2,036	—	3,894
Change in fair value of investments in equity method investees	—	(84)	—	885
Earnings from investments in equity method investees	—	18,286	—	18,286
Total other income	—	20,236	—	23,063
Media operating expenses	—	—	65,826	—
Property operating costs	—	5	—	12
General and administrative expenses	—	(290)	1,904	2,417
Depreciation and amortization	—	—	4,596	—
Income tax (benefit) expense	—	—	(915)	—
Total expenses	—	(285)	71,411	2,429
Income (loss) from discontinued operations	\$ —	\$ 25,581	\$ (5,294)	\$ 35,729
Net income attributable to noncontrolling interest	\$ —	\$ —	\$ 522	\$ —

The May 15, 2013 spin-off resulted in a \$1.2 billion reduction in the basis upon which Newcastle's management fees are computed (and an equivalent reduction in the basis upon which the incentive compensation threshold is computed), as well as a reduction in the strike price of Newcastle's then outstanding options (see Note 13).

The February 13, 2014 spin-off resulted in a \$0.4 billion reduction in the basis upon which Newcastle's management fees are computed (and an equivalent reduction in the basis upon which the incentive compensation threshold is computed), as well as a reduction in the strike price of Newcastle's then outstanding options (see Note 13).

4. SEGMENT REPORTING AND VARIABLE INTEREST ENTITIES

Newcastle conducts its business through the following segments: (i) investments in senior housing properties ("senior housing"), (ii) debt investments financed with collateralized debt obligations ("CDOs"), (iii) other debt investments ("other debt"), (iv) investment in golf properties and facilities ("golf") and (v) corporate. With respect to the CDOs and other debt segments, Newcastle is generally entitled to receive net cash flows from these structures on a periodic basis.

The corporate segment consists primarily of interest income on short term investments, general and administrative expenses, interest expense on the junior subordinated notes payable and management fees pursuant to the Management Agreement.

NEWCASTLE INVESTMENT CORP. AND SUBSIDIARIES

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

	Senior	Debt Investments (A)		Golf	Corporate	Discontinued	Total
	Housing (A)	CDOs	Other Debt (B)				
<b>Six Months Ended June 30, 2014</b>							
Interest income	\$ —	\$ 51,319	\$ 29,353	\$ 74	\$ 35	\$ —	\$ 80,781
Inter-segment elimination	—	(4,436)	—	—	—	—	(4,436)
Interest income, net	—	46,883	29,353	74	35	—	76,345
Interest expense	27,294	12,109	23,001	9,884	1,908	—	74,196
Inter-segment elimination	—	—	(1,635)	(2,801)	—	—	(4,436)
Interest expense, net	27,294	12,109	21,366	7,083	1,908	—	69,760
<b>Net interest income (expense)</b>	<b>(27,294)</b>	<b>34,774</b>	<b>7,987</b>	<b>(7,009)</b>	<b>(1,873)</b>	<b>—</b>	<b>6,585</b>
Impairment (reversal)	—	1,958	814	—	—	—	2,772
Operating revenues	117,508	—	1,104	146,663	—	—	265,275
Other income (loss)	(23)	32,895	24,630	(11)	—	—	57,491
Loan and security servicing expense	—	310	955	—	—	—	1,265
Property operating expenses	47,573	—	511	—	—	—	48,084
Operating expenses - golf (C)	—	—	—	118,914	—	—	118,914
Repairs and maintenance expenses - golf	—	—	—	4,602	—	—	4,602
Cost of sales - golf	—	—	—	14,763	—	—	14,763
General and administrative expense	1,701	—	1,874	459	3,725	—	7,759
Acquisition and transaction expenses	8,808	—	—	1,503	775	—	11,086
Management fee to affiliate	4,323	—	—	—	11,189	—	15,512
Depreciation and amortization	46,024	—	113	15,179	74	—	61,390
Income tax expense	691	—	—	144	—	—	835
Income (loss) from continuing operations	(18,929)	65,401	29,454	(15,921)	(17,636)	—	42,369
Income (loss) from discontinued operations, net of tax	—	—	—	—	—	(5,351)	(5,351)
Net income (loss)	(18,929)	65,401	29,454	(15,921)	(17,636)	(5,351)	37,018
Preferred dividends	—	—	—	—	(2,790)	—	(2,790)
Net loss attributable to noncontrolling interests	—	—	—	168	—	522	690
Income (loss) applicable to common stockholders	\$ (18,929)	\$ 65,401	\$ 29,454	\$ (15,753)	\$ (20,426)	\$ (4,829)	\$ 34,918

NEWCASTLE INVESTMENT CORP. AND SUBSIDIARIES

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	Senior Housing (A)	Debt Investments (A)		Golf	Corporate	Discontinued Operations	Total
		CDOs	Other Debt (B)				
<b>Three Months Ended June 30, 2014</b>							
Interest income	\$ —	\$ 20,596	\$ 12,401	\$ 34	\$ 25	\$ —	\$ 33,056
Inter-segment elimination	—	(3,163)	—	—	—	—	(3,163)
Interest income, net	—	17,433	12,401	34	25	—	29,893
Interest expense	13,592	5,983	10,338	6,202	953	—	37,068
Inter-segment elimination	—	—	(362)	(2,801)	—	—	(3,163)
Interest expense, net	13,592	5,983	9,976	3,401	953	—	33,905
<b>Net interest income (expense)</b>	<b>(13,592)</b>	<b>11,450</b>	<b>2,425</b>	<b>(3,367)</b>	<b>(928)</b>	<b>—</b>	<b>(4,012)</b>
Impairment (reversal)	—	1,526	—	—	—	—	1,526
Operating revenues	59,698	—	563	83,385	—	—	143,646
Other income (loss)	(22)	19,343	22,375	(11)	—	—	41,685
Loan and security servicing expense	—	154	254	—	—	—	408
Property operating expenses	24,053	—	227	—	—	—	24,280
Operating expenses - golf (C)	—	—	—	63,094	—	—	63,094
Repairs and maintenance expenses - golf	—	—	—	2,084	—	—	2,084
Cost of sales - golf	—	—	—	8,807	—	—	8,807
General and administrative expense	1,493	—	1,874	153	1,629	—	5,149
Acquisition and transaction expenses	3,368	—	—	728	388	—	4,484
Management fee to affiliate	2,179	—	—	—	5,296	—	7,475
Depreciation and amortization	23,188	—	57	7,749	37	—	31,031
Income tax expense	536	—	—	4	—	—	540
Income (loss) from continuing operations	(8,733)	29,113	22,951	(2,612)	(8,278)	—	32,441
Income (loss) from discontinued operations, net of tax	—	—	—	—	—	(46)	(46)
Net income (loss)	(8,733)	29,113	22,951	(2,612)	(8,278)	(46)	32,395
Preferred dividends	—	—	—	—	(1,395)	—	(1,395)
Net loss attributable to noncontrolling interests	—	—	—	29	—	—	29
Income (loss) applicable to common stockholders	\$ (8,733)	\$ 29,113	\$ 22,951	\$ (2,583)	\$ (9,673)	\$ (46)	\$ 31,029

NEWCASTLE INVESTMENT CORP. AND SUBSIDIARIES

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	Senior Housing (A)	Debt Investments (A)		Golf	Corporate	Discontinued Operations	Total
		CDOs	Other Debt (B)				
<b>June 30, 2014</b>							
Investments	\$ 1,651,251	\$ 651,765	\$ 457,766	\$ 350,272	\$ —	\$ —	\$ 3,111,054
Inter-segment elimination	—	(38,213)	—	—	—	—	(38,213)
Investments, net	1,651,251	613,552	457,766	350,272	—	—	3,072,841
Cash and restricted cash	47,539	1,118	489	9,526	22,953	—	81,625
Other assets	71,111	1,959	1,250	35,113	105	—	109,538
Total assets	1,769,901	616,629	459,505	394,911	23,058	—	3,264,004
Debt	1,104,182	425,346	435,182	188,791	51,234	—	2,204,735
Inter-segment elimination	—	—	(6,000)	(32,213)	—	—	(38,213)
Debt, net	1,104,182	425,346	429,182	156,578	51,234	—	2,166,522
Other liabilities	79,577	7,671	1,261	175,453	41,917	—	305,879
Total liabilities	1,183,759	433,017	430,443	332,031	93,151	—	2,472,401
Preferred stock	—	—	—	—	61,583	—	61,583
Noncontrolling interests	—	—	—	198	—	—	198
GAAP book value	\$ 586,142	\$ 183,612	\$ 29,062	\$ 62,682	\$ (131,676)	\$ —	\$ 729,822
<b>Additions to investments in real estate</b>	\$ 206,181	\$ —	\$ 32	\$ 9,670	\$ —	\$ —	\$ 215,883

NEWCASTLE INVESTMENT CORP. AND SUBSIDIARIES

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	Senior	Debt Investments (A)		Golf	Corporate	Discontinued	Total
	Housing (A)	CDOs	Other Debt (B)				
<b>Six Months Ended June 30, 2013</b>							
Interest income	\$ —	\$ 68,553	\$ 57,432	\$ —	\$ 102	\$ —	\$ 126,087
Inter-segment elimination	—	(1,931)	—	—	—	—	(1,931)
Interest income, net	—	66,622	57,432	—	102	—	124,156
Interest expense	2,478	13,962	28,293	—	1,906	—	46,639
Inter-segment elimination	—	—	(1,931)	—	—	—	(1,931)
Interest expense, net	2,478	13,962	26,362	—	1,906	—	44,708
Net interest income (expense)	(2,478)	52,660	31,070	—	(1,804)	—	79,448
Impairment (reversal)	—	11,986	(6,012)	—	—	—	5,974
Operating revenues	26,510	—	1,003	—	—	—	27,513
Other income (loss)	120	11,820	1,920	—	—	—	13,860
Loan and security servicing expense	—	384	1,671	—	—	—	2,055
Property operating expenses	16,285	—	487	—	—	—	16,772
General and administrative expense	3,496	—	24	—	10,631	—	14,151
Management fee to affiliate	1,578	—	—	—	16,135	—	17,713
Depreciation and amortization	8,039	—	110	—	—	—	8,149
Income (loss) from continuing operations	(5,246)	52,110	37,713	—	(28,570)	—	56,007
Income (loss) from discontinued operations	—	—	—	—	—	35,729	35,729
Net income (loss)	(5,246)	52,110	37,713	—	(28,570)	35,729	91,736
Preferred dividends	—	—	—	—	(2,790)	—	(2,790)
Income (loss) applicable to common stockholders	\$ (5,246)	\$ 52,110	\$ 37,713	\$ —	\$ (31,360)	\$ 35,729	\$ 88,946

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	Senior	Debt Investments (A)		Golf	Corporate	Discontinued	Total
	Housing (A)	CDOs	Other Debt (B)				
<b>Three Months Ended June 30, 2013</b>							
Interest income		36,724	\$ 27,134	—	\$ 30	—	63,888
Inter-segment elimination	—	(1,064)	—	—	—	—	(1,064)
Interest income, net	—	35,660	27,134	—	30	—	62,824
Interest expense	1,246	6,826	14,036	—	954	—	23,062
Inter-segment elimination	—	—	(1,064)	—	—	—	(1,064)
Interest expense, net	1,246	6,826	12,972	—	954	—	21,998
Net interest income (expense)	(1,246)	28,834	14,162	—	(924)	—	40,826
Impairment (reversal)	—	8,803	(5,602)	—	—	—	3,201
Operating revenues	13,513	—	500	—	—	—	14,013
Other income (loss)	112	7,249	729	—	—	—	8,090
Loan and security servicing expense	—	188	833	—	—	—	1,021
Property operating expenses	8,169	—	240	—	—	—	8,409
General and administrative expense	1,887	—	8	—	8,043	—	9,938
Management fee to affiliate	799	—	—	—	7,349	—	8,148
Depreciation and amortization	4,016	—	54	—	—	—	4,070
Income (loss) from continuing operations	(2,492)	27,092	19,858	—	(16,316)	—	28,142
Income (loss) from discontinued operations	—	—	—	—	—	25,581	25,581
Net income (loss)	(2,492)	27,092	19,858	—	(16,316)	25,581	53,723
Preferred dividends	—	—	—	—	(1,395)	—	(1,395)
Income (loss) applicable to common stockholders	\$ (2,492)	\$ 27,092	\$ 19,858	\$ —	\$ (17,711)	\$ 25,581	\$ 52,328

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(A) Assets held within non-recourse structures, including all of the assets in the senior housing and CDO segments, are not available to satisfy obligations outside of such financings, except to the extent net cash flow distributions are received from such structures. Furthermore, creditors or beneficial interest holders of these structures generally have no recourse to the general credit of Newcastle. Therefore, the exposure to the economic losses from such structures generally is limited to invested equity in them and economically their book value cannot be less than zero. Therefore, impairment recorded in excess of Newcastle's investment, which results in negative GAAP book value for a given non-recourse financing structure, cannot economically be incurred and will eventually be reversed through amortization, sales at gains, or as gains at the deconsolidation or termination of such non-recourse financing structure.

(B) The following table summarizes the investments and debt in the other debt segment:

	June 30, 2014			
	Investments		Debt	
	Outstanding Face Amount	Carrying Value	Outstanding Face Amount*	Carrying Value*
<b>Non-Recourse</b>				
Subprime mortgage loans subject to call options	\$ 406,217	\$ 406,217	\$ 406,217	\$ 406,217
Operating real estate	N/A	6,515	6,000	6,000
<b>Subtotal</b>	<b>406,217</b>	<b>412,732</b>	<b>412,217</b>	<b>412,217</b>
<b>Other</b>				
Unlevered real estate securities	168,201	9,912	—	—
Other investments	N/A	6,319	—	—
Residential mortgage loans	39,785	28,803	22,965	22,965
	<u>\$ 614,203</u>	<u>\$ 457,766</u>	<u>\$ 435,182</u>	<u>\$ 435,182</u>

\* An aggregate face amount of \$6.0 million (carrying value of \$6.0 million) of debt represents intersegment financing, which is eliminated upon consolidation.

(C) Operating expenses-golf includes rental expenses recorded under operating leases for carts and equipment in the amount of \$1.4 million and \$2.7 million for the three and six months ended June 30, 2014, respectively.

**Variable Interest Entities ("VIEs")**

The VIEs in which Newcastle has a significant interest include Newcastle's CDOs, in which Newcastle has been determined to be the primary beneficiary and therefore consolidates them (with the exception of CDO V), since it has the power to direct the activities that most significantly impact the CDOs' economic performance and would absorb a significant portion of their expected losses and receive a significant portion of their expected residual returns. Newcastle's CDOs are held in special purpose entities whose debt is treated as non-recourse secured borrowings of Newcastle.

Newcastle's subprime securitizations and CDO V are also considered VIEs, but Newcastle does not control the decisions that most significantly impact their economic performance and, no longer receives a significant portion of their returns, and therefore does not consolidate them.

In addition, Newcastle's investments in RMBS, commercial mortgage backed securities ("CMBS"), CDO securities and real estate related and other loans may be deemed to be variable interests in VIEs, depending on their structure. Newcastle monitors these investments and analyzes the potential need to consolidate the related securitization entities pursuant to the VIE consolidation requirements. These analyses require considerable judgment in determining whether an entity is a VIE and determining the primary beneficiary of a VIE since they involve subjective determinations of significance, with respect to both power and economics. The result could be the consolidation of an entity that otherwise would not have been consolidated or the deconsolidation of an entity that otherwise would have been consolidated.

As of June 30, 2014, Newcastle has not consolidated these potential VIEs. This determination is based, in part, on the assessment that Newcastle does not have the power to direct the activities that most significantly impact the economic performance of these entities, such as if Newcastle owned a majority of the currently controlling class. In addition, Newcastle is not obligated to provide, and has not provided, any financial support to these entities.

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Newcastle had variable interests in the following unconsolidated VIEs at June 30, 2014, in addition to the subprime securitizations which are described in Note 6:

Entity	Gross Assets (A)	Debt (A) (B)	Carrying Value of Newcastle's Investment (C)
Newcastle CDO V	\$ 143,578	\$ 170,874	\$ 5,973

(A) Face amount.

(B) Newcastle CDO V includes \$40.8 million face amount of debt owned by Newcastle with a carrying value of \$6.0 million at June 30, 2014.

(C) This amount represents Newcastle's maximum exposure to loss from this entity.

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5. REAL ESTATE SECURITIES

The following is a summary of Newcastle's real estate securities at June 30, 2014, all of which are classified as available-for-sale and are, therefore, reported at fair value with changes in fair value recorded in other comprehensive income, except for securities that are other-than-temporarily impaired.

Asset Type	Outstanding Face Amount	Amortized Cost Basis			Gross Unrealized		Carrying Value (A)	Number of Securities	Weighted Average				
		Before Impairment	Other-Than-Temporary Impairment	After Impairment	Gains	Losses			Rating (B)	Coupon	Yield	Life (Years) (C)	Principal Subordination (D)
CMBS-Conduit	\$ 160,893	\$ 163,393	\$ (68,980)	\$ 94,413	\$ 38,892	\$ —	\$ 133,305	27	B+	5.53%	24.26%	2.1	10.6%
CMBS- Single Borrower	79,490	79,103	(12,364)	66,739	4,092	(5)	70,826	12	BB-	6.33%	7.55%	2.2	2.3%
CMBS-Large Loan	3,229	3,229	—	3,229	—	—	3,229	1	BBB-	3.20%	3.20%	0.1	4.4%
REIT Debt	29,200	28,791	—	28,791	1,892	—	30,683	5	BB+	5.89%	6.88%	1.1	N/A
Non-Agency RMBS	90,781	98,862	(59,987)	38,875	21,633	—	60,508	33	CCC+	1.03%	14.12%	4.3	26.4%
ABS-Franchise	8,464	7,647	(7,647)	—	—	—	—	1	C	6.69%	0.00%	—	0.0%
CDO (E)	17,063	6,368	—	6,368	6,349	—	12,717	2	B	0.83%	10.00%	8.7	33.0%
Total / Average (F)	\$ 389,120	\$ 387,393	\$ (148,978)	\$ 238,415	\$ 72,858	\$ (5)	\$ 311,268	81	B	4.47%	15.16%	2.8	

(A) See Note 12 regarding the estimation of fair value, which is equal to carrying value for all securities.

(B) Represents the weighted average of the ratings of all securities in each asset type, expressed as an S&P equivalent rating. For each security rated by multiple rating agencies, the lowest rating is used. Ratings provided were determined by third party rating agencies, represent the most recent credit ratings available as of the reporting date and may not be current.

(C) The weighted average life is based on the timing of expected principal reduction on the assets.

(D) Percentage of the outstanding face amount of securities and residual interests that is subordinate to Newcastle's investments.

(E) Represents non-consolidated CDO securities, excluding nine securities with a zero value, which had an aggregate face amount of \$116.1 million.

(F) The total outstanding face amount was \$265.7 million for fixed rate securities and \$123.4 million for floating rate securities.

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Unrealized losses that are considered other-than-temporary are recognized currently in earnings. During the six months ended June 30, 2014, Newcastle recorded no other-than-temporary impairment charges (“OTTI”) with respect to real estate securities. Based on management’s analysis of the securities, the performance of the underlying loans and changes in market factors, Newcastle noted no adverse changes in the expected cash flows on certain of these securities. Unrealized losses on Newcastle’s securities were primarily the result of changes in market factors, rather than issue-specific credit impairment. Newcastle performed analyses in relation to such securities, using management’s best estimate of their cash flows, which support its belief that the carrying values of such securities were fully recoverable over their expected holding period. The following table summarizes Newcastle’s securities in an unrealized loss position as of June 30, 2014.

Securities in an Unrealized Loss Position	Outstanding Face Amount	Amortized Cost Basis			Gross Unrealized		Carrying Value	Number of Securities	Weighted Average			Life (Years)
		Before Impairment	Other-than- Temporary Impairment		Gains	Losses			Rating	Coupon	Yield	
			After Impairment	Temporary Impairment								
Less Than Twelve Months	\$ 1,869	\$ 1,867	\$ —	\$ 1,867	\$ —	\$ (5)	\$ 1,862	1	A+	4.81%	5.84%	0.2
Twelve or More Months	—	—	—	—	—	—	—	—	—	—%	—%	—
<b>Total</b>	<b>\$ 1,869</b>	<b>\$ 1,867</b>	<b>\$ —</b>	<b>\$ 1,867</b>	<b>\$ —</b>	<b>\$ (5)</b>	<b>\$ 1,862</b>	<b>1</b>	<b>A+</b>	<b>4.81%</b>	<b>5.84%</b>	<b>0.2</b>

Newcastle performed an assessment of all of its debt securities that are in an unrealized loss position (unrealized loss position exists when a security’s amortized cost basis, excluding the effect of OTTI, exceeds its fair value) and determined the following:

	June 30, 2014			
	Fair Value	Amortized Cost Basis After Impairment	Unrealized Losses	
			Credit (B)	Non-Credit (C)
Securities Newcastle intends to sell	\$ —	\$ —	\$ —	\$ N/A
Securities Newcastle is more likely than not to be required to sell (A)	—	—	—	N/A
Securities Newcastle has no intent to sell and is not more likely than not to be required to sell:				
Credit impaired securities	—	—	—	—
Non credit impaired securities	1,862	1,867	—	(5)
<b>Total debt securities in an unrealized loss position</b>	<b>\$ 1,862</b>	<b>\$ 1,867</b>	<b>\$ —</b>	<b>\$ (5)</b>

- (A) Newcastle may, at times, be more likely than not to be required to sell certain securities for liquidity purposes. While the amount of the securities to be sold may be an estimate, and the securities to be sold have not yet been identified, Newcastle must make its best estimate, which is subject to significant judgment regarding future events, and may differ materially from actual future sales.
- (B) This amount is required to be recorded as other-than-temporary impairment through earnings. In measuring the portion of credit losses, Newcastle’s management estimates the expected cash flow for each of the securities. This evaluation includes a review of the credit status and the performance of the collateral supporting those securities, including the credit of the issuer, key terms of the securities and the effect of local, industry and broader economic trends. Significant inputs in estimating the cash flows include management’s expectations of prepayment speeds, default rates and loss severities. Credit losses are measured as the decline in the present value of the expected future cash flows discounted at the investment’s effective interest rate.
- (C) This amount represents unrealized losses on securities that are due to non-credit factors and is required to be recorded through other comprehensive income.

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The following table summarizes the activity related to credit losses on debt securities for the six months ended June 30, 2014:

Beginning balance of credit losses on debt securities for which a portion of an OTTI was recognized in other comprehensive income	\$	(2,873)
Additions for credit losses on securities for which an OTTI was not previously recognized		—
Increases to credit losses on securities for which an OTTI was previously recognized and a portion of an OTTI was recognized in other comprehensive income		—
Additions for credit losses on securities for which an OTTI was previously recognized without any portion of OTTI recognized in other comprehensive income		—
Reduction for credit losses on securities for which no OTTI was recognized in other comprehensive income at the current measurement date		—
Reduction for securities sold/written off during the period		2,873
Reduction for increases in cash flows expected to be collected that are recognized over the remaining life of the security		—
Ending balance of credit losses on debt securities for which a portion of an OTTI was recognized in other comprehensive income	\$	—

The table below summarizes the geographic distribution of the collateral securing Newcastle's CMBS and asset backed securities ("ABS") at June 30, 2014:

Geographic Location	CMBS		ABS	
	Outstanding Face Amount	Percentage	Outstanding Face Amount	Percentage
Western U.S.	\$ 48,865	20.1 %	\$ 30,271	30.5 %
Northeastern U.S.	51,424	21.1 %	20,559	20.7 %
Southeastern U.S.	44,636	18.3 %	19,492	19.6 %
Midwestern U.S.	35,210	14.5 %	12,844	13.0 %
Southwestern U.S.	45,774	18.8 %	10,041	10.1 %
Other	11,022	4.5 %	6,038	6.1 %
Foreign	6,681	2.7 %	—	0.0 %
	<u>\$ 243,612</u>	<u>100.0 %</u>	<u>\$ 99,245</u>	<u>100.0 %</u>

Geographic concentrations of investments expose Newcastle to the risk of economic downturns within the relevant regions, particularly given the current unfavorable market conditions. These market conditions may make regions more vulnerable to downturns in certain market factors. Any such downturn in a region where Newcastle holds significant investments could have a material, negative impact on Newcastle.

In January 2014, Newcastle sold \$503.0 million face amount of the remaining FNMA/FHLMC securities at an average price of 105.82% for total proceeds of \$532.2 million and repaid \$516.1 million of associated repurchase agreements. Newcastle recognized a net gain of approximately \$1.9 million on the sale of these securities.

In May 2014, Newcastle sold \$68.3 million face amount of CMBS securities at an average price of 105.2% for total proceeds of \$71.9 million and repaid \$71.9 million of associated CDO bonds payable and other term loan financings. Newcastle recognized a net gain of approximately \$15.0 million on the sale of these securities.

In May 2014, Newcastle sold \$54.2 million outstanding face amount of the Sorin CDO security at an average price of 93.0% for total proceeds of \$50.4 million and repaid \$50.4 million of associated CDO bonds payable and other term loan financings. Newcastle recognized a net gain of approximately \$0.7 million on the sale of this security.

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**6. REAL ESTATE RELATED AND OTHER LOANS, RESIDENTIAL MORTGAGE LOANS AND SUBPRIME MORTGAGE LOANS**

The following is a summary of real estate related and other loans, residential mortgage loans and subprime mortgage loans at June 30, 2014. The loans contain various terms, including fixed and floating rates, self-amortizing and interest only. They are generally subject to prepayment.

Loan Type	Outstanding Face Amount	Carrying Value (A)	Loan Count	Weighted Average Yield	Weighted Average Coupon	Weighted Average Life (Years) (B)	Floating Rate Loans as a % of Face Amount	Delinquent Face Amount (C)
Mezzanine Loans	\$ 157,046	\$ 124,628	8	7.42%	7.34%	1.3	75.9%	\$ 12,000
Corporate Bank Loans	164,973	97,684	5	23.06%	13.12%	1.9	0.6%	—
B-Notes	69,912	66,420	2	5.57%	4.40%	1.6	68.2%	—
Whole Loans	380	380	1	3.95%	7.37%	0.5	0.0%	—
Total Real Estate Related and other Loans Held-for-Sale, Net	\$ 392,311	\$ 289,112	16	12.27%	9.25%	1.6	42.8%	\$ 12,000
Residential Loans (D)	43,229	32,083	165	7.22%	2.27%	5.7	100.0%	6,311
Total Residential Mortgage Loans Held-for-Sale, Net	\$ 43,229	\$ 32,083	165	7.22%	2.27%	5.7	100.0%	\$ 6,311
Subprime Mortgage Loans Subject to Call Option	\$ 406,217	\$ 406,217						

(A) Carrying value includes negligible interest receivable for the residential housing loans.

(B) The weighted average life is based on the timing of expected principal reduction on the assets.

(C) Includes loans that are 60 or more days past due (including loans that are in foreclosure, or borrower's in bankruptcy) or considered real estate owned ("REO"). As of June 30, 2014, \$87.4 million face amount of real estate related and other loans was on non-accrual status.

(D) Loans acquired at a discount for credit quality.

In May 2014, Newcastle sold its manufactured housing portfolio through a securitization. The portfolio had an outstanding face amount of \$222.2 million and was sold at 104% of par, resulting in \$231.6 million of total proceeds including accrued interest. Part of the proceeds were used to repay the current debt on the portfolio at par, including \$132.4 million of third-party debt and \$20.5 million of debt owned by CDO VIII and CDO IX. The securitization of the portfolio was accomplished through a special purpose entity, in which Newcastle holds no interests, and was treated as a sale for accounting purposes. The sale generated a gain of \$24.7 million, or \$19.4 million net after \$1.9 million of deal expenses and the write off of \$3.4 million of unamortized discount on third party debt (recorded as a loss on extinguishment of debt).

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The following is a summary of real estate related and other loans by maturities at June 30, 2014:

Year of Maturity (1)	Outstanding		Number of Loans
	Face Amount	Carrying Value	
Delinquent (2)	\$ 12,000	\$ —	1
Period from July 1, 2014 to December 31, 2014	111,104	47,651	5
2015	1,379	830	2
2016	64,891	63,274	2
2017	48,938	48,938	2
2018	22,260	18,769	1
2019	118,289	97,234	2
Thereafter	13,450	12,416	1
<b>Total</b>	<b>\$ 392,311</b>	<b>\$ 289,112</b>	<b>16</b>

(1) Based on the final extended maturity date of each loan investment as of June 30, 2014.

(2) Includes loans that are non-performing, in foreclosure, or under bankruptcy.

Activities relating to the carrying value of Newcastle's real estate related and other loans and residential mortgage loans are as follows:

	Held-for-Sale		Held-for-Investment
	Real Estate Related and Other Loans	Residential Mortgage Loans	Residential Mortgage Loans
Balance at December 31, 2013	\$ 437,530	\$ 2,185	\$ 255,450
Purchases / additional fundings	—	—	—
Interest accrued to principal balance	11,274	—	—
Principal paydowns	(167,171)	(8,226)	(9,436)
Sales	—	(206,360)	—
Transfer to held-for-sale	—	246,121	(246,121)
Valuation (allowance) reversal on loans	(1,958)	19	(833)
Accretion of loan discount and other amortization	8,867	—	115
Other	570	(1,656)	825
Balance at June 30, 2014	<b>\$ 289,112</b>	<b>\$ 32,083</b>	<b>\$ —</b>

In January 2014, Intrawest, a portfolio company of a private equity fund managed by an affiliate of Newcastle's Manager completed a \$37.5 million primary offering and a \$150.0 million secondary offering. At December 31, 2013, Newcastle had an outstanding investment balance of \$185.6 million in Intrawest's debt. Following Intrawest's public offerings, Newcastle received total cash of \$83.3 million, which reduced the face of the debt balance down to \$103.3 million at March 31, 2014.

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The following is a rollforward of the related loss allowance.

	Held-For-Sale		Held-For-Investment
	Real Estate Related and Other Loans	Residential Mortgage Loans	Residential Mortgage Loans (A)
Balance at December 31, 2013	\$ (94,037)	\$ (824)	\$ (12,247)
Charge-offs (B)	504	84	711
Sales	—	10,525	—
Transfer to held-for-sale	—	(12,369)	12,369
Valuation (allowance) reversal on loans	(1,958)	19	(833)
Balance at June 30, 2014	\$ (95,491)	\$ (2,565)	\$ —

(A) The allowance for credit losses was determined based on the guidance for loans acquired with deteriorated credit quality.

(B) The charge-offs for real estate related loans represent one loan which was under restructuring.

The table below summarizes the geographic distribution of real estate related and other loans and residential mortgage loans at June 30, 2014:

Geographic Location	Real Estate Related and Other Loans		Residential Mortgage Loans	
	Outstanding Face Amount	Percentage	Outstanding Face Amount	Percentage
	Western U.S.	\$ 43,453	18.7 %	\$ 5,291
Northeastern U.S.	31,004	13.4 %	2,067	4.8 %
Southeastern U.S.	51,733	22.3 %	30,884	71.4 %
Midwestern U.S.	8,922	3.8 %	2,201	5.1 %
Southwestern U.S.	10,468	4.5 %	2,786	6.5 %
Foreign	86,569	37.3 %	—	—%
	\$ 232,149	100.0 %	\$ 43,229	100.0 %
Other	160,162	(A)		
	\$ 392,311			

(A) Includes corporate bank loans which are not directly secured by real estate assets.

**Securitization of Subprime Mortgage Loans**

The following table presents information on the retained interests in Newcastle's securitizations of subprime mortgage loans at June 30, 2014:

	Subprime Portfolio		Total
	I	II	
Total securitized loans (unpaid principal balance) (A)	\$ 347,522	\$ 481,933	\$ 829,455
Loans subject to call option (carrying value)	\$ 299,176	\$ 107,041	\$ 406,217
Retained interests (fair value) (B)	\$ 2,608	\$ —	\$ 2,608

(A) Average loan seasoning of 107 months and 89 months for Subprime Portfolios I and II, respectively, at June 30, 2014.

(B) The retained interests include retained bonds of the securitizations. The fair value of which is estimated based on pricing models. Newcastle's residual interests were written off in 2010. The weighted average yield of the retained bonds was 25.07% as of June 30, 2014.

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Newcastle has no obligation to repurchase any loans from either of its subprime securitizations. Therefore, it is expected that its exposure to loss is limited to the carrying amount of its retained interests in the securitization entities, as described above. A subsidiary of Newcastle gave limited representations and warranties with respect to Subprime Portfolio II and is required to pay

the difference, if any, between the repurchase price of any loan in such portfolio and the price required to be paid by a third party originator for such loan. Such subsidiary, however, has no assets and does not have recourse to the general credit of Newcastle.

The following table summarizes certain characteristics of the underlying subprime mortgage loans, and related financing, in the securitizations as of June 30, 2014:

	Subprime Portfolio	
	I	II
Loan unpaid principal balance (UPB)	\$ 347,522	\$ 481,933
Weighted average coupon rate of loans	5.69 %	4.76 %
Delinquencies of 60 or more days (UPB) (A)	\$ 90,313	\$ 173,548
Net credit losses for the six months ended June 30, 2014	\$ 13,973	\$ 17,703
Cumulative net credit losses	\$ 260,778	\$ 319,277
Cumulative net credit losses as a % of original UPB	17.4 %	29.3 %
Percentage of ARM loans (B)	50.1 %	64.2 %
Percentage of loans with original loan-to-value ratio >90%	10.7 %	16.9 %
Percentage of interest-only loans	10.5 %	21.2 %
Face amount of debt (C)	\$ 343,522	\$ 481,933
Weighted average funding cost of debt (D)	0.50 %	0.42 %

(A) Delinquencies include loans 60 or more days past due, in foreclosure, under bankruptcy filing or REO.

(B) ARM loans are adjustable-rate mortgage loans. An option ARM is an adjustable-rate mortgage that provides the borrower with an option to choose from several payment amounts each month for a specified period of the loan term. None of the loans in the subprime portfolios are option ARMs.

(C) Excludes face amount of \$4.0 million of retained notes for Subprime Portfolio I at June 30, 2014.

(D) Includes the effect of applicable hedges.

Newcastle received negligible cash inflows from the retained interests of Subprime Portfolios I and II during the six months ended June 30, 2014 and 2013.

The loans subject to call option and the corresponding financing recognize interest income and expense based on the expected weighted average coupons of the loans subject to call option at the call date of 9.24% and 8.68% for Subprime Portfolio's I and II, respectively.

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## 7. INVESTMENTS IN SENIOR HOUSING AND OTHER REAL ESTATE, NET OF ACCUMULATED DEPRECIATION

The following table summarizes Newcastle's investments in real estate:

	June 30, 2014			December 31, 2013		
	Gross Carrying Amount	Accumulated Depreciation	Net Carrying Value	Gross Carrying Amount	Accumulated Depreciation	Net Carrying Value
<b>Senior Housing</b>						
Land	\$ 130,476	\$ —	\$ 130,476	\$ 102,235	\$ —	\$ 102,235
Buildings	1,366,356	(22,651)	1,343,705	1,199,672	(7,523)	1,192,149
Building improvements	21,318	(1,941)	19,377	20,704	(549)	20,155
Furniture, fixtures and equipment	61,353	(7,502)	53,851	50,711	(2,350)	48,361
Investments in Senior Housing Real Estate	<u>\$ 1,579,503</u>	<u>\$ (32,094)</u>	<u>\$ 1,547,409</u>	<u>\$ 1,373,322</u>	<u>\$ (10,422)</u>	<u>\$ 1,362,900</u>

	June 30, 2014			December 31, 2013		
	Gross Carrying Amount	Accumulated Depreciation	Net Carrying Value	Gross Carrying Amount	Accumulated Depreciation	Net Carrying Value
<b>Golf</b>						
Land	\$ 93,534	\$ —	\$ 93,534	\$ 93,534	\$ —	\$ 93,534
Buildings	50,962	(2,265)	48,697	50,615	—	50,615
Building improvements	91,934	(6,077)	85,857	90,736	—	90,736
Furniture, fixtures and equipment	20,459	(3,178)	17,281	18,353	—	18,353
Capital leases - equipment	3,830	(63)	3,767	—	—	—
Construction in progress	7,849	—	7,849	5,660	—	5,660
Golf Total	<u>268,568</u>	<u>(11,583)</u>	<u>256,985</u>	<u>258,898</u>	<u>—</u>	<u>258,898</u>

**Other Commercial Real Estate**

Land	1,106	—	1,106	1,106	—	1,106
Buildings	6,588	(1,443)	5,145	6,588	(1,356)	5,232
Building improvements	1,002	(738)	264	970	(711)	259
Furniture, fixtures and equipment	—	—	—	—	—	—
Other Commercial Real Estate Total	<u>8,696</u>	<u>(2,181)</u>	<u>6,515</u>	<u>8,664</u>	<u>(2,067)</u>	<u>6,597</u>
Investments in Other Real Estate	<u>\$ 277,264</u>	<u>\$ (13,764)</u>	<u>\$ 263,500</u>	<u>\$ 267,562</u>	<u>\$ (2,067)</u>	<u>\$ 265,495</u>

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

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**8. INTANGIBLES, NET OF ACCUMULATED AMORTIZATION**

The following table summarizes Newcastle's intangible assets related to its senior housing real estate and golf business:

	June 30, 2014			December 31, 2013		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Value	Gross Carrying Amount	Accumulated Amortization	Net Carrying Value
<b>Senior Housing</b>						
In-place resident lease intangibles	\$ 134,772	\$ (45,895)	\$ 88,877	\$ 112,267	\$ (21,902)	\$ 90,365
Non-compete intangibles	1,600	(383)	1,217	1,600	(223)	1,377
Land lease intangibles	3,442	(24)	3,418	3,498	(1)	3,497
PILOT intangible	3,700	(276)	3,424	3,700	(124)	3,576
Other intangibles	6,955	(49)	6,906	2,046	(2)	2,044
<b>Total Senior Housing</b>	<b>150,469</b>	<b>(46,627)</b>	<b>103,842</b>	<b>123,111</b>	<b>(22,252)</b>	<b>100,859</b>
<b>Golf</b>						
Trade name	700	(12)	688	700	—	700
Leasehold intangibles	52,066	(2,702)	49,364	52,066	—	52,066
Management contracts	39,000	(2,399)	36,601	39,000	—	39,000
Internally-developed software	800	(80)	720	800	—	800
Membership base	5,400	(386)	5,014	5,400	—	5,400
Nonamortizable liquor license	900	—	900	900	—	900
<b>Total Golf</b>	<b>98,866</b>	<b>(5,579)</b>	<b>93,287</b>	<b>98,866</b>	<b>—</b>	<b>98,866</b>
<b>Total Intangibles</b>	<b>\$ 249,335</b>	<b>\$ (52,206)</b>	<b>\$ 197,129</b>	<b>\$ 221,977</b>	<b>\$ (22,252)</b>	<b>\$ 199,725</b>

In the senior housing business, the gross carrying amount of the in-place resident lease intangibles is amortized on a straight-line basis over the average length of stay of the residents: 24 months for assisted living and memory care facilities and 33 months for independent living facilities. If the in-place resident lease is terminated prior to the lease expiration, the unamortized costs are written off at that time. The gross carrying amount of the non-compete intangibles is amortized on a straight-line basis of 5 years as stated within the respective agreements. The gross carrying amount of the land lease intangibles is amortized over the stated term within the respective agreements, 74 years and 82 years. The gross carrying amount of the PILOT intangible is amortized over the stated term within the agreement of 13 years. Other intangibles are amortized on a straight-line basis of 13 to 40 years.

In the golf business, the weighted average amortization periods for amortizable intangible assets are 29.5 years for trade name, 7.8 years for leasehold intangibles, 7.7 years for management contracts, 4.5 years for internally-developed software, and 6.5 years for membership base.

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9. RECEIVABLES AND OTHER ASSETS

The following table summarizes Newcastle's receivables and other assets:

	June 30, 2014	December 31, 2013
Accounts receivable, net	\$ 9,722	\$ 13,477
Deferred financing costs	38,824	42,473
Derivative assets	—	43,662
Prepaid expenses	16,990	8,631
Interest receivable	1,629	4,667
Deposits	10,178	9,915
Inventory	5,793	5,140
Miscellaneous assets, net	26,402	13,922
	<u>\$ 109,538</u>	<u>\$ 141,887</u>

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10. DEBT OBLIGATIONS

The following table presents certain information regarding Newcastle's debt obligations and related hedges at June 30, 2014:

Debt Obligation/Collateral	Month Issued	Outstanding Face Amount	Carrying Value	Final Stated Maturity	Weighted Average Coupon (A)	Weighted Average Funding Cost (B)	Weighted Average Life(Years)	Face Amount of Floating Rate Debt	Collateral (K)			Weighted Average Life (Years)	Floating Rate Face Amount (C)	Aggregate Notional Amount of Current Hedges (D)
									Outstanding Face Amount (C)	Amortized Cost Basis (C)	Carrying Value (C)			
<b>CDO Bonds Payable</b>														
CDO VI (E)	Apr 2005	\$ 92,238	\$ 92,238	Apr 2040	0.83%	5.36%	5.5	\$ 88,838	\$ 157,567	\$ 86,678	\$ 124,252	2.1	\$ 35,095	\$ 88,838
CDO VIII	Nov 2006	71,813	71,698	Nov 2052	2.11%	7.71%	2.6	64,213	249,954	178,906	194,238	1.8	113,582	84,048
CDO IX	May 2007	98,441	99,645	May 2052	0.64%	0.49%	1.1	98,441	345,022	284,291	295,062	2.3	114,869	—
		<u>262,492</u>	<u>263,581</u>			<u>4.16%</u>	<u>3.1</u>	<u>251,492</u>	<u>752,543</u>	<u>549,875</u>	<u>613,552</u>	<u>2.1</u>	<u>263,546</u>	<u>172,886</u>
<b>Other Bonds and Notes Payable</b>														
NCT 2013-VI IMM-1 (F)	Nov 2013	89,168	82,053	Apr 2040	LIBOR+0.25%	0.41%	1.7	89,168	—	—	—	—	—	—
		<u>89,168</u>	<u>82,053</u>			<u>0.41%</u>	<u>1.7</u>	<u>89,168</u>						
<b>Repurchase Agreements (G)</b>														
CDO securities (F)	Dec 2013	79,712	79,712	Jul 2014	LIBOR+1.65%	1.81%	0.1	79,712	—	—	—	—	—	—
Residential Mortgage Loans	Nov 2013	22,965	22,965	Nov 2014	LIBOR+2.00%	2.16%	0.4	22,965	34,002	24,617	24,617	6.0	34,002	—
		<u>102,677</u>	<u>102,677</u>			<u>1.88%</u>	<u>0.1</u>	<u>102,677</u>	<u>34,002</u>	<u>24,617</u>	<u>24,617</u>	<u>6.0</u>	<u>34,002</u>	<u>—</u>
<b>Mortgage Notes Payable</b>														
Fixed Rate - Managed Properties		158,000	158,434	Aug 2018 to Mar 2020	1.63% to 4.93%	(H) (I)	4.79%	4.8	N/A	N/A	182,986	182,986	N/A	N/A
Floating Rate - Managed Properties		231,400	231,400	Aug 2016 to Jan 2019	LIBOR +2.75% to LIBOR+3.75%	(J)	4.72%	3.6	231,400	N/A	308,816	308,816	N/A	N/A
Fixed Rate - Triple Net Lease Properties		714,348	714,348	Jan 2021 to Jan 2024	3.83% to 8.00%	(K)	5.10%	7.5	N/A	N/A	974,792	974,792	N/A	N/A
		<u>1,103,748</u>	<u>1,104,182</u>				<u>4.98%</u>	<u>6.3</u>	<u>231,400</u>	<u>N/A</u>	<u>1,466,594</u>	<u>1,466,594</u>	<u>N/A</u>	<u>N/A</u>
<b>Golf Credit Facilities (L)</b>														
First Lien Loan	Dec 2013	46,922	46,922	Dec 2018	LIBOR+4.00%	(M)	4.50%	3.5	46,922	—	—	—	—	—
Second Lien Loan	Dec 2013	105,575	105,575	Dec 2018	5.50%		5.50%	3.5	—	—	—	—	—	—
Vineyard I	Dec 1993	59	68	Aug 2014	11.37%		11.37%	0.1	59	—	—	—	—	—
Vineyard II	Dec 1993	200	200	Dec 2043	2.13%		2.13%	29.5	200	—	—	—	—	—
Capital Leases (Equipment)	May-June 2014	3,813	3,813	Dec 2019 to Jan 2020	7.15%		7.15%	3.3	—	—	—	—	—	—
		<u>156,569</u>	<u>156,578</u>				<u>5.24%</u>	<u>3.5</u>	<u>47,181</u>					
<b>Corporate</b>														
Junior subordinated notes payable	Mar 2006	51,004	51,234	Apr 2035	7.57%	(N)	7.39%	20.8	—	—	—	—	—	—
		<u>51,004</u>	<u>51,234</u>				<u>7.39%</u>	<u>20.8</u>	<u>—</u>					
Subtotal debt obligations		<u>1,765,658</u>	<u>1,760,305</u>				<u>4.54%</u>	<u>5.4</u>	<u>\$ 721,918</u>	<u>\$ 786,545</u>	<u>\$ 2,041,086</u>	<u>\$ 2,104,763</u>	<u>2.2</u>	<u>\$ 297,548</u>
Financing on subprime mortgage loans subject to call option (O)		<u>406,217</u>	<u>406,217</u>											
Total debt obligations		<u>\$ 2,171,875</u>	<u>\$ 2,166,522</u>											

See notes on next page.

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- (A) Weighted average, including floating and fixed rate classes.
- (B) Including the effect of applicable hedges and deferred financing cost. For fixed rate mortgage notes payable, the weighted average funding cost is calculated based on the average rate during the six months ended June 30, 2014.
- (C) Excluding (i) restricted cash held in CDOs to be used for principal and interest payments of CDO debt, and (ii) operating cash from the senior housing business.
- (D) Including the \$88.8 million portion of the notional amount of interest rate swap in CDO VI, which acted as an economic hedge that was not designated as a hedge for accounting purposes.
- (E) This CDO was not in compliance with its applicable over collateralization tests as of June 30, 2014. Newcastle is not receiving cash flows from this CDO (other than senior management fees and cash flows on senior classes of bonds that were repurchased), since net interest is being used to repay debt, and expects this CDO to remain out of compliance for the foreseeable future.
- (F) Represents refinancing of repurchased Newcastle CDO bonds where collateral is, therefore, eliminated in consolidation.
- (G) These repurchase agreements had less than \$0.1 million of accrued interest payable at June 30, 2014. \$102.7 million face amount of these repurchase agreements were renewed subsequent to June 30, 2014. The counterparties on these repurchase agreements are Bank of America (\$79.7 million) and Credit Suisse (\$23.0 million). Newcastle has margin exposure on a \$23.0 million repurchase agreement related to the financing of residential mortgage loans, and a \$79.7 million repurchase agreement related to the financing of certain Newcastle CDO VIII and CDO IX notes. To the extent that the value of the collateral underlying these repurchase agreements declines, Newcastle may be required to post margin, which could significantly impact its liquidity.
- (H) For loans totaling \$40.9 million issued in August 2013, Newcastle bought down the interest rate to 4% for the first two years. Thereafter, the interest rate will range from 5.99% to 6.76%.
- (I) For a loan with a total balance of \$11.4 million, the interest rate for the first two years is based on the applicable US Treasury Security rates. The interest rate for years 3 through 5 is 4.5%, 4.75% and 5.0%, respectively.
- (J) \$165.0 million of the floating rate mortgages have a LIBOR floor of 1.0%.
- (K) For loans with a total balance \$359.9 million and \$314.7 million, Newcastle bought down the interest rate to 4.00% and 3.83%, respectively, until January 2019. Thereafter, the interest rates will increase to 4.99% and 4.56%, respectively.
- (L) The golf credit facilities are collateralized by all of the assets of the golf business.
- (M) Interest rate on this is based on 3 month LIBOR with a LIBOR floor of 0.5%.
- (N) Issued in April 2006 and July 2007 and secured by the general credit of Newcastle. See Note 6 regarding the securitizations of Subprime Portfolio I and II.
- (O) LIBOR +2.25% after April 2016.

Each CDO financing is subject to tests that measure the amount of over collateralization and excess interest in the transaction. Failure to satisfy these tests would cause the principal and/or interest cashflow that would otherwise be distributed to more junior classes of securities (including those held by Newcastle) to be redirected to pay down the most senior class of securities outstanding until the tests are satisfied. As a result, Newcastle's cash flow and liquidity are negatively impacted upon such a failure. As of June 30, 2014, CDO VI was not in compliance with its over collateralization tests. Based upon Newcastle's current calculations, Newcastle expects this CDO to remain out of compliance for the foreseeable future.

As of June 30, 2014, Newcastle has unused borrowing capacity of \$7.6 million on the golf credit facilities.

The Golf business leases equipment under capital lease agreements. The agreements normally provide for minimum rentals plus executory costs. Lease terms are 66 months with a purchase price option at the termination of the lease.

