

Edgar Filing: Colony Financial, Inc. - Form 10-K

Colony Financial, Inc.  
Form 10-K  
February 27, 2014  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-K

✓ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended December 31, 2013

OR

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

Commission file number 001-34456

COLONY FINANCIAL, INC.

(Exact Name of Registrant as Specified in Its Charter)

Maryland  
(State or Other Jurisdiction of  
Incorporation or Organization)

27-0419483  
(I.R.S. Employer  
Identification No.)

2450 Broadway, 6th Floor  
Santa Monica, California  
(Address of Principal Executive  
Offices)

90404  
(Zip Code)

(310) 282-8820

(Registrant's Telephone Number, Including Area Code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, \$0.01 par value	New York Stock Exchange
Series A Cumulative Redeemable Preferred Stock, \$0.01 par value	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☒

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

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

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

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

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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.

Large Accelerated Filer	Accelerated Filer	“
Non-Accelerated Filer	Smaller Reporting Company	“

(Do not check if a smaller reporting company)

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

The aggregate market value of voting and non-voting common equity held by non-affiliates of the registrant was approximately \$1.3 billion as of the last business day of the registrant’s most recently completed second fiscal quarter based upon the price at which the common shares were last sold on that day.

As of February 27, 2014, 77,409,374 shares of the Registrant’s common stock, par value \$0.01 per share, were outstanding.

### DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Company’s Proxy Statement with respect to its 2014 Annual Meeting of Stockholders to be filed not later than 120 days after the end of the Company’s fiscal year are incorporated by reference into Part III of this Form 10-K.

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### FORWARD-LOOKING STATEMENTS

Some of the statements contained in this Annual Report constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and we intend such statements to be covered by the safe harbor provisions contained therein. Forward-looking statements relate to expectations, beliefs, projections, future plans and strategies, anticipated events or trends and similar expressions concerning matters that are not historical facts. In some cases, you can identify forward-looking statements by the use of forward-looking terminology such as “may,” “will,” “should,” “expects,” “intends,” “plans,” “anticipates,” “believes,” “estimates,” “predicts,” or “potential” or the negative of these words and phrases or similar words or phrases which are predictions of or indicate future events or trends and which do not relate solely to historical matters. You can also identify forward-looking statements by discussions of strategy, plans or intentions.

The forward-looking statements contained in this Annual Report reflect our current views about future events and are subject to numerous known and unknown risks, uncertainties, assumptions and changes in circumstances that may cause our actual results to differ significantly from those expressed in any forward-looking statement. Statements regarding the following subjects, among others, may be forward-looking:

- market trends in our industry, interest rates, real estate values, the debt securities markets or the general economy or the demand for commercial real estate loans;
- our business and investment strategy, including the ability of CAH Operating Partnership, L.P. (“CAH OP,” otherwise known as Colony American Homes) (in which we have a significant investment) to execute its single-family home rental strategy;
- our projected operating results;
- actions and initiatives of the U.S. government and changes to U.S. government policies and the execution and impact of these actions, initiatives and policies;
- the state of the U.S. economy generally or in specific geographic regions;
- our ability to obtain and maintain financing arrangements, including securitizations;
- the amount of commercial mortgage loans requiring refinancing in future periods;
- the availability of attractive investment opportunities;
- the availability and costs of debt financing from traditional lenders;
- the volume of short-term loan extensions;
- the demand for new capital to replace maturing loans;
- the amount of capital we intend to invest in our single-family home rental strategy in the near term;
- our expected leverage;
- general volatility of the securities markets in which we participate;
- changes in the value of our assets;
- interest rate mismatches between our target assets and any borrowings used to fund such assets;
- changes in interest rates and the market value of our target assets;
- changes in prepayment rates on our target assets;
- effects of hedging instruments on our target assets;
- rates of default or decreased recovery rates on our target assets;
- the degree to which our hedging strategies may or may not protect us from interest rate volatility;
- impact of and changes in governmental regulations, tax law and rates, accounting guidance and similar matters;
- our ability to maintain our qualification as a real estate investment trust (“REIT”) for U.S. federal income tax purposes;
- our ability to maintain our exemption from registration as an investment company under the Investment Company Act of 1940, as amended (the “1940 Act”);
- availability of opportunities to acquire commercial mortgage-related, real estate-related and other securities;
- availability of qualified personnel;
- estimates relating to our ability to make distributions to our stockholders in the future; and
- our understanding of our competition.