The future minimum lease payments required under the capital leases and the present value of the net minimum lease payments as of June 30, 2014 are as follows:

July 1, 2014 - December 31, 2014	\$	381
2015		755
2016		755
2017		755
2018		755
2019 and thereafter		1,327
<b>Total minimum lease payments</b>		<b>4,728</b>
Less: imputed interest		915
<b>Present value of net minimum lease payments</b>	<b>\$</b>	<b>3,813</b>

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Newcastle's non-CDO financings, mortgage notes payable and golf credit facilities contain various customary loan covenants. Newcastle was in compliance with all of these covenants as of June 30, 2014.

In June 2013, Newcastle completed the purchase of \$116.8 million aggregate face amount of securities that are collateralized by certain Newcastle CDO VIII Class I notes for an aggregate purchase of approximately \$103.1 million, or an average price of 88.3% of par. Simultaneously, Newcastle financed the purchase with \$60.0 million received pursuant to a master repurchase agreement with the seller of the securities ("CDO VIII Repack"). The terms of the repurchase agreement included a rate of one-month LIBOR plus 150 bps and a 30-day maturity. The purchase of the securities and the repurchase agreement were treated as a linked transaction and accordingly recorded on a net basis as a non-hedge derivative instrument, with changes in market value recorded on the statement of income. In May 2014, the CDO VIII Class I notes were repaid in full and the repurchase agreement was terminated.

**11. ACCOUNTS PAYABLE, ACCRUED EXPENSES AND OTHER LIABILITIES**

The following table summarizes Newcastle's accounts payable, accrued expenses and other liabilities:

	June 30, 2014		December 31, 2013	
Accounts payable and accrued expenses	\$	55,997	\$	50,118
Membership deposit liabilities		74,789		71,644
Deferred revenue		21,182		37,114
Security deposit payable		58,023		48,823
Unfavorable leasehold interests		21,889		23,916
Derivative liabilities		7,345		13,795
Accrued rent		9,767		6,314
Due to affiliates		6,069		5,878
Miscellaneous liabilities		14,717		18,889
	\$	269,778	\$	276,491

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12. FAIR VALUE

*Fair Value Summary Table*

The carrying values and fair values of Newcastle's assets and liabilities at June 30, 2014 were as follows:

	Principal Balance or Notional Amount	Carrying Value	Estimated Fair Value	Fair Value Method (A)	Weighted Average Yield/Funding Cost (B)	Weighted Average Life (Years)
<b>Assets</b>						
Financial instruments:						
Real estate securities, available-for-sale (C)*	\$ 389,120	\$ 311,268	\$ 311,268	Broker quotations, counterparty quotations, pricing services, pricing models	15.16%	2.8
Real estate related and other loans, held-for-sale, net	392,311	289,112	302,449	Broker quotations, counterparty quotations, pricing services, pricing models	12.27%	1.6
Residential mortgage loans, held-for-sale, net	43,229	32,083	39,699	Broker/counterparty quotations	7.22%	5.7
Subprime mortgage loans subject to call option (D)	406,217	406,217	(D)	(D)	9.09%	(D)
Restricted cash*		3,703	3,703			
Cash and cash equivalents*		77,922	77,922			
Investments in senior housing real estate, net		1,547,409				
Investments in other real estate, net		263,500				
Intangibles		197,129				
Other investments		26,123				
Receivables and other assets		109,538				
		<u>\$ 3,264,004</u>				
<b>Liabilities</b>						
Financial instruments:						
CDO bonds payable (G)	\$ 262,492	\$ 263,581	\$ 155,227	Pricing models	4.16%	3.1
Other bonds and notes payable (G)	89,168	82,053	81,446	Broker quotations, pricing models	0.41%	1.7
Repurchase agreements	102,677	102,677	102,677	Market comparables	1.88%	0.1
Mortgage notes payable	1,103,748	1,104,182	1,112,491	Pricing models	4.98%	6.3
Credit facilities and obligations under capital leases, golf	156,569	156,578	156,578	Pricing models	5.24%	3.5
Financing of subprime mortgage loans subject to call option (D)	406,217	406,217	(D)	(D)	9.09%	(D)
Junior subordinated notes payable	51,004	51,234	33,900	Pricing models	7.39%	20.8
Interest rate swaps, treated as hedges (E)(F)*	84,048	3,882	3,882	Counterparty quotations	N/A	(E)
Non-hedge derivatives (E)(F)*	158,258	3,463	3,463	Counterparty quotations	N/A	(E)
Dividends payable, accrued expenses and other liabilities		298,534				
Liabilities of discontinued operations		—				
		<u>\$ 2,472,401</u>				

\*Measured at fair value on a recurring basis.

**NEWCASTLE INVESTMENT CORP. AND SUBSIDIARIES**

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- (A) Methods are listed in order of priority. In the case of real estate securities and real estate related and other loans, broker quotations are obtained if available and practicable, otherwise counterparty quotations or pricing service valuations are obtained or, finally, internal pricing models are used. Internal pricing models are only used for (i) securities and loans that are not traded in an active market, and, therefore, have little or no price transparency, and for which significant unobservable inputs must be used in estimating fair value, or (ii) loans or debt obligations which are private and untraded.
- (B) The weighted average yield and weighted average funding cost are disclosed for financial instrument assets and liabilities, respectively.
- (C) Excludes nine CDO securities with a zero value, which had an aggregate face amount of \$116.1 million.
- (D) These two items result from an option, not an obligation, to repurchase loans from Newcastle's subprime mortgage loan securitizations (Note 6), are noneconomic until such option is exercised, and are equal and offsetting.
- (E) As of June 30, 2014, all derivative liabilities, which represent three interest rate swaps, were held within Newcastle's nonrecourse structures. An aggregate notional balance of \$242.3 million is only subject to the credit risks of the respective CDO structures. As they are senior to all the debt obligations of the respective CDOs and the fair value of each of the CDOs' total investments exceeded the fair value of each of the CDOs' derivative liabilities, no credit valuation adjustments were recorded. Newcastle's interest rate swap counterparties include Bank of America and Bank of New York Mellon. Newcastle's derivatives are included in accounts payable, accrued expenses and other liabilities in the consolidated balance sheets.
- (F) Interest rate swaps, treated as hedges:

	Year of Maturity	Weighted Average Month of Maturity	Aggregate Notional Amount	Weighted Average Fixed Pay Rate	Aggregate Fair Value
<b>Interest rate swap agreements which receive 1-Month LIBOR:</b>					
	2016	Apr	\$ 84,048	5.04 %	\$ 3,882
Non-hedge derivatives:					
	Year of Maturity	Weighted Average Month of Maturity	Aggregate Notional Amount	Weighted Average Fixed Pay Rate	Aggregate Fair Value
<b>Interest rate swap agreements which receive 1-Month LIBOR:</b>					
	2015	Mar	\$ 158,258	4.85 %	\$ 3,463

- (G) Newcastle notes that the unrealized gain on the liabilities within such structures cannot be fully realized. Assets held within CDOs and other nonrecourse structures are generally not available to satisfy obligations outside of such financings, except to the extent Newcastle receives net cash flow distributions from such structures. Furthermore, creditors or beneficial interest holders of these structures have no recourse to the general credit of Newcastle. Therefore, Newcastle's exposure to the economic losses from such structures is limited to its invested equity in them and economically their book value cannot be less than zero. As a result, the fair value of Newcastle's net investments in these non-recourse financing structures is equal to the present value of their expected future net cash flows.

**Valuation Hierarchy**

The methodologies used for valuing such instruments have been categorized into three broad levels, which form a hierarchy.

Level 1 - Quoted prices in active markets for identical instruments.

Level 2 - Valuations based principally on other observable market parameters, including

- Quoted prices in active markets for similar instruments,
- Quoted prices in less active or inactive markets for identical or similar instruments,
- Other observable inputs (such as interest rates, yield curves, volatilities, prepayment speeds, loss severities, credit risks and default rates), and
- Market corroborated inputs (derived principally from or corroborated by observable market data).

Level 3 - Valuations based significantly on unobservable inputs.

Newcastle follows this hierarchy for its financial instruments measured at fair value on a recurring basis. The classifications are based on the lowest level of input that is significant to the fair value measurement.

Newcastle has various processes and controls in place to ensure that fair value is reasonably estimated. With respect to the broker and pricing service quotations, to ensure these quotes represent a reasonable estimate of fair value, Newcastle's quarterly procedures include a comparison to quotations from different sources, outputs generated from its internal pricing models and transactions

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Newcastle has completed with respect to these or similar securities, as well as on its knowledge and experience of these markets. With respect to fair value estimates generated based on Newcastle's internal pricing models, Newcastle's management validates the inputs and outputs of the internal pricing models by comparing them to available independent third party market parameters, where available, and models for reasonableness. Newcastle believes its valuation methods and the assumptions used are appropriate and consistent with other market participants. The board of directors has reviewed Newcastle's process for determining the valuations of its investments based on information provided by the Manager and has concluded such process is reasonable and appropriate.

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

The following table summarizes such financial assets and liabilities measured at fair value on a recurring basis at June 30, 2014:

	Principal Balance or		Fair Value		
	Notional Amount	Carrying Value	Level 2	Level 3	Total
<b>Assets</b>					
Real estate securities, available-for-sale:					
CMBS	\$ 243,612	\$ 207,360	\$ —	\$ 207,360	\$ 207,360
REIT debt	29,200	30,683	30,683	—	30,683
Non-Agency RMBS	90,781	60,508	—	60,508	60,508
ABS - other real estate	8,464	—	—	—	—
CDO (A)	17,063	12,717	—	12,717	12,717
Real estate securities total	\$ 389,120	\$ 311,268	\$ 30,683	\$ 280,585	\$ 311,268
<b>Liabilities</b>					
Derivative Liabilities:					
Interest rate swaps, treated as hedges	\$ 84,048	\$ 3,882	\$ 3,882	\$ —	\$ 3,882
Interest rate swaps, not treated as hedges	158,258	3,463	3,463	—	3,463
Derivative liabilities total	\$ 242,306	\$ 7,345	\$ 7,345	\$ —	\$ 7,345

(A) Represents non-consolidated CDO securities, excluding nine securities with a zero value, which had an aggregate face amount of \$116.1 million.

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Newcastle's investments in instruments measured at fair value on a recurring basis using Level 3 inputs changed during the six months ended June 30, 2014 as follows:

	CMBS		ABS		Equity/Other Securities	Linked Transactions	Total
	Conduit	Other	Subprime	Other			
Balance at December 31, 2013	\$ 198,935	\$ 85,534	57,581	\$ —	\$ 59,757	\$ 43,662	\$ 445,469
Total gains (losses) (A)							
Included in net income (B)	15,402	—	—	—	717	12,498	28,617
Included in other comprehensive income (loss)	(13,800)	189	4,725	—	3,587	—	(5,299)
Amortization included in interest income	9,330	332	2,539	48	1,749	—	13,998
Purchases, sales and repayments							
Purchases	—	—	—	—	—	—	—
Proceeds from sales	(72,438)	—	—	—	(50,390)	—	(122,828)
Proceeds from repayments	(4,123)	(12,001)	(4,337)	(48)	(2,703)	(56,160)	(79,372)
Balance at June 30, 2014	\$ 133,306	\$ 74,054	60,508	\$ —	\$ 12,717	\$ —	\$ 280,585

(A) None of the gains (losses) recorded in earnings during the period is attributable to the change in unrealized gains (losses) relating to Level 3 assets still held at the reporting date.

(B) These gains (losses) are recorded in the following line items in the consolidated statements of income:

	Six Months Ended June 30, 2014	
Gain (loss) on settlement of investments, net	\$	16,119
Other income (loss), net		12,498
OTTI		—
Total	\$	28,617
Gain (loss) on settlement of investments, net, from investments transferred into Level 3 during the period	\$	—

**Securities Valuation**

As of June 30, 2014, Newcastle's securities valuation methodology and results are further detailed as follows:

Asset Type	Outstanding Face Amount (A)	Amortized Cost Basis (B)	Fair Value			Total
			Multiple Quotes (C)	Single Quote (D)	Internal Pricing Models (E)	
CMBS	\$ 243,612	\$ 164,381	\$ 164,907	\$ 42,453	\$ —	\$ 207,360
REIT debt	29,200	28,791	30,683	—	—	30,683
Non-Agency RMBS	90,781	38,875	60,508	—	—	60,508
ABS - other real estate	8,464	—	—	—	—	—
CDO (F)	17,063	6,368	—	6,744	5,973	12,717
Total	\$ 389,120	\$ 238,415	\$ 256,098	\$ 49,197	\$ 5,973	\$ 311,268

(A) Net of incurred losses.

(B) Net of discounts (or gross of premiums) and after OTTI, including impairment taken during the period ended June 30, 2014.

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- (C) Management generally obtained pricing service quotations or broker quotations from at least two sources, one of which was generally the seller (the party that sold us the security). Management selected one of the quotes received as being most representative of fair value and did not use an average of the quotes. Even if Newcastle receives two or more quotes on a particular security that come from non-selling brokers or pricing services, it does not use an average because management believes using an actual quote more closely represents a transactable price for the security than an average level. Furthermore, in some cases there is a wide disparity between the quotes Newcastle receives. Management believes using an average of the quotes in these cases would generally not represent the fair value of the asset. Based on Newcastle's own fair value analysis using internal models, management selects one of the quotes which are believed to more accurately reflect fair value. Newcastle never adjusts quotes received. These quotations are generally received via email and contain disclaimers which state that they are "indicative" and not "actionable" – meaning that the party giving the quotation is not bound to actually purchase the security at the quoted price.
- (D) Management was unable to obtain quotations from more than one source on these securities. The one source was generally the seller (the party that sold us the security) or a pricing service.
- (E) Securities whose fair value was estimated based on internal pricing models are further detailed as follows:

	Amortized Cost Basis (B)		Impairment	Unrealized Gains (Losses) in Accumulated OCI	Weighted Average Significant Input			
		Fair Value	Recorded In Current Period		Discount Rate	Prepayment Speed (G)	Cumulative Default Rate	Loss Severity
CDO	—	5,973	—	5,973	10.0%	3.6%	25.4%	73.7%
Total	\$ —	\$ 5,973	\$ —	\$ 5,973				

At June 30, 2014, there was no ABS or CMBS fair value based on model mark assumptions.

All of the assumptions listed have some degree of market observability, based on Newcastle's knowledge of the market, relationships with market participants, and use of common market data sources. Collateral prepayment, default and loss severity projections are in the form of "curves" or "vectors" that vary for each monthly collateral cash flow projection. Methods used to develop these projections vary by asset class (e.g., CMBS projections are developed differently than home equity ABS projections) but conform to industry conventions. Newcastle uses assumptions that generate its best estimate of future cash flows of each respective security.

The prepayment vector specifies the percentage of the collateral balance that is expected to voluntarily pay off at each point in the future. The prepayment vector is based on projections from a widely published investment bank model which considers factors such as collateral FICO score, loan-to-value ratio, debt-to-income ratio, and vintage on a loan level basis. This vector is scaled up or down to match recent collateral-specific prepayment experience, as obtained from remittance reports and market data services.

Loss severities are based on recent collateral-specific experience with additional consideration given to collateral characteristics. Collateral age is taken into consideration because severities tend to initially increase with collateral age before eventually stabilizing. Newcastle typically uses projected severities that are higher than the historic experience for collateral that is relatively new to account for this effect. Collateral characteristics such as loan size, lien position, and location (state) also effect loss severity. Newcastle considers whether a collateral pool has experienced a significant change in its composition with respect to these factors when assigning severity projections.

Default rates are determined from the current "pipeline" of loans that are more than 90 days delinquent, in foreclosure, or are REO. These significantly delinquent loans determine the first 24 months of the default vector. Beyond month 24, the default vector transitions to a steady-state value that is generally equal to or greater than that given by the widely published investment bank model.

The discount rates Newcastle uses are derived from a range of observable pricing on securities backed by similar collateral and offered in a live market. As the markets in which Newcastle transacts have become less liquid, Newcastle has had to rely on fewer data points in this analysis.

- (F) Represents non-consolidated CDO securities, excluding nine securities with a zero value, which had an aggregate face amount of \$116.1 million.
- (G) Projected annualized average prepayment rate.

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**Loan Valuation**

Loans which Newcastle does not have the ability or intent to hold into the foreseeable future are classified as held-for-sale. As a result, these held-for-sale loans are carried at the lower of amortized cost or fair value and are therefore recorded at fair value on a non-recurring basis. These loans were written down to fair value at the time of the impairment, based on broker quotations, pricing service quotations or internal pricing models. All the loans were within Level 3 of the fair value hierarchy. For real estate related and other loans, the most significant inputs used in the valuations are the amount and timing of expected future cash flows, market yields and the estimated collateral value of such loan investments. For residential mortgage loans, significant inputs include management's expectations of prepayment speeds, default rates, loss severities and discount rates that market participants would use in determining the fair values of similar pools of residential mortgage loans.

The following tables summarize certain information for real estate related and other loans and residential mortgage loans held-for-sale as of June 30, 2014:

Loan Type	Outstanding		Fair Value	Valuation Allowance/ (Reversal) In Current Year	Significant Input			
	Face Amount	Carrying Value			Range		Weighted Average	
					Discount Rate	Loss Severity	Discount Rate	Loss Severity
Mezzanine	\$ 157,046	\$ 124,628	\$ 127,673	\$ —	5.0% - 9.0%	0.0% - 100%	7.4%	19.0%
Bank Loan	164,973	97,684	107,969	5,227	22.5% - 31.0%	0.0% - 100%	23.1%	27.8%
B-Note	69,912	66,420	66,420	(3,269)	3.0% - 12.0%	0.0%	5.6%	0.0%
Whole Loan	380	380	387	—	4.0%	0.0%	4.0%	0.0%
Total Real Estate Related and other Loans Held-for-Sale, Net	\$ 392,311	\$ 289,112	\$ 302,449	\$ 1,958				

The following table summarizes certain information for residential mortgage loans held-for-sale as of June 30, 2014:

Loan Type	Outstanding		Fair Value (A)	Valuation Allowance/ (Reversal) In Current Year (B)	Significant Input (Weighted Average)			
	Face Amount	Carrying Value (A)			Discount Rate	Prepayment Speed	Constant Default Rate	Loss Severity
Residential Loans	43,229	32,083	39,699	399	7.3%	4.6%	2.8%	46.0%
Total Residential Mortgage Loans, Held-for-Sale, Net	\$ 43,229	\$ 32,083	\$ 39,699	\$ 399				

(A) Carrying value and fair value include interest receivable of \$0.1 million for the residential housing loans.

(B) The valuation allowance (reversal) excludes \$0.4 million related to the manufactured housing portfolio that was sold in May 2014.

**Derivatives**

Newcastle's derivative instruments are comprised of interest rate swaps and linked transactions. Newcastle's interest rate swaps are valued using counterparty quotations. These quotations are generally based on valuation models with model inputs that can generally be verified and which do not involve significant judgment. The significant observable inputs used in determining the fair value of Newcastle's Level 2 interest rate swap derivative contracts are contractual cash flows and market based interest rate curves. The linked transactions, which are categorized into Level 3, are evaluated on a net basis considering their underlying components, the security acquired and the related repurchase financing agreement. The securities are valued using a similar methodology to the one described in "Securities Valuation" above and this value is netted against the carrying value of the repurchase agreement (which approximates fair value as described in "Liabilities for Which Fair Value is Only Disclosed" below), adjusted for net accrued interest receivable/payable on the securities and repurchase agreement of the linked transactions (see Note 10 for a discussion of Newcastle's outstanding linked transactions).

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Newcastle's derivatives are recorded on its balance sheet as follows:

	Balance sheet location	Fair Value	
		June 30, 2014	December 31, 2013
<b>Derivative Assets</b>			
Linked transactions at fair value	Receivables and other assets	\$ —	\$ 43,662
		<u>\$ —</u>	<u>\$ 43,662</u>
<b>Derivative Liabilities</b>			
Interest rate swaps, designated as hedges	Accounts payable, accrued expenses and other liabilities	\$ 3,882	\$ 6,203
Interest rate swaps, not designated as hedges	Accounts payable, accrued expenses and other liabilities	3,463	7,592
		<u>\$ 7,345</u>	<u>\$ 13,795</u>

In May 2014, the CDO VIII Class 1 notes were repaid in full and the repurchase agreement was terminated. Therefore, the associated linked transaction was effectively terminated.

The following table summarizes information related to derivatives:

	June 30, 2014	December 31, 2013
<b>Cash flow hedges</b>		
Notional amount of interest rate swap agreements	\$ 84,048	\$ 105,031
Amount of (loss) recognized in OCI on effective portion	(4,072)	(6,117)
Deferred hedge gain (loss) related to anticipated financings, which have subsequently occurred, net of amortization	134	170
Deferred hedge gain (loss) related to dedesignation, net of amortization	(35)	(45)
Expected reclassification of deferred hedges from AOCI into earnings over the next 12 months	56	53
Expected reclassification of current hedges from AOCI into earnings over the next 12 months	(2,419)	(3,915)
<b>Non-hedge Derivatives</b>		
Notional amount of interest rate swap agreements	158,258	185,871
Notional amount of linked transactions (A)	—	116,806

(A) This represents the current face amount of the underlying financed securities comprising linked transactions.

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The following table summarizes gains (losses) recorded in relation to derivatives:

	Income statement location	Three Months Ended June 30,		Six Months Ended June 30,	
		2014	2013	2014	2013
<b>Cash flow hedges</b>					
Gain (loss) on the ineffective portion	Other income (loss)	\$ 259	\$ —	\$ 259	\$ —
Amount of gain (loss) reclassified from AOCI into income, related to effective portion	Interest expense	(1,178)	(1,703)	(2,457)	(3,568)
Deferred hedge gain reclassified from AOCI into income, related to anticipated financings	Interest expense	19	17	36	33
Deferred hedge gain (loss) reclassified from AOCI into income, related to effective portion of dedesignated hedges	Interest expense	(5)	(16)	(9)	(32)
<b>Non-hedge derivatives gain (loss)</b>					
Interest rate swaps	Other income (loss)	2,029	2,282	4,104	5,408
Linked transactions	Other income (loss)	1,825	—	12,498	—
Linked transactions	Interest expense	(89)	(8)	(211)	(8)

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*Liabilities for Which Fair Value is Only Disclosed*

The following table summarizes the level of the fair value hierarchy, valuation techniques and inputs used for estimating each class of liabilities not measured at fair value in the statement of financial position but for which fair value is disclosed:

Type of Liabilities Not Measured At Fair Value for Which Fair Value Is Disclosed	Fair Value Hierarchy	Valuation Techniques and Significant Inputs
CDO bonds payable	Level 3	Valuation technique is based on discounted cash flow. Significant inputs include: <ul style="list-style-type: none"> <li>• Underlying security and loan prepayment, default and cumulative loss expectations</li> <li>• Amount and timing of expected future cash flows</li> <li>• Market yields and credit spreads implied by comparisons to transactions of similar tranches of CDO debt by the varying levels of subordination</li> </ul>
Other bonds and notes payable	Level 3	Valuation technique is based on discounted cash flow. Significant inputs include: <ul style="list-style-type: none"> <li>• Amount and timing of expected future cash flows</li> <li>• Interest rates</li> <li>• Market yields and credit spreads implied by comparisons to transactions of similar tranches of securitized debt by the varying levels of subordination</li> </ul>
Repurchase agreements	Level 2	Valuation technique is based on market comparables. Significant variables include: <ul style="list-style-type: none"> <li>• Amount and timing of expected future cash flows</li> <li>• Interest rates</li> <li>• Collateral funding spreads</li> </ul>
Mortgage notes payable	Level 3	Valuation technique is based on discounted cash flows. Significant inputs include: <ul style="list-style-type: none"> <li>• Amount and timing of expected future cash flows</li> <li>• Interest rates</li> <li>• Collateral funding spreads</li> </ul>
Golf credit facilities	Level 3	Valuation technique is based on discounted cash flows. Significant inputs include: <ul style="list-style-type: none"> <li>• Amount and timing of expected future cash flows</li> <li>• Interest rates</li> <li>• Credit spread of golf</li> </ul>
Junior subordinated notes payable	Level 3	Valuation technique is based on discounted cash flow. Significant inputs include: <ul style="list-style-type: none"> <li>• Amount and timing of expected future cash flows</li> <li>• Interest rates</li> <li>• Market yields and the credit spread of Newcastle</li> </ul>

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## 13. EQUITY AND EARNINGS PER SHARE

## A. Stockholder's Equity

In connection with the spin-off of New Media on February 13, 2014, the strike price of each Newcastle option was reduced by \$0.89 to reflect the adjusted value of Newcastle's shares as a result of the spin-off. The adjusted value was calculated based on the five day average closing price of the New Media's shares subsequent to the spin-off date.

Newcastle's outstanding options at June 30, 2014 consisted of the following:

	Number of Options	Strike Price (A)	Maturity Date
	162,500	12.84	11/22/2014
	330,000	12.03	1/12/2015
	2,000	12.62	8/1/2015
	170,000	11.95	11/1/2016
	242,000	12.80	1/23/2017
	456,000	11.19	4/11/2017
	1,495,166	1.51	3/29/2021
	2,294,833	0.86	9/27/2021
	2,000	1.07	12/20/2021
	1,867,167	1.61	4/3/2022
	2,265,000	1.84	5/21/2022
	2,499,167	1.83	7/31/2022
	5,750,000	3.03	1/11/2023
	2,300,000	3.54	2/15/2023
	4,025,000	3.76	6/17/2023
	5,795,095	4.04	11/22/2023
Total W/A	29,655,928	\$ 3.25	

(A) The strike prices are subject to adjustment in connection with return of capital dividends. In the first quarter of 2014 strike prices were adjusted by \$0.32 reflecting the portion of Newcastle's 2013 dividends which was deemed return of capital.

As of June 30, 2014, Newcastle's outstanding options were summarized as follows:

	Issued Prior to 2011	Issued in 2011 and thereafter	Total
Held by the Manager	1,075,130	24,396,428	25,471,558
Issued to the Manager and subsequently transferred to certain of the Manager's employees	285,370	3,895,000	4,180,370
Issued to the independent directors	2,000	2,000	4,000
Total	1,362,500	28,293,428	29,655,928
Weighted average strike price	\$ 11.97	\$ 2.83	\$ 3.25

On March 14, 2014, Newcastle declared a quarterly dividend of \$0.10 per common share, and declared dividends of \$0.609375, \$0.503125 and \$0.523438 per share on the 9.750% Series B, 8.050% Series C and 8.375% Series D preferred stock, respectively, for the quarter ended March 31, 2014. Dividends totaling \$36.5 million were paid in April 2014.

On June 13, 2014, Newcastle declared a quarterly dividend of \$0.10 per common share, and declared dividends of \$0.609375, \$0.503125 and \$0.523438 per share on the 9.750% Series B, 8.050% Series C and 8.375% Series D preferred stock, respectively, for the quarter ended June 30, 2014. Dividends totaling \$36.6 million were paid in July 2014.

B. Option Exercises

In connection with his resignation, Newcastle's former COO exercised 215,000 options with a weighted average exercise price of \$1.12 on May 7, 2014. Upon exercise, 215,000 shares of Newcastle common stock were issued to the former COO. In addition, 88,650 options were forfeited and transferred back to the Manager.

C. Earnings Per Share

Newcastle is required to present both basic and diluted earnings per share ("EPS"). Basic EPS is calculated by dividing net income available for common stockholders by the weighted average number of shares of common stock outstanding during each period. Diluted EPS is calculated by dividing net income available for common stockholders by the weighted average number of shares of common stock outstanding plus the additional dilutive effect of common stock equivalents during each period. Due to rounding, income per share from continuing operations and income per share from discontinued operations may not sum to the income per share of common stock. Newcastle's common stock equivalents are its outstanding stock options. As of June 30, 2014, Newcastle had 1,362,500 antidilutive options. During the six months ended June 30, 2014 and 2013, based on the treasury stock method, Newcastle had 11,436,921 and 5,558,512 dilutive common stock equivalents, respectively, resulting from its outstanding options. During the three months ended June 30, 2014 and 2013, based on the treasury stock method, Newcastle had 11,262,505 and 6,167,876 dilutive common stock equivalents, respectively, resulting from its outstanding options. Net income available for common stockholders is equal to net income less preferred dividends and net income attributable to noncontrolling interest.

**14. COMMITMENTS AND CONTINGENCIES**

Newcastle is, from time to time, a defendant in legal actions from transactions conducted in the ordinary course of business. Management, after consultation with legal counsel, believes the ultimate liability arising from such actions, individually and in the aggregate, that existed at June 30, 2014, if any, will not materially affect Newcastle's consolidated results of operations or financial position.

As part of the June 2014 Master Tenant lease, Newcastle committed to making available \$6.5 million immediately for capital improvements and other repairs in the properties under the lease agreement and also agreed to make available to the June 2014 Master Tenant an additional \$9.0 million at certain intervals during the lease period to be used for further capital improvements. Upon funding the capital improvements, Newcastle will be entitled to a rent increase.

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## 15. INCOME TAXES

The provision for income taxes (including discontinued operations) consists of the following:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014(A)	2013
<b>Current:</b>				
Federal	\$ 518	\$ —	\$ 590	\$ —
State and Local	103	—	164	—
Total Current Provision	\$ 621	\$ —	\$ 754	\$ —
<b>Deferred:</b>				
Federal	\$ (74)	\$ —	\$ (314)	\$ —
State and Local	(7)	—	(520)	—
Total Deferred Provision	\$ (81)	\$ —	\$ (834)	\$ —
<b>Total Provision for Income Taxes</b>	<b>\$ 540</b>	<b>\$ —</b>	<b>\$ (80)</b>	<b>\$ —</b>

(A) The provision for income taxes for the six months ended June 30, 2014 includes \$0.9 million income tax benefit from New Media that is included in income (loss) from discontinued operations on the consolidated statement of income.

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets as of June 30, 2014 and December 31, 2013 are presented below:

	June 30, 2014	December 31, 2013
<b>Deferred tax assets:</b>		
Allowance for loan losses	\$ 921	\$ 2,076
Depreciation and amortization	37,524	94,880
Leaseholds	6,905	6,489
Accrued expenses	15,292	23,816
Deposits	7,787	7,787
Net operating losses	53,135	211,560
Other	373	17,036
Total deferred tax assets	121,937	363,644
Less valuation allowance	(121,567)	(363,192)
Net deferred tax assets(A)	\$ 370	\$ 452
<b>Deferred tax liabilities:</b>		
Other	—	—
Total deferred tax liabilities	\$ —	\$ —

(A) Recorded in Receivables and Other Assets on the consolidated balance sheets.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which temporary differences become deductible.

Newcastle had recorded a valuation allowance against a significant portion of its deferred tax assets as of June 30, 2014 as management does not believe that it is more likely than not that the deferred tax assets will be realized.

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During the period ended June 30, 2014, the valuation allowance decreased by \$241.6 million primarily related to the spin-off of New Media.

The following table summarizes the change in the deferred tax asset valuation allowance:

Valuation allowance at December 31, 2013	\$	363,192
Decrease due to spin-off of New Media		(244,401)
Other increase		2,776
Valuation allowance at June 30, 2014	\$	<u>121,567</u>

16. GAINS (LOSSES) ON SETTLEMENT OF INVESTMENTS, NET AND OTHER INCOME (LOSS), NET

These items are comprised of the following:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Gain (loss) on settlement of investments, net				
Gain on settlement of real estate securities	\$ 15,698	\$ 8,209	\$ 18,032	\$ 8,209
Loss on settlement of real estate securities	—	(3,592)	—	(3,592)
Gain on repayment/disposition of loans held-for-sale	24,737	—	24,737	—
Loss on repayment/disposition of loans held-for-sale	—	(354)	—	(354)
Gain on termination of derivative	—	813	—	813
Loss on disposal of long-lived assets	(32)	(10)	(34)	(13)
	<u>\$ 40,403</u>	<u>\$ 5,066</u>	<u>\$ 42,735</u>	<u>\$ 5,063</u>
Other income (loss), net				
Gain (loss) on non-hedge derivative instruments	\$ 3,855	\$ 2,282	\$ 16,603	\$ 5,408
Hedge ineffectiveness	259	—	259	—
Collateral management fee income, net	250	336	515	688
Equity in earnings of equity method investees	328	—	289	—
Other income (loss)	—	406	500	1,495
	<u>\$ 4,692</u>	<u>\$ 3,024</u>	<u>\$ 18,166</u>	<u>\$ 7,591</u>

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**17. RECLASSIFICATION FROM ACCUMULATED OTHER COMPREHENSIVE INCOME INTO NET INCOME**

The following table summarizes the amounts reclassified out of accumulated other comprehensive income into net income:

Accumulated Other Comprehensive Income Components	Income Statement Location	Three Months Ended June 30,		Six Months Ended June 30,	
		2014	2013	2014	2013
<b>Net realized gain (loss) on securities</b>					
Impairment	Other-than-temporary impairment on securities, net of portion of other-than-temporary impairment on securities recognized in other comprehensive income	\$ —	\$ (3,910)	\$ —	\$ (4,449)
Gain on settlement of real estate securities	Gain (loss) on settlement of investments, net	15,698	8,209	18,032	8,209
Loss on settlement of real estate securities	Gain (loss) on settlement of investments, net	—	(3,592)	—	(3,592)
		<u>\$ 15,698</u>	<u>\$ 707</u>	<u>\$ 18,032</u>	<u>\$ 168</u>
<b>Net realized gain (loss) on derivatives designated as cash flow hedges</b>					
Hedge ineffectiveness	Other income (loss)	\$ (259)	\$ —	\$ (259)	\$ —
Amortization of deferred gain (loss)	Interest expense	13	1	26	1
Gain (loss) reclassified from AOCI into income, related to effective portion	Interest expense	(1,178)	(1,703)	(2,457)	(3,568)
		<u>\$ (1,424)</u>	<u>\$ (1,702)</u>	<u>\$ (2,690)</u>	<u>\$ (3,567)</u>
Total reclassifications		<u>\$ 14,274</u>	<u>\$ (995)</u>	<u>\$ 15,342</u>	<u>\$ (3,399)</u>

**18. SUPPLEMENTAL NON-CASH INVESTING AND FINANCING ACTIVITIES RELATED TO CDOs**

Newcastle considers all activity in its CDOs' restricted cash accounts to be non-cash activity for purposes of its consolidated statement of cash flows since transactions conducted with restricted cash have no effect on its cash and cash equivalents. Supplemental non-cash investing and financing activities relating to CDOs are disclosed below:

	Six Months Ended June 30,	
	2014	2013
Restricted cash generated from sale of securities	\$ 72,442	\$ 135,900
Restricted cash generated from sale of loans	\$ —	\$ 9,318
Restricted cash generated from paydowns on securities and loans	\$ 221,549	\$ 179,583
Restricted cash used for repayments of CDO bonds payable	\$ 288,206	\$ 235,883
Restricted cash used for settlement of derivative instruments	\$ —	\$ 1,563

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

JUNE 30, 2014

(dollars in tables in thousands, except share data)

**19. RECENT ACTIVITIES**

These financial statements include a discussion of material events, if any, that have occurred subsequent to June 30, 2014 (referred to as “subsequent events”) through the issuance of these consolidated financial statements. Events subsequent to that date have not been considered in these financial statements.

In July 2014, Newcastle sold residential whole loans with an outstanding face amount of \$37.6 million out of the June 30, 2014 pool of \$43.2 million outstanding face amount (Note 6) at a price of 91.5% of par or \$34.8 million of proceeds. A part of the proceeds was used to repay \$23.0 million in repurchase agreements associated with these loans. Newcastle recognized a gain on settlement of investments of \$7.3 million and incurred approximately \$1.2 million of transaction expenses.

In July 2014, Newcastle financed an additional \$20.0 million face amount of previously repurchased CDO bonds payable with repurchase agreements for \$12.0 million. These repurchase agreements bear interest at one month LIBOR + 1.65%, mature in August 2014 and are subject to customary margin provisions.

In July 2014, Newcastle issued an aggregate of 15,658 shares of its common stock to its independent directors as compensation.

On August 6, 2014, Newcastle's board of directors approved a 3-for-1 reverse stock split of its common stock. Newcastle expects the reverse stock split will be effective after the close of trading on Monday, August 18, 2014, and that shares of Newcastle's common stock will begin trading on a split-adjusted basis on the New York Stock Exchange beginning at the opening of trading on Tuesday, August 19, 2014.

As a result of the reverse stock split, every three shares of Newcastle's common stock will be converted into one share of common stock, reducing the number of issued and outstanding shares of Newcastle's common stock from approximately 352 million to approximately 117 million. Newcastle's common stock will continue to trade under the symbol “NCT”.

No fractional shares will be issued in connection with the reverse stock split. Each stockholder who would otherwise be entitled to receive a fractional share of Newcastle's common stock will be entitled to receive a cash payment in lieu of a fractional share.

The reverse stock split is not subject to stockholder approval and will not change the authorized number of shares of Newcastle or the par value of Newcastle's common stock or preferred stock.

The following table presents pro forma basic and diluted earnings per share attributable to Newcastle's stockholders to reflect the effect of the 3-for-1 reverse common stock split:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
<b>Income Per Share of Common Stock</b>				
Basic	\$ 0.26	\$ 0.61	\$ 0.30	\$ 1.08
Diluted	\$ 0.26	\$ 0.59	\$ 0.29	\$ 1.06
<b>Income from continuing operations per share of common stock, after preferred dividends and noncontrolling interests</b>				
Basic	\$ 0.27	\$ 0.31	\$ 0.34	\$ 0.65
Diluted	\$ 0.26	\$ 0.30	\$ 0.33	\$ 0.63
<b>Income (loss) from discontinued operations per share of common stock</b>				
Basic	\$ —	\$ 0.30	\$ (0.05)	\$ 0.43
Diluted	\$ —	\$ 0.29	\$ (0.05)	\$ 0.42
<b>Weighted Average Number of Shares of Common Stock Outstanding</b>				
Basic	117,199,333	86,409,447	117,175,382	82,416,367
Diluted	120,953,502	88,465,406	120,987,689	84,269,204

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Management's discussion and analysis of financial condition and results of operations is intended to help the reader understand the results of operations and financial condition of Newcastle Investment Corp. ("Newcastle" or the "Company".) The following should be read in conjunction with the unaudited consolidated financial statements and notes thereto included herein, and with Part II, Item 1A, "Risk Factors."

### GENERAL

Newcastle Investment Corp. ("Newcastle") is a real estate investment trust ("REIT") that focuses on opportunistically investing in, and actively managing, a variety of real estate-related and other investments. Newcastle is externally managed and advised by an affiliate of Fortress Investment Group LLC, or Fortress (the "Manager"). Newcastle's common stock is traded on the New York Stock Exchange under the symbol "NCT".

We currently invest in (1) senior housing properties, (2) real estate debt and (3) golf and other investments. Our investment guidelines are purposefully broad to enable us to make investments in a wide array of assets, and we actively explore new business opportunities and asset categories as part of our business strategy. Our objective is to leverage our longstanding investment expertise to drive attractive risk-adjusted returns. We target stable long-term cash flows and seek to employ conservative capital structures to generate returns throughout different interest rate environments. We take an active approach centered around identifying and executing on opportunities, responding to the changing market environment, and dynamically managing our investment portfolio to enhance returns.

In our senior housing business, we acquire and own senior housing properties. We either have our properties operated pursuant to property management agreements with third parties ("managed properties") or lease our properties to third-party tenants ("triple net lease properties"). Currently, our managed properties are managed by affiliates or subsidiaries of either Holiday Acquisition Holdings LLC ("Holiday") or FHC Property Management LLC (together with its subsidiaries, "Blue Harbor"). Holiday is a portfolio company that is majority owned by private equity funds managed by an affiliate of our Manager, and Blue Harbor is an affiliate of our Manager. Our triple net lease properties are currently leased to Holiday and a third party. As of June 30, 2014, we owned 38 managed properties and 57 triple net lease properties.

During the six months ended June 30, 2014, we invested a total of \$194.7 million of cash to acquire senior housing properties. We completed the acquisition of five managed properties in three different portfolios for an aggregate purchase price of \$44.5 million plus acquisition related costs and the acquisition of six triple net lease properties in one portfolio for an aggregate purchase price of \$183.0 million plus acquisition related costs.

On June 16, 2014, Newcastle announced that its board of directors unanimously approved a plan to spin off its senior housing business. Newcastle intends to effect the spin-off by distributing shares of its subsidiary, New Senior Investment Group Inc. ("New Senior", NYSE: SNR). New Senior will be a publicly traded real estate investment trust that primarily targets senior housing related investments. New Senior has filed a registration statement with the U.S. Securities and Exchange Commission ("SEC") with respect to the planned spin-off. The spin-off is subject to certain conditions, such as the SEC declaring effective New Senior's registration statement, the filing and approval of an application to list New Senior's common stock on the NYSE and the formal declaration of the distribution by the board of directors.

On February 13, 2014, we spun off New Media Investment Group Inc. ("New Media"). The spin-off was effected as a taxable pro rata distribution by Newcastle of all of the outstanding shares of common stock we held of New Media to our common stockholders of record at the close of business on February 6, 2014. The distribution ratio was 0.0722 shares of New Media common stock for each share of Newcastle common stock.

We now conduct our business through the following segments: (i) investments in senior housing properties ("senior housing"), (ii) debt investments financed with collateralized debt obligations ("CDOs"), (iii) other debt investments ("other debt"), (iv) investment in golf properties and facilities ("golf"), and (v) corporate.

Revenues attributable to each segment, as revised for previously reported periods, primarily to reflect the spin-off of New Media on February 13, 2014 and New Residential Investment Corp. ("New Residential"), are disclosed below (in thousands):

	Debt Investments						Total
	Senior Housing	CDOs	Other Debt	Golf	Corporate		
<b>For the Six Months Ended June 30, 2014</b>							
Revenues	\$ 117,508	\$ 51,319	\$ 30,457	\$ 146,737	\$ 35	\$ 346,056	(1)
Inter-segment elimination		(4,436)				(4,436)	
Revenues, net	\$ 117,508	\$ 46,883	\$ 30,457	\$ 146,737	\$ 35	\$ 341,620	
<b>For the Six Months Ended June 30, 2013</b>							
Revenues	\$ 26,510	\$ 68,553	\$ 58,435	\$ —	\$ 102	\$ 153,600	(1)
Inter-segment elimination	—	(1,931)	—	—	—	(1,931)	
Revenues, net	\$ 26,510	\$ 66,622	\$ 58,435	\$ —	\$ 102	\$ 151,669	

(1) Excludes \$68.2 million and \$15.1 million of revenue for the six months ended June 30, 2014 and 2013, respectively, from New Media and Excess MSRs which, as previously stated, were spun-off.

Unless otherwise noted, the information provided in Management's Discussion and Analysis of Financial Condition and Results of Operations reflects only the business segments that remain part of our business following the spin-off of New Residential and New Media.

### Market Considerations

Our ability to generate income is dependent on, among other factors, our ability to raise capital and finance investments on favorable terms, deploy capital on a timely basis at attractive returns, and exit investments at favorable yields. Market conditions outside of our control, such as interest rates, credit spreads and stock market volatility affect these objectives in a variety of ways.

Our ability to execute our business strategy, particularly the growth of our investment portfolio, depends to a significant degree on our ability to obtain additional capital. During 2013, we successfully accessed the capital markets, issuing 178,700,952 shares for total net proceeds of \$1.3 billion. However, rising interest rates or stock market volatility could impair our ability to raise equity capital on attractive terms.

### Debt Investments

Short term interest rates have risen in recent months while long term rates have decreased causing the yield curve to flatten. We project short and long term rates to increase in the future, although the timing of any further increases is uncertain. We have investments in both floating and fixed rate real estate related securities and loans, which are affected by interest rates in different ways. We expect that the value of our floating rate assets would not be significantly affected by a change in interest rates (whether an increase or decrease), since the coupon tracks the movement in rates, while the value of fixed rate assets can be negatively affected by rising interest rates. However, in general, rising interest rates are usually indicative of a strengthening economic environment, which could reduce the credit risk of some of our investments. With respect to our fixed rate assets, we believe that the negative impact of rising interest rates could potentially be offset by the positive impact of reduced credit risk.

Credit spreads also affect the value of our investments in debt securities and loans. Credit spreads decreased, or "tightened," during the first six months of 2014 relative to 2013, which has had a favorable impact on the value of our portfolio. Credit spreads measure the yield relative to a specified benchmark that the market demands on securities and loans based on the credit risk of such assets. The value of our portfolio tends to increase when spreads tighten, because under these circumstances the yield on our investments will generally be higher than the yield available on comparable new investments. However, tightening spreads tend to reduce the yields available on potential new investments. Conversely, when spreads increase or "widen," the potential yields on new investments increase, but the value of our existing investments in debt securities and loans tends to decline. As a result, widening spreads negatively affect our ability to exit investments at attractive returns. Credit spreads also affect the cost of financing, with widening spreads tending to increase the cost, and tightening spreads tending to reduce it.

## Senior Housing

We believe that the senior housing sector currently presents an attractive investment opportunity. Specifically:

- we expect projected changes in demographics will drive increased demand for senior housing, creating favorable supply-demand fundamentals;
- targeting smaller portfolios enables us to reduce competition with other active REIT buyers of large portfolios;
- and
- capitalizing on the experience of our Manager in the senior housing industry, we expect to generate growth in property-level net operating income when operational and structural efficiencies are achieved.

We made four acquisitions of senior housing portfolios comprised of 11 properties during the six months ended June 30, 2014. We continue to explore opportunities to invest in additional senior housing properties across the United States. While we generally target small portfolios, we have invested in large portfolios that we believe offer attractive risk-adjusted returns.

Our senior housing acquisitions have been financed with a combination of fixed and floating rate debt. Rising interest rates would increase the cost of our floating rate financing and negatively impact the returns on our senior housing investments.

## Golf Business

With respect to our Golf business, trends in consumer discretionary spending as well as climate and weather patterns have a significant impact on the markets in which we operate. We believe improving economic conditions and improvements in local housing markets will help drive membership growth and golf rounds played.

## **APPLICATION OF CRITICAL ACCOUNTING POLICIES**

Management's discussion and analysis of financial condition and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP"). The preparation of financial statements in conformity with GAAP requires the use of estimates and assumptions that could affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities and the reported amounts of revenue and expenses. Actual results could differ from these estimates. Management believes that the estimates and assumptions utilized in the preparation of the consolidated financial statements are prudent and reasonable. Actual results historically have been in line with management's estimates and judgments used in applying each of the accounting policies described below, as modified periodically to reflect current market conditions. The following is a summary of our accounting policies that are most effected by judgments, estimates and assumptions.

### General

#### *Variable Interest Entities*

Variable interest entities ("VIEs") are defined as entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. A VIE is required to be consolidated by its primary beneficiary, and only by its primary beneficiary, which is defined as the party who has the power to direct the activities of a VIE that most significantly impact its economic performance and who has the obligation to absorb losses or the right to receive benefits from the VIE that could potentially be significant to the VIE.

The VIEs in which we have a significant interest include our CDOs. We do not have the power to direct the relevant activities of CDO V, as a result of an event of default which allows us to be removed as collateral manager of this CDO and prevents us from purchasing or selling certain collateral within this CDO, and therefore we deconsolidated this CDO as of June 17, 2011. Similar events of default in the future, if they occur, could cause us to deconsolidate additional financing structures.

Our subprime securitizations are also considered VIEs, but we do not control the decisions that most significantly impact their economic performance and no longer receive a significant portion of their returns, and therefore do not consolidate them.

In addition, our investments in RMBS, CMBS, CDO securities and real estate related and other loans may be deemed to be variable interests in VIEs, depending on their structure. We monitor these investments and analyze the potential need to consolidate the related securitization entities pursuant to the VIE consolidation requirements. These analyses require considerable judgment in determining whether an entity is a VIE and determining the primary beneficiary of a VIE since they involve subjective

determinations of significance, with respect to both power and economics. The result could be the consolidation of an entity that otherwise would not have been consolidated or the deconsolidation of an entity that otherwise would have been consolidated.

## Debt Investments

### *Valuation of Securities*

We have classified all our real estate securities as available for sale. As such, they are carried at fair value with net unrealized gains or losses reported as a component of accumulated other comprehensive income, to the extent impairment losses are considered temporary as described below. Fair value may be based upon broker quotations, counterparty quotations or pricing services quotations, which provide valuation estimates based upon reasonable market order indications or a good faith estimate thereof and are subject to significant variability based on market conditions, such as interest rates, credit spreads and market liquidity. A significant portion of our securities are currently not traded in active markets and therefore have little or no price transparency. For a further discussion of this trend, see “- Market Considerations” above. As a result, we have estimated the fair value of these illiquid securities based on internal pricing models rather than the sources described above. The determination of estimated cash flows used in pricing models is inherently subjective and imprecise. Changes in market conditions, as well as changes in the assumptions or methodology used to determine fair value, could result in a significant and immediate increase or decrease in our book equity. For securities valued with pricing models, these inputs include the discount rate, assumptions relating to prepayments, default rates and loss severities, as well as other variables.

See Note 12 to our consolidated financial statements in Part I, Item 1, “Financial Statements” for information regarding the fair value of our investments, and its estimation methodology, as of June 30, 2014.

Our securities must be categorized by the “level” of inputs used in estimating their fair values. Level 1 would be assets valued based on quoted prices for identical instruments in active markets. We have no level 1 assets. Level 2 would be assets valued based on quoted prices in active markets for similar instruments, on quoted prices in less active or inactive markets, or on other “observable” market inputs. Level 3 would be assets valued based significantly on “unobservable” market inputs. Fair value under GAAP represents an exit price in the normal course of business, not a forced liquidation price. If we were forced to sell assets in a short period to meet liquidity needs, the prices we receive could be substantially less than the recorded fair values.

We generally classify the broker and pricing service quotations we receive as level 3 inputs, except for certain liquid securities. They are quoted prices in generally inactive and illiquid markets for identical or similar securities. These quotations are generally received via email and contain disclaimers which state that they are “indicative” and not “actionable” - meaning that the party giving the quotation is not bound to actually purchase the security at the quoted price. These quotations are generally based on models prepared by the brokers, and we have little visibility into the inputs they use. Based on quarterly procedures we have performed with respect to quotations received from these brokers, including comparison to the outputs generated from our internal pricing models and transactions we have completed with respect to these securities, as well as on our knowledge and experience of these markets, we have generally determined that these quotes represent a reasonable estimate of fair value. For the \$305.3 million carrying value of securities valued using quotations as of June 30, 2014, a 100 basis point change in credit spreads would impact estimated fair value by approximately \$7.5 million.

Our estimation of the fair value of level 3 assets valued using internal models (as described below) involves significant judgment. We validated the inputs and outputs of our models by comparing them to available independent third party market parameters and models for reasonableness. We believe the assumptions we used are within the range that a market participant would use and factor in the liquidity conditions currently in the markets. In the period ended June 30, 2014, the inputs to our models, including discount rates, prepayment speeds, default rates and severity assumptions, have generally remained consistent with the assumptions used at December 31, 2013.

For securities valued with internal models, which have an aggregate fair value of \$6.0 million as of June 30, 2014, a 10% unfavorable change in our assumptions would result in the following decreases in such aggregate fair value (in thousands):

	CDO	
Outstanding face amount	\$	40,843
Fair value	\$	5,973
Effect on fair value with 10% unfavorable change in:		
Discount rate	\$	(349)
Prepayment rate	\$	238
Default rate	\$	(410)
Loss severity	\$	(639)

The sensitivity analysis is hypothetical and should be used with caution. In particular, the results are calculated by stressing a particular economic assumption independent of changes in any other assumption; in practice, changes in one factor may result in changes in another, which might counteract or amplify the sensitivities. Also, changes in the fair value based on a 10% variation in an assumption generally may not be extrapolated because the relationship of the change in the assumption to the change in fair value may not be linear.

#### *Impairment of Securities*

We must also assess whether unrealized losses on securities, if any, reflect a decline in value which is other-than-temporary and, if so, write the impaired security down to its fair value through earnings. A decline in value is deemed to be other than-temporary if (i) it is probable that we will be unable to collect all amounts due according to the contractual terms of a security which was not impaired at acquisition (there is an expected credit loss), or (ii) if we have the intent to sell a security in an unrealized loss position or it is more likely than not we will be required to sell a security in an unrealized loss position prior to its anticipated recovery (if any). For the purposes of performing this analysis, we assume the anticipated recovery period is until the respective security's expected maturity. Also, for certain securities which represent beneficial interests in securitized financial assets, whenever there is a probable adverse change in the timing or amounts of estimated cash flows of a security from the cash flows previously projected, an other-than-temporary impairment will be deemed to have occurred. Our non-Agency RMBS acquired with evidence of deteriorated credit quality for which it was deemed probable, at acquisition, that we would be unable to collect all contractually required payments as they come due, fall within the scope of loans and debt securities acquired with deteriorated credit quality, as opposed to beneficial interests in securitized financial assets. We note that primarily all of our securities, except our FNMA/FHLMC securities and our non-Agency RMBS acquired with evidence of deteriorated credit quality, fall within the definition of beneficial interests in securitized financial assets.

Temporary declines in value generally result from changes in market factors, such as market interest rates and credit spreads, or from certain macroeconomic events, including market disruptions and supply changes, which do not directly impact our ability to collect amounts contractually due. We continually evaluate the credit status of each of our securities and the collateral supporting our securities. This evaluation includes a review of the credit of the issuer of the security (if applicable), the credit rating of the security, the key terms of the security (including credit support), debt service coverage and loan to value ratios, the performance of the pool of underlying loans and the estimated value of the collateral supporting such loans, including the effect of local, industry and broader economic trends and factors. These factors include loan default expectations and loss severities, which are analyzed in connection with a particular security's credit support, as well as prepayment rates. These factors are also analyzed in relation to the amount of the unrealized loss and the period elapsed since it was incurred. The result of this evaluation is considered when determining management's estimate of cash flows, particularly with respect to developing the necessary inputs and assumptions. Each security is impacted by different factors and in different ways; generally the more negative factors which are identified with respect to a given security, the more likely we are to determine that we do not expect to receive all contractual payments when due with respect to that security. Significant judgment is required in this analysis.

As of June 30, 2014, we had 6 securities with a carrying amount of \$9.4 million that had been downgraded during the period ended June 30, 2014. We did not record a net other-than-temporary impairment charge on these securities for the period ended June 30, 2014. However, we do not depend on credit ratings in underwriting our securities, either at acquisition or on an ongoing basis. As mentioned above, a credit rating downgrade is one factor that we monitor and consider in our analysis regarding other-than-temporary impairment, but it is not determinative. Our securities generally benefit from the support of one or more subordinate classes of securities or equity or other forms of credit support. Therefore, credit rating downgrades, even to the extent they relate

to an expectation that a securitization we have invested in, on an overall basis, has credit issues, may not ultimately impact cash flow estimates for the class of securities in which we are invested.

Furthermore, the analysis of whether it is more likely than not that we will be required to sell securities in an unrealized loss position prior to an expected recovery in value (if any), the amount of such expected required sales, and the projected identification of which securities would be sold is also subject to significant judgment.

#### *Revenue Recognition on Securities*

Income on these securities is recognized using a level yield methodology based upon a number of cash flow assumptions that are subject to uncertainties and contingencies. Such assumptions include the rate and timing of principal and interest receipts (which may be subject to prepayments and defaults). These assumptions are updated on at least a quarterly basis to reflect changes related to a particular security, actual historical data, and market changes. These uncertainties and contingencies are difficult to predict and are subject to future events, and economic and market conditions, which may alter the assumptions. For securities acquired at a discount for credit losses, we recognize the excess of all cash flows expected over our investment in the securities as Interest Income on a "loss-adjusted" yield basis. The loss-adjusted yield is determined based on an evaluation of the credit status of securities, as described in connection with the analysis of impairment above.

#### *Valuation of Derivatives*

Similarly, our derivative instruments are carried at fair value. Fair value is based on counterparty quotations. Newcastle reports the fair value of derivative instruments gross of cash paid or received pursuant to credit support agreements and fair value is reflected on a net counterparty basis when Newcastle believes a legal right of offset exists under an enforceable netting agreement. To the extent they qualify as cash flow hedges, net unrealized gains or losses are reported as a component of accumulated other comprehensive income; otherwise, the net unrealized gains and losses are reported currently in income. To the extent they qualify as fair value hedges, net unrealized gains or losses on both the derivative and the related portion of the hedged item are reported currently in income. Fair values of such derivatives are subject to significant variability based on many of the same factors as the securities discussed above, including counterparty credit risk. The results of such variability, the effectiveness of our hedging strategies and the extent to which a forecasted hedged transaction remains probable of occurring, could result in a significant increase or decrease in our GAAP equity and/or earnings.

#### *Loans*

We invest in loans, including, but not limited to, real estate related and other loans, including corporate bank loans, commercial mortgage loans, residential mortgage loans, manufactured housing loans and subprime mortgage loans. Loans for which we have the intent and ability to hold for the foreseeable future, or until maturity or payoff, are classified as held-for-investment. Loans for which we do not have the intent or the ability to hold for the foreseeable future, or until maturity or payoff, are classified as held-for-sale. Loans are presented in the consolidated balance sheet net of any unamortized discount (or gross of any unamortized premium) and an allowance for loan losses. We determine at acquisition whether loans will be aggregated into pools based on common risk characteristics (credit quality, loan type, and date of origination or acquisition); loans aggregated into pools are accounted for as if each pool were a single loan.

#### *Impairment of Loans*

To the extent that they are classified as held for investment, we must periodically evaluate each of these loans or loan pools for possible impairment. Impairment is indicated when it is deemed probable that we will be unable to collect all amounts due according to the contractual terms of the loan, or, for loans acquired at a discount for credit losses, when it is deemed probable that we will be unable to collect as anticipated. Upon determination of impairment, we would establish a specific valuation allowance with a corresponding charge to earnings. We continually evaluate our loans receivable for impairment.

Our residential mortgage loans, including manufactured housing loans, are aggregated into pools for evaluation based on like characteristics, such as loan type and acquisition date. Individual loans are evaluated based on an analysis of the borrower's performance, the credit rating of the borrower, debt service coverage and loan to value ratios, the estimated value of the underlying collateral, the key terms of the loan, and the effect of local, industry and broader economic trends and factors. Pools of loans are also evaluated based on similar criteria, including historical and anticipated trends in defaults and loss severities for the type and seasoning of loans being evaluated. This information is used to estimate specific impairment charges on individual loans as well as provisions for estimated unidentified incurred losses on pools of loans.

Significant judgment is required both in determining impairment and in estimating the resulting loss allowance. Furthermore, we must assess our intent and ability to hold our loan investments on a periodic basis. If we do not have the intent to hold a loan for the foreseeable future or until its expected payoff, the loan must be classified as “held for sale” and recorded at the lower of cost or estimated value.

#### *Revenue Recognition on Loans Held for Investment*

Income on these loans is recognized similarly to that on our securities and is subject to similar uncertainties and contingencies, which are also analyzed on at least a quarterly basis. For loans acquired at a discount for credit losses, the net income recognized is based on a “loss adjusted yield” whereby a gross interest yield is recorded to Interest Income, offset by a provision for probable, incurred credit losses which is accrued on a periodic basis to Valuation Allowance. The provision is determined based on an evaluation of the loans as described under “- Impairment of Loans” above. A rollforward of the allowance is included in Note 6 to our consolidated financial statements in Part I, Item 1, “Financial Statements.”

#### *Revenue Recognition on Loans Held for Sale*

Real estate related, commercial mortgage and residential mortgage loans that are considered held for sale are carried at the lower of amortized cost or market value determined on either an individual method basis, or in the aggregate for pools of similar loans. Interest income is recognized based on the loan’s coupon rate to the extent management believes it is collectible. Purchase discounts are not amortized as interest income during the period the loan is held for sale. A change in the market value of the loan, to the extent that the value is not above the average cost basis, is recorded in Valuation Allowance. A rollforward of the allowance is included in Note 6 to our consolidated financial statements in Part I, Item 1, “Financial Statements.”

### Senior Housing

#### *Purchase Accounting*

The senior housing properties acquired and the liabilities assumed were recorded at fair value. In determining the allocation of the purchase price between net tangible and identified intangible assets acquired and liabilities assumed, management made estimates of the fair value of the tangible and intangible assets and liabilities using information obtained as a result of preacquisition due diligence, marketing, leasing activities, and independent appraisals. Management allocated the purchase price to net tangible and identified intangible assets acquired and liabilities assumed based on their fair values as of the acquisition date. The determination of fair value involved the use of significant judgment and estimation.

#### *Impairment of Investments in Real Estate and Residential Lease Intangibles*

We own senior housing properties held for investment. Intangibles and long-lived assets are tested for potential impairment annually or when changes in circumstances indicate the carrying value may not be recoverable. Indicators of impairment include material adverse changes in the projected revenues and expenses, significant underperformance relative to historical or projected future operating results, and significant negative industry or economic trends. An impairment is determined to have occurred if the future net undiscounted cash flows expected to be generated is less than the carrying value of an asset. The impairment is measured as the difference between the carrying value and the fair value. Significant judgment is required both in determining impairment and in estimating the fair value. We may use assumptions and estimates derived from a review of our operating results, business projections, expected growth rates, discount rates, and tax rates. We also make certain assumptions about future economic conditions, interest rates, and other market data. Many of the factors used in these assumptions and estimates are outside the control of management, and can change in future periods.

#### *Senior Housing Revenue Recognition*

Our triple net leases provide for periodic and determinable increases in base rent. We recognize base rental revenues under these leases on a straight-line basis over the applicable lease term when collectability is reasonably assured. Recognizing rental income on a straight-line basis generally results in recognized revenues during the first half of a lease term exceeding the cash amounts contractually due from our tenants, creating a straight-line rent receivable that is included in Receivables and Other Assets on our Consolidated Balance Sheets.

We recognize rental, care, and ancillary income, other than nonrefundable community fee income, monthly as services are provided. We recognize nonrefundable community fee income on a straight-line basis over the average resident length of stay. Our lease agreements with residents generally have a term of 24 to 33 months and are cancelable by the resident upon 30 days’ notice.

## Other Businesses

### *Purchase Accounting*

The golf assets acquired and the liabilities assumed were recorded at fair value. In determining the allocation of the purchase price between net tangible and identified intangible assets acquired and liabilities assumed, management made estimates of the fair value of the tangible and intangible assets and liabilities using information obtained as a result of preacquisition due diligence, marketing, leasing activities, and independent appraisals. Management allocated the purchase price to net tangible and identified intangible assets acquired and liabilities assumed based on their fair values as of the acquisition date. The determination of fair value involved the use of significant judgment and estimation.

### *Impairment of Investments in Real Estate*

Intangibles and long-lived assets are tested for potential impairment annually or when changes in circumstances indicate the carrying value may not be recoverable. Indicators of impairment include material adverse changes in the projected revenues and expenses, significant underperformance relative to historical or projected future operating results, and significant negative industry or economic trends. An impairment is determined to have occurred if the future net undiscounted cash flows expected to be generated is less than the carrying value of an asset. The impairment is measured as the difference between the carrying value and the fair value. Significant judgment is required both in determining impairment and in estimating the fair value. We may use assumptions and estimates derived from a review of our operating results, business projections, expected growth rates, discount rates, and tax rates. We also make certain assumptions about future economic conditions, interest rates, and other market data. Many of the factors used in these assumptions and estimates are outside the control of management, and can change in future periods.

### *Intangible Assets*

We assess the potential impairment of intangible assets with indefinite lives on an annual basis. We perform our impairment at the reporting unit level. The fair value of the applicable reporting unit is compared to its carrying value. Estimating the fair value of a reporting unit requires us to make significant judgments, estimates and assumptions. We estimate fair value by applying third-party market value indicators to projected cash flows and/or projected earnings before interest, taxes, depreciation, and amortization. In applying this methodology, we rely on a number of factors, including current operating results and cash flows, expected future operating results and cash flows, future business plans, and market data. The sum of the fair values of the reporting units are reconciled to our current market capitalization (based upon the stock market price) plus an estimated control premium.

We assess the recoverability of our definite lived intangible assets, whenever events or changes in business circumstances indicate the carrying amount of the assets, or other appropriate grouping of assets, may not be fully recoverable. The assessment of recoverability is based on comparing management's estimates of the sum of the estimated undiscounted cash flows generated by the underlying asset, or other appropriate grouping of assets, to its carrying value to determine whether an impairment existed at its lowest level of identifiable cash flows. Factors leading to impairment include significant under-performance relative to historical or projected results, significant changes in the manner of use of the acquired assets or the strategy for our overall business and significant negative industry or economic trends.

### *Recent Accounting Pronouncements*

In April 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-08, *Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity*. ASU 2014-08 changes the criteria for reporting a discontinued operation. Under the new pronouncement, a disposal of a part of an organization that has a major effect on its operations and financial results is a discontinued operation. This update is effective for Newcastle in the first quarter of 2015. Newcastle is currently evaluating the new guidance to determine the impact it may have to its consolidated financial statements.

In May 2014, the FASB and the International Accounting Standards Board ("IASB") 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 Newcastle in the first quarter of 2017. Early application is not permitted. Entities have the option of using either a full

retrospective or a modified approach to adopt the guidance in the ASU. Newcastle 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 Newcastle in the first quarter of 2015. Early application is not permitted. Disclosures are not required for comparative periods presented before the effective date. Newcastle is currently evaluating the new guidance to determine the impact 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, leases, financial instruments and hedging. Some of the proposed changes are significant and could have a material impact on Newcastle's reporting. Newcastle has not yet fully evaluated the potential impact of these proposals, but will make such an evaluation as the standards are finalized.

## RESULTS OF OPERATIONS

### Consolidated Results

The following table summarizes the changes in our results of operations for the three and six months ended June 30, 2014 compared to the three and six months ended June 30, 2013 (dollars in thousands):

	Three Months Ended June 30,		Increase (Decrease)	
	2014	2013	Amount	%
Interest income	\$ 29,893	\$ 62,824	(32,931)	(52.4)%
Interest expense	33,905	21,998	11,907	54.1%
Net interest income	(4,012)	40,826	(44,838)	(109.8)%
<b>Impairment (Reversal)</b>				
Valuation allowance (reversal) on loans	1,526	(709)	2,235	(315.2)%
Other-than-temporary impairment on securities, net	—	3,910	(3,910)	(100.0)%
	1,526	3,201	(1,675)	(52.3)%
Net interest income after impairment/reversal	(5,538)	37,625	(43,163)	(114.7)%
<b>Operating Revenues</b>	143,646	14,013	129,633	N.M
<b>Other Income</b>				
Gain on settlement of investments, net	40,403	5,066	35,337	N.M
Gain (loss) on extinguishment of debt	(3,410)	—	(3,410)	N.M
Other income, net	4,692	3,024	1,668	55.2%
	41,685	8,090	33,595	415.3%
<b>Expenses</b>				
Loan and security servicing expense	408	1,021	(613)	(60.0)%
Property operating expenses	24,280	8,409	15,871	188.7%
Operating expenses - golf	65,178	—	65,178	N.M
Cost of sales - golf	8,807	—	8,807	N.M
General and administrative expense	9,633	9,938	(305)	(3.1)%
Management fee to affiliate	7,475	8,148	(673)	(8.3)%
Depreciation and amortization	31,031	4,070	26,961	N.M
	146,812	31,586	115,226	364.8%
Income from continuing operations before income tax	\$ 32,981	\$ 28,142	\$ 4,839	17.2%

N.M. – Not meaningful.

	Six Months Ended June 30,		Increase (Decrease)	
	2014	2013	Amount	%
Interest income	\$ 76,345	\$ 124,156	(47,811)	(38.5)%
Interest expense	69,760	44,708	25,052	56.0 %
Net interest income	6,585	79,448	(72,863)	(91.7)%
<b>Impairment (Reversal)</b>				
Valuation allowance (reversal) on loans	2,772	1,525	1,247	81.8 %
Other-than-temporary impairment on securities, net	—	4,449	(4,449)	(100.0)%
	2,772	5,974	(3,202)	(53.6)%
Net interest income after impairment/reversal	3,813	73,474	(69,661)	(94.8)%
<b>Operating Revenues</b>	265,275	27,513	237,762	864.2 %
<b>Other Income</b>				
Gain on settlement of investments, net	42,735	5,063	37,672	744.1 %
Gain (loss) on extinguishment of debt	(3,410)	1,206	(4,616)	(382.8)%
Other income, net	18,166	7,591	10,575	139.3 %
	57,491	13,860	43,631	314.8 %
<b>Expenses</b>				
Loan and security servicing expense	1,265	2,055	(790)	(38.4)%
Property operating expenses	48,084	16,772	31,312	186.7 %
Operating expenses - golf	123,516	—	123,516	N.M
Cost of sales - golf	14,763	—	14,763	N.M
General and administrative expense	18,845	14,151	4,694	33.2 %
Management fee to affiliate	15,512	17,713	(2,201)	(12.4)%
Depreciation and amortization	61,390	8,149	53,241	N.M
	283,375	58,840	224,535	381.6 %
Income from continuing operations before income tax	\$ 43,204	\$ 56,007	\$ (12,803)	(22.9)%

N.M. – Not meaningful.

#### Interest Income

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

Interest income decreased by \$32.9 million during the three months ended June 30, 2014 as compared to the three months ended June 30, 2013 primarily due to (i) a \$1.1 million net decrease in interest income as a result of the sale of assets in CDO IV in May 2013, (ii) a \$6.5 million net decrease in interest income as a result of the sale of the FNMA/FHLMC assets in January 2014 and assets that were spun-off in May 2013, and (iii) a \$25.3 million net decrease in interest income as a result of an overall loan principal balance reduction of approximately \$1.2 billion at June 30, 2014 compared to June 30, 2013.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

Interest income decreased by \$47.8 million during the six months ended June 30, 2014 as compared to the six months ended June 30, 2013 primarily due to (i) a \$3.5 million net decrease in interest income as a result of the sale of the assets in CDO IV in May 2013, (ii) a \$15.4 million decrease in interest income as a result of the sale of the FNMA/FHLMC assets in January 2014 and assets that were spun-off in May 2013, and (iii) a \$28.9 million net decrease in interest income as a result of an overall loan principal balance reduction of approximately \$1.2 billion at June 30, 2014 compared to June 30, 2013.

## Interest Expense

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

Interest expense increased by \$11.9 million primarily due to a \$14.1 million increase resulting from the financing of the investments in senior housing properties and the Golf business. The increase was partially offset by (i) a \$0.9 million decrease in interest expense as a result of the sale of FHMA/FHLMC securities and the repayment of related financing in January 2014, (ii) a \$1.2 million decrease in interest expense as a result of the sale of the assets in CDO IV and the repayment of related financing in May 2013, and (iii) a \$0.1 million decrease in swap interest expense due to a lower notional balance.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

Interest expense increased by \$25.1 million primarily due to a \$30.2 million increase resulting from the financing of the investments in senior housing properties and the Golf business. The increase was partially offset by (i) a \$2.6 million decrease in interest expense as a result of the sale of the assets in CDO IV and the repayment of related financing in May 2013, (ii) a \$1.9 million decrease in interest expense as a result of the sale of FHMA/FHLMC securities and the repayment of related financing in January 2014, and (iii) a \$0.6 million decrease in interest expense on derivatives due to a lower notional balance.

## Valuation Allowance (Reversal) on Loans

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

The valuation allowance (reversal) on loans of \$2.2 million is comprised of a \$0.8 million valuation allowance recorded in the three months ended June 30, 2013 on real estate related and other loans compared to \$1.5 million valuation allowance recorded in the three months ended June 30, 2014; and a reversal of valuation allowance of \$1.5 million recorded on residential mortgage loans in the three months ended June 30, 2013.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

The valuation allowance (reversal) on loans of \$1.2 million is comprised of a \$2.0 million valuation allowance recorded in the six months ended June 30, 2014 on real estate related and other loans compared a \$2.3 million valuation allowance recorded in the six months ended June 30, 2013; and a valuation allowance of \$0.8 million recorded in the six months ended June 30, 2014 on our residential mortgage loans compared to a reversal of valuation allowance of \$0.7 million recorded in the six months ended June 30, 2013.

## Other-than-temporary Impairment on Securities, Net

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

The other-than-temporary impairment on securities decreased by \$3.9 million primarily due to market conditions improving in the quarter ended June 30, 2014. We did not record any impairment charges during the three months ended June 30, 2014, compared to an impairment charge of \$3.8 million of impairment recognized on FNMA/FHLMC securities and non-Agency RMBS in connection with the spin-off of New Residential in May 2013 and \$0.1 million on three other securities not related to the New Residential spin-off.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

The other-than-temporary impairment on securities decreased \$4.4 million primarily due to market conditions improving in 2014. We did not record any impairment charges during the six months ended June 30, 2014, compared to an impairment charge of \$3.8 million of impairment recognized on FNMA/FHLMC securities and non-Agency RMBS in connection with the spin-off of New Residential in May 2013 and \$0.7 million on four securities not related to the spin-off.

## **Operating Revenues**

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

The operating revenues increased by \$129.6 million primarily due to (i) a \$46.2 million increase resulting from the acquisitions of the senior housing properties and (ii) an \$83.4 million increase resulting from the acquisition of the Golf business in December 2013.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

The operating revenues increased by \$237.8 million primarily due to (i) a \$91.1 million increase resulting from the acquisitions of the senior housing properties and (ii) a \$146.7 million increase resulting from the acquisition of the Golf business in December 2013.

## **Gain on Settlement of Investments, Net**

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

The net gain on settlement of investments increased by \$35.3 million. During the three months ended June 30, 2014, Newcastle recorded a gain of \$15.6 million on the sale of seven securities and the payoff of one security and also recorded a gain of \$24.7 million on the sale of its manufactured housing portfolio. During the three months ended June 30, 2013, we recorded a gain of \$4.2 million on the sale of the CDO IV assets in May 2013 and a \$0.8 million gain on the CDO IV hedge termination.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

The net gain on settlement of investments increased by \$37.7 million. During the six months ended June 30, 2014, Newcastle recorded (i) a gain of \$16.1 million on the sale of eight securities and the payoff of one security, (ii) a gain of \$24.7 million on the sale of its manufactured housing portfolio, and (iii) a gain of \$1.9 million on the sale of the FNMA/FHLMC securities in January 2014. During the six months ended June 30, 2013, we recorded a gain of \$4.2 million on the sale of the CDO IV assets in May 2013 and a \$0.8 million gain on the CDO IV hedge termination.

## **Gain (loss) on Extinguishment of Debt**

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

The loss on extinguishment of debt of \$3.4 million recorded during the three months ended June 30, 2014 relates to the write-off of the unamortized discount on the manufactured housing debt upon the sale of the portfolio and the pay off of the debt in May 2014. There were no gains or losses recorded on the extinguishment of debt in the three months ended June 30, 2013.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

The gain on extinguishment of debt decreased by \$4.6 million. During the six months ended June 30, 2014, we recorded loss on extinguishment of debt of \$3.4 million related to the write-off of the unamortized discount on the manufactured housing debt upon the sale of the portfolio and the pay off of the debt in May 2014. During the six months ended June 30, 2013, we repurchased \$10.9 million face amount of our own CDO debt at an average price of 88.8% of par.

## **Other Income, Net**

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

Other income increased by \$1.7 million primarily due to \$1.8 million of unrealized gains recognized on linked transactions during the three months ended June 30, 2014. The increase was partially offset by a \$0.1 million decrease in other income due to real estate loan paydowns during the three months ended June 30, 2014.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

Other income increased by \$10.6 million primarily due to \$12.5 million of unrealized gains recognized on linked transactions during the six months ended June 30, 2014. The increase was partially offset by (i) a \$1.3 million decrease in the fair value of

certain non-hedge interest rate swap agreements as a result of changes in interest rates and (ii) a \$0.6 million decrease in other income due to real estate loan paydowns during the six months ended June 30, 2014 compared to the six months ended June 30, 2013.

#### **Loan and Security Servicing Expense**

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

Loan and security servicing expense decreased by \$0.6 million primarily due to the paydown and sale of securities and the sale of the manufactured housing portfolio during the three months ended June 30, 2014.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

Loan and security servicing expense decreased by \$0.8 million during the six months ended June 30, 2014 compared to the six months ended June 30, 2013 primarily due to the \$1.5 billion average lower face amount of total securities and loans due to paydowns and sales.

#### **Property Operating Expenses**

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

The property operating expenses increased \$15.9 million due to the acquisitions of the senior housing properties.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

The property operating expenses increased \$31.3 million due to the acquisitions of the senior housing properties.

#### **Operating Expenses - Golf**

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

The operating expenses - golf increased due to the acquisition of the Golf business in December 2013.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

The operating expenses - golf increased due to the acquisition of the Golf business in December 2013.

#### **Cost of Sales - Golf**

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

The cost of sales - golf increased due to the acquisition of the Golf business in December 2013.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

The cost of sales - golf increased due to the acquisition of the Golf business in December 2013.

#### **General and Administrative Expense**

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

General and administrative expense decreased by \$0.3 million primarily due to a decrease in our corporate expenses partially offset by an increase in general and administrative expense in businesses that we acquired during 2013 and 2014.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

General and administrative expense increased by \$4.7 million primarily due to an increase in professional fees related to our plan to spin-off our senior housing business and the acquisition costs related to investments in senior housing properties and the

acquisition of the Golf business.

**Management Fee to Affiliate**

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

Management fees decreased by \$0.7 million primarily due to decreases in gross equity aggregating \$1.6 billion due to the New Residential and New Media spin-offs, partially offset by (i) an increase in gross equity as a result of our public offerings of common stock in 2013, and (ii) an increase in property management fees in connection with the acquisitions of senior housing properties.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

Management fees decreased by \$2.2 million primarily due to decreases in gross equity aggregating \$1.6 billion due to the New Residential and New Media spin-offs, partially offset by (i) an increase in gross equity as a result of our public offerings of common stock in 2013, and (ii) an increase in property management fees in connection with the acquisitions of senior housing properties.

**Depreciation and Amortization**

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

The depreciation and amortization expense increased by \$27.0 million due to (i) an increase of \$19.2 million resulting from the acquisitions of senior housing properties and (ii) an increase of \$7.8 million resulting from the acquisition of the Golf business in December 2013.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

The depreciation and amortization expense increased \$53.2 million due to (i) an increase of \$38.0 million resulting from the acquisitions of senior housing properties and (ii) an increase of \$15.2 million resulting from the acquisition of the Golf business in December 2013.

Segment Results

Comparison of Senior Housing Results of Operations for the three and six months ended June 30, 2014 and 2013

	Three Months Ended June 30,		Increase (Decrease)	
	2014	2013	Amount	%
<b>Revenues</b>				
Rental income	\$ 54,032	\$ 11,221	\$ 42,811	381.5 %
Care and ancillary income	5,666	2,292	3,374	147.2 %
Total Revenues	59,698	13,513	46,185	341.8 %
<b>Expenses</b>				
Property operating expenses	24,053	8,169	15,884	194.4 %
General and administrative expenses	4,861	1,887	2,974	157.6 %
Depreciation and amortization	23,188	4,016	19,172	477.4 %
Interest expense, net	13,592	1,246	12,346	N.M
Property management fee to affiliate	2,179	799	1,380	172.7 %
Total Expenses	67,873	16,117	51,756	321.1 %
Other gain (loss), net	(22)	112	(134)	(119.6)%
Loss from continuing operations before income tax	\$ (8,197)	\$ (2,492)	\$ (5,705)	228.9 %

	Six Months Ended June 30,		Increase (Decrease)	
	2014	2013	Amount	%
<b>Revenues</b>				
Rental income	\$ 106,381	\$ 22,192	\$ 84,189	379.4 %
Care and ancillary income	11,127	4,318	6,809	157.7 %
Total Revenues	117,508	26,510	90,998	343.3 %
<b>Expenses</b>				
Property operating expenses	47,573	16,285	31,288	192.1 %
General and administrative expenses	10,509	3,496	7,013	200.6 %
Depreciation and amortization	46,024	8,039	37,985	472.5 %
Interest expense, net	27,294	2,478	24,816	N.M
Property management fee to affiliate	4,323	1,578	2,745	174.0 %
Total Expenses	135,723	31,876	103,847	325.8 %
Other gain (loss), net	(23)	120	(143)	(119.2)%
Loss from continuing operations before income tax	\$ (18,238)	\$ (5,246)	\$ (12,992)	247.7 %

N.M. – Not meaningful.

**Rental Income**

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

Rental income increased by \$42.8 million during the three months ended June 30, 2014 compared to the three months ended June 30, 2013 due to the acquisitions of senior housing properties.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

Rental income increased by \$84.2 million during the six months ended June 30, 2014 compared to the six months ended June 30, 2013 due to the acquisitions of senior housing properties.

**Care and Ancillary Income**

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

Care and ancillary income increased by \$3.4 million during the three months ended June 30, 2014 compared to the three months ended June 30, 2013 due to the acquisitions of senior housing properties.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

Care and ancillary income increased by \$6.8 million during the six months ended June 30, 2014 compared to the six months ended June 30, 2013 due to the acquisitions of senior housing properties.

**Property Operating Expenses**

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

Property and operating expenses increased by \$15.9 million during the three months ended June 30, 2014 compared to the three months ended June 30, 2013 due to the acquisitions of senior housing properties.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

Property and operating expenses increased by \$31.3 million during the six months ended June 30, 2014 compared to the six months ended June 30, 2013 due to the acquisitions of senior housing properties.

**General and Administrative Expense**

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

General and administrative expense increased by \$3.0 million during the three months ended June 30, 2014 compared to the three months ended June 30, 2013 primarily due to the acquisitions of senior housing properties, the plan to spin-off our senior housing business and the growth in our senior housing business.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

General and administrative expense increased by \$7.0 million during the six months ended June 30, 2014 compared to the six months ended June 30, 2013 primarily due to the acquisitions of senior housing properties, the plan to spin-off our senior housing business and the growth in our senior housing business.

**Depreciation and Amortization**

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

Depreciation and amortization increased by \$19.2 million during the three months ended June 30, 2014 compared to the three months ended June 30, 2013 due to the acquisitions of senior housing properties.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

Depreciation and amortization increased by \$38.0 million during the six months ended June 30, 2014 compared to the six months ended June 30, 2013 due to the acquisitions of senior housing properties.

## **Interest Expense, net**

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

Interest expense, net increased by \$12.3 million during the three months ended June 30, 2014 compared to the three months ended June 30, 2013 due to the acquisitions of senior housing properties and related financing.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

Interest expense, net increased by \$24.8 million during the six months ended June 30, 2014 compared to the six months ended June 30, 2013 due to the acquisitions of senior housing properties and related financing.

## **Property Management Fee to Affiliate**

*Three months ended June 30, 2014 compared to the three months ended June 30, 2013*

Property management fee to affiliate increased by \$1.4 million during the three months ended June 30, 2014 compared to the three months ended June 30, 2013 due to the acquisitions of senior housing properties.

*Six months ended June 30, 2014 compared to the six months ended June 30, 2013*

Property management fee to affiliate increased by \$2.7 million during the six months ended June 30, 2014 compared to the six months ended June 30, 2013 due to the acquisitions of senior housing properties.

## **LIQUIDITY AND CAPITAL RESOURCES**

### *Overview*

Liquidity is a measurement of our ability to meet potential cash requirements, including ongoing commitments to repay borrowings, fund and maintain investments, and other general business needs.

Our primary sources of funds for liquidity consist of net cash provided by operating activities, sales or repayments of investments, potential refinancing of existing debt, and the issuance of equity securities, when feasible. We have an effective shelf registration statement with the Securities and Exchange Commission ("SEC"), which allows us to issue common stock, preferred stock, depository shares, debt securities and warrants. Our debt obligations are generally secured directly by our investment assets, except for the junior subordinated notes payable.

### *Sources of Liquidity and Uses of Capital*

As of the date of this filing, we have sufficient liquid assets to satisfy all of our short-term recourse liabilities. Our junior subordinated notes payable are long-term obligations. With respect to the next twelve months, we expect that our cash on hand combined with our cash flow provided by operations will be sufficient to satisfy our anticipated liquidity needs with respect to our current investment portfolio, including related financings, capital expenditures, hedging activity, potential margin calls and operating expenses. In addition, we anticipate cash requirements with respect to incremental investments, including (but not limited to) senior housing properties. We may elect to meet the cash requirements of these incremental investments through proceeds from the monetization of our assets or from additional borrowings or equity offerings. While it is inherently more difficult to forecast beyond the next twelve months, we currently expect to meet our long-term liquidity requirements, specifically the repayment of our recourse debt obligations, through our cash on hand and, if needed, additional borrowings, proceeds received from repurchase agreements and similar financings, proceeds from equity offerings and the liquidation or refinancing of our assets.

These short-term and long-term expectations are forward-looking and subject to a number of uncertainties and assumptions, which are described below under "–Factors That Could Impact Our Liquidity, Capital Resources and Capital Obligations" as well as Part II, Item 1A, "Risk Factors." If our assumptions about our liquidity prove to be incorrect, we could be subject to a shortfall in liquidity in the future, and this short-fall may occur rapidly and with little or no notice, which would limit our ability to address the shortfall on a timely basis.

Cash flow provided by operations constitutes a critical component of our liquidity. Essentially, our cash flow provided by operations is equal to (i) revenues received from our senior housing properties and Golf business, (ii) the net cash flow from our CDOs that have not failed their over collateralization or interest coverage tests, plus (iii) the net cash flow from our non-CDO investments

that are not subject to mandatory debt repayment, including principal and sales proceeds, less (iv) operating expenses (primarily management fees, property operating expenses, professional fees, insurance and taxes), less (v) interest on the junior subordinated notes payable and debt related to our senior housing and Golf segments, and less (vi) preferred dividends.

Our cash flow provided by operations differs from our net income (loss) due to these primary factors: (i) accretion of discount or premium on our real estate securities and loans (including the accrual of interest and fees payable at maturity), discount on our debt obligations, deferred financing costs, and deferred hedge gains and losses, (ii) gains and losses from sales of assets financed with CDOs, (iii) the valuation allowance recorded in connection with our loan assets, as well as other-than-temporary impairment on our securities, (iv) unrealized gains or losses on our non-hedge derivatives, (v) the non-cash gains or losses associated with our early extinguishment of debt, (vi) depreciation and amortization, and (vii) net income (loss) generated within CDOs that have failed their over collateralization or interest coverage tests. Proceeds from the sale of assets which serve as collateral for our CDO financings, including gains thereon, are required to be retained in the CDO structure until the related bonds are retired and are, therefore, not available to fund current cash needs outside of these structures.

#### *REIT Compliance Requirements*

To maintain our status as a REIT under the Code, we must distribute annually at least 90% of our REIT taxable income. On May 15, 2013, we distributed, in a taxable distribution, 100% of the common stock of New Residential Investment Corp. with a value of \$1.7 billion for tax purposes. As a result, we do not believe that there will be any additional REIT distribution requirements for the year ended December 31, 2013. As of December 31, 2012, we had a loss carryforward, inclusive of net operating loss and capital loss, of approximately \$750.2 million. The net operating loss carryforward and capital loss carryforward can generally be used to offset future ordinary taxable income and capital gain, for up to twenty years and five years, respectively. In January 2013, we experienced an “ownership change” for purposes of Section 382 of the Code, which limits our ability to utilize our net operating loss and net capital loss carryforwards to reduce our future taxable income and potentially increases our related REIT distribution requirement. We do not believe that the limitation as a result of the January 2013 ownership change will prevent us from satisfying our REIT distribution requirement for the current year or future years. No assurance, however, can be given that we will be able to satisfy our distribution requirement following a current or future ownership change or otherwise. We note that a portion of this requirement may be able to be met in future years through stock dividends, rather than cash, subject to limitations based on the value of our stock.

#### *Update on Liquidity, Capital Resources and Capital Obligations*

Certain details regarding our liquidity, current financings and capital obligations as of July 28, 2014 are set forth below:

- *Unrestricted Cash Available to Invest after Commitments* – We are currently fully invested after commitments;
- *Margin Exposure and Recourse Financings* – We have margin exposure on a \$91.8 million repurchase agreement related to the financing of certain senior notes issued by Newcastle CDO VIII and CDO IX.

The following table compares our recourse financings excluding the junior subordinated notes (in thousands):

<u>Recourse Financings</u>	<u>July 28, 2014</u>	<u>June 30, 2014</u>	<u>December 31, 2013</u>
CDO Securities	\$ 91,752	\$ 79,712	\$ 15,094
Residential mortgage loans	—	22,965	25,119
Linked transactions	—	—	60,646
Non-FNMA/FHLMC recourse financings	91,752	102,677	100,859
FNMA/FHLMC securities (1)	—	—	516,134
<b>Total recourse financings</b>	<b>\$ 91,752</b>	<b>\$ 102,677</b>	<b>\$ 616,993</b>

- (1) In January 2014, we sold \$503.0 million face of remaining FNMA/FHLMC securities at an average price of 105.82% for total proceeds of \$532.2 million and repaid \$516.1 million of associated repurchase agreements.

It is important for readers to understand that our liquidity, available capital resources and capital obligations could change rapidly due to a variety of factors, many of which are beyond our control. Set forth below is a discussion of some of the factors that could impact our liquidity, available capital resources and capital obligations.

We refer readers to our discussions in other sections of this report for the following information:

- For a further discussion of recent trends and events affecting our liquidity, see “– Market Considerations” above;
- As described above, under “– Update on Liquidity, Capital Resources and Capital Obligations,” we are subject to margin calls in connection with our repurchase agreements;
- Our match funded investments are financed long term, and their credit status is continuously monitored, which is described under "Quantitative and Qualitative Disclosures About Market Risk — Interest Rate Exposure" below. Our remaining investments, generally financed with short term debt or short term repurchase agreements, are also subject to refinancing risk upon the maturity of the related debt. See “– Debt Obligations” below; and
- For a further discussion of a number of risks that could affect our liquidity, access to capital resources and our capital obligations, see Part II, Item 1A, “Risk Factors” below.

In addition to the information referenced above, the following factors could affect our liquidity, access to capital resources and our capital obligations. As such, if their outcomes do not fall within our expectations, changes in these factors could negatively affect our liquidity.

- *Access to Financing from Counterparties* – Decisions by investors, counterparties and lenders to enter into transactions with us will depend upon a number of factors, such as our historical and projected financial performance, compliance with the terms of our current credit and derivative arrangements, industry and market trends, the availability of capital and our investors’, counterparties’ and lenders’ policies and rates applicable thereto, and the relative attractiveness of alternative investment or lending opportunities. Our business strategy is dependent upon our investments at rates that provide a positive net spread.
- *Impact of Rating Downgrades on CDO Cash Flows* – Ratings downgrades of assets in our CDOs can negatively impact compliance with the CDOs’ over collateralization tests. Generally, the over collateralization test measures the principal balance of the specified pool of assets in a CDO against the corresponding liabilities issued by the CDO. However, based on ratings downgrades, the principal balance of an asset or of a specified percentage of assets in a CDO may be deemed to be reduced below their current balance to levels set forth in the related CDO documents for purposes of calculating the over collateralization test. As a result, ratings downgrades can reduce the assumed principal balance of the assets used in the over collateralization test relative to the corresponding liabilities in the test, thereby reducing the over collateralization percentage. In addition, actual defaults of assets would also negatively impact compliance with the over collateralization tests. Failure to satisfy an over collateralization test could result in the redirection of cashflows, or, in certain cases, in the potential removal of Newcastle as collateral manager of the affected CDO. See “– Debt Obligations” below for a summary of assets on negative watch for possible downgrade in our CDOs.
- *Impact of Expected Repayment or Forecasted Sale on Cash Flows* – The timing of and proceeds from the repayment or sale of certain investments may be different than expected or may not occur as expected. Proceeds from sales of assets in the current illiquid market environment are unpredictable and may vary materially from their estimated fair value and their carrying value.

Investment Portfolio

The following summarizes our consolidated investment portfolio at June 30, 2014 (dollars in millions).

	Outstanding Face Amount	Amortized Cost Basis (1)	Percentage of Total Amortized Cost Basis	Carrying Value	Number of Investments	Credit (2)	Weighted Average Life (years) (3)
<b>Debt Investment</b>							
<b>Commercial Assets</b>							
CMBS	\$ 244	\$ 164	6.3%	\$ 207	40	B+	2.1
Mezzanine Loans	157	125	4.8%	125	8	86%	1.3
B-Notes	70	66	2.6%	66	2	84%	1.6
Whole Loans	1	1	—%	1	1	2%	0.5
CDO Securities (4)	17	6	0.2%	13	2	B	8.7
Other Investments (5)	26	26	1.0%	26	1	—	—
<b>Total Commercial Assets</b>	<b>515</b>	<b>388</b>	<b>14.9%</b>	<b>438</b>			<b>2.0</b>
<b>Residential Assets</b>							
Residential Loans	43	32	1.2%	32	165	709	5.7
Non-Agency RMBS	91	39	1.6%	61	33	CCC+	4.3
Real Estate ABS	8	—	0.0%	—	1	C	0.0
<b>Total Residential Assets</b>	<b>142</b>	<b>71</b>	<b>2.8%</b>	<b>93</b>			<b>4.5</b>
<b>Corporate Assets</b>							
REIT Debt	29	29	1.1%	31	5	BB+	1.1
Corporate Bank Loans	165	98	3.8%	98	5	C	1.9
<b>Total Corporate Assets</b>	<b>194</b>	<b>127</b>	<b>4.9%</b>	<b>129</b>			<b>1.8</b>
<b>Total Debt Investments</b>	<b>851</b>	<b>586</b>	<b>22.7%</b>	<b>660</b>			<b>2.4</b>
<b>Other Investments</b>							
<b>Senior Housing Investments (6)</b>	<b>1,730</b>	<b>1,651</b>	<b>63.8%</b>	<b>1,651</b>			
<b>Golf Investment (6)</b>	<b>367</b>	<b>350</b>	<b>13.5%</b>	<b>350</b>			
<b>Total Portfolio/Weighted Average</b>	<b>\$ 2,948</b>	<b>\$ 2,587</b>	<b>100.0%</b>	<b>\$ 2,661</b>			
Reconciliation to GAAP total assets:							
Other Assets							
Subprime mortgage loans subject to call option (7)				406			
Other commercial real estate				7			
Cash and restricted cash				82			
Other				108			
<b>GAAP total assets</b>				<b>\$ 3,264</b>			

WA – Weighted average, in all tables.

- (1) Net of impairment.
- (2) Credit represents the weighted average of minimum rating for rated assets, the loan-to-value ratio (based on the appraised value at the time of purchase or refinancing) for non-rated commercial assets, or the FICO score for non-rated residential assets. Ratings provided above were determined by third party rating agencies, represent the most recent credit ratings available as of the reporting date and may not be current.
- (3) Weighted average life is based on the timing of expected principal reduction on the asset.
- (4) Represents non-consolidated CDO securities, excluding nine securities with a zero value, which had an aggregate face amount of \$116.1 million.
- (5) Represents an equity investment in a real estate owned property.
- (6) Face amount of senior housing and golf investments represents the gross carrying amount, including intangibles, and excludes accumulated depreciation and amortization.
- (7) Our subprime mortgage loans subject to call option are excluded from the presentation of our consolidated investment portfolio because they represent an option, not an obligation, to repurchase loans and the option is a noneconomic interest until exercised, and is offset by a liability in an amount equal to the GAAP asset on the consolidated balance sheet.

#### **Debt Investments**

The following table reflects the spread between the yield and the cost of financing our portfolio of financial instruments as of June 30, 2014:

Weighted average asset yield	13.44 %
Weighted average funding cost	2.95 %
Net interest spread	<u>10.49 %</u>

#### **CMBS**

<u>Deal Vintage (A)</u>	<u>Average Minimum Rating (B)</u>	<u>Number</u>	<u>Outstanding Face Amount</u>	<u>Amortized Cost Basis</u>	<u>Percentage of Total Amortized Cost Basis</u>	<u>Carrying Value</u>	<u>Delinquency 60+/FC/REO (C)</u>	<u>Principal Subordination (D)</u>	<u>Weighted Average Life (years) (E)</u>
Pre 2004	CCC+	5	\$ 9,311	\$ 8,342	5.1%	\$ 9,059	24.0%	49.9%	0.8
2004	BB	9	33,155	27,510	16.7%	31,867	3.9%	8.4%	0.8
2005	B	7	57,434	20,966	12.8%	42,276	4.2%	4.9%	1.0
2006	B	9	57,146	35,151	21.4%	42,186	3.4%	9.9%	1.5
2007	CCC+	3	13,237	2,640	1.6%	3,268	5.7%	7.7%	0.6
2010	BB-	2	23,000	22,578	13.7%	24,958	0.0%	0.0%	6.0
2011	BB+	5	50,329	47,194	28.7%	53,746	0.3%	4.1%	3.8
Total / WA	B+	40	\$ 243,612	\$ 164,381	100.0%	\$ 207,360	3.6%	7.8%	2.1

- (A) The year in which the securities were issued.
- (B) Ratings provided above were determined by third party rating agencies, represent the most recent credit ratings available as of the reporting date and may not be current. We had no CMBS assets that were on negative watch for possible downgrade by at least one rating agency as of June 30, 2014.
- (C) The percentage of underlying loans that are 60+ days delinquent, in foreclosure or considered real estate owned ("REO").
- (D) The percentage of the outstanding face amount of securities that is subordinate to our investments.
- (E) Weighted average life is based on the timing of expected principal reduction on the asset.

In May 2014, we sold \$68.3 million face amount of CMBS securities at an average price of 105.2% for total proceeds of \$71.9 million and repaid \$71.9 million of associated CDO bonds payable and other term loan financings. We recognized a net gain of approximately \$15.0 million on the sale of these securities.