While forward-looking statements reflect our good faith beliefs, assumptions and expectations, they are not guarantees of future performance. Furthermore, we disclaim any obligation to publicly update or revise any forward-looking

statement to reflect changes in underlying assumptions or factors, of new information, data or methods, future events or other changes. We caution investors not to place undue reliance on these forward-looking statements and urge you to carefully review the disclosures we make concerning risks in sections entitled “Risk Factors” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations.”

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PART I

ITEM 1. Business.

In this Annual Report on Form 10-K (this “Annual Report”) we refer to Colony Financial, Inc. as “we,” “us,” “Company,” or “our,” unless we specifically state otherwise or the context indicates otherwise. We refer to our manager, Colony Financial Manager, LLC, as our “Manager,” and the parent company of our Manager, Colony Capital, LLC, together with its consolidated subsidiaries (other than us), as “Colony Capital.”

**Our Company**

Colony Financial, Inc. is a real estate investment and finance company that is focused on acquiring, originating and managing a diversified portfolio of real estate-related debt and equity investments at attractive risk-adjusted returns. Our investment portfolio and target assets are primarily composed of interests in: (i) real estate and real estate-related debt, including loans acquired at a discount to par in the secondary market and new originations; and (ii) real estate equity, including single family homes held as rental investment properties. Secondary debt purchases may include performing, sub-performing or non-performing loans (including loan-to-own strategies). We were organized on June 23, 2009 as a Maryland corporation and completed our initial public offering (“IPO”) in September 2009. Our objective is to provide attractive risk-adjusted returns to our investors through a diversified portfolio of real estate-related debt and equity investments, including single-family homes to be rented to tenants. The total return profile of our investments is composed of both current yield, which is distributed through regular-way dividends, and capital appreciation potential, which is distributed through regular-way and/or special dividends.

We are organized and conduct our operations to qualify as a REIT, and generally are not subject to U.S. federal income taxes on our taxable income to the extent that we annually distribute all of our taxable income to stockholders and maintain qualification as a REIT, although we are subject to U.S. federal income tax on income earned through our taxable subsidiaries. We also operate our business in a manner that will permit us to maintain our exemption from registration as an investment company under the 1940 Act.

We are externally managed and advised by our Manager pursuant to the terms of a management agreement. Our Manager is a wholly-owned subsidiary of Colony Capital, a privately held independent global real estate investment firm founded in 1991 by Thomas J. Barrack, Jr., our Executive Chairman.

Our principal executive offices are located at 2450 Broadway, 6<sup>th</sup> Floor, Santa Monica, CA, 90404. Our telephone number is (310) 282-8820, and our website address is [www.colonyfinancial.com](http://www.colonyfinancial.com).

**Our Investment Strategy**

We seek to provide attractive risk-adjusted returns to our investors, primarily through real estate and real estate-related debt and equity investments and active management of a diversified portfolio of our target assets. The primary tenet upon which this objective relies is our ability to identify assets from which we can extract value through a combination of current yield and/or capital appreciation. This approach is driven by a disciplined investment strategy, focused on the following:

capitalizing on asset level underwriting experience and market analytics to identify investments with pricing dislocations and attractive risk-return profiles that can be purchased at meaningful discounts to our estimates of intrinsic value;

creating capital appreciation opportunities by resolving sub-performing or non-performing loans through repositioning, restructuring and active management of those assets;

seeking to acquire assets held for sale that are undervalued as a result of operating uncertainty or liquidity constraints; originating and structuring senior and/or junior loans with attractive return profiles relative to the underlying value and financial operating performance of the real estate collateral and the strength and quality of the sponsorship; retaining control, where possible, over the formulation and execution of the management strategies with respect to our assets, including the restructuring of non-performing or sub-performing loans, the negotiation of discounted pay-offs or other modification of the terms governing a loan, and, if necessary, the foreclosure and active management of assets underlying non-performing loans in order to reposition them for disposition; and

structuring transactions with a prudent amount of leverage, if any, given the risk of the underlying asset's cash flows, attempting to match the structure and duration of the financing with the underlying asset's cash flows, including through the use of hedges, as appropriate.

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In implementing our investment strategy, we utilize our Manager's and its affiliates' expertise in identifying attractive investment opportunities primarily within the target asset classes described below, as well as their transaction sourcing, underwriting, execution and asset management and disposition capabilities. Our Manager makes decisions based on a variety of factors, including expected risk-adjusted returns, underlying real estate and credit fundamentals, liquidity, availability of adequate financing, borrowing costs and macro-economic conditions. In addition, all investment decisions are made with a view to maintaining our qualification as a REIT and our exemption from registration as an investment company under the 1940 Act.

We believe there are abundant opportunities among our target assets that currently present attractive risk-return profiles. However, our investment strategy is dynamic and flexible, which enables us to adapt to shifts in economic, real estate and capital market conditions and to exploit inefficiencies around the world. Consistent with this strategy, in order to capitalize on the investment opportunities that may be present in various other points of an economic cycle, we may expand or change our investment strategy or target assets over time in response to opportunities available in different economic and capital market conditions. We believe that the diversification of the portfolio of assets that we have acquired, our ability to acquire, originate and manage our target assets and the flexibility of our strategy will position us to identify undervalued opportunities and to generate attractive long-term returns for our stockholders in a variety of market conditions.

For detailed information about our investments, see "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations—Our Investments"

### **Our Target Assets**

Our primary target asset classes and the principal assets within each class are as follows:

**Loan Acquisitions.** The acquisition of mortgage loans, or portfolios of mortgage loans, secured by first or second liens on commercial properties, including office buildings, industrial or warehouse properties, hotels, retail properties, apartments and properties within other commercial real estate sectors, which may include performing, sub-performing and non-performing loans. In particular, we have invested and intend to continue to invest in portfolios of commercial whole loans acquired from the Federal Deposit Insurance Corporation (the "FDIC"), other governmental agencies and financial institutions. In some cases, we may also acquire a pari passu or junior participation in a whole loan.

**Mortgage Loan Originations.** The origination of whole mortgage loans to commercial property owners and developers. In some cases, we may originate and fund a first mortgage loan with the intention of structuring and selling a senior tranche ("A-note") and retaining the subordinated tranche ("B-note"). In other cases, we may co-originate and fund a B-note alongside another lender who co-originate and contemporaneously funds the A-note. We may also seek to finance a mortgage loan or loan participation with non-recourse, matched term financing either individually or by contributing a loan into a pooled securitized financing structure.

**Mezzanine Loans.** The origination or acquisition of loans made to property owners that are subordinate to mortgage debt and are typically secured by pledges of the borrower's ownership interests in the property and/or direct or indirect entities that own the property.

**Preferred Equity.** The origination or acquisition of a preferred equity investment in an existing or to-be-built commercial property or portfolio of commercial real estate, typically structured to receive cash distributions in seniority to a more junior class of equity. Equity interests may be subordinate to other forms of mortgage or property-level debt. Preferred equity may have a current pay requirement or an ability to accrue the preferred return but in the latter case, accruals usually must be paid current prior to distributions to the more junior equity class.

**Common Equity.** Investment in the common equity of an existing or to-be-built commercial property or portfolio of commercial real estate, typically targeting a higher yielding, opportunistic strategy to reposition, recapitalize, renovate or otherwise stabilize the underlying property or properties. We may also include third-party operating and/or other financial partners in these transactions.

**Real Estate Platforms.** Investment in real estate operating platforms that typically are focused on specific property types and/or geographic markets with high quality, experienced management teams. These real estate operating platforms may raise equity capital from other investors or limited partners and our investment would typically involve



taking an ownership stake in the manager or general partner interest.

- Triple Net Lease Properties. The acquisition of real property that is capable of being, or already, occupied by creditworthy tenants subject to long-term, triple net leases.

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Home Ownership/Rental Program. Through our interest in CAH OP, we may acquire residential homes from trustee sales, Multiple Listing Service ("MLS"), private investors, financial institutions, government sponsored entities such as Fannie Mae and Freddie Mac, and other sources, which are rented to tenants and held for investment purposes.