### Mezzanine Loans, B-Notes and Whole Loans

Asset Type	Number	Outstanding Face Amount	Amortized Cost Basis	Percentage of Total Amortized Cost Basis	Carrying Value	Weighted Average First Dollar Loan to Value (A)	Weighted Average Last Dollar to Loan Value (A)	Delinquency (B)
Mezzanine Loans	8	\$ 157,046	\$ 124,628	65.1%	\$ 124,628	72.5%	86.0%	7.6%
B-Notes	2	69,912	66,420	34.7%	66,420	75.2%	83.7%	—%
Whole Loans	1	380	380	0.2%	380	0.0%	1.5%	—%
Total/WA	11	\$ 227,338	\$ 191,428	100.0%	\$ 191,428	73.2%	85.1%	5.3%

(A) Loan to value is based on the appraised value at the time of purchase or refinancing.

(B) The percentage of underlying loans that are non-performing, in foreclosure, under bankruptcy filing or considered real estate owned.

### CDO Securities (A)

Collateral Manager	Primary Collateral Type	Number	Average Minimum Rating (B)	Outstanding Face Amount	Amortized Cost Basis	Percentage of Total Amortized Cost Basis	Carrying Value	Principal Subordination (C)
Newcastle	CMBS	1	CCC-	\$ 9,955	\$ —	0.0%	\$ 5,973	16.1%
Sorin	CMBS	1	BBB-	7,108	6,368	100.0%	6,744	56.8%
TOTAL/WA		2	B	\$ 17,063	\$ 6,368	100.0%	\$ 12,717	33.0%

(A) Represents non-consolidated CDO securities, excluding nine securities with a zero value, which had an aggregate face amount of \$116.1 million.

(B) Ratings provided above were determined by third party rating agencies, represent the most recent credit ratings available as of the reporting date and may not be current. We had no CDO assets that were on negative watch for possible downgrade by at least one rating agency as of June 30, 2014.

(C) The percentage of the outstanding face amount of securities that is subordinate to our investments.

In May 2014, we sold \$54.2 million outstanding face amount of the Sorin CDO security at an average price of 93.0% for total proceeds of \$50.4 million and repaid \$50.4 million of associated CDO bonds payable and other term loan financings. We recognized a net gain of approximately \$0.7 million on the sale of this security.

### Residential Loans

Deal	Average FICO Score (A)	Outstanding Face Amount	Amortized Cost Basis(B)	Percentage of Total Amortized Cost Basis	Carrying Value(B)	Average Loan Age (years)	Original Balance	Delinquency 90+/FC/REO (C)	Cumulative Loss to Date
Residential Loans Portfolio I	707	39,785	28,731	89.8%	28,731	11.3	646,357	15.9%	0.5%
Residential Loans Portfolio II	737	3,444	3,274	10.2%	3,274	8.9	83,950	0.0%	0.0%
Total / WA	709	\$ 43,229	\$ 32,005	100.0%	\$ 32,005	11.1	\$ 730,307	14.6%	0.5%

(A) Based on original FICO scores for the residential loan portfolios as the loan servicers of the residential loan portfolios do not provide updated FICO scores.

(B) Amortized cost basis and carrying value excludes negligible interest receivable for the residential housing loans.

(C) The percentage of loans that are 90+ days delinquent or in foreclosure or considered REO.

In May 2014, Newcastle sold its manufactured housing portfolio through a securitization. The portfolio had an outstanding face amount of \$222.2 million and was sold at 104% of par, resulting in \$231.6 million of total proceeds including accrued interest. Part of the proceeds were used to repay the current debt on the portfolio at par, including \$132.4 million of third-party debt and \$20.5 million of debt owned by CDO VIII and CDO IX. The securitization of the portfolio was accomplished through a special purpose entity, in which Newcastle holds no interests, and was treated as a sale for accounting purposes. The sale generated a gain of \$24.7 million, or \$19.4 million net after \$1.9 million of deal expenses and the write off of \$3.4 million of unamortized discount on third party debt (recorded as a loss on extinguishment of debt).

Non-Agency RMBS (A)

## Security Characteristics

<u>Vintage (B)</u>	<u>Average Minimum Rating (C)</u>	<u>Number of Securities</u>	<u>Outstanding Face Amount</u>	<u>Amortized Cost Basis</u>	<u>Percentage of Total Amortized Cost Basis</u>	<u>Carrying Value</u>	<u>Principal Subordination (D)</u>	<u>Excess Spread (E)</u>
Pre 2004	D	3	\$ 1,127	\$ 236	0.6%	\$ 664	5.5%	4.0%
2004	CCC	5	4,467	1,007	2.6%	2,534	5.1%	2.3%
2005	CCC-	16	42,771	7,833	20.1%	19,682	17.9%	4.0%
2006	B	5	31,681	22,025	56.7%	28,101	42.2%	3.9%
2007	CCC+	4	10,735	7,774	20.0%	9,527	24.6%	4.1%
Total / WA	CCC+	33	\$ 90,781	\$ 38,875	100.0%	\$ 60,508	26.4%	3.9%

## Collateral Characteristics

<u>Vintage (B)</u>	<u>Average Loan Age (years)</u>	<u>Collateral Factor (F)</u>	<u>3 Month CPR (G)</u>	<u>Delinquency (H)</u>	<u>Cumulative Losses to Date</u>
Pre 2004	11.2	0.06	10.3%	19.3%	2.7%
2004	10.0	0.12	15.0%	10.3%	3.1%
2005	9.3	0.15	9.4%	21.1%	12.2%
2006	8.3	0.22	7.4%	22.5%	23.6%
2007	7.5	0.33	10.2%	19.3%	29.5%
Total / WA	8.8	0.20	9.1%	20.8%	17.6%

(A) This includes subprime retained securities in the securitization of Subprime Portfolio I. For further information on this securitization, see Note 6 to our consolidated financial statements included herein.

(B) The year in which the securities were issued.

(C) Ratings provided above were determined by third party rating agencies, represent the most recent credit ratings available as of the reporting date and may not be current. We had no ABS assets that were on negative watch for possible downgrade by at least one rating agency as of June 30, 2014.

(D) The percentage of the outstanding face amount of securities and residual interests that is subordinate to our investments.

(E) The annualized amount of interest received on the underlying loans in excess of the interest paid on the securities, as a percentage of the outstanding collateral balance.

(F) The ratio of original unpaid principal balance of loans still outstanding.

(G) Three month average constant prepayment rate.

(H) The percentage of underlying loans that are 90+ days delinquent, or in foreclosure or considered REO.

Agency ARM RMBS (FNMA/FHLMC Securities)

In January 2014, Newcastle sold \$503.0 million face amount of the remaining FNMA/FHLMC securities at an average price of 105.82% for total proceeds of \$532.2 million and repaid \$516.1 million of associated repurchase agreements. We recognized a net gain of approximately \$1.9 million on the sale of these securities.

## REIT Debt

Industry	Average Minimum Rating (A)	Number	Outstanding Face Amount	Amortized Cost Basis	Percentage of Total Amortized Cost Basis	Carrying Value
Retail	A-	1	\$ 4,500	\$ 4,228	14.7 %	\$ 4,770
Diversified	B-	1	12,000	11,997	41.6 %	12,420
Multifamily	BBB	1	5,000	4,989	17.3 %	5,125
Healthcare	BBB+	2	7,700	7,577	26.3 %	8,368
Total / WA	BB+	5	\$ 29,200	\$ 28,791	100.0 %	\$ 30,683

## Corporate Bank Loans

Industry	Average Minimum Rating (A)	Number	Outstanding Face Amount	Amortized Cost Basis(B)	Percentage of Total Amortized Cost Basis	Carrying Value(B)
Resorts	NR	3	\$ 153,033	\$ 91,274	93.6 %	91,274
Restaurant	B	2	11,940	6,289	6.4 %	6,289
Total / WA	D	5	\$ 164,973	\$ 97,563	100.0 %	\$ 97,563

(A) Ratings provided above were determined by third party rating agencies, represent the most recent credit ratings available as of the reporting date and may not be current. We had no corporate assets that were on negative watch for possible downgrade by at least one rating agency as of June 30, 2014.

(B) Amortized cost basis and carrying value excludes \$0.1 million of interest receivable for one corporate bank loan.

## Other Investments

### Senior Housing Investments

We currently own 51 dedicated independent living ("IL-only") properties that are triple net leased to Holiday. We also own 6 properties with 1 IL only property, 1 property with some combination of independent living, assisted living or memory care ("AL/MC"), and 4 continuing care retirement communities ("CCRC") that are triple net leased to a third party. We have 38 managed properties, including 4 IL-only properties and 34 AL/MC properties. Our properties are located across 27 states. IL-only properties are age-restricted, multifamily rental properties with central dining that provide residents access to meals and other services such as housekeeping, linen service, transportation and social and recreational activities. A typical resident is 80 to 85 years old and is relatively healthy. Residents are typically charged all-inclusive monthly rates. AL/MC properties are state-regulated rental properties that provide the same services as IL-only and additionally have staff to provide residents assistance with activities of daily living, such as management of medications, bathing, dressing, toileting, ambulating and eating. AL/MC properties may include memory care facilities that specifically provide care for individuals with Alzheimer's disease and other forms of dementia or memory loss. The average age of an AL/MC resident is similar to that of an IL-only resident, but AL/MC residents typically have greater healthcare needs. Residents are typically charged all-inclusive monthly rates for IL-only services and additional "care charges" for AL/MC services, which vary depending on the types of services required. AL/MC properties are generally private pay, though many states will allow residents to cover a portion of the cost with Medicaid. A CCRC is a particular type of retirement community that offers several levels (generally more than three) of health care at one facility or campus, often including independent living, assisted living/memory care and skilled nursing home. CCRCs offer a tiered approach to the aging process, accommodating residents' changing needs as they age. The table below sets forth key characteristics of our portfolio.

Asset type	Real Estate Property Investments as of June 30, 2014					Revenues for the Six Months Ended June 30, 2014			
	Number of Communities	Number of Beds	Percent of Total		Real Estate	Total Revenues (1)	Percent of Total		Number of States
			Real Estate Property Investment	Real Estate Property Investment	Property Investment per Bed		Total Revenues	Total Revenues	
Managed Properties	38	4,870	\$ 474,077	30.0%	\$ 97.3	\$ 72,862	62.0%	14	
Triple Net Lease Property	57	7,107	1,105,426	70.0%	155.5	44,646	38.0%	24	
<b>Total</b>	<b>95</b>	<b>11,977</b>	<b>\$ 1,579,503</b>	<b>100.0%</b>		<b>\$ 117,508</b>	<b>100%</b>		

(1) Revenues relate to the period the properties were owned by us in 2014 and, therefore, are not indicative of full-year results for all properties.

Our portfolio of senior housing properties is broadly diversified by geographic location throughout the United States. The following table shows the geographic location of our senior housing properties as of June 30, 2014, and the percentage of total revenues by geographic location for the six months ended June 30, 2014.

Managed Properties:

Location	Number of Communities	Number of Beds	Percent of Revenue
Arizona	1	108	3.29 %
California	3	328	11.32 %
Florida	16	2,330	39.39 %
Idaho	1	121	4.25 %
Michigan	1	144	1.69 %
New Hampshire	3	147	0.81 %
New York	1	118	2.43 %
North Carolina	1	176	3.33 %
Ohio	1	117	2.59 %
Oregon	2	164	6.51 %
Pennsylvania	2	291	8.55 %
Texas	1	230	4.36 %
Utah	4	475	9.85 %
Virginia	1	121	1.63 %
	<b>38</b>	<b>4,870</b>	<b>100.00 %</b>

Triple Net Lease Properties:

Location	Number of Communities	Number of Beds	Percent of Revenue
Arizona	1	115	1.40 %
California	2	235	4.99 %
Colorado	4	439	6.62 %
Connecticut	2	276	5.65 %
Florida	3	370	6.45 %
Illinois	1	111	1.62 %
Iowa	2	215	2.73 %
Kansas	2	238	3.66 %
Kentucky	1	117	2.62 %
Louisiana	1	103	0.65 %
Michigan	1	121	1.68 %
Mississippi	1	93	0.91 %
Missouri	3	320	6.67 %
Montana	1	115	1.87 %
Nevada	1	121	2.32 %
New York	2	234	5.16 %
North Carolina	2	240	5.04 %
Oregon	6	600	9.80 %
Pennsylvania	3	345	7.36 %
Tennessee	1	109	1.17 %
Texas	14	2,237	15.05 %
Utah	1	117	2.09 %
Virginia	1	120	2.44 %
Wisconsin	1	116	2.05 %
	57	7,107	100.00 %

*Managed Properties*

As of June 30, 2014, either Blue Harbor or Holiday managed all of our managed properties. We pay annual property management fees pursuant to long-term property management agreements. Currently, all of our property management agreements have initial 10-year terms, with successive automatic 1-year renewal periods. For AL/MC properties, we pay base management fees equal to 6% of revenue for the first two years and 7% thereafter. For IL-only properties, we pay base management fees of 5% of revenues. As managers, Blue Harbor and Holiday do not lease our properties and, therefore, we are not directly exposed to their credit risk in the same manner or to the same extent as a triple net lease tenant. However, we rely on our managers' personnel, expertise, technical resources and information systems, proprietary information, good faith and judgment to manage our senior housing operations efficiently and effectively. We also rely on our managers to set appropriate resident fees and to otherwise operate our seniors housing communities in compliance with the terms of our management agreements and all applicable laws and regulations. Although we have various rights as the property owner under our management agreements, including various rights to set budget guidelines and to terminate and exercise remedies under those agreements as provided therein, Blue Harbor's or Holiday's failure, inability or unwillingness to satisfy its respective obligations under those agreements, to efficiently and effectively manage our properties or to provide timely and accurate accounting information with respect thereto could have a material adverse effect on us.

### *Triple Net Lease Properties*

The Holiday Portfolio is leased to Holiday pursuant to two triple net master leases on nearly identical terms. Each master lease has a term of approximately 17 years and first-year rent equal to 6.5% of the purchase price with annual increases during the following three years of 4.5% and annual increases thereafter varying from 3.5% to 3.75%. Under each master lease, the respective Master Tenant is responsible for (i) operating its portion of the Holiday Portfolio and bearing the related costs, including repairs, maintenance, capital expenditures, utilities, taxes, insurance, and the payroll expense of property-level employees, and (ii) complying with the terms of the mortgage financing documents.

On June 30, 2014, Newcastle also entered into a triple net lease of six properties with a third party (the "June 2014 Master Tenant"). The lease has a 15-year term with two five-year renewal options and first-year rent equal to approximately \$14.2 million with annual increases during each of the following three years of 3.75% and up to 2.5% thereafter. Under the lease, the June 2014 Master Tenant is responsible for (i) operating the properties and bearing the related costs, including maintenance, utilities, taxes, insurance, repairs and capital improvements, and (ii) complying with the terms of the mortgage financing documents.

### *Robust Pipeline*

As of June 30, 2014, we have signed either purchase and sale agreements or letters of intent granting us the exclusive right to negotiate purchase and sale agreements with respect to 8 properties with an aggregate estimated value of over \$131.9 million. There can be no assurance that we will complete any particular investment including those that are under contract, which may be subject to material closing conditions such as the completion of due diligence, financing, negotiation of definitive agreements, and board approval in certain circumstances. Moreover, any senior housing property that we acquire in the future may have different characteristics and expected returns than those in our existing portfolio and may expose us to additional regulatory and operational risks. See "Risks Related to Our Business."

### Golf Investment

In December 2013, we restructured a debt investment that resulted in our acquisition of National Golf and American Golf. National Golf owns 27 golf properties and leases them to American Golf. American Golf also leases 52 golf properties owned by third parties and manages 11 golf properties owned by third parties. We categorize our owned and leased golf properties as public or private. Set forth below is additional information about our golf properties.

*Public Properties.* Public properties generate revenues principally through daily green fees, golf cart rentals and food, beverage and merchandise sales. Amenities at these properties generally include practice facilities, and pro shops with food and beverage facilities. Our public properties generally have small clubhouses with banquet facilities.

*Private Properties.* Private properties are open to members only and generate revenues principally through initiation fees, membership dues, guest fees, and food, beverage and merchandise sales. Amenities at these properties typically include practice facilities, full service clubhouses with a pro shop, locker room facilities and multiple food and beverage outlets, including grills, restaurants and banquet facilities.

*Managed Properties.* Our 11 managed properties are properties that American Golf manages pursuant to a management agreement with the owner. We will recognize revenue from these properties in an amount equal to the respective management fee.

The following table summarizes certain information about our golf properties as of June 30, 2014:

	Number of Properties	Number of Golf Holes
<i>Leased:</i>		
Public	45	828
Private	7	189
Total Leased	52	1,017
<i>Owned:</i>		
Public	12	234
Private	15	306
Total Owned	27	540
<i>Managed:</i>	11	198
<b>Total</b>	<b>90</b>	<b>1,755</b>
<b>Location</b>		
California	52	990
Florida	2	81
Georgia	10	171
Hawaii	1	18
Idaho	1	18
Michigan	1	18
New Jersey	2	36
New Mexico	1	27
New York	6	126
Oklahoma	3	54
Oregon	4	90
Tennessee	2	36
Texas	3	54
Virginia	1	18
Washington	1	18
	<b>90</b>	<b>1,755</b>

## Debt Obligations

Our debt obligations including capital lease obligations, as summarized in Note 10 to our consolidated financial statements included herein, existing at June 30, 2014 (gross of \$5.4 million of discounts) had contractual maturities as follows (in thousands):

	Nonrecourse	Recourse	Total
Period from July 1, 2014 through December 31, 2014	\$ 7,809	\$ 102,677	\$ 110,486
2015	17,526	—	17,526
2016	42,237	—	42,237
2017	241,782	—	241,782
2018	174,353	—	174,353
2019	128,359	—	128,359
Thereafter	1,406,128	51,004	1,457,132
Total	<u>\$ 2,018,194</u>	<u>\$ 153,681</u>	<u>\$ 2,171,875</u>

Certain of the debt obligations included above are obligations of our consolidated subsidiaries which own the related collateral. In some cases, including the CDO Bonds Payable and Other Bonds Payable, such collateral is not available to other creditors of ours.

In January 2014, we sold \$503.0 million face amount of the remaining FNMA/FHLMC securities at an average price of 105.82% for total proceeds of \$532.2 million and repaid all \$516.1 million of repurchase agreements. On February 13, 2014, Newcastle completed the spin-off of its media business which included \$178.0 million of credit facilities.

As of June 30, 2014, Newcastle has a borrowing capacity of \$7.6 million on the golf credit facilities.

The financing of certain of our senior housing properties, and our Golf business as well as our other non-CDO debt obligations, contain various customary loan covenants, in some cases including a debt service coverage ratio, debt yield and/or minimum net worth requirement. We were in compliance with all of the covenants in these financings as of June 30, 2014. In addition, as of June 30, 2014, we had complied with the general investment guidelines adopted by our board of directors that limit total leverage.

### Repurchase Agreements

The following table provides additional information regarding short-term borrowings. The outstanding short-term borrowings were used to finance our investments in certain senior notes issued by Newcastle CDO VIII, CDO IX and Residential Mortgage Loans. All of the repurchase agreements have full recourse to Newcastle.

	Outstanding Balance at June 30, 2014 *	Three Months Ended June 30, 2014			Six Months Ended June 30, 2014		
		Average Daily Amount Outstanding	Maximum Amount Outstanding	Weighted Average Interest Rate	Average Daily Amount Outstanding	Maximum Amount Outstanding	Weighted Average Interest Rate
FNMA/FHLMC	\$ —	\$ —	\$ —	N/A	\$ 64,212	\$ 516,134	0.40%
CDO Securities	79,712	52,380	79,712	1.80%	48,375	79,712	1.80%
Linked transactions	—	36,046	58,563	1.65%	47,154	60,646	1.65%
Residential Mortgage Loans	22,965	23,613	25,363	2.15%	24,379	25,363	2.16%

\*All of which was recourse to us.

The weighted average differences between the fair value of the assets and the face amount of financing of the CDO securities and Residential Mortgage Loans repurchase agreements were 25% and 20%, respectively, during the six months ended June 30, 2014.

Each of our CDO financings contains tests that measure the amount of over collateralization and excess interest in the transaction. At issuance, each of our CDOs passed all of these tests. Failure to satisfy these tests would generally cause (or has caused) the cash flow that would otherwise be distributed to the more junior classes of securities (including those held by Newcastle) to be redirected to pay down the most senior class of securities outstanding until the tests are satisfied. As a result, our cash flow and liquidity are negatively impacted upon such a failure, and the impact could be (and has been) material. The table set forth below presents data, including the most recent quarterly cash flows received by Newcastle, for each of our consolidated CDOs, and sets

forth which of the CDOs have satisfied these tests in the most recent quarter. The amounts set forth are as of June 30, 2014 unless otherwise noted (dollars in thousands). For those CDOs that have failed their applicable over collateralization tests, the impact of failing is already reflected in the cash flow set forth in the table. For those CDOs that have satisfied their applicable over collateralization tests, we could potentially lose substantially all of the cash flows from those CDOs in future quarters if we fail to satisfy the tests in the future. The amounts in the table reflect data at the CDO level and thus are different from the GAAP balance sheet due to intercompany amounts eliminated in Newcastle's consolidated balance sheet.

	CDO VI			CDO VIII			CDO IX			
<b>Balance Sheet:</b>										
Assets Face Amount	\$		157,566	\$		340,618	\$		452,411	
Assets Fair Value			124,252			261,037			368,270	
Issued Debt Face Amount (1)			181,407			143,341			148,441	
Derivative Net Liabilities Fair Value			3,319			3,813			—	
<b>Cash Receipts:</b>										
Quarterly net cash receipts (2)	\$		47	\$		1,314	\$		3,620	
<b>Collateral Composition (3):</b>										
		Face	Fair Value		Face	Fair Value		Face	Fair Value	
CMBS	\$	93,271	\$ 77,950	BB-	\$ 46,745	\$ 44,278	B-	\$ 80,701	\$ 84,594	BB
REIT Debt		29,200	30,683	BB+	—	—	—	—	—	—
ABS		35,095	15,619	CC	44,462	41,089	BB-	400	400	CCC
Bank Loans		—	—	—	79,407	47,128	C	91,567	66,720	D
Mezzanine Loans / B-Notes / Whole Loans		—	—	—	108,476	81,475	CC	189,386	145,219	CCC
CDO		—	—	—	61,528	47,067	D	67,108	58,059	CCC+
Residential Loans		—	—	—	—	—	—	3,444	3,298	NR
Other Investments		—	—	—	—	—	—	19,805	9,980	—
Cash for Reinvestment		—	—	—	—	—	—	—	—	—
Total	\$	<u>157,566</u>	\$ <u>124,252</u>	B+	\$ <u>340,618</u>	\$ <u>261,037</u>	CCC-	\$ <u>452,411</u>	\$ <u>368,270</u>	CCC
Collateral on Negative Watch (4)	\$	—			\$	—		\$	—	

Continued on next page.

<u>CDO Cash Flow Triggers (5):</u>				
<u>Over Collateralization (6):</u>				
As of Jun-2014 remittance				
Cushion (Deficit) (\$)	\$	(187,042)	\$	100,187 \$ 162,500
As of Jul-2014 remittance				
Cushion (Deficit) (\$)	\$	(180,780)	\$	103,140 \$ 164,999
<u>Interest Coverage (6):</u>				
As of Jun-2014 remittance				
Cushion (Deficit) (%)		(195.2)%		50.8% 318.5%
As of Jul-2014 remittance				
Cushion (Deficit) (%)		(235.5)%		41.3% 312.4%
<u>CDO Overview:</u>				
Effective		Aug-05	Mar-07	Jul-07
Reinvestment Period End (7)		Passed	Passed	Passed
Optional Call (8)		Passed	Passed	Passed
Auction Call (9)		Apr-15	Nov-16	May-17
WA Debt Spread (bps) (10)		38	117	137

See notes on next page.

- (1) Includes CDO bonds issued to third parties and held by Newcastle's consolidated CDOs.
- (2) Represents net cash received from each CDO based on all of our interests in such CDO (including senior management fees but excluding principal received from senior CDO bonds owned by Newcastle) for the six months ended June 30, 2014. Cash receipts for this period include \$0.5 million of senior collateral management fees, and may not be indicative of cash receipts for subsequent periods. Excluded from the quarterly net cash receipts was \$112.3 million of unrestricted cash received from principal repayments on senior CDO bonds owned by Newcastle. This cash represents a return of principal and the realization of the difference between par and the discounted purchase price of these bonds. See "Cautionary Note Regarding Forward Looking Statements" for risks and uncertainties that could cause our receipts for subsequent periods to differ materially from these amounts.
- (3) Collateral composition is calculated as a percentage of the face amount of collateral and includes CDO bonds of \$121.6 million issued by Newcastle, bank loans of \$6.0 million, collateralized by Newcastle real estate properties and a third party CDO security, and \$70.5 million of mezzanine loans, which are eliminated in consolidation. The fair value of this CDO bond, other bonds and notes payable, bank loans and mezzanine loans was \$98.4 million, \$6.0 million, \$32.2 million and \$32.2 million at June 30, 2014, respectively. Also reflected are weighted average credit ratings, which were determined by third party rating agencies, represent the most recent credit ratings available as of the reporting date and may not be current.
- (4) Represents the face amount of collateral on negative watch for possible downgrade by at least one rating agency (Moody's, S&P or Fitch) as of the determination date in June 2014 for all CDOs. The amount does not include any bonds issued by Newcastle, which are eliminated in consolidation and not reflected in the investment portfolio disclosures.
- (5) Each of our CDO financings contains tests that measure the amount of over collateralization and excess interest in the transaction. Failure to satisfy these tests would cause the principal and/or interest cashflow that would otherwise be distributed to more junior classes of securities (including those held by Newcastle) to be redirected to pay down the most senior class of securities outstanding until the tests are satisfied. As a result, our cash flow and liquidity are negatively impacted upon such a failure, and the impact could be material. Each CDO contains tests at various over collateralization and interest coverage percentage levels. The trigger percentages used above represent the first threshold at which cashflows would be redirected as described in this footnote. The data presented is as of the most recent remittance date on or before June 30, 2014 and may change or have changed subsequent to that date. In addition, our CDOs may also contain specific over collateralization tests that, if failed, can result in the occurrence of an event of default or our being removed as collateral manager of the CDO. Failure of the over collateralization tests can also cause a "phantom income" issue if cash that constitutes income is diverted to pay down debt instead of being distributed to us. As of the June 2014 remittance date, we were not receiving cash flows from CDO VI (other than senior management fees and cash flows on senior classes of bonds we own). Based upon our current calculations, we expect CDO VI to remain out of compliance for the foreseeable future. Moreover, given current market conditions, it is possible that all of our CDOs could be out of compliance with their over collateralization tests as of one or more measurement dates within the next twelve months. Our ability to rebalance will depend upon the availability of suitable securities, market prices, and other factors that are beyond our control. Such rebalancing efforts may be extremely difficult given current market conditions and we cannot assure you that we will be successful in our rebalancing efforts. If the liabilities of our CDOs are downgraded by Moody's to certain predetermined levels, our discretion to rebalance the applicable CDO portfolios may be negatively impacted. Moreover, if we bring these coverage tests into compliance, we cannot assure you that they will not fall out of compliance in the future or that we will be able to correct any noncompliance. For a more detailed discussion of the impact of CDO financings on our cash flows, see Part II, Item 1A, "Risk Factors – Risks Relating to our Business – The coverage tests applicable to our CDO financings may have a negative impact on our operating results and cash flows."
- (6) Represents excess or deficiency under the applicable over collateralization or interest coverage tests to the first threshold at which cash flow would be redirected. We generally do not receive material cash flow from the junior classes of a CDO until a deficiency is corrected. Ratings downgrades of assets in our CDOs can negatively impact compliance with the over collateralization tests. Generally, the over collateralization test measures the principal balance of the specified pool of assets in a CDO against the corresponding liabilities issued by the CDO. However, based on ratings downgrades, the principal balance of an asset or of a specified percentage of assets in a CDO may be deemed reduced below their current balance to levels set forth in the related CDO documents for purposes of calculating the over collateralization test. As a result, ratings downgrades can reduce the principal balance of the assets used in the over collateralization test relative to the corresponding liabilities in the test, thereby reducing the over collateralization percentage. In addition, actual defaults of an asset would also negatively impact compliance with the over collateralization tests. Failure to satisfy an over collateralization test could result in the redirection of cashflows as described in footnote 5 above or, in certain circumstances, in our removal as manager of the applicable portfolio.
- (7) Our CDO financings typically have a 5-year reinvestment period. Generally, after such period ends, principal payments on the collateral are used to paydown the most senior debt outstanding. Prior to the end of the reinvestment period, principal payments received on the collateral are reinvested.
- (8) At the option call date, Newcastle, as the equity holder, has the right to payoff the CDO bonds at their related redemption price.
- (9) At the auction call date, there is a mandatory auction of the assets pursuant to which the collateral manager will solicit bids for the CDO assets. If the aggregate amounts of the bids are sufficient to pay off the outstanding CDO bonds set forth in the CDO governing document, the assets will be sold and the CDO bonds will be redeemed. However, if the aggregate amount of the bids is insufficient to pay off the outstanding CDO bonds set forth in the CDO governing document, the assets will not be sold and the redemption of CDO bonds will not occur.
- (10) Debt spread represents the spread above the benchmark interest rate (LIBOR or U.S. Treasuries) that Newcastle pays on its debt.

The following table sets forth further information with respect to the bonds of our consolidated CDO financings as of June 30, 2014 (dollars in thousands):

Class	Original Face Amount	Current Face Amount (1)				Total	Stated Interest Rate
		Held By					
		Third Parties	Newcastle CDOs (2)	Newcastle Outside of its CDOs (3)			
<b>CDO VI</b>							
Class I-MM	\$ 323,000	\$ 89,169	\$ —	\$ 10,973	100,142	LIBOR + 0.25%	
Class I-B	59,000	59,000	—	—	59,000	LIBOR + 0.40%	
Class II	33,000	23,881	—	10,384	34,265	LIBOR + 0.50%	
Class III-FL	15,000	5,290	—	10,579	15,869	LIBOR + 0.80%	
Class III-FX	5,000	—	—	6,761	6,761	5.67 %	
Class IV-FL	9,600	667	—	9,995	10,662	LIBOR + 1.70%	
Class IV-FX	2,400	3,400	—	—	3,400	6.55 %	
Class V	21,000	—	—	31,810	31,810	7.81 %	
Preferred	32,000	—	—	32,000	32,000	N/A	
	<u>\$ 500,000</u>	<u>\$ 181,407</u>	<u>\$ —</u>	<u>\$ 112,502</u>	<u>\$ 293,909</u>		
<b>CDO VIII</b>							
Class I-A	\$ 462,500	\$ —	\$ —	\$ —	\$ —	LIBOR + 0.28%	
Class I-AR	60,000	—	—	—	—	LIBOR + 0.34%	
Class I-B	38,000	—	—	22,839	22,839	LIBOR + 0.36%	
Class II	42,750	—	29,000	13,750	42,750	LIBOR + 0.42%	
Class III	42,750	—	22,750	20,000	42,750	LIBOR + 0.50%	
Class IV	28,500	—	—	—	—	LIBOR + 0.60%	
Class V	28,500	28,500	—	—	28,500	LIBOR + 0.75%	
Class VI	27,312	—	—	—	—	LIBOR + 0.80%	
Class VII	21,375	—	—	—	—	LIBOR + 0.90%	
Class VIII	22,563	11,063	8,250	3,250	22,563	LIBOR + 1.45%	
Class IX-FL	6,000	6,000	—	—	6,000	LIBOR + 1.80%	
Class IX-FX	7,600	7,600	—	—	7,600	6.80 %	
Class X	19,650	18,650	—	—	18,650	LIBOR + 2.25%	
Class XI	26,125	—	—	24,125	24,125	LIBOR + 2.50%	
Class XII	28,500	—	11,528	17,042	28,570	7.50 %	
Preferred	87,875	—	—	87,875	87,875	N/A	
	<u>\$ 950,000</u>	<u>\$ 71,813</u>	<u>\$ 71,528</u>	<u>\$ 188,881</u>	<u>\$ 332,222</u>		

Continued on next page.

Class	Original Face Amount	Current Face Amount (1)				Total	Stated Interest Rate
		Held By					
		Third Parties	Newcastle CDOs (2)	Newcastle Outside of its CDOs (3)			
<b>CDO IX</b>							
Class A-1	\$ 379,500	\$ 22,816	\$ —	\$ —	\$ 22,816	LIBOR + 0.26%	
Class A-2	115,500	40,500	—	75,000	115,500	LIBOR + 0.47%	
Class B	37,125	35,125	—	2,000	37,125	LIBOR + 0.65%	
Class C	33,000	—	—	—	—	LIBOR + 0.93%	
Class D	20,625	—	—	—	—	LIBOR + 1.00%	
Class E	24,750	—	—	24,750	24,750	LIBOR + 1.10%	
Class F	18,562	—	—	18,562	18,562	LIBOR + 1.30%	
Class G	18,562	—	—	11,262	11,262	LIBOR + 1.50%	
Class H	21,656	—	8,751	9,305	18,056	LIBOR + 2.50%	
Class J	21,656	—	21,656	—	21,656	LIBOR + 3.00%	
Class K	19,593	—	19,593	—	19,593	LIBOR + 3.50%	
Class L	23,718	—	—	23,718	23,718	7.50 %	
Class M	39,187	—	—	39,187	39,187	8.00 %	
Preferred	51,566	—	—	51,566	51,566	N/A	
	<u>\$ 825,000</u>	<u>\$ 98,441</u>	<u>\$ 50,000</u>	<u>\$ 255,350</u>	<u>\$ 403,791</u>		

- (1) The amounts presented in these columns exclude the face amount of any canceled bonds within an applicable class.
- (2) Amounts in this column represent the amount of bonds of the applicable class held by Newcastle's consolidated CDOs. These bonds are eliminated in Newcastle's consolidated balance sheet.
- (3) Amounts in this column represent the amount of bonds of the applicable class held as investments by Newcastle outside of its non-recourse financing structures. These bonds are eliminated in Newcastle's consolidated balance sheet.

#### *Stockholders' Equity*

##### Common Stock

At June 30, 2014, we had 351,709,903 shares of common stock outstanding.

In connection with the spin-off of New Residential on May 15, 2013, 21.5 million options that were held by the Manager, or by the directors, officers or employees of the Manager, were converted into an adjusted Newcastle option and a new New Residential option. The exercise price of each adjusted Newcastle option and New Residential option was set to collectively maintain the intrinsic value of the Newcastle option immediately prior to the spin-off and to maintain the ratio of the exercise price of the adjusted Newcastle option and the New Residential option, respectively, to the fair market value of the underlying shares as of the spin-off date, in each case based on the five day average closing price subsequent to the spin-off date.

In connection with the spin-off of New Media on February 13, 2014, the strike price of each Newcastle option was reduced by \$0.89 to reflect the adjusted value of Newcastle's shares as a result of the spin-off. The adjusted value was calculated based on the five day average closing price of the New Media's shares subsequent to the spin-off date.

Newcastle's outstanding options at June 30, 2014 consisted of the following:

	Number of Options	Strike Price (A)	Maturity Date
	162,500	12.84	11/22/2014
	330,000	12.03	1/12/2015
	2,000	12.62	8/1/2015
	170,000	11.95	11/1/2016
	242,000	12.80	1/23/2017
	456,000	11.19	4/11/2017
	1,495,166	1.51	3/29/2021
	2,294,833	0.86	9/27/2021
	2,000	1.07	12/20/2021
	1,867,167	1.61	4/3/2022
	2,265,000	1.84	5/21/2022
	2,499,167	1.83	7/31/2022
	5,750,000	3.03	1/11/2023
	2,300,000	3.54	2/15/2023
	4,025,000	3.76	6/17/2023
	5,795,095	4.04	11/22/2023
<b>Total W/A</b>	<b>29,655,928</b>	<b>\$ 3.25</b>	

(A) The strike prices are subject to adjustment in connection with return of capital dividends. In the first quarter of 2014 strike prices were adjusted by \$0.32 reflecting the portion of Newcastle's 2013 dividends which was deemed return of capital.

Our outstanding options at June 30, 2014 were summarized as follows:

	Issued Prior to 2011	Issued in 2011 and thereafter	Total
Held by the Manager	1,075,130	24,396,428	25,471,558
Issued to the Manager and subsequently transferred to certain of the Manager's employees	285,370	3,895,000	4,180,370
Issued to the independent directors	2,000	2,000	4,000
<b>Total</b>	<b>1,362,500</b>	<b>28,293,428</b>	<b>29,655,928</b>
<b>Weighted average strike price</b>	<b>\$ 11.97</b>	<b>\$ 2.83</b>	<b>\$ 3.25</b>

On May 7, 2014, Newcastle's former COO exercised 215,000 options with a weighted average exercise price of \$1.12. Upon exercise, 215,000 shares of our common stock were issued.

#### Common Stock Dividends Paid

<u>Declared for the Period Ended</u>	<u>Paid</u>	<u>Amount Per Share</u>
March 31, 2014	April 2014	\$ 0.10
June 30, 2014	July 2014	\$ 0.10

Preferred Stock Dividends Paid

Declared for the Period Ended	Paid	Amount Per Share			
		Series B	Series C	Series D	
January 31, 2014	January 2014	\$ 0.609	\$ 0.503	\$ 0.523	
April 30, 2014	April 2014	\$ 0.609	\$ 0.503	\$ 0.523	
July 31, 2014	July 2014	\$ 0.609	\$ 0.503	\$ 0.523	

Accumulated Other Comprehensive Income (Loss)

During the six months ended June 30, 2014, our accumulated other comprehensive income (loss) changed due to the following factors (in thousands):

	Gains (Losses) on Cash Flow Hedges	Gains (Losses) on Securities	Other	Total Accumulated Other Comprehensive Income (Loss)
Accumulated other comprehensive income (loss), December 31, 2013	\$ (5,992)	\$ 82,408	\$ 458	\$ 76,874
Net unrealized gain (loss) on securities	—	8,477	—	8,477
Reclassification of net realized (gain) loss on securities into earnings	—	(18,032)	—	(18,032)
Net unrecognized gain and pension prior service cost	—	—	9	9
Net unrealized gain (loss) on derivatives designated as cash flow hedges	1,786	—	—	1,786
Reclassification of net realized (gain) loss on derivatives designated as cash flow hedges into earnings	233	—	—	233
Spin-off of New Media	—	—	(467)	(467)
Accumulated other comprehensive income (loss), June 30, 2014	\$ (3,973)	\$ 72,853	\$ —	\$ 68,880

Our GAAP equity changes as our real estate securities portfolio and derivatives are marked to market each quarter, among other factors. The primary causes of mark to market changes are changes in interest rates and credit spreads. Net unrealized gains on our real estate securities decreased for the six months ended June 30, 2014 in accumulative other comprehensive income primarily as a result of the sale of FNMA/FHLMC and CMBS securities, which was partially offset by an increase in unrealized gains caused by a net tightening of credit spreads. Net unrealized losses on derivatives designated as cash flow hedges decreased for the six months ended June 30, 2014, primarily as a result of swap interest payments.

See “- Market Considerations” above for a further discussion of recent trends and events affecting our unrealized gains and losses as well as our liquidity.

*Cash Flow*

Operating Activities

Net cash flow provided by operating activities decreased to \$16.2 million for these six months ended June 30, 2014 from \$45.2 million for the six months ended June 30, 2013. This change resulted primarily from the factors described below:

- Net cash receipts from our CDOs decreased approximately \$25.1 million for these six months ended June 30, 2014 compared to the six months ended June 30, 2013 primarily due to lower interest proceeds from CDO VIII and IX, as a result of paydowns during 2013 and 2014 and increased interest expenses paid for additional repurchase agreements on retained CDO bonds.
- Net cash receipts from our other debt portfolios decreased approximately \$9.9 million due to the sale of the FNMA/FHLMC securities in January 2014, paydowns and sale on our manufactured housing loan portfolios, lower receipts of delinquent interest on certain securities and decreased interest receipts from a real estate related loan that was restructured in November 2013.

- Cash receipts from excess mortgage servicing income decreased approximately \$19.3 million in the six months ended June 30, 2014 compared to the six months ended June 30, 2013 due to the spin-off of these investments to New Residential in May 2013.
- Negative operating cash flow of \$7.2 million generated by the golf business we acquired on December 30, 2013, primarily due to the winter season and its impact on the demand for outdoor activities along with the higher property operating expenses needed to prepare the properties following the cold weather season.
- Negative operating cash flow of \$1.5 million generated by our investment in New Media as a result of lower advertising revenues in the period from January 1, 2014 through the February 13, 2014 spin-off.
- Receipts from our senior housing investments increased approximately \$24.8 million due to increased acquisition activity. During 2013 and the six months ended June 30, 2014, we purchased 83 senior housing properties in 12 different portfolios.
- Management fees paid decreased approximately \$7.0 million for the six months ended June 30, 2014 compared to the six months ended June 30, 2013 due to a decrease in gross equity as a result of the spin-offs of New Residential in May 2013 and New Media in February 2014 which was partially offset by an increase in gross equity as a result of the public offerings of our common stock in 2013.
- A decrease of approximately \$5.3 million in general and administrative expenses paid during the six months ended June 30, 2014 compared to the six months ended June 30, 2013.

#### Investing Activities

Investing activities provided (used) \$715.2 million and (\$1,389) million during the six months ended June 30, 2014 and 2013, respectively. Uses of cash flows from investing activities consisted primarily of investments made in senior housing properties, golf course properties, real estate securities, real estate related and other loans, and contributions to equity method investees. Proceeds from cash flows from investing activities consisted primarily of sale of investments, repayments from loans and securities and distributions of capital from equity method investees.

#### Financing Activities

Financing activities provided (used) (\$759.5) million and \$1,383 million during the six months ended June 30, 2014 and 2013, respectively. Borrowings under repurchase agreements and mortgage notes payable and the public offerings of common stock served as the primary sources of cash flow from financing activities. Uses of cash flow from financing activities included the repayment of debt, the repurchases of CDO bonds payable, the payment of financing costs related to our common stock offerings and the payment of common and preferred dividends.

#### **INTEREST RATE, CREDIT AND SPREAD RISK**

We are subject to interest rate, credit and spread risk with respect to our investments. These risks are further described in "Quantitative and Qualitative Disclosures About Market Risk."

#### **OFF-BALANCE SHEET ARRANGEMENTS**

As of June 30, 2014, we had the following material off-balance sheet arrangements.

- In April 2006, we securitized our Subprime Portfolio I. The loans were sold to a securitization trust, of which 80% were treated as a sale, which is an off-balance sheet financing.
- In July 2007, we securitized our Subprime Portfolio II. The loans were sold to a securitization trust, of which 90% were treated as a sale, which is an off-balance sheet financing.
- On June 17, 2011, we deconsolidated CDO V, which is now effectively an off-balance sheet financing.

We have no obligation to repurchase any loans from either of our subprime securitizations. Therefore, it is expected that our exposure to loss is limited to the carrying amount of our retained interests in the securitization entities, as described above. A subsidiary of ours gave limited representations and warranties with respect to the second securitization; however, it has no assets and does not have recourse to the general credit of Newcastle.

## CONTRACTUAL OBLIGATIONS

During the six months ended June 30, 2014, we had all of the material contractual obligations referred to in our annual report on Form 10-K for the year ended December 31, 2013, excluding the debt which was repaid, spun-off or repurchased, as described in “– Liquidity and Capital Resources.”

In addition we had the following material contractual obligations that we executed during the six months ended June 30, 2014:

- Mortgage Notes Payable – We obtained mortgages to finance newly acquired senior housing properties.
- Management Agreements – We entered into new property management agreements with Holiday and Blue Harbor to manage newly acquired senior housing properties.
- Capital Leases - We entered into capital leases for golf carts and other equipment related to our Golf business.
- Capital Commitments - As part of the June 2014 Master Tenant lease, Newcastle committed to making available \$6.5 million immediately for capital improvements and other repairs in the properties under the lease agreement and also agreed to make available to the June 2014 Master Tenant an additional \$9.0 million at certain intervals during the lease period to be used for further capital improvements. Upon funding the capital improvements, we will be entitled to a rent increase.

## INFLATION

For our assets and liabilities that are financial in nature, interest rates and other factors affect our performance more so than inflation, although inflation rates can often have a meaningful influence over the direction of interest rates. Furthermore, our financial statements are prepared in accordance with GAAP and our distributions are determined by our board of directors primarily based on our taxable income, and, in each case, our activities and balance sheet are measured with reference to historical cost and/or fair market value without considering inflation. See "Quantitative and Qualitative Disclosure About Market Risk - Interest Rate Exposure" below.

## CORE EARNINGS

Newcastle has the following primary variables that impact its operating performance: (i) the current yield earned on its investments that are not included in non-recourse financing structures (i.e., unlevered investments, including investments in equity method investees and investments subject to recourse debt), (ii) the net yield it earns from its non-recourse financing structures, (iii) the interest expense and dividends incurred under its recourse debt and preferred stock, (iv) the net operating income on its real estate and golf investments, (v) its operating expenses and (vi) its realized and unrealized gains or losses, including any impairment, on its investments, derivatives and debt obligations. Core earnings is a non-GAAP measure of the operating performance of Newcastle excluding the sixth variable listed above and adjusting the consumer loans portfolio accounting to a level yield methodology. It also excludes depreciation and amortization charges, including the accretion of the membership deposit liability, and acquisition and spin-off related expenses. Core earnings is used by management to gauge the current performance of Newcastle without taking into account gains and losses, which, although they represent a part of our recurring operations, are subject to significant variability and are only a potential indicator of future economic performance. It is the judgment of management that depreciation and amortization charges are not indicative of operating performance and that acquisition and spin-off related expenses are not part of our core operations. Management believes that the exclusion from Core earnings of the items specified above allows investors and analysts to readily identify the operating performance of the assets that form the core of our activity, assists in comparing the core operating results between periods, and enables investors to evaluate Newcastle's current performance using the same measure that management uses to operate the business, which is among the factors considered when determining the amount of distributions to our shareholders.

Core earnings does not represent cash generated from operating activities in accordance with GAAP and therefore should not be considered an alternative to net income as an indicator of our operating performance or as an alternative to cash flow as a measure of our liquidity and is not necessarily indicative of cash available to fund cash needs. For a further description of the differences between cash flow provided by operations and net income, see “– Liquidity and Capital Resource” above. Our calculation of core earnings may be different from the calculation used by other companies and, therefore, comparability may be limited. Set forth below is a reconciliation of core earnings to the most directly comparable GAAP financial measure.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Income available for common stockholders	\$ 31,029	\$ 52,328	\$ 34,918	\$ 88,946
Add (Deduct):				
Impairment (reversal)	1,526	3,201	2,772	5,974
Other (income) loss(A)	(39,488)	(8,090)	(55,335)	(13,860)
Impairment (reversal), other (income) loss, depreciation and amortization and other adjustments from discontinued operations	—	(6,808)	5,792	(3,968)
Depreciation and amortization(B)	32,405	4,070	64,444	8,149
Acquisition and spin-off related expenses	4,484	4,466	11,086	4,963
Core earnings	\$ 29,956	\$ 49,167	\$ 63,677	\$ 90,204

(A) Net of \$1.9 million of deal expenses relating to the sale of the manufactured housing portfolio which were recorded to general and administrative expense under GAAP during 2014.

(B) Including accretion of membership deposit liability of \$1.4 million and \$3.1 million in the three and six months ended June 30, 2014, respectively.

#### Pro Forma Core Earnings

Pro forma core earnings reflect our core earnings as adjusted to give effect to the New Media spin-off transactions as if they had taken place on January 1, 2014.

	Six Months Ended June 30, 2014	
	2014	
Income available for common stockholders	\$	34,918
Adjustment to give effect to spin-offs		4,772
Pro forma income (loss) from continuing operations after preferred dividends		39,690
Add (Deduct):		
Impairment (reversal)		2,772
Other (income) loss(A)		(55,335)
Depreciation and amortization(B)		64,444
Acquisition and spin-off related expenses		11,086
Pro forma core earnings	\$	62,657

(A) Net of \$1.9 million of deal expenses relating to the sale of the manufactured housing portfolio which were recorded to general and administrative expense under GAAP during 2014.

(B) Including accretion of membership deposit liability of \$1.4 million and \$3.1 million in the three and six months ended June 30, 2014, respectively.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is the exposure to loss resulting from changes in interest rates, credit spreads, foreign currency exchange rates, commodity prices and equity prices. The primary market risks that we are exposed to are interest rate risk and credit spread risk. These risks are highly sensitive to many factors, including governmental monetary and tax policies, domestic and international economic and political considerations and other factors beyond our control. All of our market risk sensitive assets, liabilities and derivative positions are for non-trading purposes only. For a further understanding of how market risk may affect our financial position or results of operations, please refer to "Management's Discussion and Analysis of Financial Condition and Results of Operations – Application of Critical Accounting Policies."

#### Interest Rate Exposure

Changes in interest rates, including changes in expected interest rates or "yield curves," affect our investments in two distinct ways, each of which is discussed below.