Loan-to-Own. The acquisition of mortgage loans or other real estate-related loans or debt investments with the expectation of subsequently foreclosing on, or otherwise taking control of, the property securing the loan or investment, which are generally referred to as "loan-to-own" investments.

Real Estate Owned ("REO") Properties. In certain instances, we also may invest in commercial and residential REO properties, which are properties owned by a governmental agency or lender after a loan default and subsequent seizure of collateral.

Commercial Real Estate-Backed Securities. CMBS, collateralized debt obligations ("CDOs") and certain collateralized loan obligations ("CLOs") are securities that are collateralized by, or evidence ownership interests in, a single commercial mortgage loan or a partial or entire pool of mortgage loans secured by commercial properties and/or securities backed by interests in commercial property loans.

Other Assets. We may also invest in other commercial real estate-related debt investments, such as loans to REITs and real estate operating companies ("REOCs") and corporate bonds of REITs and REOCs; debtor-in-possession ("DIP") loans, minority equity ownership interests in banks, residential mortgage-backed securities ("RMBS"); construction/rehabilitation loans; loans to providers of real estate net lease financing; residential mortgage loans or other interests in residential properties; other real estate-related financial assets and investments, including preferred stock and convertible debt securities of REITs and REOCs, credit default swaps and other derivative securities; collateralized debt obligations; and non-real estate-related debt investments.

### Our Investment Guidelines

Our board of directors has adopted a set of investment guidelines that set out the asset classes and other criteria to be used to evaluate the merits of specific investments as well as our overall portfolio composition. We pursue investments that have the potential to generate attractive risk-adjusted returns, consistent with maintaining our qualification as a REIT for U.S. federal income tax purposes and our exemption from registration under the 1940 Act. However, we have no prescribed limitation on any particular investment type.

Our board of directors has adopted the following investment guidelines:

- no investment shall be made that would cause us to fail to qualify as a REIT for U.S. federal income tax purposes;
- no investment shall be made that would cause us to be regulated as an investment company under the 1940 Act; and

until appropriate investments can be identified, our Manager may invest the proceeds of our equity offerings in interest-bearing, short-term investments, including money market accounts and/or U.S. treasury securities, that are consistent with our intention to maintain our status as a REIT and our exemption from registration under the 1940 Act.

Any investment of our capital of up to \$10 million requires the approval of our chief executive officer; any investment in excess of \$10 million but less than \$150 million requires the approval of our Investment Committee; and any investment greater than or equal to \$150 million requires the approval of our board of directors.

Our investment guidelines do not limit the amount of our equity that may be invested in any particular class or type within our target asset classes. Our investment decisions depend upon prevailing market conditions and may change over time in response to opportunities available in different economic and capital market environments. As a result, we cannot predict the percentage of our equity that will be invested in any particular asset at any given time. We believe that the flexibility of our investment strategy, combined with our Manager's and its affiliates' experience executing various investment strategies, enables us to exploit changes in the capital markets and provides attractive risk-adjusted long-term returns to our stockholders throughout the various stages of an economic cycle.

These investment guidelines may be changed or waived from time to time by our board of directors (which must include a majority of our independent directors) without the approval of our stockholders, and we expect to disclose any such changes or waivers to our investment guidelines in the periodic reports we file with the Securities and Exchange Commission (the "SEC").

### Segments

We currently operate in three reportable segments: (1) real estate debt investments, which include originated and acquired commercial real estate debt, mortgage-backed securities, and other debt-related investments, (2) single-family residential rentals through our investment in CAH OP, and (3) other real estate equity investments. For operating and financial

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information about segments, see Note 18 to our consolidated financial statements included in this Annual Report and “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations.”

### **Risk Management**

Risk management is a significant component of our strategy to deliver consistent risk-adjusted returns to our stockholders. Subject to maintaining our qualification as a REIT for U.S. federal income tax purposes and our exemption from registration under the 1940 Act, our Manager closely monitors our portfolio and actively manages risks associated with, among other things, our assets and interest rates. In addition, the Audit Committee of our board of directors, in consultation with management, periodically reviews our policies with respect to risk assessment and risk management, including key risks to which we are subject, including credit risk, liquidity risk, financing risk, foreign currency risk and market risk, and the steps that management has taken to monitor and control such risks.