First, changes in interest rates affect our net interest income, which is the difference between the interest income earned on assets and the interest expense incurred in connection with our debt obligations and hedges.

One component of our financing strategy includes the use of match funded structures, when appropriate and available. This means that we seek to match the maturities of our debt obligations with the maturities of our assets to reduce the risk that we have to refinance our liabilities prior to the maturities of our assets, and to reduce the impact of changing interest rates on our earnings. In addition, we seek to match fund interest rates on our assets with like-kind debt (i.e., fixed rate assets are financed with fixed rate debt and floating rate assets are financed with floating rate debt), directly or through the use of interest rate swaps, caps or other financial instruments (see below), or through a combination of these strategies, which we believe allows us to reduce the impact of changing interest rates on our earnings.

However, increases in interest rates can nonetheless reduce our net interest income to the extent that we are not completely match funded.

Furthermore, a period of rising interest rates can negatively impact our return on certain floating rate investments. Although these investments may be financed with floating rate debt, the interest rate on the debt may reset prior to, and in some cases more frequently than, the interest rate on the assets, causing a decrease in return on equity during a period of rising interest rates. See further disclosure regarding Agency ARM RMBS under "Management's Discussion and Analysis of Financial Condition and Results of Operations - Investment Portfolio – Agency ARM RMBS" for information about the reset terms and "Management's Discussion and Analysis of Financial Condition and Results of Operations – Liquidity and Capital Resources – Update on Liquidity, Capital Resources and Capital Obligations" for information on related debt.

As of June 30, 2014, a 100 basis point increase in short term interest rates would decrease our earnings by approximately \$0.9 million per annum, based on the current net floating rate exposure from our investments, financings and interest rate derivatives.

Second, changes in the level of interest rates also affect the yields required by the marketplace on debt. Increasing interest rates would decrease the value of the fixed rate assets we hold at the time because higher required yields result in lower prices on existing fixed rate assets in order to adjust their yield upward to meet the market.

Changes in unrealized gains or losses resulting from changes in market interest rates do not directly affect our cash flows, or our ability to pay a dividend, to the extent the related assets are expected to be held, as their fair value is not relevant to their underlying cash flows. Our assets are largely financed to maturity through long term CDO financings that are not redeemable as a result of book value changes. As long as these fixed rate assets continue to perform as expected, our cash flows from these assets would not be affected by increasing interest rates. Changes in unrealized gains or losses would impact our ability to realize gains on existing investments if they were sold. Furthermore, with respect to changes in unrealized gains or losses on investments which are carried at fair value, changes in unrealized gains or losses would impact our net book value and, in the cases of impaired assets and non-hedge derivatives, our net income.

Changes in the value of our assets could affect our ability to borrow and access capital. Also, if the value of our assets subject to short term financing were to decline, it could cause us to fund margin and affect our ability to refinance such assets upon the maturity of the related financings, adversely impacting our rate of return on such securities.

As of June 30, 2014, a 100 basis point change in short term interest rates would impact our net book value by approximately \$8.4 million, based on the current net fixed rate exposure from our investments and interest rate derivatives.

Interest rate swaps are agreements in which a series of interest rate flows are exchanged with a third party (counterparty) over a prescribed period. The notional amount on which swaps are based is not exchanged. In general, our swaps are “pay fixed” swaps involving the exchange of floating rate interest payments from the counterparty for fixed interest payments from us. This can effectively convert a floating rate debt obligation into a fixed rate debt obligation. Interest rate swaps may be subject to margin calls. Similarly, an interest rate cap or floor agreement is a contract in which we purchase a cap or floor contract on a notional face amount. We will make an up-front payment to the counterparty for which the counterparty agrees to make future payments to us should the reference rate (typically LIBOR) rise above (cap agreements) or fall below (floor agreements) the “strike” rate specified in the contract. Payments on an annualized basis will equal the contractual notional face amount multiplied by the difference between the actual reference rate and the contracted strike rate.

While a REIT may utilize these types of derivative instruments to hedge interest rate risk on its liabilities or for other purposes, such derivative instruments could generate income that is not qualified income for purposes of maintaining REIT status. As a consequence, we may only engage in such instruments to hedge such risks within the constraints of maintaining our standing as a REIT. We do not enter into derivative contracts for speculative purposes or as a hedge against changes in credit risk.

Our hedging transactions using derivative instruments also involve certain additional risks such as counterparty credit risk, the enforceability of hedging contracts and the risk that unanticipated and significant changes in interest rates will cause a significant loss of basis in the contract. There can be no assurance that we will be able to adequately protect against the foregoing risks and will ultimately realize an economic benefit that exceeds the related amounts incurred in connection with engaging in such hedging strategies.

### **Credit Spread Exposure**

Credit spreads measure the yield demanded on loans and securities by the market based on their credit relative to U.S. Treasuries, for fixed rate credit, or LIBOR, for floating rate credit. Our fixed rate loans and securities are valued based on a market credit spread over the rate payable on fixed rate U.S. Treasuries of like maturity. Our floating rate loans and securities are valued based on a market credit spread over LIBOR. Excessive supply of such loans and securities combined with reduced demand will generally cause the market to require a higher yield on such loans and securities, resulting in the use of a higher (or “wider”) spread over the benchmark rate to value them.

Widening credit spreads would result in higher yields being required by the marketplace on loans and securities. This widening would reduce the value of the loans and securities we hold at the time because higher required yields result in lower prices on existing securities in order to adjust their yield upward to meet the market. The effects of such a decrease in values on our financial position, results of operations and liquidity are discussed above under “- Interest Rate Exposure.”

As of June 30, 2014, a 25 basis point movement in credit spreads would impact our net book value by approximately \$3.3 million, assuming a static portfolio of current investments and financings, but would not directly affect our earnings or cash flow.

Our financing strategy is dependent on our ability to place the match funded debt we use to finance our investments at rates that provide a positive net spread. Currently, spreads for such liabilities have widened and demand for such liabilities has become extremely limited, therefore restricting our ability to execute future financings.

In an environment where spreads are tightening, if spreads tighten on the assets we purchase to a greater degree than they tighten the liabilities we issue, our net spread will be reduced.

### **Credit Risk**

In addition to the above described market risks, Newcastle is subject to credit risk.

Credit risk refers to the ability of each individual borrower under our loans and securities to make required interest and principal payments on the scheduled due dates. The commercial mortgage and asset backed securities we invest in are generally junior in right of payment of interest and principal to one or more senior classes, but benefit from the support of one or more subordinate classes of securities or other form of credit support (which absorbs losses before the securities in which we invest) within a securitization transaction. The senior unsecured REIT debt securities we invest in reflect comparable credit risk. The value of the subordinated securities has generally been reduced or, in some cases, eliminated, which could leave our securities economically in a first loss position. We also invest in loans and securities which represent “first loss” pieces; in other words, they do not benefit from credit support although we believe they predominantly benefit from underlying collateral value in excess of their carrying amounts. Corporate bank loans are also subject to the risk of a bankruptcy filing of the related entity.

We seek to reduce credit risk by actively monitoring our asset portfolio and the underlying credit quality of our holdings and, where appropriate and achievable, repositioning our investments to upgrade their credit quality. In the event of a significant rising interest rate environment and/or economic downturn, loan and collateral defaults may increase and result in credit losses that would adversely affect our liquidity and operating results. As described in “Management’s Discussion and Analysis of Financial Condition and Results of Operations – Market Considerations” and elsewhere in this quarterly report, adverse market and credit conditions have resulted in our recording of other-than-temporary impairment in certain securities and loans.

#### **Margin**

We are subject to margin calls on our repurchase agreements. Furthermore, we may, from time to time, be a party to derivative agreements or financing arrangements that are subject to margin calls based on the value of such instruments. We seek to maintain adequate cash reserves and other sources of available liquidity to meet any margin calls resulting from decreases in value related to a reasonably possible (in the opinion of management) change in interest rates.

#### **Interest Rate and Credit Spread Risk Sensitive Instruments and Fair Value**

Our holdings of such financial instruments, and their fair values and the estimation methodology thereof, are detailed in Note 12 to our consolidated financial statements included herein. For information regarding the impact of prepayment, reinvestment, and expected loss factors on the timing of realization of our investments, please refer to the consolidated financial statements included herein and in our Annual Report on Form 10-K for the year ended December 31, 2013. For information regarding the impact of changes in these factors on the value of securities valued with internal models, see Part I, Item 2, “Management’s Discussion and Analysis of Financial Condition and Results of Operations – Critical Accounting Policies.”

We note that the values of our investments in real estate securities, loans, Excess MSRs and derivative instruments are sensitive to changes in market interest rates, credit spreads and other market factors. The value of these investments can vary, and has varied, materially from period to period.

#### **Trends**

See “Management’s Discussion and Analysis of Financial Condition and Results of Operations – Market Considerations” above for a further discussion of recent trends and events affecting our liquidity, unrealized gains and losses.

#### **ITEM 4. CONTROLS AND PROCEDURES**

- (a) Disclosure Controls and Procedures. The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this report. The Company's disclosure controls and procedures are designed to provide reasonable assurance that information is recorded, processed, summarized and reported accurately and on a timely basis. Based on such evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, the Company's disclosure controls and procedures are effective.
- (b) Changes in Internal Control Over Financial Reporting. There have not been any changes in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## PART II. OTHER INFORMATION

### Item 1. Legal Proceedings

From time to time, we are or may be involved in various disputes and litigation matters that arise in the ordinary course of business. The Company is not party to any material legal proceedings as of the date on which this report is filed.

### Item 1A. Risk Factors

*Before you invest in our common stock, you should carefully consider the risks involved, including the risks set forth below.*

#### Risks Related to the Financial Markets

#### **Market conditions could negatively impact our business, results of operations and financial condition.**

The markets in which we operate are affected by a number of factors that are largely beyond our control but can nonetheless have a potentially significant, negative impact on us. These factors include, among other things:

- Interest rates and credit spreads;
- The availability of credit, including the price, terms and conditions under which it can be obtained;
- The quality, pricing and availability of suitable investments and credit losses with respect to our investments;
- The ability to obtain accurate market-based valuations;
- Loan values relative to the value of the underlying real estate assets;
- Default rates on both residential and commercial mortgages and the amount of the related losses;
- Prepayment speeds;
- The actual and perceived state of the real estate markets, market for dividend-paying stocks and the U.S. economy and public capital markets generally;
- Unemployment rates; and
- The attractiveness of other types of investments relative to investments in real estate or REITs generally.

Changes in these factors are difficult to predict, and a change in one factor can affect other factors. For example, during 2007, increased default rates in the subprime mortgage market played a role in causing credit spreads to widen, reducing availability of credit on favorable terms, reducing liquidity and price transparency of real estate related assets, resulting in difficulty in obtaining accurate mark-to-market valuations, and causing a negative perception of the state of the real estate markets and of REITs generally. These conditions worsened during 2008, and intensified meaningfully during the fourth quarter of 2008 as a result of the global credit and liquidity crisis, resulting in extraordinarily challenging market conditions. Since then, market conditions have generally improved, but they could deteriorate in the future for a variety of reasons.

#### **A prolonged economic slowdown, a lengthy or severe recession, or declining real estate values could harm our results of operations.**

We believe the risks associated with our business are more severe during periods in which an economic slowdown or recession is accompanied by declining real estate values. Declining real estate values generally reduce the level of new mortgage loan originations, since borrowers often use increases in the value of their existing properties to support the purchase of, or investment in, additional properties. Borrowers may also be less able to pay principal and interest on our loans, and the loans underlying our securities, if the economy weakens. Further, declining real estate values significantly increase the likelihood that we will incur losses on our loans and securities in the event of default because the value of our collateral may be insufficient to cover our basis. Any sustained period of increased payment delinquencies, foreclosures or losses could adversely affect our net interest income from loans and securities in our portfolio, as well as our ability to sell and securitize loans, which would significantly harm our

revenues, results of operations, financial condition, liquidity, business prospects and our ability to make distributions to our stockholders. In addition, an economic slowdown, recession or weakness in the housing market could also harm our senior housing business. See “Due to the dependency of our senior housing revenues on private pay sources, events which adversely affect the ability of seniors to afford the monthly resident fees could cause our occupancy rates, revenues and results of operations to decline.” For more information on the impact of market conditions on our business and results of operations generally, see the section entitled “Management’s Discussion and Analysis of Financial Condition and Results of Operations-Market Considerations” in this report.

In our golf business, a substantial portion of our revenue is derived from discretionary or leisure spending by our members and guests, and such spending can be particularly sensitive to changes in general economic conditions. An economic downturn, whether local, regional, national or global, may lead to increases in unemployment, loss of consumer confidence and a reduction in discretionary spending, which would likely result in increased attrition (i.e., resignations of members of our private properties), a decrease in the rate of new memberships, a decrease in rounds played at our daily fee properties and reduced spending by our members and guests. As a result, our golf business, financial condition and results of operations may be materially adversely affected by an economic downturn.

**The Dodd-Frank Act has affected our business and may continue to do so.**

On July 21, 2010, the United States enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act” or “Act”). The Dodd-Frank Act affects almost every aspect of the U.S. financial services industry, including certain aspects of the markets in which we operate. The Act imposes new regulations on us and how we conduct our business. For example, the Act will impose additional disclosure requirements for public companies and generally require issuers or originators of asset-backed securities to retain at least five percent of the credit risk associated with the securitized assets. In addition, as a result of the Act, we were required to register as an investment adviser with the SEC, which increases our regulatory compliance costs and subjects us to the Investment Advisers Act of 1940, as amended (the “Advisers Act”). The Advisers Act imposes numerous obligations on registered investment advisers, including record-keeping, reporting, operational and marketing requirements, disclosure obligations and prohibitions on fraudulent activities. The SEC is authorized to institute proceedings and impose sanctions for violations of the Advisers Act, ranging from fines and censure to termination of an investment adviser’s registration. Investment advisers also are subject to certain state securities laws and regulations. Non-compliance with the Advisers Act or other federal and state securities laws and regulations could result in investigations, sanctions, disgorgement, fines and reputational damage.

The Act imposes mandatory clearing, exchange-trading and margin requirements on many derivatives transactions (including formerly unregulated over-the-counter derivatives) in which we may engage. These requirements may impact our ability to enter into derivatives transactions, including derivatives transactions used for hedging purposes. The Act also creates new categories of regulated market participants, such as “swap-dealers,” “security-based swap dealers,” “major swap participants” and “major security-based swap participants,” that are subject to significant new capital, registration, recordkeeping, reporting, disclosure, business conduct and other regulatory requirements that will give rise to new administrative costs.

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

**We do not know what impact certain U.S. government programs intended to stabilize the economy and the financial markets will have on our business**

In recent years, the U.S. government has taken a number of steps to attempt to strengthen the financial markets and U.S. economy, including direct government investments in, and guarantees of, troubled financial institutions as well as government-sponsored programs such as the Term Asset-Backed Securities Loan Facility program (TALF) and the Public Private Investment Partnership Program (PPIP). The U.S. government continues to evaluate or implement an array of other measures and programs intended to help improve U.S. financial and market conditions. While conditions appear to have improved relative to the depths of the global financial crisis, it is not clear whether this improvement is real or will last for a significant period of time. It is not clear what impact the government’s future actions to improve financial and market conditions will have on our business. To date, we have not benefited in a direct, material way from any government programs, and we may not derive any meaningful benefit from these

programs in the future. Moreover, if any of our competitors are able to benefit from one or more of these initiatives, they may gain a significant competitive advantage over us.

**Legislation that permits modifications to the terms of outstanding loans has negatively affected our business, financial condition and results of operations.**

The U.S. government has enacted legislation that enables government agencies to modify the terms of a significant number of residential and other loans to provide relief to borrowers without the applicable investor's consent. These modifications allow for outstanding principal to be deferred, interest rates to be reduced, the term of the loan to be extended or other terms to be changed in ways that can permanently eliminate the cash flow (principal and interest) associated with a portion of the loan. These modifications are currently reducing, or in the future may reduce, the value of a number of our current or future investments, including investments in mortgage-backed securities. As a result, such loan modifications could negatively affect our business, results of operations and financial condition. Additional legislation intended to provide relief to borrowers may be enacted and could further harm our business, results of operations and financial condition.

Risks Related to Our Manager

**We are dependent on our manager and may not find a suitable replacement if our manager terminates the management agreement.**

None of our officers or other senior employees who perform services for us is an employee of Newcastle. Instead, these individuals are employees of our manager. In addition, in our senior housing business, we rely on services provided by individuals who are employees of affiliates of our manager or companies owned by private equity funds managed by affiliates of our manager. Accordingly, we are completely reliant on our manager, which has significant discretion as to the implementation of our operating policies and strategies, to conduct our business. Furthermore, we are dependent on the services of certain key employees of our manager whose compensation is partially dependent upon the amount of incentive or management compensation earned by our manager and whose continued service is not guaranteed, and the loss of such services could adversely affect our operations. We are subject to the risk that our manager will terminate the management agreement and that we will not be able to find a suitable replacement for our manager in a timely manner, at a reasonable cost or at all. We may also be adversely affected by operational risks, including cyber security attacks, that could disrupt our manager's financial, accounting and other data processing systems.

**There are conflicts of interest in our relationship with our manager.**

There are conflicts of interest inherent in our relationship with our manager. It is possible that actual, potential or perceived conflicts could give rise to investor dissatisfaction, litigation or regulatory enforcement actions. Appropriately dealing with conflicts of interest is complex and difficult, and our reputation could be damaged if we fail, or appear to fail, to deal appropriately with one or more potential, actual or perceived conflicts of interest. Regulatory scrutiny of, or litigation in connection with, conflicts of interest could have a material adverse effect on our reputation, which could materially adversely affect our business in a number of ways, including causing an inability to raise additional funds, a reluctance of counterparties to do business with us, a decrease in the prices of our common and preferred securities and a resulting increased risk of litigation and regulatory enforcement actions.

Our management agreement with our manager was not negotiated at arm's-length, and its terms, including fees payable, may not be as favorable to us as if it had been negotiated with an unaffiliated third party. Our management agreement does not limit or restrict our manager or its affiliates from engaging in any business or managing other pooled investment vehicles that make investments that meet our investment objectives. Entities managed by our manager or its affiliates- including investment funds, private investment funds, or businesses managed by our manager-have investment objectives that overlap with our investment objectives. Certain investments appropriate for us may also be appropriate for one or more of these other investment vehicles. These entities may invest in assets that meet our investment objectives, including real estate securities, real estate related and other loans, senior housing properties and other operating real estate, and other assets. Our manager or its affiliates may have investments in and/or earn fees from such other investment vehicles that are higher than their economic interests in us and which may therefore create an incentive to allocate investments to such other investment vehicles. Our manager or its affiliates may determine, in their discretion, to make a particular investment through an investment vehicle other than us and have no obligation to offer to us the opportunity to participate in any particular investment opportunity.

Certain members of our board of directors, including our chairman, are officers of our manager. Certain employees of our manager who perform services for us also perform services for companies and funds that compete with us. These employees may serve as officers and/or directors of these other entities. The ability of our manager and its officers and employees to engage in other business activities may reduce the amount of time our manager, its officers or other employees spend managing us.

In addition, we have engaged or may engage (subject to our investment guidelines) in material transactions with our manager or an entity managed by our manager or one of its affiliates, including, but not limited to, certain financing arrangements, purchases of debt, co-investments, acquisitions of senior housing properties and other assets, that present an actual, potential or perceived conflict of interest. We may invest in portfolio companies of private equity funds managed by our manager (or an affiliate thereof). We currently have debt investments in a portfolio company.

The management compensation structure that we have agreed to with our manager, as well as compensation arrangements that we may enter into with our manager in the future (in connection with new lines of business or other activities), may incentivize our manager to invest in high risk investments or to pursue separation transactions, such as the spin-offs of New Residential and New Media and the potential spin-off of our senior housing business. See “-Risks Related to Our Business-Our agreements with New Residential may not reflect terms that would have resulted from arm’s-length negotiations among unaffiliated third parties, and we have agreed to indemnify New Residential for certain liabilities.” In addition to its management fee, our manager is entitled to receive incentive compensation based in part upon our achievement of targeted levels of funds from operations (as defined in the management agreement). In evaluating investments and other management strategies, the opportunity to earn incentive compensation based on funds from operations or, in the case of any future incentive compensation arrangement, other financial measures on which incentive compensation may be based, may lead our manager to place undue emphasis on the maximization of such measures at the expense of other criteria, such as preservation of capital, in order to achieve higher incentive compensation, particularly in light of the fact that our manager has not received any incentive compensation from us since 2008. Investments with higher yield potential are generally riskier or more speculative than lower-yielding investments.

Our manager is eligible to receive compensation in the form of options in connection with the completion of our common equity offerings. Therefore, our manager may be incentivized to cause us to issue additional common stock, which could be dilutive to existing stockholders. On April 8, 2014, our board of directors adopted the 2014 Newcastle Investment Corp. Nonqualified Stock Option and Incentive Award Plan (the “2014 Plan”), which is subject to approval by our stockholders at the 2014 annual meeting of stockholders. If our stockholders vote to approve the 2014 Plan, 1,000,000 shares of our common stock will be available for grants of equity awards thereunder, as increased on the date of any equity issuance by us during the one-year term of the 2014 Plan by ten percent of the equity securities issued by us in such equity issuance. In addition to the shares available for issuance under the 2012 Newcastle Nonqualified Stock Option and Incentive Plan, the 2014 Plan or any successor plan thereto (collectively, the “Option Plans”), our board of directors may also determine to grant options to our manager that are not issued pursuant to the Option Plans, provided that the number of shares underlying any options granted to our manager in connection with any capital raising efforts will not exceed 10% of the shares sold in such offering and would be subject to NYSE rules.

**It would be difficult and costly to terminate our management agreement with our manager.**

It would be difficult and costly for us to terminate our management agreement with our manager. The management agreement may only be terminated annually upon (i) the affirmative vote of at least two-thirds of our independent directors, or by a vote of the holders of a simple majority of the outstanding shares of our common stock, that there has been unsatisfactory performance by our manager that is materially detrimental to us or (ii) a determination by a simple majority of our independent directors that the management fee payable to our manager is not fair, subject to our manager’s right to prevent such a termination by accepting a mutually acceptable reduction of fees. Our manager will be provided 60 days’ prior notice of any such termination and will be paid a termination fee equal to the amount of the management fee earned by the manager during the twelve-month period preceding such termination. In addition, following any termination of the management agreement, the manager may require us to purchase its right to receive incentive compensation at a price determined as if our assets were sold for their fair market value (as determined by an appraisal, taking into account, among other things, the expected future value of the underlying investments) or otherwise we may continue to pay the incentive compensation to our manager. These provisions may increase the effective cost to us of terminating the management agreement, thereby adversely affecting our ability to terminate our manager without cause.

**Our directors have approved very broad investment guidelines for our manager, and we are not required to obtain stockholder consent to change our investment strategy or asset portfolio.**

Our manager is authorized to follow very broad investment guidelines, and our directors do not approve each investment decision made by our manager. Our investment guidelines are purposefully broad to enable our manager to make investments in a wide array of assets, including, but not limited to, any type of assets that can be held by a REIT. Our manager’s investment decisions are based on a variety of factors, such as changing market conditions. Investment opportunities that present unattractive risk-return profiles relative to other available investment opportunities under particular market conditions may become relatively attractive under changed market conditions, and changes in market conditions may therefore result in changes in the investments we target. We do not have policies requiring the allocation of equity to different investment categories, although our investment guidelines do restrict investments of more than 20% of our total equity (as determined on the date of such investment) in any single asset. Consequently, our manager has great latitude in determining which investments are appropriate for us, including the

latitude to build concentrations in certain positions and to invest in asset classes that may differ significantly from those in our existing portfolio. Our directors periodically review our investment guidelines and our investment portfolio. However, our directors rely primarily on information provided to them by our manager, and they do not review or pre-approve each proposed investment or the related financing arrangements. A transaction entered into by our manager that contravenes the terms of our management agreement may be difficult or impossible to unwind by the time it is reviewed by our directors. In addition, we are not required to obtain stockholder consent in order to change our investment strategy and asset portfolio, which may result in making investments that are different, riskier or less profitable than our current investments.

Our investment strategy and asset portfolio have undergone meaningful changes in recent years and will continue to evolve in light of existing market conditions and investment opportunities. As part of our continuing efforts to provide value to our stockholders, we are currently considering a spin-off of our senior housing business from the remainder of our investment portfolio. If the transaction resulted in our senior housing business being held in a stand-alone entity, we expect that such entity would elect and qualify to be taxed as a REIT. Our board has not formally evaluated any such transaction, and there can be no assurance as to the timing, terms, structure or completion of any such transaction. Any such transaction would be subject to a number of risks and uncertainties, could have tax implications for the holders of shares of our common stock, and could adversely affect the price of shares of our common stock. See “-Risks Related to Our Business-We are actively exploring new business opportunities and asset categories, which could entail significant risks and adversely affect our financial condition, results of operations and liquidity” and “We recently acquired a golf business, which is subject to various risks that could have a negative impact on our financial results.”

**Our manager will not be liable to us for any acts or omissions performed in accordance with the management agreement, including with respect to the performance of our investments.**

Pursuant to our management agreement, our manager will not assume any responsibility other than to render the services called for thereunder and will not be responsible for any action of our board of directors in following or declining to follow its advice or recommendations. Under the terms of our management agreement, our manager, its officers, partners, members, managers, directors, personnel, other agents, any person controlling or controlled by our manager and any person providing sub-advisory services to our manager will not be liable to us, any subsidiary of ours, our directors, our stockholders or any subsidiary’s stockholders or partners for acts or omissions performed in accordance with and pursuant to our management agreement, except because of acts constituting bad faith, willful misconduct or gross negligence, as determined by a final non-appealable order of a court of competent jurisdiction. In addition, we have agreed to indemnify our manager, its officers, partners, members, managers, directors, personnel, other agents, any person controlling or controlled by our manager and any person providing sub-advisory services to our manager with respect to all expenses, losses, damages, liabilities, demands, charges and claims arising from acts of our manager not constituting bad faith, willful misconduct or gross negligence, pursuant to our management agreement.

**Our manager’s due diligence of investment opportunities or other transactions may not identify all pertinent risks, which could materially affect our business, financial condition, liquidity and results of operations.**

Our manager intends to conduct due diligence with respect to each investment opportunity or other transaction it pursues. It is possible, however, that our manager’s due diligence processes will not uncover all relevant facts, particularly with respect to any assets we acquire from third parties. In these cases, our manager may be given limited access to information about the investment and will rely on information provided by the target of the investment. In addition, if investment opportunities are scarce, the process for selecting bidders is competitive, or the time-frame in which we are required to complete diligence is short, our ability to conduct a due diligence investigation may be limited, and we would be required to make investment decisions based upon a less thorough diligence process than would otherwise be the case. Accordingly, investments and other transactions that initially appear to be viable may prove not to be over time due to the limitations of the due diligence process or other factors.

Risks Related to Our Business

**We are actively exploring new business opportunities and asset categories, which could entail a meaningful change in our investment focus and operations and pose significant risks to our financial condition, results of operations and liquidity.**

Consistent with our broad investment guidelines and our investment objectives, we have acquired and/or are pursuing a variety of assets that differ from the assets in our legacy portfolio, such as senior housing properties, a golf business, Excess MSRs (which we spun-off in May 2013) and media assets (which we spun-off in February 2014). As previously disclosed, we are considering a spin-off of our senior housing business. Our board has not formally evaluated any such transaction, and there can be no assurance as to the timing, terms, structure or completion of any such transaction. Any such transaction would be subject to a number of risks and uncertainties, could have tax implications for the holders of shares of our common stock, and could adversely affect the

price of shares of our common stock. Although we currently believe that we will have significant investment opportunities in the future, these opportunities may not materialize. In addition, our ability to act on new investment opportunities may be constrained by the requirements of the Investment Company Act of 1940, as amended (the "1940 Act"), or federal tax law. See "-Risks Related to Our REIT Status and the 1940 Act."

New investments may not be profitable (or as profitable as we expect), may increase our exposure to certain industries (such as the golf industry), may increase our exposure to interest rate, foreign currency, real estate market or credit market fluctuations, may divert managerial attention from more profitable opportunities, and may require significant financial resources. A change in our investment strategy may also increase our use of non-match-funded financing, increase the guarantee obligations we agree to incur or increase the number of transactions we enter into with affiliates. Moreover, new investments may present risks that are difficult for us to adequately assess, given our lack of familiarity with a particular asset class or other reasons. The risks related to new asset categories or the financing risks associated with such assets could adversely affect our results of operations, financial condition and liquidity, and could impair our ability to pay dividends on both our common stock and preferred stock. See "-Risks Related to Our Manager-Our directors have approved very broad investment guidelines for our manager, and we are not required to obtain stockholder consent to change our investment strategy or asset portfolio."

**We recently acquired a golf business, which is subject to various risks that could have a negative impact on our financial results.**

In December 2013, we completed a restructuring of an investment in mezzanine debt issued by NGP, the indirect parent of National Golf. National Golf owns 27 golf properties across 8 states, and leases these courses to American Golf, an affiliated operating company. American Golf also leases an additional 52 golf properties and manages 11 properties owned by third parties, respectively. As part of the restructuring, we acquired the equity of NGP and American Golf's indirect parent, AGC, and therefore began consolidating these entities as of December 31, 2013.

We have never owned or operated a golf business, and there can be no assurance that we will be able to successfully manage this business. Our ability to attract and retain members and increase usage at our golf facilities is critical to the success of our golf business, and there can be no assurance that we will be able to do so. See "-We are actively exploring new business opportunities and asset categories, which could entail significant risks and adversely affect our financial condition, results of operations and liquidity." Moreover, the golf industry generally, has experienced a period of declining revenue and profitability. See "-We have invested in operating businesses in distressed industries, such as golf, and such investments are subject to operational and other business risks."

Our golf business is subject to various risks that may not apply to our other operations. For example, unusual weather patterns and extreme weather events, such as heavy rains, prolonged snow accumulations, high winds, extended heat waves and drought, could negatively affect the income generated by our facilities. The maintenance of satisfactory turf grass conditions on our golf courses requires significant amounts of water. Our ability to irrigate a golf course could be adversely affected by a drought or other cause of water shortage, such as government imposed restrictions on water usage. Additionally, we may be subject to significant increases in the cost of water. We have a concentration of golf facilities in states (such as California, Georgia, and New York) that experience periods of unusually hot, cold, dry or rainy weather. Unfavorable weather patterns in such states, or any other circumstance or event that causes a prolonged disruption in the operations of our facilities in such states (including, without limitation, economic and demographic changes in these areas), could have a particularly adverse impact on our golf business. See "-A prolonged economic slowdown, a lengthy or severe recession or declining real estate values could harm our results of operations."

Seasonality will affect our golf business's results of operations. Usage of golf facilities tends to decline significantly during the first and fourth quarters, when colder temperatures and shorter days reduce the demand for outdoor activities. As a result, we expect the golf business to generate a disproportionate share of its annual revenue in the second and third quarters of each year. Accordingly, our golf business is especially vulnerable to events that may negatively impact its operations during the second and third quarters, when guest and member usage is highest.

In addition, we may be required to make significant cash outlays in connection with "initiation deposits." Members of our private properties are generally required to pay an initiation deposit upon their acceptance as a member and, in most cases, such deposits are fully refundable after a fixed number of years (typically, 30 years) and upon the occurrence of other contract-specific conditions. While we will make a refund to any member whose initiation deposit is eligible to be refunded, we may be subject to various states' escheatment laws with respect to initiation deposits that have not been refunded to members. All states have escheatment laws and generally require companies to remit to the state cash in an amount equal to unclaimed and abandoned property after a specified period of dormancy, which is typically 3 to 5 years. Moreover, most of the states in which we conduct business hire

independent agents to conduct unclaimed and abandoned property audits. We currently do not remit to states any amounts relating to initiation deposits that are eligible to be refunded to members based upon our interpretation of the applicability of such laws to initiation deposits. The analysis of the potential application of escheatment laws to our initiation deposits is complex, involving an analysis of constitutional and statutory provisions and contractual and factual issues. While we do not believe that initiation deposits must be escheated, we may be forced to remit such amounts if we are challenged and fail to prevail in our position.

If one or more of the foregoing risks were to materialize, our golf business could be adversely affected, which could have a material adverse effect on our financial condition, results of operations and liquidity.

**The geographic distribution of the mortgage loans underlying, and collateral securing, certain of our investments subjects us to geographic real estate market risks, which could adversely affect the performance of our investments, our results of operations and our financial condition.**

The geographic distribution of the commercial and residential mortgage loans underlying, and collateral securing, certain of our investments, including our mortgage-backed securities, exposes us to risks associated with the real estate industry in general within the states and regions in which we hold significant investments. These risks include, without limitation: possible declines in the value of real estate; risks related to general and local economic conditions; possible lack of availability of mortgage funds; overbuilding; extended vacancies of properties; increases in competition, property taxes and operating expenses; changes in zoning laws; costs resulting from the clean-up of, and liability to third parties for damages resulting from, environmental problems; casualty or condemnation losses; uninsured damages from floods, earthquakes or other natural disasters; and changes in interest rates. To the extent any of the foregoing risks arise in states and regions where we hold significant investments, the performance of our investments, our results of operations and our financial condition could suffer a material adverse effect.

**The coverage tests applicable to our CDO financings may have a negative impact on our operating results and cash flows.**

We have retained, and may in the future retain or repurchase, subordinate classes of bonds issued by certain of our subsidiaries in our CDO financings. Each of our CDO financings contains tests that measure the amount of over collateralization and excess interest in the transaction. Failure to satisfy these tests would generally result in principal and/or interest cash flow that would otherwise be distributed to more junior classes of securities (including those held by us) to be redirected to pay down the most senior class of securities outstanding until the tests are satisfied. As a result, failure to satisfy the coverage tests could adversely affect our operating results and cash flows by temporarily or permanently directing funds that would otherwise come to us to holders of the senior classes of bonds. In addition, the redirected funds would be used to pay down financing, thereby reducing our future returns from the affected CDO. The ratings assigned to the assets in each CDO affect the results of the tests governing whether a CDO can distribute cash to the various classes of securities in the CDO. As a result, ratings downgrades of the assets in a CDO can result in a CDO failing its tests and thereby cause us not to receive cash flows from the affected CDO.

We had no assets in our consolidated CDOs as of June 30, 2014 under negative watch for possible downgrade by at least one of the rating agencies. One or more of the rating agencies could downgrade some or all of these assets at any time, and any such downgrade could negatively affect-and possibly materially affect-our future cash flows. As of the June 2014 remittance date for CDO VI, this CDO was not in compliance with its applicable over collateralization tests and consequently, we are not receiving residual cash flows from this CDO, other than senior management fees and cash flow distributions from senior classes of bonds we own. Based upon our current calculations, we expect CDO VI to remain out of compliance for the foreseeable future. Moreover, given current market conditions, it is possible that all of our CDOs could be out of compliance with their over collateralization tests as of one or more measurement dates within the next twelve months.

Our ability to rebalance will depend upon a variety of factors, such as the availability of suitable securities, market prices, available cash, and other factors that may be beyond our control. For example, one strategy we have employed to facilitate compliance with over collateralization tests has been to repurchase notes issued by our CDOs and subsequently cancel them in accordance with the terms of the relevant governing documentation. However, there can be no assurance that the trustee of our CDOs will not impose guidelines for such cancellations that would make it more difficult or impossible to employ this strategy in the future. While there are other permissible methods to rebalance or otherwise correct CDO test failures, such methods may be extremely difficult to employ as a result of market conditions or other factors, and we cannot assure you that we will be successful in our rebalancing efforts. If the liabilities of our CDOs are downgraded by Moody's Investors Service to certain predetermined levels, our discretion to rebalance the applicable CDO portfolios may be negatively impacted. Moreover, if we bring these coverage tests into compliance, we cannot assure you that they will not fall out of compliance in the future or that we will be able to correct any noncompliance.

Failure of the over collateralization tests can also cause a “phantom income” issue if cash that constitutes income is diverted to pay down debt instead of distributed to us. For more information regarding noncompliance with the terms of certain of our CDO financings in the near future, please see the section entitled “Management’s Discussion and Analysis of Financial Condition and Results of Operations-Liquidity and Capital Resources” in this report.

**We may experience an event of default or be removed as collateral manager under one or more of our CDOs, which would negatively affect us in a number of ways.**

The documentation governing our CDOs specifies certain events of default, which, if they occur, would negatively affect us. Events of default include, among other things, failure to pay interest on senior classes of securities within the CDO, breaches of covenants, representations or warranties, bankruptcy, and failure to satisfy specific over collateralization tests. If an event of default occurs under any of our CDOs, it could negatively affect our cash flows, business, results of operations and financial condition.

In addition, we can be removed as manager of a CDO if certain events occur, including, among other things, the failure to satisfy specific over collateralization tests, failure to satisfy certain “key man” requirements or an event of default occurring for the failure to pay interest on certain senior classes of securities of the CDO. If we are removed as collateral manager, we would no longer receive management fees from-and no longer be able to manage the assets of-the applicable CDO, which could negatively affect our cash flows, business, results of operations and financial condition. On June 17, 2011, CDO V failed certain over collateralization tests. The consequences of failing these tests are that an event of default has occurred, and we may be removed as the collateral manager under the documentation governing CDO V. So long as the event of default continues, we will not be permitted to purchase or sell any collateral in CDO V. If we are removed as the collateral manager of CDO V, we would no longer receive the senior management fees from such CDO. As of the date of this report, we have not been removed as collateral manager. Based upon our current calculations, we estimate that if we are removed as the collateral manager of CDO V, the loss of senior management fees would not have a material negative impact on our cash flows, business, results of operations or financial condition. Given current market conditions, it is possible that events of default constituting manager termination events, or other manager termination events, may occur in other CDOs, and we could be removed as the collateral manager of those CDOs if such events of default occur. Moreover, our cash flows, business, results of operations and/or financial condition could be materially and negatively impacted if such events of default occur.

**We have assumed the role of manager of numerous CDOs previously managed by a third party, and we may assume the role of manager of additional CDOs in the future. Each such engagement exposes us to a number of potential risks.**

Changes within our industry may result in CDO collateral managers being replaced. In such instances, we may seek to be engaged as the collateral manager of CDOs currently managed by third parties. For example, in February 2011, one of our subsidiaries became the collateral manager of certain CDOs previously managed by C-BASS Investment Management LLC (“C-BASS”).

While being engaged as the collateral manager of such CDOs potentially enables us to grow our business, it also entails a number of risks that could harm our reputation, results of operations and financial condition. For example, we purchased the management rights with respect to the C-BASS CDOs pursuant to a bankruptcy proceeding. As a result, we were not able to conduct extensive due diligence on the CDO assets even though many classes of securities issued by the CDOs were rated as “distressed” by the rating agencies as of the most recent rating date prior to our becoming the collateral manager of the CDOs. We may willingly or unknowingly assume actual or contingent liabilities for significant expenses, we may become subject to new laws and regulations with which we are not familiar, and we may become subject to increased risk of litigation, regulatory investigation or negative publicity. For example, we determined that it would be prudent to register the subsidiary that became the collateral manager of the C-BASS CDOs as a registered investment adviser, which has increased our regulatory compliance costs. In addition to defending against litigation and complying with regulatory requirements, being engaged as collateral manager may require us to invest other resources for various other reasons, which could detract from our ability to capitalize on future opportunities. Moreover, being engaged as collateral manager may require us to integrate complex technological, accounting and management systems, which may be difficult, expensive and time-consuming and which we may not be successful in integrating into our current systems. In addition to the risk that we face if we are successful in becoming the manager of additional CDOs, we may attempt but fail to become the collateral manager of CDOs in the future, which could harm our reputation and subject us to costly litigation. Finally, if we include the financial performance of the C-BASS CDOs or other CDOs for which we become the collateral manager in our public filings, we are subject to the risk that, particularly during the period immediately after we become the collateral manager, this information may prove to be inaccurate or incomplete. The occurrence of any of these negative integration events could negatively impact our reputation with both regulators and investors, which could, in turn, subject us to additional regulatory scrutiny and impair our relationships with the investment community. The occurrence of any of these problems could negatively affect our reputation, financial condition and results of operations.

**Our investments may be subject to significant impairment charges, which would adversely affect our results of operations.**

We are required to periodically evaluate our investments for impairment indicators. The value of an investment is impaired when our analysis indicates that, with respect to a loan, it is probable that we will not be able to collect the full amount we intended to collect from the loan or, with respect to a security, it is probable that the value of the security is other than temporarily impaired. The judgment regarding the existence of impairment indicators is based on a variety of factors depending upon the nature of the investment and the manner in which the income related to such investment was calculated for purposes of our financial statements. If we determine that an impairment has occurred, we are required to make an adjustment to the net carrying value of the investment and the amount of accrued interest recognized as income from such investment, which could have a material adverse effect on our results of operations and our ability to pay dividends to our stockholders.

Market turmoil beginning in 2007 resulted in a number of financial institutions recording an unprecedented amount of impairment charges, and we were also affected by these conditions. These challenging conditions have reduced the market trading activity for many real estate securities, resulting in less liquid markets for those securities. These lower valuations have affected us by, among other things, decreasing our net book value and contributing to our decision to record impairment charges. In addition, the amount we ultimately realize from certain of our debt investments may be dependent on our ability to execute long-term strategies involving corporate reorganizations of the applicable issuer.

**The lenders under our repurchase agreements may elect not to extend financing to us, which could quickly and seriously impair our liquidity.**

We have historically financed a meaningful portion of our investments in securities and loans with repurchase agreements, which are short-term financing arrangements, and we may enter into additional repurchase agreements in the future. Under the terms of these agreements, we sell a security or loan to a counterparty for a specified price and concurrently agree to repurchase the same security or loan from our counterparty at a later date for a higher specified price. During the term of the repurchase agreement—generally 30 days—the counterparty makes funds available to us and holds the security or loan as collateral. Our counterparties can also require us to post additional margin as collateral at any time during the term of the agreement. When the term of a repurchase agreement ends, we are required to repurchase the security or loan for the specified repurchase price, with the difference between the sale and repurchase prices serving as the equivalent of paying interest to the counterparty in return for extending financing to us. If we want to continue to finance the security or loan with a repurchase agreement, we ask the counterparty to extend-or “roll”—the repurchase agreement for another term.

Our counterparties are not required to roll our repurchase agreements upon the expiration of their stated terms, which subjects us to a number of risks. As we have experienced in the past and may experience in the future, counterparties electing to roll our repurchase agreements may charge higher spreads and impose more onerous terms upon us, including the requirement that we post additional margin as collateral. More significantly, if a repurchase agreement counterparty elects not to extend our financing, we would be required to pay the counterparty the full repurchase price on the maturity date and find an alternate source of financing. Alternate sources of financing may be more expensive, contain more onerous terms, may not be available in a timely manner or at all. If we were unable to pay the repurchase price for any security or loan financed with a repurchase agreement, the counterparty has the right to sell the underlying security or loan being held as collateral and require us to compensate for any shortfall between the value of our obligation to the counterparty and the amount for which the collateral was sold (which may be a significantly discounted price). As of June 30, 2014, we had \$102.7 million outstanding under repurchase agreement financings. These repurchase agreement obligations are with two counterparties.

**Our determination of how much leverage to apply to our investments may adversely affect our return on our investments and may reduce cash available for distribution.**

We leverage a meaningful portion of our portfolio through borrowings, generally through the use of credit facilities, warehouse facilities, repurchase agreements, mortgage loans on real estate, securitizations, including the issuance of CDOs, private or public offerings of debt by subsidiaries, loans to entities in which we hold, directly or indirectly, interests in pools of properties or loans, and other borrowings. Our investment policies do not limit the amount of leverage we may incur with respect to any specific asset or pool of assets, subject to an overall limit on our use of leverage to 90% (as defined in our governing documents) of the value of our assets on an aggregate basis. During the 2007–2008 financial crisis, the return we were able to earn on our investments and cash available for distribution to our stockholders was significantly reduced due to changes in market conditions causing the cost of our financing to increase relative to the income that can be derived from our assets. While our liquidity position has improved, we cannot assure you that we will be able to sustain our improved liquidity position.

**We are party to agreements that require cash payments upon the occurrence of certain events, and the failure to make such payments may adversely affect our business, financial condition and results of operations.**

We are currently party to repurchase agreements that may require us to post additional margin as collateral at any time during the term of the agreement, based on the value of the collateral. We may become party to additional financing agreements that require us to make cash payments at periodic intervals or upon the occurrence of certain events. Events could occur or circumstances could arise, which we may not be able to foresee, that may cause us to be unable to make any such cash payments when they become due. Failure to make the payments required under our financing documents would give the lenders the right to require us to repay all amounts owed to them under the applicable financing immediately.

**We are subject to counterparty default and concentration risks.**

In the ordinary course of our business, we enter into various types of financing arrangements with counterparties. Currently, the majority of our financing arrangements take the form of repurchase agreements, securitization vehicles, loans, hedge contracts and other derivative and non-derivative contracts. The terms of these contracts are often customized and complex, and many of these arrangements occur in markets or relate to products that are not subject to regulatory oversight.

We are subject to the risk that the counterparty to one or more of these contracts defaults, either voluntarily or involuntarily, on its performance under the contract. Any such counterparty default may occur rapidly and without notice to us. Moreover, if a counterparty defaults, we may be unable to take action to cover our exposure, either because we lack the contractual ability or because market conditions make it difficult to take effective action. This inability could occur in times of market stress, which are precisely the times when defaults may be most likely to occur.

In addition, our risk-management processes may not accurately anticipate the impact of market stress or counterparty financial condition, and as a result, we may not take sufficient action to reduce our risks effectively. Although we monitor our credit exposures, default risk may arise from events or circumstances that are difficult to detect, foresee or evaluate. In addition, concerns about, or a default by, one large participant could lead to significant liquidity problems for other participants, which may in turn expose us to significant losses.

In the event of a counterparty default, particularly a default by a major investment bank, we could incur material losses rapidly, and the resulting market impact of a major counterparty default could seriously harm our business, results of operations and financial condition. In the event that one of our counterparties becomes insolvent or files for bankruptcy, our ability to eventually recover any losses suffered as a result of that counterparty's default may be limited by the liquidity of the counterparty or the applicable legal regime governing the bankruptcy proceeding.

In addition, with respect to our CDOs, certain of our derivative counterparties are required to maintain certain ratings to avoid having to post collateral or transfer the derivative to another counterparty. If a counterparty was downgraded below these levels, it may not be able to satisfy its obligations under the derivative, which could have a material negative effect on the applicable CDO.

The consolidation and elimination of counterparties has increased our counterparty concentration risk. We are not restricted from dealing with any particular counterparty or from concentrating any or all of our transactions with a few counterparties. As of the date of this report, we had obligations to repurchase assets pursuant to repurchase agreements with six different counterparties. If any of our counterparties elected not to roll these repurchase agreements, we may not be able to find a replacement counterparty. In addition, counterparties have generally tightened their underwriting standards and increased their margin requirements for financing, which has negatively impacted us in several ways, including, decreasing the number of counterparties willing to provide financing to us, decreasing the overall amount of leverage available to us, and increasing the costs of borrowing.

Any loss suffered by us as a result of a counterparty defaulting, refusing to conduct business with us or imposing more onerous terms on us would also negatively affect our business, results of operations and financial condition.

**We may not match fund certain of our investments, which may increase the risks associated with these investments.**

One component of our investment strategy is to use match funded financing structures for certain of our investments, which match assets and liabilities with respect to maturities and interest rates. When available, this strategy mitigates the risk of not being able to refinance an investment on favorable terms or at all. However, our manager may elect for us to bear a level of refinancing risk on a short-term or longer-term basis, as in the case of investments financed with repurchase agreements, when, based on its analysis, our manager determines that bearing such risk is advisable or unavoidable (which is generally the case with respect to

the residential mortgage loans and FNMA/FHLMC securities in which we invest). In addition, we may be unable, as a result of conditions in the credit markets, to match fund our investments. For example, since the 2008 recession, non-recourse term financing not subject to margin requirements has been more difficult to obtain, which impairs our ability to match fund our investments. Moreover, we may not be able to enter into interest rate swaps. Lastly, lenders may be unwilling to finance certain types of assets because of the challenges with perfecting security interests in the underlying collateral. A decision not to, or the inability to, match fund certain investments, exposes us to additional risks.

Furthermore, we anticipate that, in most cases, for any period during which our floating rate assets are not match funded with respect to maturity, the income from such assets may respond more slowly to interest rate fluctuations than the cost of our borrowings. Because of this dynamic, interest income from such investments may rise more slowly than the related interest expense, with a consequent decrease in our net income. Interest rate fluctuations resulting in our interest expense exceeding interest income would result in operating losses for us from these investments.

Accordingly, if we do not or are unable to match fund our investments with respect to maturities and interest rates, we will be exposed to the risk that we may not be able to finance or refinance our investments on economically favorable terms or may have to liquidate assets at a loss.