### **Underwriting**

Prior to making any debt or equity investment, our Manager’s underwriting team, in conjunction with third party providers, undertakes a rigorous asset-level due diligence process, involving intensive data collection and analysis, to ensure that we understand fully the state of the market and the risk-reward profile of the asset. The credit risk of any particular loan investment, whether an originated loan or an acquired loan or portfolio of loans, is built into the pricing in the form of contractual interest rates, related fees charged to the borrower, estimated transaction costs, discount to acquired principal balance, among other things. Key metrics considered during the underwriting process include, but are not limited to, loan-to-collateral value ratios (“LTV”), debt service coverage ratios (“DSCR”), debt yields, sponsor credit ratings and history, and tenant credit ratings and diversity. In addition to evaluating the merits of any particular proposed investment, our Manager evaluates the diversification of our portfolio of assets. Prior to making a final investment decision, our Manager determines whether a target asset will cause our portfolio of assets to be too heavily concentrated with, or cause too much risk exposure to, any one borrower, real estate sector, geographic region, source of cash flow for payment or other geopolitical issues. If our Manager determines that a proposed acquisition presents excessive concentration risk, it may determine not to acquire an otherwise attractive asset.

### **Asset Management**

For each asset that we originate or acquire, Colony Capital’s asset management team engages in active management of the asset, the intensity of which depends on the attendant risks. Once an asset manager has been assigned to a particular asset, the manager works collaboratively with the underwriting team to formulate a strategic plan for the particular asset, which includes evaluating the underlying collateral and updating valuation assumptions to reflect changes in the real estate market and the general economy. This plan also generally outlines several strategies for the asset to extract the maximum amount of value from each asset under a variety of market conditions. Such strategies vary depending on the type of asset, our position in the capitalization of the investment, the availability of refinancing options and in the case of debt investments, recourse and maturity. As long as an asset is in our portfolio, our Manager and its affiliates track the progress of an asset against the original business plan to ensure that the attendant risks of continuing to own the asset do not outweigh the associated rewards.

Asset management strategies for our debt investments may include, among others, the restructuring of non-performing or sub-performing loans, the negotiation of discounted pay-offs or other modification of the terms governing a loan, and the foreclosure and management of assets underlying non-performing loans in order to reposition them for profitable disposition. We monitor and evaluate period to period changes in portfolio credit risk, focusing on borrower payment history and delinquencies and, if warranted, LTV. We do not have a policy to obtain routine valuations on the underlying loan collateral if there are no indicators of significant change in the value of that collateral. We may also review other information such as (i) financial data (DSCR, debt yields, delinquencies and performing status), (ii) collateral characteristics (property occupancy, tenant profiles, rental rates, operating expenses, site inspections, capitalization and discount rates), (iii) the borrower/sponsor’s exit plan, and (iv) current credit spreads and discussions with market participants. Because of the diverse nature of acquired loans, the availability and relevance of these metrics vary significantly by loan.

We actively manage our equity investments in commercial real estate with similar rigor. We regularly reassess whether major decisions such as financing, leasing, capital expenditures, property management or disposition need to

be taken to optimize the performance of the underlying investment. These decisions are generally made after a thorough review of asset and market specific factors that may include (i) property financial data including historic and budgeted financial statements, liquidity and capital expenditure plans, and debt financing (ii) property operating metrics (including occupancy, leasing activity, lease expirations, sales information, tenant credit review, tenant delinquency reports, operating expense efficiency and property management efficacy) and (iii) local real estate market conditions including vacancy rates, absorption, new supply, rent levels and comparable sale transactions. Subject to maintaining our qualification as a REIT for U.S. federal income tax purposes and our exemption from registration under the 1940 Act, we currently expect that we will typically hold assets that we originate or acquire for between

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three and ten years. However, in order to maximize returns and manage portfolio risk while remaining opportunistic, we may dispose of an asset earlier than anticipated or hold an asset longer than anticipated if we determine it to be appropriate depending upon prevailing market conditions or factors regarding a particular asset. We can provide no assurances, however, that we will be successful in identifying or managing all of the risks associated with acquiring, holding or disposing of a particular asset or that we will not realize losses on certain assets.

### Interest Rate and Foreign Currency Hedging

Subject to maintaining our qualification as a REIT for U.S. federal income tax purposes and our exemption from registration under the 1940 Act, we may mitigate the risk of interest rate volatility through the use of hedging instruments, such as interest rate swap agreements and interest rate cap agreements. The goal of our interest rate management strategy is to minimize or eliminate the effects of interest rate changes on the value of our assets, to improve risk-adjusted returns and, where possible, to lock in, on a long-term basis, a favorable spread between the yield on our assets and the cost of financing such assets. In addition, because we are exposed to foreign currency exchange rate fluctuations, we employ foreign currency risk management strategies, including the use of, among others, currency hedges. We can provide no assurances, however, that our efforts to manage interest rate and foreign currency exchange rate volatility will successfully mitigate the risks of such volatility on our portfolio.

### Leverage Policies

We may use limited investment-level financing such as the seller financing provided by the FDIC and non-recourse financing on some of our loan portfolios and equity investments, with a debt-to-equity ratio of less than 3-to-1 in the aggregate for the Company, including temporary borrowings from our general corporate credit and warehouse facilities. While we believe we can achieve attractive yields on an unleveraged basis, we will continue to use prudent amounts of leverage to increase potential returns to our stockholders and/or to finance future investments. We consider these leverage ratios to be prudent for our target asset classes. Our decision to use leverage currently or in the future to finance our assets will be based on our Manager's assessment of a variety of factors, including, among others, the anticipated liquidity and price volatility of the assets in our investment portfolio, the potential for losses and extension risk in our portfolio, the ability to raise additional equity to reduce leverage and create liquidity for future investments, the availability of credit at favorable prices or at all, the credit quality of our assets and our outlook for borrowing costs relative to the interest income earned on our assets. Our decision to use leverage in the future to finance our assets will be at the discretion of our Manager and will not be subject to the approval of our stockholders, and we are not restricted by our governing documents or otherwise in the amount of leverage that we may use. To the extent that we use leverage in the future, we may mitigate interest rate risk through utilization of hedging instruments, primarily interest rate swap and cap agreements, to serve as a hedge against future interest rate increases on our borrowings.

### Our Manager

We are externally managed and advised by our Manager. Each of our officers is an executive of Colony Capital. However, Darren J. Tangen, our chief operating officer and chief financial officer, is seconded exclusively to us pursuant to a secondment agreement with Colony Capital.

Our Manager provides the day-to-day management of our operations in conformity with the investment guidelines and other policies that are approved and monitored by our board of directors. Our Manager is responsible for (1) the selection, purchase and sale of our portfolio investments, (2) our financing activities, and (3) providing us with investment advisory services.

### Co-Investment Funds

Certain current or future private investment funds or other investment vehicles managed by Colony Capital or its affiliates (collectively, "Co-Investment Funds") may have the right to co-invest with us in our target assets, subject to us and each Co-Investment Fund having capital available for investment and the determination by our Manager and the general partner of each Co-Investment Fund (which is or will be an affiliate of Colony Capital) that the proposed investment is suitable for us and such Co-Investment Fund, respectively.

To address certain potential conflicts arising from our relationship with Colony Capital or its affiliates, pursuant to an investment allocation agreement among our Manager, Colony Capital and us, our Manager and Colony Capital have agreed that, for so long as the management agreement is in effect, neither they nor any of their affiliates will sponsor

or manage (i) any additional publicly traded investment vehicle that will primarily acquire or originate assets secured by U.S. collateral that are substantially similar to our target assets, (ii) any publicly traded investment vehicle that will primarily acquire or originate assets secured by non-U.S. collateral that are substantially similar to our target assets or (iii) any private investment vehicle that will primarily acquire or originate assets that are substantially similar to our target assets, without providing us with the right (but not the obligation) to contribute, subject to our investment guidelines, our availability of capital and maintaining our qualification as a REIT for U.S. federal income tax purposes and our exemption from registration under the 1940 Act, at least