**We may not be able to finance our securities and loan investments on attractive terms or at all.**

When we acquire securities and loans that we finance on a short-term basis with a view to securitization or other long-term financing, we bear the risk of being unable to securitize the assets or otherwise finance them on a long-term basis at attractive prices or in a timely matter, or at all. If it is not possible or economical for us to securitize or otherwise finance such assets on a long-term basis, we may be unable to pay down our short-term credit facilities, or be required to liquidate the assets at a loss in order to do so. For example, our ability to finance investments with securitizations or other long-term non-recourse financing not subject to margin requirements has been impaired since 2007 as a result of market conditions. These conditions make it highly likely that we will have to use less efficient forms of financing for any new investments, which will likely require a larger portion of our cash flows to be put toward making the initial investment and thereby reduce the amount of cash available for distribution to our stockholders and funds available for operations and investments, and which will also likely require us to assume higher levels of risk when financing our investments.

**As non-recourse long-term financing structures become available to us and are utilized, such structures expose us to risks that could result in losses to us.**

We may use securitization and other non-recourse long-term financing for our investments to the extent available. In such structures, our lenders typically would have only a claim against the assets included in the securitizations rather than a general claim against us as an entity. Prior to any such financing, we would seek to finance our investments with relatively short-term facilities until a sufficient portfolio is accumulated. As a result, we would be subject to the risk that we would not be able to acquire, during the period that any short-term facilities are available, sufficient eligible assets or securities to maximize the efficiency of a securitization. We also bear the risk that we would not be able to obtain new short-term facilities or would not be able to renew any short-term facilities after they expire should we need more time to seek and acquire sufficient eligible assets or securities for a securitization. In addition, conditions in the capital markets may make the issuance of any such securitization less attractive to us even when we do have sufficient eligible assets or securities. While we would intend to retain the unrated equity component of securitizations and, therefore, still have exposure to any investments included in such securitizations, our inability to enter into such securitizations may increase our overall exposure to risks associated with direct ownership of such investments, including the risk of default. Our inability to refinance any short-term facilities would also increase our risk because borrowings thereunder would likely be recourse to us as an entity. If we are unable to obtain and renew short-term facilities or to consummate securitizations to finance our investments on a long-term basis, we may be required to seek other forms of potentially less attractive financing or to liquidate assets at an inopportune time or price.

**Our investments in loans, and the loans underlying our investments in securities, are subject to delinquency, foreclosure and loss, and we may convert a debt position into an equity position in order to preserve the value of our investment, which could result in losses to us and expose us to additional risks.**

Commercial mortgage loans are secured by multifamily or commercial property and are subject to risks of delinquency and foreclosure, and risks of loss. The ability of a borrower to repay a loan secured by an income-producing property typically is dependent primarily upon the successful operation of such property rather than upon the existence of independent income or assets of the borrower. If the net operating income of the property is reduced, the borrower's ability to repay the loan may be impaired. Net operating income of an income-producing property can be affected by, among other things: tenant mix, success of tenant

businesses, property management decisions, property location and condition, competition from comparable types of properties, changes in laws that increase operating expense or limit rents that may be charged, any need to address environmental contamination at the property, the occurrence of any uninsured casualty at the property, changes in national, regional or local economic conditions and/or specific industry segments, declines in regional or local real estate values, declines in regional or local rental or occupancy rates, increases in interest rates, changes in the availability of credit on favorable terms, real estate tax rates and other operating expenses, changes in governmental rules, regulations and fiscal policies, including environmental legislation, acts of God, terrorism, social unrest and civil disturbances.

Residential mortgage loans, manufactured housing loans and subprime mortgage loans are secured by single-family residential property and are also subject to risks of delinquency and foreclosure, and risks of loss. The ability of a borrower to repay a loan secured by a residential property is dependent upon the income or assets of the borrower. A number of factors may impair borrowers' abilities to repay their loans, including, among other things, changes in the borrower's employment status, changes in national, regional or local economic conditions, changes in interest rates or the availability of credit on favorable terms, changes in regional or local real estate values, changes in regional or local rental rates and changes in real estate taxes.

In the event of a default under a loan held directly by us, we will bear a risk of loss of principal to the extent of any deficiency between the value of the collateral and the outstanding principal and accrued but unpaid interest of the loan, which could adversely affect our financial condition, earnings and cash flow from operations. Foreclosure of a loan, particularly a commercial loan, or any other restructuring activities related to an investment, can be an expensive and lengthy process, which would negatively affect our anticipated return on the foreclosed loan or such other investment. In addition, as part of any foreclosure or other restructuring, we may acquire control of a property securing a defaulted loan, which would expose us to additional risks specific to the property, including, but not limited to, the risks related to any business conducted on such property. As part of a restructuring, we may also exchange our debt for, or otherwise acquire, equity of an entity, which may involve contested negotiations and expose us to risks associated with owning the entity.

Mortgage and asset-backed securities are bonds or notes backed by loans and/or other financial assets and include commercial mortgage-backed securities, FNMA/FHLMC securities, and real estate related asset-backed securities. The ability of a borrower to repay these loans or other financial assets is dependent upon the income or assets of these borrowers. If a borrower has insufficient income or assets to repay these loans, it will default on its loan. While we intend to focus on real estate related asset-backed securities, there can be no assurance that we will not invest in other types of asset-backed securities.

Our investments in mortgage and asset-backed securities will be adversely affected by defaults under the loans underlying such securities. To the extent losses are realized on the loans underlying the securities in which we invest, we may not recover the amount invested in, or, in extreme cases, any of our investment in such securities.

**Our investments in debt securities are subject to specific risks relating to the particular issuer of the securities and to the general risks of investing in subordinated real estate securities.**

Our investments in debt securities involve special risks. REITs generally are required to invest substantially in real estate or real estate-related assets and are subject to the inherent risks associated with real estate-related investments discussed in this report. Our investments in debt are subject to the risks described above with respect to mortgage loans and mortgage-backed securities and similar risks, including:

- risks of delinquency and foreclosure, and risks of loss in the event thereof;
- the dependence upon the successful operation of and net income from real property;
- risks generally incident to interests in real property; and
- risks that may be presented by the type and use of a particular property.

Debt securities may be unsecured and may also be subordinated to other obligations of the issuer. We may also invest in debt securities that are rated below investment grade. As a result, investments in debt securities are also subject to risks of:

- limited liquidity in the secondary trading market;
- substantial market price volatility resulting from changes in prevailing interest rates or credit spreads;

- subordination to the prior claims of senior lenders to the issuer;
- the possibility that earnings of the debt security issuer may be insufficient to meet its debt service; and
- the declining creditworthiness and potential for insolvency of the issuer of such debt securities.

These risks may adversely affect the value of outstanding debt securities and the ability of the issuers thereof to repay principal and interest.

**We are subject to significant competition, and we may not compete successfully.**

We are subject to significant competition in seeking investments. We compete with other companies, including other REITs, insurance companies and other investors, including funds and companies affiliated with our manager. Our management agreement, as amended, does not limit or restrict our manager or its affiliates from engaging in any business or managing other pooled investment vehicles that make investments that meet our investment objectives. See “-Risks Related to Our Manager-There are conflicts of interest in our relationship with our manager.”

Some of our competitors have greater resources than we possess or have greater access to capital or various types of financing structures than are available to us, and we may not be able to compete successfully for investments or provide attractive investment returns relative to our competitors. These competitors may be willing to accept lower returns on their investments or to compromise underwriting standards and, as a result, our origination volume and profit margins could be adversely affected. Furthermore, competition for investments that are suitable for us may lead to the returns available from such investments decreasing, which may further limit our ability to generate our desired returns. We cannot assure you that other companies will not be formed that compete with us for investments or otherwise pursue investment strategies similar to ours or that we will be able to complete successfully against any such companies.

Our manager or its affiliates have and may in the future raise, acquire or manage investment vehicles that are entitled to a priority or exclusive right to invest in certain types of assets. If such an investment vehicle exists, that vehicle’s exclusivity would prevent us from investing in the assets over which the investment vehicle has exclusivity because we do not have the exclusive right to invest in any particular type of asset. This dynamic may reduce the type of assets in which we are able to invest.

Our golf facilities compete on a local and regional level with other golf facilities. Competition tends to be based on market penetration, demographic and quality factors and price factors. The level of competition and primary competitors vary by region and are subject to change as existing facilities are renovated or new facilities are developed. An increase in the number or quality of similar facilities in a particular region could significantly increase competition, which could have a negative impact on the results of operations for our golf segment.

For competition risk related to our senior housing business, see “-Competition may affect our senior housing property managers’ and tenant operators’ ability to meet their obligations to us or make it difficult for us to identify and purchase, or develop, suitable senior housing properties to grow our investment portfolio.”

**Our returns will be adversely affected when investments held in CDOs are prepaid or sold subsequent to the reinvestment period.**

Real estate securities and loans are subject to prepayment risk. In addition, we may sell, and realize gains (or losses) on, investments. To the extent such assets were held in CDOs subsequent to the end of the reinvestment period, the proceeds are fully utilized to pay down the related CDO’s debt. This causes the leverage on the CDO to decrease, thereby lowering our returns on equity.

**Our investments in senior unsecured REIT securities are subject to specific risks relating to the particular REIT issuer and to the general risks of investing in subordinated real estate securities, which may result in losses to us.**

Our investments in REIT securities involve special risks relating to the particular REIT issuer of the securities, including the financial condition and business outlook of the issuer. REITs generally are required to substantially invest in operating real estate or real estate related assets and are subject to the inherent risks associated with real estate related investments discussed in this report.

Our investments in REIT securities are also subject to the risks described above with respect to mortgage loans and mortgage-backed securities and similar risks, including (i) risks of delinquency and foreclosure, and risks of loss in the event thereof, (ii)

the dependence upon the successful operation of and net income from real property, (iii) risks generally incident to interests in real property, and (iv) risks that may be presented by the type and use of a particular commercial property.

REIT securities are generally unsecured and may also be subordinated to other obligations of the issuer. We may also invest in REIT securities that are rated below investment grade. As a result, investments in REIT securities are also subject to risks of: (i) limited liquidity in the secondary trading market, (ii) substantial market price volatility resulting from changes in prevailing interest rates, (iii) subordination to the prior claims of banks and other senior lenders to the issuer, (iv) the operation of mandatory sinking fund or call/redemption provisions during periods of declining interest rates that could cause the issuer to reinvest premature redemption proceeds in lower yielding assets, (v) the possibility that earnings of the REIT issuer may be insufficient to meet its debt service and dividend obligations and (vi) the declining creditworthiness and potential for insolvency of the issuer of such REIT securities during periods of rising interest rates and economic downturn. These risks may adversely affect the value of outstanding REIT securities and the ability of the issuers thereof to repay principal and interest or make dividend payments.

**Our investments in real estate related and other loans and other direct and indirect interests in pools of real estate properties or other loans may be subject to additional risks relating to the structure and terms of these transactions, which may result in losses to us.**

We have investments in real estate related and other loans and other direct and indirect interests in pools of real estate properties or loans, such as mezzanine loans and “B Note” mortgage loans. We have invested in mezzanine loans that take the form of subordinated loans secured by second mortgages on the underlying real property or other business assets or revenue streams or loans secured by a pledge of the ownership interests of the entity owning real property or other business assets or revenue streams (or the ownership interest of the parent of such entity). These types of investments involve a higher degree of risk than long-term senior lending secured by business assets or income producing real property because the investment may become unsecured as a result of foreclosure by a senior lender. In the event of a bankruptcy of the entity providing the pledge of its ownership interests as security, we may not have full recourse to the assets of such entity, or the assets of the entity may not be sufficient to repay our mezzanine loan. If a borrower defaults on our mezzanine loan or debt senior to our loan, or in the event of a borrower bankruptcy, our mezzanine loan will be satisfied only after the senior debt is repaid in full. As a result, we may not recover some or all of our investment. In addition, mezzanine loans may have higher loan to value ratios than conventional mortgage loans, resulting in less equity in the property and increasing the risk of loss of principal.

We also have investments in B Notes-mortgage loans that while secured by a first mortgage on a single large commercial property or group of related properties are subordinated to an “A Note” secured by the same first mortgage on the same collateral. As a result, if an issuer defaults, there may not be sufficient funds remaining for B Note holders. B Notes reflect similar credit risks to comparably rated commercial mortgage-backed securities. In addition, we invest, directly or indirectly, in pools of real estate properties or loans. Since each transaction is privately negotiated, these investments can vary in their structural characteristics and risks. For example, the rights of holders of B Notes to control the process following a borrower default may vary from transaction to transaction, while investments in pools of real estate properties or loans may be subject to varying contractual arrangements with third party co-investors in such pools. Further, B Notes typically are secured by a single property, and so reflect the risks associated with significant concentration. These investments also are less liquid than commercial mortgage-backed securities.

**Investment in non-investment grade loans may involve increased risk of loss.**

We have acquired and may continue to acquire in the future certain loans that do not conform to conventional loan criteria applied by traditional lenders and are not rated or are rated as non-investment grade (for example, for investments rated by Moody’s Investors Service, ratings lower than Baa3, and for Standard & Poor’s, BBB- or below). The non-investment grade ratings for these loans typically result from the overall leverage of the loans, the lack of a strong operating history for the properties or businesses underlying the loans, the borrowers’ credit history, the properties’ underlying cash flow or other factors. As a result, these loans have a higher risk of default and loss than conventional loans. Any loss we incur may reduce distributions to our stockholders. There are no limits on the percentage of unrated or non-investment grade assets we may hold in our portfolio.

**Insurance on real estate in which we have interests (including the real estate serving as collateral for our real estate securities and loans) may not cover all losses.**

There are certain types of losses, generally of a catastrophic nature, such as earthquakes, floods, hurricanes, terrorism or acts of war, that may be uninsurable or not economically insurable. Inflation, changes in building codes and ordinances, environmental considerations, and other factors, including terrorism or acts of war, also might make the insurance proceeds insufficient to repair or replace a property if it is damaged or destroyed. Under such circumstances, the insurance proceeds received might not be

adequate to restore our economic position with respect to the affected real property. As a result of the events of September 11, 2001, insurance companies have limited or excluded coverage for acts of terrorism in insurance policies. As a result, we may suffer losses from acts of terrorism that are not covered by insurance.

In addition, the mortgage loans that are secured by certain of the properties in which we have interests contain customary covenants, including covenants that require property insurance to be maintained in an amount equal to the replacement cost of the properties. There can be no assurance that the lenders under these mortgage loans will not take the position that exclusions from coverage for losses due to terrorist acts is a breach of a covenant which, if uncured, could allow the lenders to declare an event of default and accelerate repayment of the mortgage loans.

**Many of our investments are illiquid, and this lack of liquidity could significantly impede our ability to vary our portfolio in response to changes in economic and other conditions or to realize the value at which such investments are carried if we are required to dispose of them.**

The real estate properties that we own and operate and our other direct and indirect investments in real estate, real estate related and other assets are generally illiquid. In addition, the real estate securities that we purchase in connection with privately negotiated transactions are not registered under the relevant securities laws, resulting in a prohibition against their transfer, sale, pledge or other disposition except in a transaction that is exempt from the registration requirements of, or is otherwise in accordance with, those laws. In addition, there are no established trading markets for a majority of our investments. As a result, our ability to vary our portfolio in response to changes in economic and other conditions may be limited.

Our securities have historically been valued based primarily on third party quotations, which are subject to significant variability based on the liquidity and price transparency created by market trading activity. In the past, dislocation in the trading markets has reduced the trading for many real estate securities, resulting in less transparent prices for those securities. During such times, it is more difficult for us to sell many of our assets because, if we were to sell such assets, we would likely not have access to readily ascertainable market prices when establishing valuations of them. If we are required to liquidate all or a portion of our illiquid investments quickly, we may realize significantly less than the amount at which we have previously valued these investments.

**Interest rate fluctuations and shifts in the yield curve may cause losses.**

Interest rates are highly sensitive to many factors, including governmental monetary and tax policies, domestic and international economic and political considerations and other factors beyond our control. Our primary interest rate exposures relate to our real estate securities, loans, floating rate debt obligations and interest rate swaps. Changes in interest rates, including changes in expected interest rates or "yield curves," affect our business in a number of ways. Changes in the general level of interest rates can affect our net interest income, which is the difference between the interest income earned on our interest-earning assets and the interest expense incurred in connection with our interest-bearing liabilities and hedges. Changes in the level of interest rates also can affect, among other things, our ability to acquire real estate securities and loans at attractive prices, the value of our real estate securities, loans and derivatives and our ability to realize gains from the sale of such assets. In the past, we have utilized hedging transactions to protect our positions from interest rate fluctuations, but as a result of current market conditions we face significant obstacles to entering into new hedging transactions. As a result, we may not be able to protect new investments from interest rate fluctuations to the same degree as in the past, which could adversely affect our financial condition and results of operations. In the event of a significant rising interest rate environment and/or economic downturn, loan and collateral defaults may increase and result in credit losses that would adversely affect our liquidity and operating results.

Our ability to execute our business strategy, particularly the growth of our investment portfolio, depends to a significant degree on our ability to obtain additional capital. Our financing strategy is dependent on our ability to place the match funded debt we use to finance our investments at rates that provide a positive net spread. If spreads for such liabilities widen or if demand for such liabilities ceases to exist, then our ability to execute future financings will be severely restricted.

Interest rate changes may also impact our net book value as our real estate securities, real estate related and other loans and hedge derivatives are marked to market each quarter. Debt obligations are not marked to market. Generally, as interest rates increase, the value of our fixed rate securities decreases, which will decrease the book value of our equity.

Furthermore, shifts in the U.S. Treasury yield curve reflecting an increase in interest rates would also affect the yield required on our real estate securities and therefore their value. For example, increasing interest rates would reduce the value of the fixed rate assets we hold at the time because the higher yields required by increased interest rates result in lower market prices on existing fixed rate assets in order to adjust the yield upward to meet the market, and vice versa. This would have similar effects on our real estate securities portfolio and our financial position and operations to a change in interest rates generally.

**We have invested in RMBS collateralized by subprime mortgage loans, which are subject to increased risks.**

We have invested in RMBS backed by collateral pools of subprime residential mortgage loans. “Subprime” mortgage loans refer to mortgage loans that have been originated using underwriting standards that are less restrictive than the underwriting requirements used as standards for other first and junior lien mortgage loan purchase programs, such as the programs of FNMA and FHLMC. These lower standards include mortgage loans made to borrowers having imperfect or impaired credit histories (including outstanding judgments or prior bankruptcies), mortgage loans where the amount of the loan at origination is 80% or more of the value of the mortgage property, mortgage loans made to borrowers with low credit scores, mortgage loans made to borrowers who have other debt that represents a large portion of their income and mortgage loans made to borrowers whose income is not required to be disclosed or verified. Due to economic conditions, including increased interest rates and lower home prices, as well as aggressive lending practices, subprime mortgage loans have in recent periods experienced increased rates of delinquency, foreclosure, bankruptcy and loss, and they are likely to continue to experience delinquency, foreclosure, bankruptcy and loss rates that are higher, and that may be substantially higher, than those experienced by mortgage loans underwritten in a more traditional manner. Thus, because of the higher delinquency rates and losses associated with subprime mortgage loans, the performance of RMBS backed by subprime mortgage loans in which we have invested could be correspondingly adversely affected, which could adversely impact our results of operations, financial condition and business.

**The value of our RMBS may be adversely affected by deficiencies in servicing and foreclosure practices, as well as related delays in the foreclosure process.**

Allegations of deficiencies in servicing and foreclosure practices among several large sellers and servicers of residential mortgage loans that surfaced in 2010 raised various concerns relating to such practices, including the improper execution of the documents used in foreclosure proceedings (so-called “robo signing”), inadequate documentation of transfers and registrations of mortgages and assignments of loans, improper modifications of loans, violations of representations and warranties at the date of securitization and failure to enforce put-backs.

As a result of alleged deficiencies in foreclosure practices, a number of servicers temporarily suspended foreclosure proceedings beginning in the second half of 2010 while they evaluated their foreclosure practices. In late 2010, a group of state attorneys general and state bank and mortgage regulators representing nearly all 50 states and the District of Columbia, along with the U.S. Department of Justice and the Department of Housing and Urban Development, began an investigation into foreclosure practices of banks and servicers. The investigations and lawsuits by several state attorneys general led to a settlement agreement in early February 2012 with five of the nation’s largest banks, pursuant to which the banks agreed to pay more than \$25 billion to settle claims relating to improper foreclosure practices. The settlement does not prohibit the states, the federal government, individuals or investors in RMBS from pursuing additional actions against the banks and servicers in the future.

The integrity of the servicing and foreclosure processes are critical to the value of the mortgage loan portfolios underlying our RMBS, and our financial results could be adversely affected by deficiencies in the conduct of those processes. For example, delays in the foreclosure process that have resulted from investigations into improper servicing practices may adversely affect the values of, and our losses on, our non-Agency RMBS. Foreclosure delays may also increase the administrative expenses of the securitization trusts for the non-Agency RMBS, thereby reducing the amount of funds available for distribution to investors. In addition, the subordinate classes of securities issued by the securitization trusts may continue to receive interest payments while the defaulted loans remain in the trusts, rather than absorbing the default losses. This may reduce the amount of credit support available for the senior classes we own, thus possibly adversely affecting these securities. Additionally, a substantial portion of the \$25 billion settlement described above is intended to be a “credit” to the banks and servicers for principal write-downs or reductions they may make to certain mortgages underlying RMBS. There remains considerable uncertainty as to how these principal reductions will work and what effect they will have on the value of related RMBS; as a result, there can be no assurance that any such principal reductions will not adversely affect the value of certain of our RMBS.

While we believe that the sellers and servicers would be in violation of their servicing contracts to the extent that they have improperly serviced mortgage loans or improperly executed documents in foreclosure or bankruptcy proceedings, or do not comply with the terms of servicing contracts when deciding whether to apply principal reductions, it may be difficult, expensive, and time consuming for us to enforce our contractual rights. We continue to monitor and review the issues raised by the alleged improper foreclosure practices. While we cannot predict exactly how the servicing and foreclosure matters or the resulting litigation or settlement agreements will affect our business, there can be no assurance that these matters will not have an adverse impact on our results of operations and financial condition.

**We invest in senior housing properties, which are subject to various risks that could have a negative impact on our financial results.**

Subject to maintaining our qualification as a REIT, we intend to continue to purchase senior housing properties and engage third parties (including affiliates of our Manager) to manage the operations or lease the properties. The income we recognize from any senior housing properties that we engage third parties to manage would be dependent on the ability of the property manager(s) of such facilities to successfully manage these properties. The property manager(s) would compete with other companies on a number of different levels, including: the quality of care provided, reputation, the physical appearance of a facility, price and range of services offered, alternatives for healthcare delivery, the supply of competing properties, physicians, staff, referral sources, location, the size and demographics of the population in surrounding areas, and the financial condition of tenants and managers. A property manager's inability to successfully compete with other companies on one or more of the foregoing levels could adversely affect the senior housing property and materially reduce the income we would receive from an investment in such facility.

As a result of any new investment in senior housing properties, we may be required to consolidate additional entities, and, therefore, to document and test effective internal controls over the financial reporting of these entities in accordance with Section 404, which we may not be able to do. Even if we are able to do so, there could be significant costs and delays, particularly if these entities were not subject to Section 404 prior to being acquired by us. Under certain circumstances, the SEC permits newly acquired businesses to be excluded for a limited period of time from management's annual assessment of the effectiveness of internal controls. We temporarily excluded the senior housing properties acquired in 2013 from management's annual assessment of the effectiveness of internal control in 2013 pursuant to a one-year deferral permissible under PCAOB and SEC guidelines and may avail ourselves of this flexibility with respect to any newly acquired business. If we are not able to maintain or document effective internal control over financial reporting, our independent registered public accounting firm would not be able to certify as to the effectiveness of our internal control over financial reporting as of the required dates, which could subject us to adverse regulatory consequences, including sanctions or investigations by the SEC, or violations of applicable stock exchange listing rules. There could also be a negative reaction in the financial markets due to a loss of investor confidence in us and the reliability of our financial statements, which could lead to a decline in our share price, impair our ability to raise capital and other adverse consequences.

In addition, private, federal and state payment programs as well as the effect of laws and regulations may also have a significant impact on the profitability of such facilities. The failure of a manager to comply with any of these laws could result in the loss of accreditation, denial of reimbursement, imposition of fines, suspension or decertification from federal and state healthcare programs, loss of license or closure of the property. These events, among others, could result in the loss of part or all of any investment we make in a senior housing property.

Furthermore, the ability to successfully manage a senior housing property depends on occupancy levels. A material decline in occupancy levels and revenues may make it more difficult for the manager of any senior housing property in which we invest to successfully generate income for us. Alternatively, to avoid a decline in occupancy, a manager may reduce the rates charged, which would also reduce our revenues and therefore negatively impact the ability to generate income.

Our ability to acquire senior housing properties will be subject to the applicable REIT qualification tests, and we may have to hold certain interests through taxable REIT subsidiaries ("TRS"), which may negatively impact our returns from these assets.

**We are not permitted to operate our AL/MC properties, and we are dependent on the property managers of our AL/MC properties and on tenants for our triple net lease properties.**

Because federal income tax laws generally restrict REITs and their pass-through subsidiaries from operating healthcare properties, we do not manage our AL/MC senior housing properties. Instead, AL/MC investments are structured to be compliant with the REIT Investment Diversification Empowerment Act of 2007 ("RIDEA").

The RIDEA structure permits a REIT to lease facilities to a subsidiary that qualifies as a taxable REIT subsidiary ("TRS") if the TRS hires an eligible independent contractor ("EIK") to manage the property. Under this structure, the REIT leases health care properties to the TRS and receives rent while the TRS earns income from the properties' operations, and pays a management fee to the EIK and rent to the REIT property owner.

Accordingly, our TRS has retained Blue Harbor and Holiday to manage facilities that are leased to it by us. Although we have various rights as the tenant under our management agreements, we rely upon our property managers' personnel, expertise, technical resources and information systems, proprietary information, good faith and judgment to manage our senior housing operations

efficiently and effectively. We also rely on our property managers to provide accurate property- level financial results for our properties in a timely manner and to otherwise operate our facilities in compliance with the terms of our management agreements and all applicable laws and regulations. We rely on Holiday and Blue Harbor to attract and retain skilled management personnel and property level personnel who are responsible for the day-to-day operations of our facilities. Increases in labor costs and other property operating expenses, or significant changes in Holiday's or Blue Harbor's ability to manage our facilities efficiently and effectively could adversely affect the income we receive from our facilities and have a material adverse effect on us. As managers, our property managers do not lease our facilities, and, therefore, we are not directly exposed to their credit risk in the same manner or to the same extent as our triple net tenants. However, any adverse developments in Holiday's or Blue Harbor's business and affairs or financial condition could impair its ability to manage our properties efficiently and effectively and could have a material adverse effect on us.

While we monitor our property managers' and tenants' performance, we have limited recourse under our management agreements if we believe that the property managers or tenants are not performing adequately. In addition, our property managers or tenants may manage, own or invest in, properties that compete with our properties, which may result in conflicts of interest. As a result, our property managers or tenants may make decisions regarding competing properties that are not in our best interests.

The triple net lease structure also provides us with a REIT-eligible structure for owning health care facilities. The triple net lease structure permits a REIT to lease facilities to a third-party operator and collect rent from the operator. Unlike the RIDEA structure, the triple net lease structure creates credit risk from the tenant.

**Our triple net leases generate a meaningful portion of our revenues and operating income, and any failure, inability or unwillingness by our tenants to satisfy their obligations to us could adversely affect us.**

The properties that we own under triple net lease arrangements account for a meaningful portion of our total revenues and net operating income from our senior housing business. Under a triple net lease, we depend on the tenant to pay all insurance, taxes, utilities and maintenance and repair expenses in connection with the leased properties. We currently have two tenants, Holiday and Life Care Companies LLC ("LCS"). We cannot assure you that our tenants will have sufficient assets, income and access to financing to enable them to satisfy their respective obligations to us, and any failure, inability or unwillingness by our tenants to do so could have a material adverse effect on us. In addition, any failure by our tenants to effectively conduct its operations or to maintain and improve our properties could adversely affect its business reputation and its ability to attract and retain patients and residents in our properties, which could have a material adverse effect on us. In addition, although subsidiaries of Holiday and LCS provided a lease guaranty in connection with their respective leases and have agreed to indemnify, defend and hold us harmless from and against various claims, litigation and liabilities arising in connection with their respective businesses, we cannot assure you that the guaranties will be sufficient to satisfy their respective obligations to us and we cannot assure you that Holiday or LCS will have sufficient assets, income, access to financing and insurance coverage to enable them to satisfy their respective obligations to us.

**If we must replace any of our tenants, we might be unable to reposition the properties on as favorable terms, or at all, and we could be subject to delays, limitations and expenses, which could have a material adverse effect on us.**

If we exercise our right to replace a tenant in default, rental payments on the related properties could decline or cease altogether while we reposition the properties with a suitable replacement tenant. We also might not be successful in identifying suitable replacements or entering into leases or other arrangements with new tenants on a timely basis or on terms as favorable to us as our current leases, if at all, and we may be required to fund certain expenses and obligations (e.g. real estate taxes, debt costs and maintenance expenses) to preserve the value of, and avoid the imposition of liens on, our properties while they are being repositioned. In addition, we may incur certain obligations and liabilities, including obligations to indemnify the replacement tenant, which could have a material adverse effect on us.

In the event of a tenant default, our ability to reposition our properties with a suitable replacement tenant or operator could be significantly delayed or limited by state licensing, receivership, CON or other laws, as well as by the Medicare or Medicaid change-of-ownership proceedings. Any such delays, limitations and expenses could adversely impact our ability to collect rent, obtain possession of leased properties or otherwise exercise remedies for tenant default and could have a material adverse effect on us.

**Due to the dependency of our senior housing revenues on private pay sources, events which adversely affect the ability of seniors to afford the monthly resident fees could cause our occupancy rates, revenues and results of operations to decline.**

Costs to seniors associated with independent and certain assisted living services are not generally reimbursable under government reimbursement programs such as Medicaid. Economic downturns, softness in the housing market, higher levels of unemployment among resident family members, lower levels of consumer confidence, changes to social security benefits, stock market

volatility, interest rate volatility, adverse changes to fixed income arrangements and/or changes in demographics could adversely affect the ability of seniors to afford our resident fees. If we are unable to retain and/or attract seniors with sufficient income, assets or other resources required to pay the fees associated with independent and assisted living services and other service offerings, our occupancy rates, revenues and results of operations could decline.

**Increases in labor costs at our senior housing properties may have a material adverse effect on us.**

Wages and employee benefits represent a significant part of the expenses of any senior housing property. In connection with our RIDEA, AL/MC properties and in connection with our IL-only properties that are managed by our property managers, we rely on our property managers to attract and retain skilled management personnel and property level personnel who are responsible for the day-to-day operations of our facilities.

The market for qualified nurses and healthcare professionals is highly competitive. Periodic and geographic area shortages of nurses or other trained personnel may require our property managers to increase the wages and benefits offered to its employees in order to attract and retain these personnel or to hire more expensive temporary personnel. Also, our property managers may have to compete with numerous other employers for lesser skilled workers.

As we acquire additional facilities, we may be required to pay increased compensation or offer other incentives to retain key personnel and other employees. Employee benefits costs, including employee health insurance and workers' compensation insurance costs, have materially increased in recent years. Increasing employee health and workers' compensation insurance costs may materially and negatively affect our earnings at our senior housing properties. We cannot assure you that labor costs at our senior housing properties will not increase or that any increase will be matched by corresponding increases in rates charged to residents. Any significant failure by our property managers to control labor costs or to pass on any such increased labor costs to residents through rate increases could have a material adverse effect on our business, financial condition and results of operations. In addition, if the Master Tenants of the Holiday Portfolio fail to attract and retain qualified personnel, their ability to satisfy their obligations to us could be impaired.

**Termination of assisted living resident agreements and resident attrition could adversely affect our revenues and earnings at our senior housing properties.**

State regulations governing assisted living facilities typically require a written resident agreement with each resident. Most of these regulations also require that each resident have the right to terminate these assisted living resident agreements for any reason on reasonable notice. Consistent with these regulations, most resident agreements at our senior housing properties allow residents to terminate their agreements on 30 days' notice. Thus, our property managers may be unable to contract with assisted living residents to stay for longer periods of time, unlike typical apartment leasing arrangements that involve lease agreements with terms of up to a year or longer. If a large number of residents elected to terminate their resident agreements at or around the same time, our revenues and earnings from our assisted living facilities could be materially and adversely affected. In addition, the advanced ages of the residents at our senior housing properties makes the resident turnover rate in these facilities difficult to predict.

**Our property managers and tenants (including the Master Tenants) may be faced with significant potential litigation and rising insurance costs that not only affect their ability to obtain and maintain adequate liability and other insurance, but also may affect their ability to pay their lease payments and fulfill their insurance and indemnification obligations to us.**

In some states, advocacy groups monitor the quality of care at assisted and independent living communities, and these groups have brought litigation against operators. Also, in several instances, private litigation by assisted and independent living community residents or their families have succeeded in winning very large damage awards for alleged neglect. The effect of this litigation and potential litigation has been to materially increase the costs of monitoring and reporting quality of care compliance. The cost of liability and medical malpractice insurance has increased and may continue to increase so long as the present litigation environment in many parts of the United States continues. This may affect the ability of some of our property managers and tenants (including the Master Tenants) to obtain and maintain adequate liability and other insurance and manage their related risk exposures. In addition to causing some of our property managers and tenants (including the Master Tenants) to be unable to fulfill their insurance, indemnification and other obligations to us under their property management agreements or leases and thereby potentially exposing us to those risks, these litigation risks and costs could cause some of our property managers and future tenants to become unable to pay rents due to us. Such nonpayment could potentially affect our ability to meet future monetary obligations under our financing arrangements.

**The failure of our property managers and tenants (including the Master Tenants) to comply with laws relating to the operation of our property managers' and tenants' (including the Master Tenants') facilities may have a material adverse effect on the ability of our tenants (including the Master Tenants) to pay us rent, the profitability of our managed facilities and the values of our properties.**

We and our property managers and tenants (including the Master Tenants) are subject to or impacted by extensive, frequently changing federal, state and local laws and regulations. Some of these laws and regulations include: state and local licensure laws; laws protecting consumers against deceptive practices; laws relating to the operation of our properties and how our property managers and tenants (including the Master Tenants) conduct their operations, such as fire, health and safety laws and privacy laws; federal and state laws affecting communities that participate in Medicaid; the Americans with Disabilities Act and similar state and local laws; and safety and health standards set by the Occupational Safety and Health Administration. We and our property managers and tenants (including the Master Tenants) expend significant resources to maintain compliance with these laws and regulations, and responding to any allegations of noncompliance also results in the expenditure of significant resources. If we or our property managers or tenants (including the Master Tenants) fail to comply with any applicable legal requirements, or are unable to cure deficiencies, certain sanctions may be imposed and, if imposed, may adversely affect our tenants' (including the Master Tenants') ability to pay their rent, the profitability of affected facilities managed by our property managers and the values of our properties. Further, changes in the regulatory framework could have a material adverse effect on the ability of our tenants (including the Master Tenants) to pay us rent (and any such nonpayment could potentially affect our ability to meet future monetary obligations under our financing arrangements), the profitability of our facilities managed by our property managers and the values of our properties.

We and our property managers and our tenants (including the Master Tenants) are required to comply with federal and state laws governing the privacy, security, use and disclosure of individually identifiable information, including financial information and protected health information. Under the federal Health Insurance Portability and Accountability Act of 1996 ("HIPAA"), we and our property managers and tenants (including the Master Tenants) are required to comply with the HIPAA privacy rule, security standards, and standards for electronic healthcare transactions. State laws also govern the privacy of individual health information, and these laws are, in some jurisdictions, more stringent than HIPAA. Other federal and state laws govern the privacy of individually identifiable information. If we or our property managers or tenants (including the Master Tenants) fail to comply with applicable federal or state standards, we or they could be subject to civil sanctions and criminal penalties, which could materially and adversely affect our business, financial condition and results of operations.

**Our properties and their operations are subject to extensive regulations.**

Various governmental authorities mandate certain physical characteristics of senior housing properties. Changes in laws and regulations relating to these matters may require significant expenditures. Our property management agreements and leases generally require our managers and tenants to maintain our properties in compliance with applicable laws and regulations, and we expend resources to monitor their compliance. However, our property managers and tenants (including the Master Tenants) may neglect maintenance of our properties if they suffer financial distress. We may agree to fund capital expenditures in return for rent increases or other concessions. Our available financial resources or those of our property managers and tenants (including the Master Tenants) may be insufficient to fund the expenditures required to operate our properties in accordance with applicable laws and regulations. If we fund these expenditures, our tenants' (including the Master Tenants') financial resources may be insufficient to satisfy their increased rental payments to us or other incremental obligations.

Licensing and Medicaid laws may also require some or all of our senior housing property managers and tenants to comply with extensive standards governing their operations. In addition, certain laws prohibit fraud by senior housing operators and other healthcare communities, including civil and criminal laws that prohibit false claims in, Medicaid, Medicare and other programs and that regulate patient referrals. In recent years, the federal and state governments have devoted increasing resources to monitoring the quality of care at senior housing communities and to anti-fraud investigations in healthcare operations generally. When violations of applicable laws are identified, federal or state authorities may impose civil monetary damages, treble damages, repayment requirements and criminal sanctions. Healthcare communities may also be subject to license revocation or conditional licensure and exclusion from Medicaid or Medicare participation or conditional participation. When quality of care deficiencies or improper billing are identified, various laws may authorize civil money penalties or fines; the suspension, modification, or revocation of a license or Medicaid or Medicare participation; the suspension or denial of admissions of residents; the denial of payments in full or in part; the implementation of state oversight, temporary management or receivership; and the imposition of criminal penalties. We, our property managers and our future tenants (including the Master Tenants) may receive notices of potential sanctions from time to time, and governmental authorities may impose such sanctions from time to time on our facilities. If our property managers and future tenants (including the Master Tenants) are unable to cure deficiencies which have been identified or which are identified in the future, these sanctions may be imposed, and if imposed, may adversely affect our future

tenants' (including the Master Tenants') ability to pay rents to us (and any such nonpayment could potentially affect our ability to meet future monetary obligations under our financing arrangements), and our ability to identify substitute property managers or tenants. Federal and state requirements for change in control of healthcare communities, including, as applicable, approvals of the proposed operator for licensure, certificate of need and Medicaid or Medicare participation, may also limit or delay our ability to find substitute tenants or property managers. If any of our property managers or future tenants (including the Master Tenants) becomes unable to operate our properties, or if any of our future tenants becomes unable to pay its rent because it has violated government regulations or payment laws, we may experience difficulty in finding a substitute tenant or property manager or selling the affected property for a fair and commercially reasonable price, and the value of an affected property may decline materially.

Our golf business is also subject to extensive regulations, including, without limitation, labor, health and safety, environmental, zoning and land-use laws. For more information, see "Business-Government Regulation of Our Golf Business."

**Changes in reimbursement rates or methods of payment from government and other third-party payors, including Medicaid and Medicare, could have a material adverse effect on certain our tenants and us.**

Certain of our tenants and our Managers rely on reimbursement from third-party payors, including the Medicare and Medicaid programs. Medicare and Medicaid programs, as well as numerous private insurance and managed care plans, generally require participating providers to accept government-determined reimbursement levels as payment in full for services rendered, without regard to the facility's charges. Changes in the reimbursement rate or methods of payment from third-party payors, including Medicare and Medicaid, or the implementation of other measures to reduce reimbursements for services provided by our managers or our tenants, could result in a substantial reduction in our and our tenant's revenues. In addition, the implementation of the Resource Utilization Group, Version Four, or "RUG-IV", which revises the payment classification system for skilled nursing facilities, may impact our tenants by revising the classifications of certain patients. The federal reimbursement for certain facilities, such as skilled nursing facilities, incorporates adjustments to account for facility case-mix. Additionally, revenue under third-party payor agreements can change after examination and retroactive adjustment by payors during the claims settlement processes or as a result of post-payment audits. Payors may disallow requests for reimbursement based on determinations that certain costs are not reimbursable or reasonable or because additional documentation is necessary or because certain services were not covered or were not medically necessary. We cannot assure you that our tenants or our Managers who currently depend on governmental or private payor reimbursement will be adequately reimbursed for the services they provide. Significant limits by governmental and private third-party payors on the scope of services reimbursed or on reimbursement rates and fees, whether from legislation, administrative actions or private payor efforts, could have a material adverse effect on liquidity, financial condition and results of operations, which could affect adversely their ability to comply with the terms of our leases and have a material adverse effect on us.

**Our acquisitions of senior housing properties may not be successful.**

We intend to acquire additional senior housing properties. We cannot assure that we will be able to consummate attractive acquisition opportunities or that acquisitions we make will be successful. We might encounter unanticipated difficulties and expenditures relating to any acquired properties. Newly acquired properties might require significant management attention. We might never realize the anticipated benefits of our acquisitions. Notwithstanding pre-acquisition due diligence, we do not believe that it is possible to fully understand a property before it is owned and operated for an extended period of time. For example, we could acquire a property that contains undisclosed defects in design or construction. In addition, after our acquisition of a property, the market in which the acquired property is located may experience unexpected changes that adversely affect the property's value. The occupancy of properties that we acquire may decline during our ownership, and rents or returns that are in effect or expected at the time a property is acquired may decline thereafter. Also, our property operating costs for acquisitions may be higher than we anticipate and acquisitions of properties may not yield the returns we expect and, if financed using debt or new equity issuances, may result in stockholder dilution. For these reasons, among others, any acquisitions of additional properties may not succeed or may cause us to experience losses.

**Competition may affect our senior housing property managers' and tenant operators' ability to meet their obligations to us or make it difficult for us to identify and purchase, or develop, suitable senior housing properties to grow our investment portfolio.**

We face significant competition from other REITs, investment companies, private equity and hedge fund investors, sovereign funds, healthcare operators, lenders, developers and other institutional investors, some of whom may have greater resources and lower costs of capital than we do. Increased competition makes it more challenging for us to identify and successfully capitalize on opportunities that meet our business goals and could improve the bargaining power of property owners seeking to sell, thereby impeding our investment, acquisition and development activities. If we cannot identify and purchase a sufficient quantity of senior

housing properties at favorable prices or if we are unable to finance acquisitions on commercially favorable terms, it could have a material adverse effect on our business, financial condition and results of operations.

The healthcare industry is also highly competitive, and our operators, tenants and managers may encounter increased competition for residents and patients, including with respect to the scope and quality of care and services provided, reputation and financial condition, physical appearance of the properties, price and location. The operations of our AL/MC, RIDEA properties and our IL-only owned and managed properties depend on the competitiveness and financial viability of the facilities. If our managers are unable to successfully compete with other operators and managers by maintaining profitable occupancy and rate levels, their ability to generate income for us may be materially adversely affected. The operations of our triple net lease tenants also depend upon their ability to successfully compete with other operators and managers. If our tenants are unable to successfully compete, their ability to fulfill their obligations to us, including the ability to make rent payments to us, may be materially adversely affected. We cannot assure you that future changes in government regulation will not adversely affect the healthcare industry, including our seniors housing and healthcare operations, tenants and operators, nor can we be certain that our tenants, operators and managers will achieve and maintain occupancy and rate levels that will enable them to satisfy their obligations to us. Any adverse changes in the regulation of the healthcare industry or the competitiveness of our tenants, operators and managers could have a more pronounced effect on us than if we had investments outside the seniors housing and healthcare industries.

**Our tenant operators (including the Master Tenants) may become subject to bankruptcy or insolvency proceedings.**

Our tenant operators (including the Master Tenants) may not be able to meet the rent or other payments due us, which may result in a tenant bankruptcy or insolvency, or that a tenant might become subject to bankruptcy or insolvency proceedings for other reasons. Although our operating lease agreements provide us with the right to evict tenant operators, demand immediate payment of rent and exercise other remedies, the bankruptcy and insolvency laws afford certain rights to a party that has filed for bankruptcy or reorganization. A tenant in bankruptcy or subject to insolvency proceedings may be able to limit or delay our ability to collect unpaid rent and to exercise other rights and remedies.

We may be required to fund certain expenses (e.g., real estate taxes and maintenance) to preserve the value of an investment property, avoid the imposition of liens on a property and/or transition a property to a new tenant. If we cannot transition a leased property to a new tenant, we may take possession of that property, which may expose us to certain successor liabilities. Should such events occur, our revenue and operating cash flow may be adversely affected.

**Transfers of health care facilities may require regulatory approvals and these facilities may not have efficient alternative uses.**

Transfers of health care facilities to successor operators frequently are subject to regulatory approvals or notifications, including, but not limited to, change of ownership approvals under certificate of need ("CON") or determination of need laws, state licensure laws and Medicaid provider arrangements, that are not required for transfers of other types of real estate. The replacement of a health care facility operator could be delayed by the approval process of any federal, state or local agency necessary for the transfer of the facility or the replacement of the operator licensed to manage the facility. Alternatively, given the specialized nature of our facilities, we may be required to spend substantial time and funds to adapt these properties to other uses. If we are unable to timely transfer properties to successor operators or find efficient alternative uses, our revenue and operations may be adversely affected.

**Certain of our properties may require a license or registration to operate.**

Failure to obtain a license or registration or loss of a required license or registration would prevent a facility from operating in the manner intended by the property managers or tenant operators. These events could materially adversely affect our property managers' ability to generate income for us or our tenant operators' ability to make rent payments to us. State and local laws also may regulate the expansion, including the addition of new beds or services or acquisition of medical equipment, and the construction or renovation of health care facilities, by requiring a CON or other similar approval from a state agency.

**The impact of the comprehensive healthcare regulation enacted in 2010 on us and our property managers and tenant operators cannot accurately be predicted.**

The Health Reform Laws provide states with an increased federal medical assistance percentage under certain conditions. On June 28, 2012, The United States Supreme Court upheld the individual mandate of the Health Reform Laws but partially invalidated the expansion of Medicaid. The ruling on Medicaid expansion will allow states not to participate in the expansion-and to forego funding for the Medicaid expansion-without losing their existing Medicaid funding. Given that the federal government substantially funds the Medicaid expansion, it is unclear whether any state will pursue this option, although at least some appear to be considering

this option at this time. The participation by states in the Medicaid expansion could have the dual effect of increasing our property managers' and tenant operators' revenues, through new patients, but further straining state budgets. While the federal government will pay for approximately 100% of those additional costs from 2014 to 2016, states will be expected to begin paying for part of those additional costs in 2017. With increasingly strained budgets, it is unclear how states will pay their share of these additional Medicaid costs and what other health care expenditures could be reduced as a result. A significant reduction in other health care related spending by states to pay for increased Medicaid costs could affect our property managers' and tenant operators' revenue streams, which could materially and adversely affect our business, financial condition and results of operations.

**Overbuilding in markets in which our senior housing properties are located could adversely affect our future occupancy rates, operating margins and profitability.**

The senior housing industry generally has limited barriers to entry, and, as a consequence, the development of new senior housing properties could outpace demand. If development outpaces demand for those asset types in the markets in which our properties are located, those markets may become saturated and we could experience decreased occupancy, reduced operating margins and lower profitability.

**The geographic concentration of our senior housing properties in Florida and Texas may result in losses due to our significant exposure to the effects of economic and real estate conditions in those markets.**

As of June 30, 2014, approximately 22.5% and 20.6% of the beds in our senior housing portfolios are located in Florida and Texas, respectively. As a result of this concentration, a material portion of our portfolios are significantly exposed to the effects of economic and real estate conditions in those particular markets, such as the supply of competing properties, home prices, income levels, the financial condition of our tenants, and general levels of employment and economic activity. To the extent that weak economic or real estate conditions affect Florida or Texas more severely than other areas of the country, our financial performance could be negatively impacted.

**We rely on information technology in our operations, and any material failure, inadequacy, interruption or security failure of that technology could harm our business.**

We rely on information technology networks and systems, including the Internet, to process, transmit and store electronic information and to manage or support a variety of our business processes, including financial transactions and maintenance of records, which in the case of our senior housing and golf businesses, may include personal identifying information. We rely on commercially available systems, software, tools and monitoring to provide security for processing, transmitting and storing this confidential information, such as individually identifiable information relating to financial accounts. Although we have taken steps to protect the security of the data maintained in our information systems, it is possible that our security measures will not be able to prevent the systems' improper functioning, or the improper disclosure of personally identifiable information such as in the event of cyber attacks. Security breaches, including physical or electronic break-ins, computer viruses, attacks by hackers and similar breaches, can create system disruptions, shutdowns or unauthorized disclosure of confidential information. Any failure to maintain proper function, security and availability of our information systems could interrupt our operations, damage our reputation, subject us to liability claims or regulatory penalties and could materially and adversely affect our business, financial condition and results of operations.

**Our investments in debt securities and loans are subject to changes in credit spreads, which could adversely affect our ability to realize gains on the sale of such investments.**

Debt securities and loans are subject to changes in credit spreads. Credit spreads measure the yield demanded on securities and loans by the market based on their credit relative to a specific benchmark.

Fixed rate securities and loans are valued based on a market credit spread over the rate payable on fixed rate U.S. Treasuries of like maturity. Floating rate securities and loans are valued based on a market credit spread over LIBOR and are affected similarly by changes in LIBOR spreads. Excessive supply of these securities combined with reduced demand will generally cause the market to require a higher yield on these securities and loans, resulting in the use of a higher, or "wider," spread over the benchmark rate to value such securities. Under such conditions, the value of our debt securities and loan portfolios would tend to decline. Conversely, if the spread used to value such securities were to decrease, or "tighten," the value of our debt securities portfolio would tend to increase. Such changes in the market value of our debt securities and loan portfolios may affect our net equity, net income or cash flow directly through their impact on unrealized gains or losses on available-for-sale securities, and therefore our ability to realize gains on such securities, or indirectly through their impact on our ability to borrow and access capital. During 2008 through the first quarter of 2009, credit spreads widened substantially. This widening of credit spreads caused the net

unrealized gains on our securities, loans and derivatives, recorded in accumulated other comprehensive income or retained earnings, and therefore our book value per share, to decrease and resulted in net losses.

In addition, if the value of our loans subject to financing agreements were to decline, it could affect our ability to refinance such loans upon the maturity of the related repurchase agreements. Any credit or spread related losses incurred with respect to our loans would affect us in the same way as similar losses on our real estate securities portfolio as described above.

**Any hedging transactions that we enter into may limit our gains or result in losses.**

We have used (and may continue to use, when feasible and appropriate) derivatives to hedge a portion of our interest rate exposure, and this approach has certain risks, including the risk that losses on a hedge position will reduce the cash available for distribution to stockholders and that such losses may exceed the amount invested in such instruments. We have adopted a general policy with respect to the use of derivatives, which generally allows us to use derivatives where appropriate, but does not set forth specific policies and procedures or require that we hedge any specific amount of risk. From time to time, we use derivative instruments, including forwards, futures, swaps and options, in our risk management strategy to limit the effects of changes in interest rates on our operations. A hedge may not be effective in eliminating all of the risks inherent in any particular position. Our profitability may be adversely affected during any period as a result of the use of derivatives.

There are limits to the ability of any hedging strategy to protect us completely against interest rate risks. When rates change, we expect the gain or loss on derivatives to be offset by a related but inverse change in the value of the items, generally our liabilities, that we hedge. We cannot assure you, however, that our use of derivatives will offset the risks related to changes in interest rates. We cannot assure you that our hedging strategy and the derivatives that we use will adequately offset the risk of interest rate volatility or that our hedging transactions will not result in losses. In addition, our hedging strategy may limit our flexibility by causing us to refrain from taking certain actions that would be potentially profitable but would cause adverse consequences under the terms of our hedging arrangements.

The REIT provisions of the Internal Revenue Code of 1986, as amended (the "Code"), limit our ability to hedge. In managing our hedge instruments, we consider the effect of the expected hedging income on the REIT qualification tests that limit the amount of gross income that a REIT may receive from hedging. We need to carefully monitor, and may have to limit, our hedging strategy to assure that we do not realize hedging income, or hold hedges having a value, in excess of the amounts that would cause us to fail the REIT gross income and asset tests. In addition, our ability to hedge is limited by certain undertakings that we made to the U.S. Commodity Futures Trading Commission in order to avail ourselves of no-action relief from the requirement to register as a commodity pool operator.

Accounting for derivatives under U.S. generally accepted accounting principles ("GAAP"), is extremely complicated. Any failure by us to account for our derivatives properly in accordance with GAAP in our financial statements could adversely affect our earnings.

**Under certain conditions, increases in prepayment rates can adversely affect yields on many of our investments.**

The value of many of the assets in which we invest may be affected by prepayment rates on these assets. Prepayment rates are influenced by changes in current interest rates and a variety of economic, geographic and other factors beyond our control, and consequently, prepayment rates cannot be predicted with certainty. In periods of declining mortgage interest rates, prepayments on loans generally increase. If general interest rates decline as well, the proceeds of such prepayments received during such periods are likely to be reinvested by us in assets yielding less than the yields on the assets that were prepaid. In addition, the market value of floating rate assets may, because of the risk of prepayment, benefit less than fixed rate assets from declining interest rates. Conversely, in periods of rising interest rates, prepayments on loans generally decrease, in which case we would not have the prepayment proceeds available to invest in assets with higher yields. Under certain interest rate and prepayment scenarios we may fail to recoup fully our cost of acquisition of certain investments.

In addition, when market conditions lead us to increase the portion of our CDO investments that are comprised of floating rate securities, the risk of assets inside our CDOs prepaying increases. Since our CDO financing costs are locked in, reinvestment of such prepayment proceeds at lower yields than the initial investments, as a result of changes in the interest rate or credit spread environment, will result in a decrease of the return on our equity and therefore our net income.

**Changes in accounting rules could occur at any time and could impact us in significantly negative ways that we are unable to predict or protect against.**

As has been widely publicized, the SEC, the Financial Accounting Standards Board and other regulatory bodies that establish the accounting rules applicable to us have recently proposed or enacted a wide array of changes to accounting rules. Moreover, in the future these regulators may propose additional changes that we do not currently anticipate. Changes to accounting rules that apply to us could significantly impact our business or our reported financial performance in negative ways that we cannot predict or protect against. We cannot predict whether any changes to current accounting rules will occur or what impact any codified changes will have on our business, results of operations, liquidity or financial condition.

**Failure to maintain effective internal control over financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act could have a material adverse effect on our business and stock price.**

As a public company, we are required to maintain effective internal control over financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act of 2002. Internal control over financial reporting is complex and may be revised over time to adapt to changes in our business, or changes in applicable accounting rules. In connection with new investments, we may be required to consolidate additional entities, and, therefore, to document and test effective internal controls over the financial reporting of these entities in accordance with Section 404, which we may not be able to do. Even if we are able to do so, there could be significant costs and delays, particularly if these entities were not subject to Section 404 prior to being acquired by us. Under certain circumstances, the SEC permits newly acquired businesses to be excluded for a limited period of time from management's annual assessment of the effectiveness of internal control. We have excluded certain assets from management's annual assessment of the effectiveness of internal control in 2013 pursuant to a one-year deferral permissible under PCAOB and SEC guidelines, and we may avail ourselves of this flexibility in the future with respect to other newly acquired businesses. Our management identified a material weakness in our internal controls with respect to our financial statements for the year ended December 31, 2011. Although this was remediated, we cannot assure you that our internal control over financial reporting will be effective in the future or that a material weakness will not be discovered with respect to a prior period for which we believe that internal controls were effective. If we are not able to maintain or document effective internal control over financial reporting, our independent registered public accounting firm may not be able to certify as to the effectiveness of our internal control over financial reporting as of the required dates. Matters impacting our internal controls may cause us to be unable to report our financial information on a timely basis, or may cause us to restate previously issued financial information, and thereby subject us to adverse regulatory consequences, including sanctions or investigations by the SEC, or violations of applicable stock exchange listing rules. There could also be a negative reaction in the financial markets due to a loss of investor confidence in us and the reliability of our financial statements. Confidence in the reliability of our financial statements is also likely to suffer if we or our independent registered public accounting firm reports a material weakness in our internal control over financial reporting. This could materially adversely affect us by, for example, leading to a decline in our share price and impairing our ability to raise capital.

**Environmental compliance costs and liabilities related to real estate that we own, or in which we have interests, may adversely affect our results of operations.**

Our operating costs may be affected by the cost of complying with existing or future environmental laws, ordinances and regulations with respect to the properties, or loans secured by such properties, or by environmental problems that materially impair the value of such properties. Under various federal, state and local environmental laws, ordinances and regulations, a current or previous owner or operator of real property may be liable for the costs of removal or remediation of hazardous or toxic substances on, under, or in such property. Such laws often impose liability whether or not the owner or operator knew of, or was responsible for, the presence of such hazardous or toxic substances. In addition, the presence of hazardous or toxic substances, or the failure to remediate properly, may adversely affect the owner's ability to borrow using such real property as collateral. Certain environmental laws and common law principles could be used to impose liability for releases of hazardous materials, including asbestos-containing materials, into the environment, and third parties may seek recovery from owners or operators of real properties for personal injury associated with exposure to released asbestos-containing materials or other hazardous materials. Environmental laws may also impose restrictions on the manner in which a property may be used or transferred or in which businesses it may be operated, and these restrictions may require expenditures. In connection with the direct or indirect ownership and operation of properties, we may be potentially liable for any such costs. The cost of defending against claims of liability or remediating contaminated property and the cost of complying with environmental laws could adversely affect our results of operations and financial condition.

**Lawsuits, investigations and indemnification claims could result in significant liabilities and reputational harm, which could materially adversely affect our results of operations, financial condition and liquidity.**

From time to time, we may be involved in lawsuits or investigations or receive claims for indemnification. Our efforts to resolve any such lawsuits, investigations or claims could be very expensive and highly damaging to our reputation, even if the underlying claims are without merit. We could potentially be found liable for significant damages or indemnification obligations. Such developments could have a material adverse effect on our business, results of operations and financial condition.

Our risk of litigation includes lawsuits that could be brought by residents of our senior housing properties, users of our golf courses or property-level employees in our senior housing and golf businesses. For instance, we are subject to federal and state laws governing minimum wage requirements, overtime compensation, discrimination and family and medical leave. Any lawsuit alleging a violation of any such laws could result in a settlement or other resolution that requires us to make a substantial payment, which could have a material adverse effect on our financial condition and results of operations. In addition, accidents or injuries in connection with our senior housing or golf properties could subject us to liability and reputational harm.

**We have invested in operating businesses in distressed industries, such as golf, and such investments are subject to operational and other business risks.**

We opportunistically pursue a variety of investments, such as our recent restructuring of a debt investment in National Golf and, as a consequence, we are subject to risks of the industries in which we may invest, which may include non-real estate related operating businesses in distressed industries. These investments are subject to the risks of the industry in which such business(es) operate, and we expect any businesses we acquire to be subject to similar issues and risks. Businesses operating in distressed industries can face declining revenues, profitability, margins, customer base, product acceptance and growth prospects as well as concerns regarding increased fixed costs, lack of available financing or lack of a viable long-term strategy. Some or all of these risks may exist in any investment we make in a distressed business or industry. As a result, investments in distressed operating businesses involve heightened risks, and we cannot assure you that any such investments will be profitable. We may acquire significant positions in distressed businesses for strategic reasons, which may require us to expend significant capital on investments that differ from, and involve a higher degree of risk than, other assets currently in our portfolio. In addition, acquiring an operating business exposes us to some or all of the meaningful risks associated with owning an operating business. Any loss of invested capital in such businesses would adversely affect our results of operation, profitability and the amount of funds available for distribution as a dividend to our stockholders. See “-We recently acquired a golf business, which is subject to various risks that could have a negative impact on our financial results.”

**Our agreements with New Residential may not reflect terms that would have resulted from arm’s-length negotiations among unaffiliated third parties, and we have agreed to indemnify New Residential for certain liabilities.**

We completed a spin-off of New Residential in May 2013. The terms of the agreements related to the spin-off of New Residential, including a Separation and Distribution Agreement dated April 26, 2013 (the “Separation and Distribution Agreement”) between us and New Residential and a management agreement between our manager and New Residential, were not negotiated among unaffiliated third parties. Such terms were proposed by our officers and other employees of our manager and approved by our board of directors. As a result, these terms may be less favorable to us than the terms that would have resulted from arm’s-length negotiations among unaffiliated third parties.

In the Separation and Distribution Agreement, we have agreed to indemnify New Residential and its affiliates and representatives against losses arising from: (a) any liability related to our junior subordinated notes due 2035; (b) any other liability that has not been defined as a liability of New Residential; (c) any failure by us and our subsidiaries (other than New Residential and its subsidiaries) (collectively, the “Newcastle Group”) to pay, perform or otherwise promptly discharge any liability listed under (a) and (b) above in accordance with their respective terms, whether prior to, at or after the time of effectiveness of the Separation and Distribution Agreement; (d) any breach by any member of the Newcastle Group of any provision of the Separation and Distribution Agreement and any agreements ancillary thereto (if any), subject to any limitations of liability provisions and other provisions applicable to any such breach set forth therein; and (e) any untrue statement or alleged untrue statement of a material fact or omission or alleged omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, with respect to all information contained in the information statement or the registration statement of which the information statement is a part that relates solely to any assets owned, directly or indirectly by us, other than New Residential’s initial portfolio of assets. Any indemnification payments that we may be required to make could have a significantly negative effect on our liquidity and results of operations.

**Qualifying as a REIT involves highly technical and complex provisions of the Code, and our failure to qualify as a REIT would result in higher taxes and reduced cash available for distribution to our stockholders.**

We operate in a manner intended to qualify us as a REIT for federal income tax purposes. Qualification as a REIT involves the application of highly technical and complex Code provisions for which only limited judicial and administrative authorities exist. Even a technical or inadvertent violation could jeopardize our REIT qualification. Our qualification as a REIT will depend on our satisfaction of certain asset, income, organizational, distribution, stockholder ownership and other requirements on a continuing basis. Compliance with these requirements must be carefully monitored on a continuing basis, and there can be no assurance that our manager's personnel responsible for doing so will be able to successfully monitor our compliance.

Our ability to satisfy the asset tests depends upon our analysis of the fair market values of our assets, some of which are not susceptible to a precise determination, and for which we do not obtain independent appraisals. Our compliance with the REIT income and quarterly asset requirements also depends upon our ability to successfully manage the composition of our income and assets on an ongoing basis. Moreover, the proper classification of an instrument as debt or equity for federal income tax purposes, and the tax treatment of participation interests that we hold in mortgage loans and mezzanine loans, may be uncertain in some circumstances, which could affect the application of the REIT qualification requirements. Accordingly, there can be no assurance that the Internal Revenue Service (the "IRS") will not contend that our interests in subsidiaries or other issuers violate the REIT requirements.

If we were to fail to qualify as a REIT in any taxable year, we would be subject to federal income tax, including any applicable alternative minimum tax, on our taxable income at regular corporate rates, and distributions to stockholders would not be deductible by us in computing our taxable income. Any such corporate tax liability could be substantial and would reduce the amount of cash available for distribution to our stockholders, which in turn could have an adverse impact on the value of, and trading prices for, our stock. Unless entitled to relief under certain provisions of the Code, we also would be disqualified from taxation as a REIT for the four taxable years following the year during which we initially ceased to qualify as a REIT.

**Our failure to qualify as a REIT would create issues under a number of our financings and other agreements and would cause our common and preferred stock to be delisted from the NYSE.**

Our failure to qualify as a REIT would create issues under a number of our financing and other agreements. In addition, the NYSE requires, as a condition to the continued listing of our common and preferred stock, that we maintain our REIT status. Consequently, if we fail to maintain our REIT status, our common and preferred stock would promptly be delisted from the NYSE, which would decrease the trading activity of such shares. This could make it difficult to sell shares and would likely cause the market volume of the shares trading to decline.

If we were delisted as a result of losing our REIT status and desired to relist our stock on the NYSE, we would have to reapply to the NYSE to be listed as a domestic corporation. As the NYSE's listing standards for REITs are less onerous than its standards for domestic corporations, it would be more difficult for us to become a listed company under these heightened standards. We might not be able to satisfy the NYSE's listing standards for a domestic corporation. As a result, if we were delisted from the NYSE, we might not be able to relist as a domestic corporation, in which case our common and preferred stock could not trade on the NYSE.

**Our failure to qualify as a REIT would potentially give rise to a claim for damages from New Residential.**

In connection with the spin-off of New Residential, which was completed in May 2013, we represented in the Separation and Distribution Agreement that we have no knowledge of any fact or circumstance that would cause us to fail to qualify as a REIT. We also covenanted in the Separation and Distribution Agreement to use our reasonable best efforts to maintain our REIT status for each of our taxable years ending on or before December 31, 2014 (unless we obtain an opinion from a nationally recognized tax counsel or a private letter ruling from the IRS to the effect that our failure to maintain our REIT status will not cause New Residential to fail to qualify as a REIT under the successor REIT rules). In the event of a breach of this representation or covenant, New Residential may be able to seek damages from us, which could have a significantly negative effect on our liquidity and results of operations.

**If New Residential fails to qualify as a REIT for 2013, it would significantly affect our ability to maintain our REIT status.**

For federal income tax purposes we recorded approximately \$600 million of gain as a result of the spin-off of New Residential in May 2013. If New Residential qualified for taxation as a REIT for 2013, that gain is qualifying income for purposes of our 2013 REIT income tests. If, however, New Residential failed to qualify as a REIT for 2013, that gain is non-qualifying income for purposes of the 75% gross income test. Although New Residential covenanted in the Separation and Distribution Agreement to use reasonable best efforts to qualify as a REIT in 2013, no assurance can be given that it so qualified. If New Residential failed to qualify, it could cause us to fail our 2013 REIT income tests, which could cause us to lose our REIT status and thereby materially negatively impact our business, financial condition and potentially impair our ability to continue operating in the future.

**The failure of assets subject to repurchase agreements to qualify as real estate assets could adversely affect our ability to qualify as a REIT.**

We have historically financed a meaningful portion of our investments in securities and loans with repurchase agreements, which are short-term financing arrangements and we may enter into additional repurchase agreements in the future. Under these agreements, we nominally sell certain of our assets to a counterparty and simultaneously enter into an agreement to repurchase these assets at a later date in exchange for a purchase price. Economically, these agreements are financings that are secured by the assets sold pursuant thereto. We believe that, for purposes of the REIT asset and income tests, we should be treated as the owner of the assets that are the subject of any such sale and repurchase agreement, notwithstanding that those agreements may transfer record ownership of the assets to the counterparty during the term of the agreement. It is possible, however, that the IRS could assert that we did not own the assets during the term of the sale and repurchase agreement, in which case we might fail to qualify as a REIT.

**Rapid changes in the values of assets that we hold may make it more difficult for us to maintain our qualification as a REIT or our exclusion from the 1940 Act.**

If the market value or income potential of qualifying assets for purposes of our qualification as a REIT or our exclusion from registration as an investment company under the 1940 Act declines as a result of increased interest rates, changes in prepayment rates or other factors, or the market value or income potential from non-qualifying assets increases, we may need to increase our investments in qualifying assets and/or liquidate our non-qualifying assets to maintain our REIT qualification or our exclusion from registration under the 1940 Act. If the change in market values or income occurs quickly, this may be especially difficult to accomplish. This difficulty may be exacerbated by the illiquid nature of any non-qualifying assets we may own. We may have to make investment decisions that we otherwise would not make absent the intent to maintain our qualification as a REIT and exclusion from registration under the 1940 Act.

**Dividends payable by REITs do not qualify for the reduced tax rates.**

Dividends payable to domestic stockholders that are individuals, trusts or estates are generally taxed at reduced rates. Dividends payable by REITs, however, are generally not eligible for the reduced rates. Although these rules do not adversely affect the taxation of REITs or dividends paid by REITs, the more favorable rates applicable to regular corporate dividends could cause investors who are individuals, trusts and estates to perceive investments in REITs to be relatively less attractive than investments in the stocks of non-REIT corporations that pay dividends, which could adversely affect the value of the stock of REITs, including our common stock. In addition, the relative attractiveness of real estate in general may be adversely affected by the favorable tax treatment given to corporate dividends, which could affect the value of our real estate assets negatively.

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

In order to maintain our tax status as a REIT, we are generally required to distribute at least 90% of our REIT taxable income (determined without regard to the dividends paid deduction and not including net capital gains) each year to our stockholders. We intend to make distributions to our stockholders to comply with the requirements of the Code. However, differences in timing between the recognition of taxable income and the actual receipt of cash could require us to sell assets or borrow funds on a short-term or long-term basis to meet the 90% distribution requirement of the Code. Certain of our assets may generate substantial mismatches between taxable income and available cash. As a result, the requirement to distribute a substantial portion of our net taxable income could cause us to: (i) sell assets in adverse market conditions, (ii) borrow on unfavorable terms, (iii) distribute amounts that would otherwise be invested in future acquisitions, capital expenditures or repayment of debt, or (iv) make taxable distributions of our capital stock in order to comply with REIT requirements. Further, amounts distributed will not be available to fund investment activities. If we fail to obtain debt or equity capital in the future, it could limit our ability to satisfy our liquidity needs, which could adversely affect the value of our common stock.

**In January 2013, we experienced an “ownership change” for purposes of Section 382 of the Code, which limits our ability to utilize our net operating loss and net capital loss carryforwards and certain built-in losses to reduce our future taxable income, potentially increases our related REIT distribution requirement, and potentially adversely affects our liquidity.**

In order to maintain our tax status as a REIT, we are generally required to distribute at least 90% of our REIT taxable income (determined without regard to the dividends paid deduction and not including net capital gains) each year to our stockholders. To qualify for the tax benefits accorded to REITs, we intend to make distributions to our stockholders such that we distribute all or substantially all our net taxable income (if any) each year, subject to certain adjustments. In the past, we have used net operating loss and net capital loss carryforwards to facilitate the satisfaction of our distribution requirements. As a result of our January 2013 “ownership change,” our future ability to utilize our net operating loss and net capital loss carryforwards to reduce our taxable income may be limited by certain provisions of the Code.

Specifically, the Code limits the ability of a company that undergoes an “ownership change” to utilize its net operating loss and net capital loss carryforwards and certain built-in losses to offset taxable income earned in years after the ownership change. An ownership change occurs if, during a three-year testing period, more than 50% of the stock of a company is acquired by one or more persons (or certain groups of persons) who own, directly or constructively, 5% or more of the stock of such company. An ownership change can occur as a result of a public offering of stock, as well as through secondary market purchases of our stock and certain types of reorganization transactions. Generally, when an ownership change occurs, the annual limitation on the use of net operating loss and net capital loss carryforwards and certain built-in losses is equal to the product of the applicable long-term tax exempt rate and the value of the company’s stock immediately before the ownership change. We have substantial net operating and net capital loss carry forwards which we have used, and will continue to use, to offset our tax and distribution requirements. In January 2013, an “ownership change” for purposes of Section 382 of the Code occurred. Therefore, the provisions of Section 382 of the Code impose an annual limit on the amount of net operating loss and net capital loss carryforwards and built in losses that we can use to offset future taxable income. Such limitation may increase our dividend distribution requirement in the future, which could adversely affect our liquidity. We do not believe that the limitation as a result of the January 2013 ownership change will prevent us from satisfying our REIT distribution requirement for the current year and future years. No assurance, however, can be given that we will be able to satisfy our distribution requirement following a current or future ownership change or otherwise. If we were to fail to satisfy our distribution requirement, it would cause us to lose our REIT status and thereby materially negatively impact our business, financial condition and potentially impair our ability to continue operating in the future.

**Certain properties are leased to our TRSs pursuant to special provisions of the Code.**

We currently lease certain “qualified healthcare properties” to our TRSs (or a limited liability company of which a TRS is a member). These TRSs in turn contract with an affiliate of our manager to manage the healthcare operations at these properties. The rents paid by the TRSs in this structure will be treated as qualifying rents from real property for purposes of the REIT requirements if (i) they are paid pursuant to an arm’s-length lease of a qualified healthcare property and (ii) the operator qualifies as an “eligible independent contractor” with respect to the property. An operator will qualify as an eligible independent contractor if it meets certain ownership tests with respect to us, and if, at the time the operator enters into the management agreement, the operator is actively engaged in the trade or business of operating qualified healthcare properties for any person who is not a related person to us or the lessee. If any of the above conditions were not satisfied, then the rents would not be considered income from a qualifying source for purposes of the REIT rules, which could cause us to incur penalty taxes or to fail to qualify as a REIT.

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

We may acquire debt instruments in the secondary market for less than their face amount. The amount of such discount will generally be treated as “market discount” for federal income tax purposes. Accrued market discount is generally recognized as taxable income over our holding period in the instrument in advance of the receipt of cash. If we collect less on the debt instrument than our purchase price plus the market discount we had previously reported as income, we may not be able to benefit from any offsetting loss deductions.

In addition, we may acquire debt investments that are subsequently modified by agreement with the borrower. If the amendments to the outstanding debt are “significant modifications” under the applicable Treasury regulations, the modified debt may be considered to have been reissued to us in a debt-for-debt exchange with the borrower. In that event, we may be required to recognize taxable gain to the extent the principal amount of the modified debt exceeds our adjusted tax basis in the unmodified debt, even if the value of the debt or the payment expectations have not changed. Following such a taxable modification, we would hold the modified loan with a cost basis equal to its principal amount for federal tax purposes.

Moreover, in the event that any debt instruments acquired by us are delinquent as to mandatory principal and interest payments, or in the event payments with respect to a particular debt instrument are not made when due, we may nonetheless be required to continue to recognize the unpaid interest as taxable income. Similarly, we may be required to accrue interest income with respect to subordinate mortgage-backed securities at the stated rate regardless of whether corresponding cash payments are received.

**The IRS tax rules regarding recognizing capital losses and ordinary income for our non-recourse financings, coupled with current REIT distribution requirements, could result in our recognizing significant taxable net income without receiving an equivalent amount of cash proceeds from which to make required distributions. This disconnect could have a serious, negative effect on us.**

We may experience issues regarding the characterization of income for tax purposes. For example, we may recognize significant ordinary income, which we would not be able to offset with capital losses, which would, in turn, increase the amount of income we would be required to distribute to stockholders in order to maintain our REIT status. We expect that this disconnect will occur in the case of one or more of our non-recourse financing structures, including off balance sheet structures such as our subprime securitizations and non-consolidated CDOs, where we incur capital losses on the related assets, and ordinary income from the cancellation of the related non-recourse financing if the ultimate proceeds from the assets are insufficient to repay such debt. Through June 30, 2014, no such cancellation of CDO debt had been effected as a result of losses incurred. However, we expect that such cancellation of indebtedness within our CDOs, consolidated or non-consolidated, may occur in the future. In the case of our subprime securitizations, \$123.6 million of such cancellations had been effected through June 30, 2014, and we expect such cancellations will continue as losses are realized. This disconnect could also occur, and has occurred, as a result of the repurchase of our outstanding debt at a discount as the gain recorded upon the cancellation of indebtedness is characterized as ordinary income for tax purposes. We have repurchased our debt at a discount in the past, and we intend to attempt to do so in the future. During 2009 and 2010, we repurchased \$787.8 million face amount of our outstanding CDO debt and junior subordinated notes at a discount, and recorded \$521.1 million of gain. In compliance with tax laws, we had the ability to defer the ordinary income recorded as a result of this cancellation of indebtedness to future years and have deferred or intend to defer all or a portion of such gain for 2009 and 2010. While such deferral may postpone the effect of the disconnect on the ability to offset taxable income and losses, it does not eliminate it. Furthermore, cancellation of indebtedness income recognized on or after January 1, 2011 cannot be deferred and must generally be recognized as ordinary income in the year of such cancellation. During the years ended 2013, 2012 and 2011, we repurchased \$35.9 million, \$34.1 million and \$188.9 million face amount of our outstanding CDO debt and notes payable at a discount and recorded \$4.6 million, \$23.2 million and \$81.1 million of gain for tax purposes, respectively (of which only \$4.6 million, \$24.1 million and \$66.1 million of gain relating to \$35.9 million, \$39.3 million and \$171.8 million face amount of debt repurchased, respectively, was recognized for GAAP purposes). During the six months ended June 30, 2014, we did not repurchase any of our outstanding CDO debt and notes payable. The elimination of the ability to defer the recognition of cancellation of indebtedness income introduces additional tax implications that may significantly reduce the economic benefit of repurchasing our outstanding CDO debt.

When we experience any of these disconnects, and to the extent that a distribution through stock dividends is not viable, we may not have sufficient cash flow to make the distributions necessary to satisfy our REIT distribution requirements, which would cause us to lose our REIT status and thereby materially negatively impact our business, financial condition and potentially impair our ability to continue operating in the future. Under current market conditions, this type of disconnect between taxable income and cash proceeds would be likely to occur at some point in the future if the current regulations that create the disconnect are not revised, but we cannot predict at this time when such a disconnect might occur.

**We may be unable to generate sufficient revenue from operations to pay our operating expenses and to pay distributions to our stockholders.**

As a REIT, we are generally required to distribute at least 90% of our REIT taxable income (determined without regard to the dividends paid deduction and not including net capital losses) each year to our stockholders. To qualify for the tax benefits accorded to REITs, we intend to make distributions to our stockholders in amounts such that we distribute all or substantially all of our net taxable income each year, subject to certain adjustments. However, our ability to make distributions may be adversely affected by the risk factors described herein. In the event of a sustained downturn in our operating results and financial performance relative to previous periods or sustained declines in the value of our asset portfolio, we may be unable to declare or pay quarterly distributions or make distributions to our stockholders, and we may elect to comply with our REIT distribution requirements by, after completing various procedural steps, distributing, under certain circumstances, a portion of the required amount in the form of common shares in lieu of cash. The timing and amount of distributions are in the sole discretion of our board of directors, which considers, among other factors, our earnings, financial condition, debt service obligations and applicable debt covenants, REIT qualification requirements and other tax considerations and capital expenditure requirements as our board of directors may deem relevant from time to time.

**The stock ownership limit imposed by the Code for REITs and our charter may inhibit market activity in our stock and restrict our business combination opportunities.**

In order for us to maintain our qualification as a REIT under the Code, not more than 50% in value of our outstanding stock may be owned, directly or indirectly, by five or fewer individuals (as defined in the Code to include certain entities) at any time during the last half of each taxable year after our first year. Our charter, with certain exceptions, authorizes our board of directors to take the actions that are necessary and desirable to preserve our qualification as a REIT. Unless exempted by our board of directors, no person may own more than 8% of the aggregate value of our outstanding capital stock, treating classes and series of our stock in the aggregate, or more than 25% of the outstanding shares of our Series B Preferred Stock, Series C Preferred Stock or Series D Preferred Stock. Our board may grant an exemption in its sole discretion, subject to such conditions, representations and undertakings as it may determine in its sole discretion. These ownership limits could delay or prevent a transaction or a change in our control that might involve a premium price for our common stock or otherwise not be in the best interest of our stockholders.

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

Even if we remain qualified for taxation as a REIT, we may be subject to certain federal, state and local taxes on our income and assets, including taxes on any undistributed income, tax on income from some activities conducted as a result of a foreclosure, and state or local income, property and transfer taxes, such as mortgage recording taxes. Moreover, if a REIT distributes less than 85% of its taxable income to its stockholders during any calendar year (including any distributions declared by the last day of the calendar year but paid in the subsequent year), then it is required to pay an excise tax of 4% on any shortfall between the required 85% and the amount that was actually distributed. Any of these taxes would decrease cash available for distribution to our stockholders. In addition, in order to meet the REIT qualification requirements, or to avert the imposition of a 100% tax that applies to certain gains derived by a REIT from dealer property or inventory, we may hold some of our assets through TRSs. Such subsidiaries will be subject to corporate level income tax at regular rates.

**Complying with REIT requirements may cause us to forego, liquidate or contribute to a TRS otherwise attractive opportunities.**

To qualify as a REIT for federal income tax purposes, we must continually satisfy tests concerning, among other things, the sources of our income, the nature and diversification of our assets, the amounts we distribute to our stockholders and the ownership of our stock. As a result of these tests, we may be required to make distributions to stockholders at disadvantageous times or when we do not have funds readily available for distribution, forego otherwise attractive investment opportunities, liquidate assets in adverse market conditions or contribute assets to a TRS that is subject to regular corporate federal income tax. Thus, compliance with the REIT requirements may hinder our ability to make and retain certain attractive investments.

**Complying with REIT requirements may limit our ability to hedge effectively.**

The existing REIT provisions of the Code may substantially limit our ability to hedge our operations because a significant amount of the income from those hedging transactions is likely to be treated as non-qualifying income for purposes of both REIT gross income tests. In addition, we must limit our aggregate income from non-qualified hedging transactions, from our provision of services and from other non-qualifying sources, to less than 5% of our annual gross income (determined without regard to gross income from qualified hedging transactions). As a result, we may have to limit our use of certain hedging techniques or implement those hedges through total return swaps. This could result in greater risks associated with changes in interest rates than we would otherwise want to incur or could increase the cost of our hedging activities. If we fail to comply with these limitations, we could lose our REIT qualification for federal income tax purposes, unless our failure was due to reasonable cause, and not due to willful neglect, and we meet certain other technical requirements. Even if our failure were due to reasonable cause, we might incur a penalty tax.

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

Certain of our securitizations have resulted in the creation of taxable mortgage pools for federal income tax purposes. As a REIT, so long as we own 100% of the equity interests in a taxable mortgage pool, we would generally not be adversely affected by the characterization of the securitization as a taxable mortgage pool. Certain categories of stockholders, however, such as foreign stockholders eligible for treaty or other benefits, stockholders with net operating losses, and certain tax-exempt stockholders that are subject to unrelated business income tax, could be subject to increased taxes on a portion of their dividend income from us that is attributable to the taxable mortgage pool. In addition, to the extent that our stock is owned by tax-exempt “disqualified

organizations,” such as certain government-related entities and charitable remainder trusts that are not subject to tax on unrelated business income, we could incur a corporate level tax on a portion of our income from the taxable mortgage pool. In that case, we might reduce the amount of our distributions to any disqualified organization whose stock ownership gave rise to the tax. Moreover, we may be precluded from selling equity interests in these securities to outside investors, or selling any debt securities issued in connection with these securitizations that might be considered to be equity interests for tax purposes. These limitations may prevent us from using certain techniques to maximize our returns from securitization transactions.

**Distributions to tax-exempt investors may be classified as unrelated business taxable income.**

Neither ordinary nor capital gain distributions with respect to our stock nor gain from the sale of stock should generally constitute unrelated business taxable income to a tax-exempt investor. However, there are certain exceptions to this rule. In particular:

- part of the income and gain recognized by certain qualified employee pension trusts with respect to our stock may be treated as unrelated business taxable income if shares of our stock are predominantly held by qualified employee pension trusts, and we are required to rely on a special look-through rule for purposes of meeting one of the REIT ownership tests, and we are not operated in a manner to avoid treatment of such income or gain as unrelated business taxable income;
- part of the income and gain recognized by a tax-exempt investor with respect to our stock would constitute unrelated business taxable income if the investor incurs debt in order to acquire the stock; and
- to the extent that we are (or a part of us, or a disregarded subsidiary of ours, is) a “taxable mortgage pool,” or if we hold residual interests in a real estate mortgage investment conduit, a portion of the distributions paid to a tax-exempt stockholder that is allocable to excess inclusion income may be treated as unrelated business taxable income.

**The tax on prohibited transactions will limit our ability to engage in transactions which would be treated as prohibited transactions for U.S. federal income tax purposes.**

Net income that we derive from a prohibited transaction is subject to a 100% tax. The term “prohibited transaction” generally includes a sale or other disposition of property (including mortgage loans, but other than foreclosure property, as discussed below) that is held primarily for sale to customers in the ordinary course of our trade or business. We might be subject to this tax if we were to dispose of or securitize loans or certain other assets in a manner that was treated as a prohibited transaction for U.S. federal income tax purposes.

We intend to conduct our operations so that no asset that we own (or are treated as owning) will be treated as, or as having been, held for sale to customers, and that a sale of any such asset will not be treated as having been in the ordinary course of our business. As a result, we may choose not to engage in certain sales of loans or certain other assets at the REIT level, and may limit the structures we utilize for our securitization transactions, even though the sales or structures might otherwise be beneficial to us. In addition, whether property is held “primarily for sale to customers in the ordinary course of a trade or business” depends on the particular facts and circumstances. No assurance can be given that any property that we sell will not be treated as property held for sale to customers, or that we can comply with certain safe-harbor provisions of the Code that would prevent such treatment. The 100% prohibited transaction tax does not apply to gains from the sale of property that is held through a TRS or other taxable corporation, although such income will be subject to tax in the hands of the corporation at regular corporate rates. We intend to structure our activities to prevent prohibited transaction characterization.

**New legislation or administrative or judicial action, in each instance potentially with retroactive effect, could make it more difficult or impossible for us to qualify as a REIT.**

The present U.S. federal income tax treatment of REITs may be modified, possibly with retroactive effect, by legislative, judicial or administrative action at any time, which could affect the U.S. federal income tax treatment of an investment in us. The U.S. federal income tax rules dealing with REITs constantly are under review by persons involved in the legislative process, the IRS and the U.S. Treasury Department, which results in statutory changes as well as frequent revisions to regulations and interpretations. Revisions in U.S. federal tax laws and interpretations thereof could affect or cause us to change our investments and commitments and affect the tax considerations of an investment in us.

**Liquidation of assets may jeopardize our REIT qualification or create additional tax liability for us.**

To qualify as a REIT, we must comply with requirements regarding the composition of our assets and our sources of income. If we are compelled to liquidate our investments to repay obligations to our lenders, we may be unable to comply with these

requirements, ultimately jeopardizing our qualification as a REIT, or we may be subject to a 100% tax on any resultant gain if we sell assets that are treated as dealer property or inventory.

#### **Maintenance of our 1940 Act exclusion imposes limits on our operations.**

We conduct our operations in reliance on an exclusion from the 1940 Act, which we refer to as the Section 3(c)(5)(C) exclusion, which is available for entities “primarily engaged in the business of purchasing or otherwise acquiring mortgages and other liens on and interests in real estate.”

Reliance on this exclusion limits our ability to make certain investments. The Section 3(c)(5)(C) exclusion generally requires that at least 55% of our assets be comprised of qualifying real estate assets and at least 80% of our assets be comprised of a combination of qualifying real estate assets and real estate related assets. In satisfying the 55% requirement under the Section 3(c)(5)(C) exclusion, based on guidance from the SEC and its staff, we treat whole pool Agency ARM RMBS issued with respect to an underlying pool of mortgage loans in which we hold all of the certificates issued by the pool as qualifying real estate assets. The SEC and its staff have not issued guidance with respect to whole pool non-Agency RMBS for purposes of the Section 3(c)(5)(C) exclusion. Accordingly, based on our own judgment and analysis of the guidance from the SEC and its staff identifying Agency whole pool certificates as qualifying real estate assets under the Section 3(c)(5)(C) exclusion, we treat whole pool non-Agency ARM RMBS issued with respect to an underlying pool of mortgage loans in which we hold all of the certificates issued by the pool as qualifying real estate assets. We also treat whole mortgage loans that we acquire directly as qualifying real estate assets provided that 100% of the loan is secured by real estate when we acquire the loan and we have the unilateral right to foreclose on the mortgage. In addition, we treat investments in Agency partial pool RMBS and non-Agency partial pool RMBS as real estate related assets for purposes of satisfying the 80% test under the Section 3(c)(5)(C) exclusion. The Section 3(c)(5)(C) exclusion generally limits the amount of our investments in non-real estate assets, including consumer loans, to no more than 20% of our total assets. To the extent that we acquire significant non-real estate assets in the future, in order to maintain our exclusion under the 1940 Act, we may need to offset those acquisitions with additional qualifying real estate and real estate related assets, which may not generate risk-adjusted returns as attractive as those generated by non-real estate related assets.

In August 2011, the SEC issued a concept release soliciting public comments on a wide range of issues relating to companies, which are typically REITs, engaged in the business of acquiring mortgages and mortgage-related instruments and that rely on Section 3(c)(5)(C) of the 1940 Act, including the nature of the assets that qualify for purposes of the Section 3(c)(5)(C) exclusion and whether mortgage REITs like us should be regulated in a manner similar to investment companies. Therefore, there can be no assurance that the laws and regulations governing the 1940 Act status of REITs, or guidance from the SEC or its staff regarding the Section 3(c)(5)(C) exclusion, will not change in a manner that adversely affects our operations. If we fail to maintain an exclusion or exception from the 1940 Act, we could, among other things, be required either to (a) change the manner in which we conduct our operations to avoid being required to register as an investment company, (b) effect sales of our assets in a manner that, or at a time when, we would not otherwise choose to do so, or (c) register as an investment company (which, among other things, would require us to comply with the leverage constraints applicable to investment companies), any of which could negatively affect the value of our common stock, the sustainability of our business model, and our ability to make distributions.

#### Risks Related to Our Common Stock

**Our stock price has fluctuated meaningfully, particularly on a percentage basis, and may fluctuate meaningfully in the future. Accordingly, you may not be able to resell your shares at or above the price at which you purchased them.**

The trading price of our common stock has fluctuated significantly in the past. The trading price of our common stock could fluctuate significantly in the future and could be negatively affected in response to various factors, including:

- market conditions in the broader stock market in general, or in the REIT or real estate industry in particular;
- our ability to make investments with attractive risk-adjusted returns;
- market perception of our current and projected financial condition, potential growth, future earnings and future cash dividends;
- announcements we make regarding dividends;
- actual or anticipated fluctuations in our quarterly financial and operating results;

- market perception or media coverage of our manager or its affiliates;
- additional offerings of our common stock;
- actions by rating agencies;
- short sales of our common stock;
- any decision to pursue a distribution or disposition of a meaningful portion of our assets;
- issuance of new or changed securities analysts' reports or recommendations;
- media coverage of us, other REITs or the outlook of the real estate industry;
- major reductions in trading volumes on the exchanges on which we operate;
- credit deterioration within our portfolio;
- legislative or regulatory developments, including changes in the status of our regulatory approvals or licenses;
- litigation and governmental investigations; and
- any decision to pursue a spin-off of a portion of our assets.

These and other factors may cause the market price and demand for our common stock to fluctuate substantially, which may negatively affect the price or liquidity of our common stock. When the market price of a stock has been volatile or has decreased significantly in the past, holders of that stock have, at times, instituted securities class action litigation against the company that issued the stock. If any of our stockholders brought a lawsuit against us, we could incur substantial costs defending, settling or paying any resulting judgments related to the lawsuit. Such a lawsuit could also divert the time and attention of our management from our business and hurt our share price.

In addition, we expect to complete a 1 for 3 reverse stock split of our common stock on August 18, 2014. There can be no assurance that the reverse stock split will have the anticipated benefits. For instance, there can be no assurance that the market price per share of our common stock after the reverse stock split will rise in proportion to the reduction in the number of shares of our common stock outstanding before the reverse stock split, or that the reverse stock split will result in a market price per share that will attract brokers and investors who do not trade in lower priced stocks.

Additionally, the liquidity of our common stock could be adversely affected by the reduced number of shares resulting from the reverse stock split, which, in turn, could result in greater volatility in the price per share of our common stock. The potential volatility in the price per share of our common stock may also make short-selling more attractive, which could put additional downward pressure on the price of our common stock.

Furthermore, a reverse stock split may result in some shareholders owning "odd lots" of less than one hundred shares of our common stock on a post-split basis. Odd lots may be more difficult to sell, or require greater transaction costs per share to sell, than shares in "round lots" of even multiples of one hundred shares.

**We may be unable or elect not to pay dividends on our common or preferred stock in the future, which would negatively impact our business in a number of ways and decrease the price of our common and preferred stock.**

While we are required to make distributions in order to maintain our REIT status (as described above under "-Risks Related to Our REIT Status and the 1940 Act-We may be unable to generate sufficient revenue from operations to pay our operating expenses and to pay distributions to our stockholders"), we may elect not to maintain our REIT status, in which case we would no longer be required to make such distributions. Moreover, even if we do elect to maintain our REIT status, we may elect to comply with the applicable requirements by, after completing various procedural steps, distributing, under certain circumstances, a portion of the required amount in the form of shares of our common stock in lieu of cash. If we elect not to maintain our REIT status or to satisfy any required distributions in common stock in lieu of cash, such action could negatively affect our business and financial condition as well as the price of both our common and preferred stock. No assurance can be given that we will pay any dividends on our common stock in the future.

We do not currently have unpaid accrued dividends on our preferred stock. However, to the extent we do, we cannot pay any dividends on our common stock, pay any consideration to repurchase or otherwise acquire shares of our common stock or redeem any shares of any series of our preferred stock without redeeming all of our outstanding preferred shares in accordance with the governing documentation. Consequently, the failure to pay dividends on our preferred stock restricts the actions that we may take with respect to our common stock and preferred stock. Moreover, if we do not pay dividends on any series of preferred stock for six or more periods, then holders of each affected series obtain the right to call a special meeting and elect two members to our board of directors. We cannot predict whether the holders of our preferred stock would take such action or, if taken, how long the process would take or what impact the two new directors on our board of directors would have on our company (other than increasing our director compensation costs). However, the election of additional directors would affect the composition of our board of directors and, thus, could affect the management of our business.

**We may choose to pay dividends in our own stock, or make a distribution of a subsidiary's common stock, in which case you could be required to pay income taxes in excess of the cash dividends you receive.**

We may in the future distribute taxable dividends that are payable in cash and shares of our common stock at the election of each stockholder. We may also determine to distribute a taxable dividend in the stock of a subsidiary in connection with a spin-off or other transaction, as in the case of our spin-off of New Residential in May 2013 and our spin-off of New Media in February 2014. We are currently considering a spin-off of our senior housing business, which could result in the distribution of a taxable dividend, although there can be no assurance as to the timing, terms, structure or completion of any such transaction. Taxable stockholders receiving such distributions will be required to include the full amount of the distribution as ordinary income to the extent of our current and accumulated earnings and profits for federal income tax purposes. As a result, stockholders may be required to pay income taxes with respect to such dividends in excess of the cash dividends received. If a U.S. stockholder sells the stock that it receives as a dividend in order to pay this tax, the sale proceeds may be less than the amount included in income with respect to the dividend, depending on the market price of our stock at the time of the sale. Furthermore, with respect to certain non-U.S. stockholders, we may be required to withhold U.S. tax with respect to such dividends, including in respect of all or a portion of such dividend that is payable in stock. In addition, if a significant number of our stockholders determine to sell shares of our common stock in order to pay taxes owed on dividends, it may put downward pressure on the trading price of our common stock.

It is unclear whether and to what extent we will be able to pay taxable dividends in cash and stock. Moreover, various aspects of such a taxable cash/stock dividend are uncertain and have not yet been addressed by the IRS. No assurance can be given that the IRS will not impose additional requirements in the future with respect to taxable cash/stock dividends, including on a retroactive basis, or assert that the requirements for such taxable cash/stock dividends have not been met.

**Shares eligible for future sale may adversely affect our common stock price.**

Sales of our common stock or other securities in the public or private market, or the perception that these sales may occur, could cause the market price of our common stock to decline. This could also impair our ability to raise additional capital through the sale of our equity securities. Under our certificate of incorporation, we are authorized to issue up to 1,000,000,000 shares of common stock and we are authorized to reclassify a portion of our authorized preferred stock into common stock, and there were 351,725,561 shares of our common stock outstanding as of July 28, 2014. We cannot predict the size of future issuances of our common stock or other securities or the effect, if any, that future sales and issuances would have on the market price of our common stock.

**An increase in market interest rates may have an adverse effect on the market price of our common stock.**

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

**ERISA may restrict investments by plans in our common stock.**

A plan fiduciary considering an investment in our common stock should consider, among other things, whether such an investment

is consistent with the fiduciary obligations under the Employee Retirement Income Security Act of 1974, as amended (“ERISA”), including whether such investment might constitute or give rise to a prohibited transaction under ERISA, the Code or any substantially similar federal, state or local law and, if so, whether an exemption from such prohibited transaction rules is available.

**Maryland takeover statutes may prevent a change of our control, which could depress our stock price.**

Under Maryland law, “business combinations” between a Maryland corporation and an interested stockholder or an affiliate of an interested stockholder are prohibited for five years after the most recent date on which the interested stockholder becomes an interested stockholder. These business combinations include certain mergers, consolidations, share exchanges, or, in circumstances specified in the statute, an asset transfer or issuance or reclassification of equity securities or a liquidation or dissolution. An interested stockholder is defined as:

- any person who beneficially owns 10% or more of the voting power of the corporation’s outstanding shares;  
or
- an affiliate or associate of a corporation who, at any time within the two-year period prior to the date in question, was the beneficial owner of 10% or more of the voting power of the then outstanding stock of the corporation.
- A person is not an interested stockholder under the statute if the board of directors approved in advance the transaction by which he or she otherwise would have become an interested stockholder.
- After the five-year prohibition, any business combination between the Maryland corporation and an interested stockholder generally must be recommended by the board of directors of the corporation and approved by the affirmative vote of at least:
- 80% of the votes entitled to be cast by holders of outstanding shares of voting stock of the corporation voting together as a single group;  
and
- two-thirds of the votes entitled to be cast by holders of voting stock of the corporation other than shares held by the interested stockholder with whom or with whose affiliate the business combination is to be effected or held by an affiliate or associate of the interested stockholder voting together as a single voting group.

The business combination statute may discourage others from trying to acquire control of us and increase the difficulty of consummating any offer, including potential acquisitions that might involve a premium price for our common stock or otherwise be in the best interest of our stockholders.

**Our staggered board and other provisions of our charter and bylaws may prevent a change in our control.**

Our board of directors is divided into three classes of directors. Directors of each class are chosen for three-year terms upon the expiration of their current terms, and each year one class of directors is elected by the stockholders. The staggered terms of our directors may reduce the possibility of a tender offer or an attempt at a change in control, even though a tender offer or change in control might be in the best interest of our stockholders. In addition, our charter and bylaws also contain other provisions that may delay or prevent a transaction or a change in control that might involve a premium price for our common stock or otherwise be in the best interest of our stockholders.

Our charter authorizes us to issue additional authorized but unissued shares of our common stock or preferred stock. In addition, our board of directors may classify or reclassify any unissued shares of our common stock or preferred stock and may set the preferences, rights and other terms of the classified or reclassified shares. As a result, our board may establish a series of preferred stock that could delay or prevent a transaction or a change in control that might involve a premium price for our common stock or otherwise be in the best interest of our stockholders.

Risks Related to the Spin-Off of New Senior

**We may not be able to complete the spin-off on the terms anticipated or at all.**

Our board of directors has determined upon careful review and consideration in accordance with the applicable standard of review under Maryland law that a spin-off of certain of our senior housing assets is in our best interests. The spin-off will be effected as a distribution to the holders of our common stock of shares of New Senior, which is currently our wholly owned subsidiary. New Senior intends to elect and qualify to be taxed as a REIT and to be listed on the NYSE. New Senior will be externally managed by our manager pursuant to a new management agreement. Following the spin-off, we currently expect New Senior’s business strategy will be primarily focused on investments in senior housing properties.

We currently expect that New Senior will primarily target investments in senior housing related investments. New Senior's investment guidelines will be purposefully broad to enable it to make investments in a wide array of assets.

We are targeting distribution of New Senior's shares in the second half of 2014. However, there can be no assurance that the spin-off will be completed as anticipated or at all. Our ability to complete the spin-off is subject to, among other things, the SEC declaring the registration statement filed with regard to the spin-off effective, the filing and approval of an application to list New Senior's common stock on the NYSE and the formal declaration of the distribution by our board of directors. Failure to complete the spin-off could negatively affect the price of the shares of our common stock. Stockholder approval will not be required or sought in connection with the spin-off.

**The spin-off may not have the benefits we anticipate.**

The spin-off may not have the full or any strategic and financial benefits that we expect, or such benefits may be delayed or may not materialize at all. The anticipated benefits of the spin-off are based on a number of assumptions, which may prove incorrect. For example, we believe that analysts and investors will regard New Senior's investment strategy and asset portfolio more favorably as a separate company than as part of our existing portfolio and strategy and thus place a greater value on New Senior as a stand-alone business than as a business that is a part of us. In the event that the spin-off does not have these and other expected benefits, because of the diversification of New Senior's portfolio or for any other reason, the costs associated with the transaction, including an expected increase in management compensation and general and administrative expenses, could have a negative effect on our financial condition and each company's ability to make distributions to the stockholders of each company. Stockholder approval will not be required or sought in connection with the spin-off.

**New Senior may not be able to successfully implement its business strategy.**

Assuming the spin-off is completed, there can be no assurance that New Senior will be able to generate sufficient returns to pay its operating expenses and make satisfactory distributions to its stockholders, or any distributions at all, once it commences operations as an independent company. New Senior's financial condition, results of operations and cash flows will be affected by the expenses it will incur as a stand-alone public company, including fees paid to its manager, legal, accounting, compliance and other costs associated with being a public company with equity securities traded on the NYSE. In addition, its results of operations and its ability to make or sustain distributions to its stockholders depend on the availability of opportunities to acquire attractive assets, the level and volatility of interest rates, the availability of adequate short- and long-term financing, conditions in the real estate market, the financial markets and economic conditions, among other factors described in the registration statement for the transaction. After the separation, we will not be required, and do not intend, to provide New Senior with funds to finance its working capital or other cash requirements, so New Senior would need to obtain additional financing from banks, through public offerings or private placements of debt or equity securities, strategic relationships or other arrangements.

**Our agreements with New Senior may not reflect terms that would have resulted from arm's-length negotiations among unaffiliated third parties.**

The terms of the agreements related to New Senior's separation from us, including a separation and distribution agreement and a management agreement between our manager and New Senior, will not be negotiated among unaffiliated third parties. Such terms will be proposed by our officers and other employees of our manager and approved by our board of directors. As a result, these terms may be less favorable to us or New Senior than the terms that would result from arm's-length negotiations among unaffiliated third parties.

For example, the terms of New Senior's management agreement with our manager will be substantially similar to the terms of our existing management agreement. As a result, our manager will be entitled to earn a management fee from New Senior and will be eligible to receive incentive compensation based in part upon New Senior's achievement of targeted levels of funds from operations tested from the date of the spin-off and without regard to our prior performance.

**Our board of directors has reserved the right, in its sole discretion to abandon the spin-off of New Senior at any time prior to the date of the distribution of New Senior's common stock to the shareholders of Newcastle (the "Distribution Date"). In addition, the spin-off is subject to the satisfaction or waiver (by our board of directors in its sole discretion) of a number of conditions. We cannot assure that any or all of these conditions will be satisfied or waived.**

Our board of directors has reserved the right, in its sole discretion to abandon the spin-off at any time prior to the Distribution Date. This means Newcastle may cancel or delay the planned distribution of common stock of New Senior if at any time our board of directors determines that the distribution of such common stock is not in the best interests of Newcastle or that market conditions are such that it is not advisable to separate New Senior from Newcastle. If our board of directors determines to cancel the spin-off, our stockholders will not receive any distribution of New Senior common stock and we will be under no obligation to our

stockholders to distribute such shares. In addition, the spin-off is subject to the satisfaction or waiver (by our board of directors in its sole discretion) of a number of conditions. We cannot assure you that any or all of these conditions will be satisfied or waived. The fulfillment of the conditions to the spin-off will not create any obligation on our part to effect the distribution.

**The distribution of New Senior common stock will not qualify for tax-free treatment and may be taxable to you as a dividend.**

The distribution of New Senior common stock will not qualify for tax-free treatment. An amount equal to the fair market value of the shares of New Senior common stock received by each holder of record on the date of the distribution will be treated as a taxable dividend to the extent of each such holder's ratable share of our current or accumulated earnings and profits, as determined under federal income tax principles, with the excess treated first as a non-taxable return of capital to the extent of each such holder's tax basis in shares of our common stock and then as a taxable capital gain. In addition, we or other applicable withholding agents may be required or permitted to withhold at the applicable rate on all or a portion of the distribution payable to non-U.S. stockholders, and the company or any such agent would satisfy any such withholding obligation by withholding and selling a portion of the New Senior stock otherwise distributable to non-U.S. stockholders or by withholding from other property held in the non-U.S. stockholder's account with the withholding agent. A holder's tax basis in shares of our stock held at the time of the distribution will be reduced (but not below zero) to the extent the fair market value of the shares of New Senior common stock distributed to such holder if the distribution exceeds such holder's ratable share of the current and accumulated earnings and profits. A holder's holding period for such shares of our common stock will not be affected by the distribution. We will not be able to provide stockholders the amount of our current or accumulated earnings and profits until after the end of the 2014 calendar year.

Although we will be ascribing a value to New Senior's shares in the distribution for tax purposes, this valuation is not binding on the IRS or any other tax authority. These taxing authorities could ascribe a higher valuation to your shares, particularly if New Senior's stock trades at prices significantly above the value ascribed to the shares by us in the period following the distribution. Such a higher valuation may cause a larger reduction in the tax basis of your shares of us or may cause you to recognize additional dividend or capital gain income. You should consult your own tax advisor as to the particular tax consequences of the distribution to you.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

On May 7, 2014, a former employee of the Manager exercised 215,000 options with a weighted average exercise price of \$1.12, for an aggregate exercise price of \$0.2 million. Upon exercise, 215,000 shares of common stock of Newcastle were issued to the former employee. This transaction was exempt from registration pursuant to Section 4(a)(2) of the Securities Act.

**Item 3. Defaults upon Senior Securities**

None.

**Item 4. Mine Safety Disclosures**

None.

**Item 5. Other Information***Appointment of Principal Accounting Officer*

On August 6, 2014, our Board of Directors appointed Julien Hontang, 42, as our Principal Accounting Officer, effective as of August 11, 2014. Mr. Hontang will also become an employee of Fortress. Prior to joining Fortress, Mr. Hontang was a Business Unit Leader at KPMG and has over 18 years of accounting experience.

The Company's officers are appointed annually by the Board of Directors. There is no arrangement or understanding between Mr. Hontang and any other person pursuant to which he was appointed as an officer of Newcastle. There are also no family relationships between Mr. Hontang and any director or executive officer of the Company.

The Company's officers are not employees of the Company and do not receive direct cash compensation for services rendered to the Company. Rather, they are employees of the Company's manager and are compensated by the manager for their services to the Company as well as other entities affiliated with the manager. The manager has informed the Company that, because the services performed by the individuals who serve as officers of the Company are not performed exclusively for the Company, the manager cannot segregate and identify that portion of compensation awarded to, earned by or paid to the Company's officers, including Mr. Hontang, that relates solely to his services to the Company. Outside of the fees and compensation paid to the manager by the Company, Mr. Hontang does not have any direct or indirect material interests in any transaction with the Company or in any currently proposed transaction to which the Company is a party. Effective as of August 11, 2014, Mr. Jonathan Brown will resign as Principal Accounting Officer of the Company, but remains the Chief Accounting Officer of New Residential Investment Corp., a former subsidiary of Newcastle that was spun-off in May 2013.

*Director and Officer Indemnification Agreements*

On August 6, 2014, we entered into indemnification agreements with each of Wesley R. Edens, Kevin J. Finnerty, Stuart A. McFarland, David K. McKown and Alan L. Tyson as the directors of the Company, with Kenneth M. Riis as a director and officer of the Company and with each of Justine Cheng, Jonathan R. Brown and Randal A. Nardone as officers of the Company. In connection with the appointment of Mr. Hontang, we will have also entered into an indemnification agreement with Mr. Hontang, effective as of August 11, 2014.

Under the indemnification agreement with the Company's directors and officers, we, subject to certain limitations, have agreed to indemnify our directors and officers against certain liabilities arising out of service as a director or officer of the Company.

## Item 6. Exhibits

- 2.1 Separation and Distribution Agreement dated April 26, 2013, between New Residential Investment Corp. and the Registrant (incorporated by reference to the Registrant's Quarterly Report on Form 10-Q, Exhibit 2.1, filed on May 3, 2013).
- 3.1 Articles of Amendment and Restatement (incorporated by reference to the Registrant's Registration Statement on Form S-11 (File No. 333-90578), Exhibit 3.1).
- 3.2 Articles Supplementary relating to the Series B Preferred Stock (incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the period ended March 31, 2003, Exhibit 3.3).
- 3.3 Articles Supplementary Relating to the Series C Preferred Stock (incorporated by reference to the Registrant's Report on Form 8-K, Exhibit 3.3, filed on October 25, 2005).
- 3.4 Articles Supplementary Relating to the Series D Preferred Stock (incorporated by reference to the Registrant's Report on Form 8-A, Exhibit 3.1, filed on March 14, 2007).
- 3.5 Articles of Amendment (incorporated by reference to the Registrant's Report on Form 8-K, Exhibit 3.1, filed on June 10, 2013).
- 3.6 Amended and Restated By-laws (incorporated by reference to the Registrant's Registration Statement on Form 8-K, Exhibit 3.1, filed on May 5, 2006).
- 4.1 Junior Subordinated Indenture between Newcastle Investment Corp. and The Bank of New York Mellon Trust Company, National Association, dated April 30, 2009 (incorporated by reference to the Registrant's Report on Form 8-K, Exhibit 4.1, filed on May 4, 2009).
- 4.2 Pledge and Security Agreement between Newcastle Investment Corp. and The Bank of New York Mellon Trust Company, National Association, as trustee, dated April 30, 2009 (incorporated by reference to the Registrant's Report on Form 8-K, Exhibit 4.2, filed on May 4, 2009).
- 4.3 Pledge, Security Agreement and Account Control Agreement among Newcastle Investment Corp., NIC TP LLC, as pledgor, and The Bank of New York Mellon Trust Company, National Association, as bank and trustee, dated April 30, 2009 (incorporated by reference to the Registrant's Report on Form 8-K, Exhibit 4.3, filed on May 4, 2009).
- 10.1 Amended and Restated Management and Advisory Agreement by and among the Registrant and FIG LLC, dated April 25, 2013 (incorporated by reference to the Registrant's Quarterly Report on Form 10-Q, Exhibit 10.1, filed on May 3, 2013).
- 10.2 2012 Newcastle Investment Corp. Nonqualified Stock Option and Incentive Award Plan, adopted as of May 7, 2012 (incorporated by reference to the Registrant's Report on Form 10-K for the year ended December 31, 2012, Exhibit 10.3).
- 10.3 Exchange Agreement between Newcastle Investment Corp. and Taberna Preferred Funding IV, Ltd., Taberna Preferred Funding V, Ltd., Taberna Preferred Funding VI, Ltd. And Taberna Preferred Funding VII, Ltd., dated April 30, 2009 (incorporated by reference to the Registrant's Report on Form 8-K, Exhibit 10.1, filed on May 4, 2009).
- 10.4 Exchange Agreement, dated as of January 29, 2010, by and among Newcastle Investment Corp., Taberna Capital Management, LLC, Taberna Preferred Funding IV, Ltd., Taberna Preferred Funding V, Ltd., Taberna Preferred Funding VI, Ltd. And Taberna Preferred Funding VII, Ltd. (incorporated by reference to the Registrant's Report on Form 8-K, Exhibit 10.1, filed on February 2, 2010).
- 10.5 Master Designation Agreement, dated as of July 17, 2012, among B Healthcare Properties LLC and the designees listed on the signature pages attached thereto (incorporated by reference to the Registrant's Report on Form 8-K, Exhibit 10.1, filed on July 23, 2012).
- 10.6 Amended and Restated Purchase Agreement, dated as of February 27, 2012, by and among the Purchasers named therein, the Sellers named therein, the Former Sellers named therein and Walter C. Bowen (incorporated by reference to the Registrant's Report on Form 8-K, Exhibit 10.2, filed on July 23, 2012).
- 10.7 Amendment No. 1 to the Amended and Restated Purchase Agreement, dated as of March 30, 2012, among the Purchasers named therein, the Sellers named therein, BDC/West Covina II, LLC and Walter C. Bowen (incorporated by reference to the Registrant's Report on Form 8-K, Exhibit 10.3, filed on July 23, 2012).

- 10.8 Amendment No. 2 to the Amended and Restated Purchase Agreement, dated as of April 11, 2012, among the Purchasers named therein, the Sellers named therein and Walter C. Bowen (incorporated by reference to the Registrant's Report on Form 8-K, Exhibit 10.4, filed on July 23, 2012).
- 10.9 Amendment No. 3 to the Amended and Restated Purchase Agreement, dated as of April 27, 2012, among the Purchasers named therein, the Sellers named therein and Walter C. Bowen (incorporated by reference to the Registrant's Report on Form 8-K, Exhibit 10.5, filed on July 23, 2012).
- 10.10 Amendment No. 4 to the Amended and Restated Purchase Agreement, dated as of June 14, 2012, among the Purchasers named therein, the Sellers named therein and Walter C. Bowen (incorporated by reference to the Registrant's Report on Form 8-K, Exhibit 10.6, filed on July 23, 2012).
- 10.11 Amendment No. 5 to the Amended and Restated Purchase Agreement, dated as of July 16, 2012, among the Purchasers named therein, the Sellers named therein and Walter C. Bowen (incorporated by reference to the Registrant's Report on Form 8-K, Exhibit 10.7, filed on July 23, 2012).
- 10.12 Master Credit Facility Agreement, dated as of July 18, 2012, by and among the Borrowers named therein, Propco LLC, TRS LLC and Oak Grove Commercial Mortgage, LLC (incorporated by reference to the Registrant's Report on Form 8-K, Exhibit 10.8, filed on July 23, 2012).
- 10.13 Assignment of Master Credit Facility Agreement and Other Loan Documents, dated as of July 18, 2012, from Oak Grove Commercial Mortgage, LLC to Fannie Mae (incorporated by reference to the Registrant's Report on Form 8-K, Exhibit 10.9, filed on July 23, 2012).
- 10.14 Management Agreement, dated as of July 5, 2012, between Willow Park Management LLC and Willow Park Leasing LLC (incorporated by reference to the Registrant's Report on Form 8-K, Exhibit 10.10, filed on July 23, 2012).
- 10.15 Sale and Cooperation Agreement, dated September 7, 2012, among Newcastle Investment Corp., Barclays Bank PLC and ED LIMITED (incorporated by reference to the Registrant's Report on Form 10-Q, Exhibit 10.33, filed on October 26, 2012).
- 10.16 Purchase and Sale Agreement, dated November 18, 2013, by and between the Sellers named therein and the Purchasers named therein (incorporated by reference to the Registrant's Annual Report on Form 10-K, Exhibit 10.16, filed on March 3, 2014).
- 10.17 Master Lease, dated December 23, 2013, by and among the Landlords named therein and NCT Master Tenant I LLC (incorporated by reference to the Registrant's Annual Report on Form 10-K, Exhibit 10.17, filed on March 3, 2014).
- 10.18 Guaranty of Lease, dated December 23, 2013, by Holiday AL Holdings LP in favor of the Landlords named therein (incorporated by reference to the Registrant's Annual Report on Form 10-K, Exhibit 10.18, filed on March 3, 2014).
- 10.19 Form of Indemnification Agreement.
- 31.1 Certification of Chief Executive Officer as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of Chief Financial Officer as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101.INS\* XBRL Instance Document.
- 101.SCH\* XBRL Taxonomy Extension Schema Document.
- 101.CAL\* XBRL Taxonomy Extension Calculation Linkbase Document.
- 101.DEF\* XBRL Taxonomy Extension Definition Linkbase Document.
- 101.LAB\* XBRL Taxonomy Extension Label Linkbase Document.
- 101.PRE\* XBRL Taxonomy Extension Presentation Linkbase Document.

\*XBRL (Extensible Business Reporting Language) information is furnished and not filed for purposes of Sections 11 and 12 of the Securities Act of 1933 and Section 18 of the Securities Exchange Act of 1934.

The following management agreements are being omitted in reliance on Instruction 2 to Item 601 of Regulation S-K, as discussed in Item 1.01 on Form 8-K filed on July 23, 2012:

Management Agreement, dated as of July 5, 2012, between Sun Oak Management LLC and Sun Oak Leasing LLC.

Management Agreement, dated as of July 5, 2012, between Orchard Park Management LLC and Orchard Park Leasing LLC.

Management Agreement, dated as of July 5, 2012, between Desert Flower Management LLC and Desert Flower Leasing LLC.

Management Agreement, dated as of July 5, 2012, between Canyon Creek Property Management LLC and Canyon Creek Leasing LLC.

Management Agreement, dated as of July 5, 2012, between Regent Court Management LLC and Regent Court Leasing LLC.

Management Agreement, dated as of July 5, 2012, between Sunshine Villa Management LLC and Sunshine Villa Leasing LLC.

Management Agreement, dated as of July 5, 2012, between Sheldon Park Management LLC and Sheldon Park Leasing LLC.

In addition, the following Master Lease and Guaranty of Lease are substantially identical in all material respects, except as to the parties thereto, to the Master Lease and Guaranty of Lease that are filed as Exhibits 10.17 and 10.18, respectively, hereto and are being omitted in reliance on Instruction 2 to Item 601 of Regulation S-K:

- Master Lease, dated December 23, 2013, by and among the Landlords named therein and NCT Master Tenant II LLC.
- Guaranty of Lease, dated December 23, 2013, by Holiday AL Holdings LP in favor of the Landlords named therein.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized:

NEWCASTLE INVESTMENT CORP.

By: /s/ Kenneth M. Riis

Kenneth M. Riis

Chief Executive Officer and President

August 8, 2014

By: /s/ Justine A. Cheng

Justine A. Cheng

Chief Financial Officer, Chief Operating Officer and Treasurer

August 8, 2014

By: /s/ Jonathan R. Brown

Jonathan R. Brown

Principal Accounting Officer

August 8, 2014

EXHIBIT 10.19

FORM OF INDEMNIFICATION AGREEMENT

[FORM OF]  
INDEMNIFICATION AGREEMENT

AGREEMENT, dated as of \_\_\_\_\_, 2014 (this "Agreement"), between Newcastle Investment Corp., a Maryland corporation (the "Company"), and ("Indemnitee").

WHEREAS, it is essential to the Company to retain and attract as directors and officers the most capable persons available;

WHEREAS, Indemnitee is a director and/or officer of the Company;

WHEREAS, both the Company and Indemnitee recognize the increased risk of litigation and other claims being asserted against directors and officers of public companies in today's environment;

WHEREAS, the Company's Articles of Amendment and Restatement, as amended from time to time ("Charter"), and Amended and Restated Bylaws, as amended from time to time ("Bylaws"), require the Company to indemnify and advance expenses to its directors and officers to the fullest extent permitted by law and the Indemnitee has been serving and continues to serve as a director and/or officer of the Company in part in reliance on such Charter and Bylaws;

WHEREAS, uncertainties as to the availability of indemnification created by recent court decisions may increase the risk that the Company will be unable to retain and attract as directors and officers the most capable persons available;

WHEREAS, the board of directors of the Company ("Board of Directors") has determined that the inability of the Company to retain and attract as directors and officers the most capable persons would be detrimental to the interests of the Company and that the Company therefore should seek to assure such persons that indemnification and insurance coverage will be available in the future;

WHEREAS, the parties intend that any rights the Indemnitee may have from Indemnitee-Related Entities (as defined herein) shall be secondary to the primary obligation of the Company to indemnify and hold harmless the Indemnitee under this Agreement; and

WHEREAS, in recognition of Indemnitee's need for protection against personal liability, and in part to provide Indemnitee with specific contractual assurance that the protection promised by the Charter and Bylaws will be available to Indemnitee (regardless of, among other things, any amendment to or revocation of such Charter and Bylaws or any change in the composition of the Company's Board of Directors or acquisition transaction relating to the Company), the Company wishes to provide in this Agreement for the indemnification of and the advancing of expenses to Indemnitee to the fullest extent (whether partial or complete) permitted by law and as set forth in this Agreement, and for the continued coverage of Indemnitee under the directors' and officers' liability insurance policy of the Company.

NOW, THEREFORE, in consideration of the premises and of Indemnitee continuing to serve the Company directly or, at its request, another enterprise, and intending to be legally bound hereby, the parties hereto agree as follows:

1. Certain Definitions. In addition to terms defined elsewhere herein, the following terms have the following meanings when used in this Agreement:
-

- (a) Change in Control: shall be deemed to have occurred if (i) any “person” (as such term is used in Sections 13(d) and 14(d) of the Securities Exchange Act of 1934, as amended), other than Fortress Investment Group LLC and its affiliates and other than a trustee or other fiduciary holding securities under an employee benefit plan of the Company or a corporation owned directly or indirectly by the stockholders of the Company in substantially the same proportions as their ownership of shares of the Company, is or becomes the “beneficial owner” (as defined in Rule 13d-3 under said Act), directly or indirectly, of securities of the Company representing 20% or more of the total voting power represented by the Company’s then outstanding Voting Securities, or (ii) during any period of two consecutive years, individuals who at the beginning of such period constitute the Board of Directors and any new director whose election by the Board of Directors or nomination for election by the Company’s stockholders was approved by a vote of at least two-thirds (2/3) of the directors then still in office who either were directors at the beginning of the period or whose election or nomination for election was previously so approved, cease for any reason to constitute a majority thereof, or (iii) the stockholders of the Company approve a merger or consolidation of the Company with any other entity other than a merger or consolidation which would result in the Voting Securities of the Company outstanding immediately prior thereto continuing to represent (either by remaining outstanding or by being converted into Voting Securities of the surviving entity) at least 80% of the total voting power represented by the Voting Securities of the Company or such surviving entity outstanding immediately after such merger or consolidation, or the stockholders of the Company approve a plan of complete liquidation of the Company or an agreement for the sale or disposition by the Company of (in one transaction or a series of transactions) all or substantially all of the Company’s assets.
- (b) Claim: means any threatened, asserted, pending or completed action, suit or proceeding, whether civil, criminal, administrative, investigative or other, including any arbitration or other alternative dispute resolution mechanism, or any appeal of any kind thereof, or any inquiry or investigation, whether instituted by (or in the right of) the Company or any governmental agency or any other person or entity, in which Indemnitee was, is, may be or will be involved as a party, witness or otherwise.
- (c) ERISA: means the Employee Retirement Income Security Act of 1974, as amended.
- (d) Expenses: include attorneys’ fees and all other direct or indirect costs, expenses and obligations, including judgments, fines, penalties, interest, appeal bonds, amounts paid in settlement with the approval of the Company, and counsel fees and disbursements (including, without limitation, experts’ fees, court costs, retainers, appeal bond premiums, transcript fees, duplicating, printing and binding costs, as well as telecommunications, postage and courier charges) paid or incurred in connection with investigating, prosecuting, defending, being a witness in or participating in (including on appeal), or preparing to investigate, prosecute, defend, be a witness in or participate in, any Claim relating to any Indemnifiable Event, and shall include (without limitation) all attorneys’ fees and all other expenses incurred by or on behalf of an Indemnitee in connection with preparing and submitting any requests or statements for indemnification, advancement or any other right provided by this Agreement (including, without limitation, such fees or expenses incurred in connection with legal proceedings contemplated by Section 2(d) hereof).

- (e) Indemnifiable Amounts: means (i) any and all liabilities, Expenses, damages, judgments, fines, penalties, ERISA excise taxes and amounts paid in settlement (including all interest, assessments and other charges paid or payable in connection with or in respect of such liabilities, Expenses, damages, judgments, fines, penalties, ERISA excise taxes or amounts paid in settlement) arising out of or resulting from any Claim relating to an Indemnifiable Event, (ii) any liability pursuant to a loan guaranty or otherwise, for any indebtedness of the Company or any subsidiary of the Company, including, without limitation, any indebtedness which the Company or any subsidiary of the Company has assumed or taken subject to, and (iii) any liabilities which an Indemnitee incurs as a result of acting on behalf of the Company (whether as a fiduciary or otherwise) in connection with the operation, administration or maintenance of an employee benefit plan or any related trust or funding mechanism (whether such liabilities are in the form of excise taxes assessed by the United States Internal Revenue Service, penalties assessed by the Department of Labor, restitutions to such a plan or trust or other funding mechanism or to a participant or beneficiary of such plan, trust or other funding mechanism, or otherwise).
- (f) Indemnifiable Event: means any event or occurrence, whether occurring before, on or after the date of this Agreement, related to the fact that Indemnitee is or was a director and/or officer or fiduciary of the Company, or is or was serving at the request of the Company as a director, officer, employee, manager, member, partner, tax matter partner, trustee, agent, fiduciary or similar capacity, of another company, corporation, limited liability company, partnership, joint venture, employee benefit plan, trust or other entity or enterprise, or by reason of anything done or not done by Indemnitee in any such capacity (in all cases whether or not Indemnitee is acting or serving in any such capacity or has such status at the time any Indemnifiable Amount is incurred for which indemnification, advancement or any other right can be provided by this Agreement). The term "Company," where the context requires when used in this Agreement, may be construed to include such other company, corporation, limited liability company, partnership, joint venture, employee benefit plan, trust or other entity or enterprise.
- (g) Indemnitee-Related Entities: means any company, corporation, limited liability company, partnership, joint venture, trust, employee benefit plan or other entity or enterprise (other than the Company or any other company, corporation, limited liability company, partnership, joint venture, trust, employee benefit plan or other entity or enterprise Indemnitee has agreed, on behalf of the Company or at the Company's request, to serve as a director, officer, employee or agent and which service is covered by the indemnity described in this Agreement) from whom an Indemnitee may be entitled to indemnification or advancement of Expenses with respect to which, in whole or in part, the Company may also have an indemnification or advancement obligation.
- (h) Independent Legal Counsel: means an attorney or firm of attorneys (following a Change in Control, selected in accordance with the provisions of Section 3 hereof) who is experienced in matters of corporate law and who shall not have otherwise performed services for the Company or Indemnitee within the last five years (other than with respect to matters concerning the rights of Indemnitee under this Agreement, or of other indemnitees under similar indemnity agreements).
- (i) Jointly Indemnifiable Claim: means any Claim for which the Indemnitee may be entitled to indemnification from both an Indemnitee-Related Entity and the Company pursuant to applicable law, any indemnification agreement or the Charter,

by-laws, partnership agreement, operating agreement, certificate of formation, certificate of limited partnership or comparable organizational documents of the Company and an Indemnitee-Related Entity.

- (j) Reviewing Party: means any appropriate person or body consisting of a member or members of the Board of Directors or any other person or body appointed by the Board of Directors who is not a party to the particular Claim for which Indemnitee is seeking indemnification, or Independent Legal Counsel.
- (k) Voting Securities: means any securities of the Company which vote generally in the election of directors.

2. Basic Indemnification Arrangement: Advancement of Expenses

- (a) In the event Indemnitee was, is or becomes a party to or witness or other participant in, or is threatened to be made a party to or witness or other participant in, a Claim by reason of (or arising in part out of) an Indemnifiable Event, the Company shall indemnify Indemnitee, or cause Indemnitee to be indemnified, to the fullest extent permitted by law as soon as practicable but in any event no later than thirty (30) days after written demand is presented to the Company, and hold Indemnitee harmless against any and all Indemnifiable Amounts.
- (b) If so requested by Indemnitee, the Company shall advance, or cause to be advanced (within two business days of such request), any and all Expenses incurred by Indemnitee (an "Expense Advance"). The Company shall, in accordance with such request (but without duplication), either (i) pay, or cause to be paid, such Expenses on behalf of Indemnitee, or (ii) reimburse, or cause the reimbursement of, Indemnitee for such Expenses. Subject to Section 2(d), Indemnitee's right to an Expense Advance is absolute and shall not be subject to any prior determination by the Reviewing Party that the Indemnitee has satisfied any applicable standard of conduct for indemnification.
- (c) Notwithstanding anything in this Agreement to the contrary, Indemnitee shall not be entitled to indemnification or advancement of Expenses pursuant to this Agreement in connection with any Claim initiated by Indemnitee unless (i) the Company has joined in or the Board of Directors has authorized or consented to the initiation of such Claim or (ii) the Claim is one to enforce Indemnitee's rights under this Agreement.
- (d) Notwithstanding the foregoing, (i) the indemnification obligations of the Company under Section 2(a) shall be subject to the condition that the Reviewing Party shall not have determined (in a written legal opinion, in any case in which the Independent Legal Counsel is involved as required by Section 3 hereof) that Indemnitee would not be permitted to be indemnified under applicable law, and (ii) the obligation of the Company to make an Expense Advance pursuant to Section 2(b) shall be subject to the condition that, if, when and to the extent that the Reviewing Party determines (in a written legal opinion, in any case in which the Independent Legal Counsel is involved as required by Section 3 hereof) that Indemnitee would not be permitted to be so indemnified under applicable law, the Company shall be entitled to be reimbursed by Indemnitee (who hereby agrees to reimburse the Company) for all such amounts theretofore paid (it being understood and agreed that the foregoing agreement by Indemnitee shall be deemed to satisfy any requirement that Indemnitee provide the Company with an undertaking to repay any Expense Advance if it is ultimately determined that the Indemnitee is not entitled to

indemnification under applicable law); provided, however, that if Indemnitee has commenced or thereafter commences legal proceedings in a court of competent jurisdiction to secure a determination that Indemnitee should be indemnified under applicable law, any determination made by the Reviewing Party that Indemnitee would not be permitted to be indemnified under applicable law shall not be binding and Indemnitee shall not be required to reimburse the Company for any Expense Advance until a final judicial determination is made with respect thereto (as to which all rights of appeal therefrom have been exhausted or lapsed). Indemnitee's undertaking to repay such Expense Advances shall be unsecured and interest-free. If there has not been a Change in Control, the Reviewing Party shall be selected by the Board of Directors, and if there has been such a Change in Control, the Reviewing Party shall be the Independent Legal Counsel referred to in Section 3 hereof. If there has been no determination by the Reviewing Party within thirty (30) days after written demand is presented to the Company or if the Reviewing Party determines that Indemnitee would not be permitted to be indemnified in whole or in part under applicable law, Indemnitee shall have the right to commence litigation in any court in the State of New York or the State of Maryland having subject matter jurisdiction thereof and in which venue is proper seeking an initial determination by the court or challenging any such determination by the Reviewing Party or any aspect thereof, including the legal or factual bases therefor, and the Company hereby consents to service of process and to appear in any such proceeding. Any determination by the Reviewing Party otherwise shall be conclusive and binding on the Company and Indemnitee.

3. Change in Control. The Company agrees that if there is a Change in Control then with respect to all matters thereafter arising concerning the rights of Indemnitee to indemnity payments and Expense Advances under this Agreement or any provision of the Charter or the Bylaws now or hereafter in effect, the Company shall seek legal advice only from Independent Legal Counsel selected by Indemnitee and approved by the Company (which approval shall not be unreasonably delayed, conditioned or withheld). Such counsel, among other things, shall render its written opinion to the Company and Indemnitee as to whether and to what extent the Indemnitee would be permitted to be indemnified under applicable law. The Company agrees to pay the reasonable fees of the Independent Legal Counsel and to indemnify fully such counsel against any and all expenses (including attorneys' fees), claims, liabilities and damages arising out of or relating to this Agreement or its engagement pursuant hereto.

4. Indemnification for Additional Expenses. The Company shall indemnify, or cause the indemnification of, Indemnitee against any and all Expenses and, if requested by Indemnitee, shall advance such Expenses to Indemnitee subject to and in accordance with Section 2(b), which are incurred by Indemnitee in connection with any action brought by Indemnitee for (i) indemnification or an Expense Advance by the Company under this Agreement or any provision of the Charter or the Bylaws now or hereafter in effect and/or (ii) recovery under any directors' and officers' liability insurance policies maintained by the Company, regardless of whether Indemnitee ultimately is determined to be entitled to such indemnification, Expense Advance or insurance recovery, as the case may be; provided that Indemnitee shall be required to reimburse such Expenses in the event that a final judicial determination is made (as to which all rights of appeal therefrom have been exhausted or lapsed) that such action brought by Indemnitee, or the defense by Indemnitee of an action brought by the Company or any other person, as applicable, was frivolous or in bad faith.

5. Partial Indemnity, Etc. If Indemnitee is entitled under any provision of this Agreement to indemnification by the Company for some or a portion of the Expenses or other Indemnifiable Amounts in respect of a Claim but not, however, for all of the total amount thereof, the Company shall nevertheless indemnify Indemnitee for the portion thereof to which Indemnitee is entitled. Moreover, notwithstanding any other provision of this Agreement, to the extent that Indemnitee has been successful on the merits or otherwise in defense of any or all Claims relating in whole or in part to an Indemnifiable Event or in defense of any issue

or matter therein, including dismissal without prejudice, Indemnitee shall be indemnified against all Expenses incurred in connection therewith.

6. Burden of Proof, Etc. In connection with any determination by the Reviewing Party or otherwise as to whether Indemnitee is entitled to be indemnified hereunder the Reviewing Party, court, any finder of fact or other relevant person shall presume that the Indemnitee has satisfied the applicable standard of conduct and is entitled to indemnification, and the burden of proof shall be on the Company (or any other person or entity disputing such conclusions) to establish, by clear and convincing evidence, that Indemnitee is not so entitled.

7. Reliance as Safe Harbor. For purposes of this Agreement, Indemnitee shall be deemed to have acted in good faith and in a manner he or she reasonably believed to be in or not opposed to the best interests of the Company if Indemnitee's actions or omissions to act are taken in good faith reliance upon the records of the Company, including its financial statements, or upon information, opinions, reports or statements furnished to Indemnitee by the officers or employees of the Company in the course of their duties, or by committees of the Board of Directors, or by any other person (including legal counsel, accountants and financial advisors) as to matters Indemnitee reasonably believes are within such other person's professional or expert competence and who has been selected with reasonable care by or on behalf of the Company. In addition, the knowledge and/or actions, or failures to act, of any director, officer, agent or employee of the Company shall not be imputed to Indemnitee for purposes of determining the right to indemnity hereunder.

8. No Other Presumptions. For purposes of this Agreement, the termination of any Claim by judgment, order, settlement (whether with or without court approval) or conviction, or upon a plea of nolo contendere, or its equivalent, shall not create a presumption that Indemnitee did not meet any particular standard of conduct or have any particular belief or that a court has determined that indemnification is not permitted by applicable law. In addition, neither the failure of the Reviewing Party to have made a determination as to whether Indemnitee has met any particular standard of conduct or had any particular belief, nor an actual determination by the Reviewing Party that Indemnitee has not met such standard of conduct or did not have such belief, prior to the commencement of legal proceedings by Indemnitee to secure a judicial determination that Indemnitee should be indemnified under applicable law shall be a defense to Indemnitee's claim or create a presumption that Indemnitee has not met any particular standard of conduct or did not have any particular belief.

9. Nonexclusivity, Etc. The rights of the Indemnitee hereunder shall be in addition to any other rights Indemnitee may have under the Charter, the Bylaws or the Maryland General Corporation Law or otherwise. To the extent that a change in applicable law (whether by statute or judicial decision) permits greater indemnification by agreement than would be afforded currently under the Charter, the Bylaws or this Agreement, it is the intent of the parties hereto that Indemnitee shall enjoy by this Agreement the greater benefits so afforded by such change. To the extent that there is a conflict or inconsistency between the terms of this Agreement, the Charter or the Bylaws, it is the intent of the parties hereto that the Indemnitee shall enjoy the greater benefits regardless of whether contained herein or in the Charter or the Bylaws. No amendment or alteration of the Charter or the Bylaws or any other agreement shall adversely affect the rights provided to Indemnitee under this Agreement.

10. Liability Insurance. To the extent the Company maintains an insurance policy or policies providing directors' and officers' liability insurance, the Indemnitee shall be covered by such policy or policies in accordance with its or their terms to the maximum extent of the coverage available for the Company's directors and officers. If the Company has such insurance in effect at the time the Company receives from Indemnitee any notice of the commencement of an action, suit or proceeding, the Company shall give prompt notice of the commencement of such action, suit or proceeding to the insurers in accordance with the procedures set forth in the policy. The Company shall thereafter take all necessary or desirable action to cause such insurers to pay, on behalf of Indemnitee, all amounts payable as a result of such proceeding in accordance with the terms of such policy.

11. Period of Limitations. No legal action shall be brought and no cause of action shall be asserted by or in the right of the Company against Indemnitee, Indemnitee's spouse, heirs, executors or personal or legal representatives after the expiration of two years from the date of accrual of such cause of action, and any claim or cause of action of the Company shall be extinguished and deemed released unless asserted by the timely filing of a legal action within such two-year period; provided, however, that if any shorter period of limitations is otherwise applicable to any such cause of action such shorter period shall govern.

12. Amendments, Etc. No supplement, modification or amendment of this Agreement shall be binding unless executed in writing by both of the parties hereto. No waiver of any of the provisions of this Agreement shall be deemed or shall constitute a waiver of any other provisions hereof (whether or not similar) nor shall such waiver constitute a continuing waiver.

13. Subrogation. Subject to Section 14 hereof, in the event of payment under this Agreement, the Company shall be subrogated to the extent of such payment to all of the rights of recovery of Indemnitee, who shall execute all papers reasonably required and shall do everything that may be reasonably necessary to secure such rights, including the execution of such documents necessary to enable the Company effectively to bring suit to enforce such rights. The Company shall pay or reimburse all Expenses actually and reasonably incurred by Indemnitee in connection with such subrogation.

14. Jointly Indemnifiable Claims. Given that certain Jointly Indemnifiable Claims may arise due to the relationship between the Indemnitee-Related Entities and the Company and the service of the Indemnitee as a director and/or officer of the Company at the request of the Indemnitee-Related Entities, the Company acknowledges and agrees that the Company shall be fully and primarily responsible for the payment to the Indemnitee in respect of indemnification and advancement of expenses in connection with any such Jointly Indemnifiable Claim, pursuant to and in accordance with the terms of this Agreement, irrespective of any right of recovery the Indemnitee may have from the Indemnitee-Related Entities. Under no circumstance shall the Company be entitled to any right of subrogation or contribution by the Indemnitee-Related Entities and no right of recovery the Indemnitee may have from the Indemnitee-Related Entities shall reduce or otherwise alter the rights of the Indemnitee or the obligations of the Company hereunder. In the event that any of the Indemnitee-Related Entities shall make any payment to the Indemnitee in respect of indemnification or advancement of Expenses with respect to any Jointly Indemnifiable Claim, the Company agrees that such payment or advancement shall not extinguish or affect in any way the rights of the Indemnitee under this Agreement and further agrees that the Indemnitee-Related Entity making such payment shall be subrogated to the extent of such payment to all of the rights of recovery of the Indemnitee against the Company. Each of the Indemnitee-Related Entities shall be third-party beneficiaries with respect to this Section 14, entitled to enforce this Section 14 against the Company as though each such Indemnitee-Related Entity were a party to this Agreement.

15. No Duplication of Payments. Subject to Section 14 hereof, the Company shall not be liable under this Agreement to make any payment in connection with any Claim made against Indemnitee to the extent Indemnitee has otherwise actually received payment (under any insurance policy, or any provision of the Charter or the Bylaws or otherwise) of the amounts otherwise indemnifiable hereunder.

16. Defense of Claims. The Company shall be entitled to participate in the defense of any Claim relating to an Indemnifiable Event or to assume the defense thereof, with counsel reasonably satisfactory to the Indemnitee; provided that if Indemnitee believes, after consultation with counsel selected by Indemnitee, that (i) the use of counsel chosen by the Company to represent Indemnitee would present such counsel with an actual or potential conflict of interest, (ii) the named parties in any such Claim (including any impleaded parties) include both the Company, or any subsidiary of the Company, and Indemnitee and Indemnitee concludes that there may be one or more legal defenses available to him or her that are different from or in addition to those available to the Company or any subsidiary of the Company, or (iii) any such representation by such counsel would be precluded under the applicable standards of professional conduct then prevailing, then Indemnitee shall be entitled to retain separate counsel (but not more than one law firm plus, if applicable, local counsel in respect of any particular Claim) at the Company's expense. The Company shall not be liable

to Indemnitee under this Agreement for any amounts paid in settlement of any Claim relating to an Indemnifiable Event effected without the Company's prior written consent. The Company shall not, without the prior written consent of the Indemnitee, effect any settlement of any Claim relating to an Indemnifiable Event which the Indemnitee is or could have been a party unless such settlement solely involves the payment of money and includes a complete and unconditional release of Indemnitee from all liability on all claims that are the subject matter of such Claim. Neither the Company nor Indemnitee shall unreasonably withhold, condition or delay its or his or her consent to any proposed settlement; provided that Indemnitee may withhold consent to any settlement that does not provide a complete and unconditional release of Indemnitee. In no event shall Indemnitee be required to waive, prejudice or limit attorney-client privilege or work-product protection or other applicable privilege or protection.

17. No Adverse Settlement. The Company shall not seek, nor shall it agree to, consent to, support, or agree not to contest any settlement or other resolution of any Claim(s), or settlement or other resolution of any other claim, action, proceeding, demand, investigation or other matter that has the actual or purported effect of extinguishing, limiting or impairing Indemnitee's rights hereunder, including without limitation the entry of any bar order or other order, decree or stipulation, pursuant to 15 U.S.C. § 78u-4 (the Private Securities Litigation Reform Act), or any similar foreign, federal or state statute, regulation, rule or law.

18. Binding Effect, Etc. This Agreement shall be binding upon and inure to the benefit of and be enforceable by the parties hereto and their respective successors, (including any direct or indirect successor or continuing company by purchase, merger, consolidation or otherwise to all or substantially all of the business and/or assets of the Company), assigns, spouses, heirs, executors and personal and legal representatives. The Company shall require and cause any successor (whether direct or indirect by purchase, merger, consolidation, or otherwise) to all or substantially all of the business and/or assets of the Company, by written agreement in form and substance satisfactory to Indemnitee and his or her counsel, expressly to assume and agree to perform this Agreement in the same manner and to the same extent that the Company would be required to perform if no such succession had taken place. This Agreement shall continue in effect regardless of whether Indemnitee continues to serve as an officer and/or director of the Company or of any other entity or enterprise at the Company's request.

19. Security. To the extent requested by Indemnitee and approved by the Board of Directors, the Company may at any time and from time to time provide security to Indemnitee for the obligations of the Company hereunder through an irrevocable bank line of credit, funded trust or other collateral or by other means. Any such security, once provided to Indemnitee, may not be revoked or released without the prior written consent of such Indemnitee.

20. Severability. If any provision or provisions of this Agreement shall be held to be invalid, illegal or unenforceable for any reason whatsoever, (a) the validity, legality and enforceability of the remaining provisions of this Agreement (including, without limitation, all portions of any paragraph of this Agreement containing any such provision held to be invalid, illegal or unenforceable, that are not themselves invalid, illegal or unenforceable) shall not in any way be affected or impaired thereby and (b) to the fullest extent possible, the provisions of this Agreement (including, without limitation, all portions of any paragraph of this Agreement containing any such provision held to be invalid, illegal or unenforceable) shall be construed so as to give effect to the intent manifested by the provision held invalid, illegal or unenforceable and to give effect to the terms of this Agreement.

21. Specific Performance, Etc. The parties recognize that if any provision of this Agreement is violated by the Company, Indemnitee may be without an adequate remedy at law. Accordingly, in the event of any such violation, Indemnitee shall be entitled, if Indemnitee so elects, to institute proceedings, either in law or at equity, to obtain damages, to enforce specific performance, to enjoin such violation, or to obtain any relief or any combination of the foregoing as Indemnitee may elect to pursue.

22. Notices. All notices, requests, consents and other communications hereunder to any party shall be deemed to be sufficient if contained in a written document delivered in person or sent by facsimile, nationally recognized overnight courier or personal delivery, addressed to such party at the address set forth below or such other address as may hereafter be designated on the signature pages of this Agreement or in writing by such party to the other parties:

(a) If to the Company, to:

Newcastle Investment Corp.  
c/o FIG LLC  
1345 Avenue of the Americas  
New York, New York 10105  
Attention: Randal A. Nardone  
Fax: [ ]

with a copy (which shall not constitute notice) to:

Skadden, Arps, Slate, Meagher & Flom LLP  
Four Times Square  
New York, New York 10036-6522  
Fax: (212) 735-2000  
Attn: Gregory Fericola, Esq.

(b) If to the Indemnitee, to the address set forth on Annex A hereto.

All such notices, requests, consents and other communications shall be deemed to have been given or made if and when received (including by overnight courier) by the parties at the above addresses or sent by electronic transmission, with confirmation received, to the facsimile numbers specified above (or at such other address or facsimile number for a party as shall be specified by like notice). Any notice delivered by any party hereto to any other party hereto shall also be delivered to each other party hereto simultaneously with delivery to the first party receiving such notice.

23. Counterparts. This Agreement may be executed in counterparts, each of which shall for all purposes be deemed to be an original but all of which together shall constitute one and the same agreement. Only one such counterpart signed by the party against whom enforceability is sought needs to be produced to evidence the existence of this Agreement.

24. Headings. The headings of the sections and paragraphs of this Agreement are inserted for convenience only and shall not be deemed to constitute part of this Agreement or to affect the construction or interpretation thereof.

25. Governing Law. This Agreement shall be governed by and construed and enforced in accordance with the laws of the State of Maryland applicable to contracts made and to be performed in such state without giving effect to the principles of conflicts of laws.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the date first above written.

NEWCASTLE INVESTMENT CORP.

Name: \_\_\_\_\_  
Title: \_\_\_\_\_

By: \_\_\_\_\_

\_\_\_\_\_  
[Indemnitee]

[SIGNATURE PAGE TO INDEMNIFICATION AGREEMENT]

EXHIBIT 31.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER

I, Kenneth M. Riis, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Newcastle Investment Corp.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

August 8, 2014

/s/ Kenneth M. Riis

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Kenneth M. Riis

Chief Executive Officer

**EXHIBIT 31.2**

**CERTIFICATION OF CHIEF FINANCIAL OFFICER**

I, Justine A. Cheng, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Newcastle Investment Corp.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

August 8, 2014

/s/ Justine A. Cheng

Justine A. Cheng

Chief Financial Officer, Chief Operating Officer and Treasurer

**EXHIBIT 32.1**

**CERTIFICATION OF CEO PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-Q of Newcastle Investment Corp. (the "Company") for the quarterly period ended June 30, 2014 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), Kenneth M. Riis, as Chief Executive Officer of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of his knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934;  
and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Kenneth M. Riis

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Kenneth M. Riis

Chief Executive Officer

August 8, 2014

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.

A signed original of this written statement required by Section 906 of the Sarbanes-Oxley Act of 2002 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

**EXHIBIT 32.2**

**CERTIFICATION OF CFO PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-Q of Newcastle Investment Corp. (the "Company") for the quarterly period ended June 30, 2014 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), Justine A. Cheng, as Chief Financial Officer of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of his knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934;  
and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Justine A. Cheng

Justine A. Cheng

Chief Financial Officer, Chief Operating Officer and Treasurer

August 8, 2014

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.

A signed original of this written statement required by Section 906 of the Sarbanes-Oxley Act of 2002 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.