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one-half of the capital to be funded by such investment vehicles in assets secured by U.S. collateral (or at least one-third for assets secured by non-U.S. collateral) that are substantially similar to our target assets, subject to change if agreed upon by a majority of our independent directors. To date, with respect to certain of our co-investments, we have contributed less than our full entitlement in order to maintain our qualification as a REIT, our exemption from registration under the 1940 Act, liquidity constraints and/or diversification of our assets. All such co-investments where we contributed less than our full entitlement were approved by our independent directors. To the extent that we do not have sufficient capital to contribute our full entitlement of the capital required for any such proposed investment by such investment vehicles, the allocation agreement provides for a fair and equitable allocation of investment opportunities among all such vehicles and us, in each case, taking into account the suitability of each investment opportunity for the particular vehicle and us and each such vehicle's and our availability of capital for investment. This allocation agreement also will apply to any existing Co-Investment Funds. Our board of directors will re-evaluate the allocation agreement from time to time.

Our Manager and Colony Capital have also agreed that, for so long as the management agreement is in effect, with respect to public or private investment vehicles sponsored or managed by Colony Capital or its affiliates that do not primarily acquire or originate assets that are substantially similar to our target assets, the allocation agreement provides for a fair and equitable allocation of investment opportunities in assets that are substantially similar to our target assets among all such vehicles and us, in each case taking into account the suitability of each investment opportunity for the particular vehicle and us, each such vehicle's and our availability of capital for investment and the sourcing of such investment.

### Operating and Regulatory Structure

#### REIT Qualification

We have elected to be taxed as a REIT for U.S. federal income tax purposes. So long as we qualify as a REIT, we generally will not be subject to U.S. federal income tax at the REIT level on our REIT taxable income that we distribute currently to our stockholders. Our qualification as a REIT depends upon our ability to meet, on a continuing basis, various complex requirements under the Internal Revenue Code relating to, among other things, the sources of our gross income and the composition and values of our assets (which, based on the types of assets we own, can fluctuate rapidly, significantly and unpredictably), our distribution levels and the diversity of ownership of our shares. We believe that we have been organized and have operated in conformity with the requirements for qualification and taxation as a REIT under the Internal Revenue Code and that our intended method of operation will enable us to continue to meet the requirements for qualification and taxation as a REIT. In addition, we hold certain of our assets through taxable REIT subsidiaries (each a "TRS"), which are subject to U.S. federal and applicable state and local income taxes (and any applicable non-U.S. taxes) at regular corporate rates. Due to the nature of the assets in which we invest, our TRSs may have a material amount of assets and net taxable income.

#### 1940 Act Exemption

We intend to continue to conduct our operations so that we are not required to register as an investment company under the 1940 Act. Section 3(a)(1)(A) of the 1940 Act defines an investment company as any issuer that is or holds itself out as being engaged primarily in the business of investing, reinvesting or trading in securities.

Section 3(a)(1)(C) of the 1940 Act defines an investment company as any issuer that is engaged or proposes to engage in the business of investing, reinvesting, owning, holding or trading in securities and owns or proposes to acquire investment securities having a value exceeding 40% of the value of the issuer's total assets (exclusive of U.S. Government securities and cash items) on an unconsolidated basis. Excluded from the term "investment securities," among other things, are U.S. Government securities and securities issued by majority-owned subsidiaries that are not themselves investment companies and are not relying on the exception from the definition of investment company set forth in Section 3(c)(1) or Section 3(c)(7) of the 1940 Act.

We are organized as a holding company that conducts its businesses primarily through wholly-owned or majority-owned subsidiaries, and we intend to continue to conduct our operations so that we do not come within the definition of an investment company because less than 40% of the value of our total assets on an unconsolidated basis will consist of "investment securities." The securities issued to us by any wholly-owned or majority-owned subsidiaries that we form that are relying on the exception from the definition of "investment company" contained in Section 3(c)(1)



or 3(c)(7) of the 1940 Act, together with any other investment securities we may own, may not have a value in excess of 40% of the value of our total assets on an unconsolidated basis. We monitor our holdings to ensure continuing and ongoing compliance with this test. In addition, we believe we are not considered an investment company under Section 3(a)(1)(A) of the 1940 Act because we do not engage primarily and do not hold ourselves out as being engaged primarily in the business of investing, reinvesting or trading in securities. Rather, through our wholly-owned and majority-owned subsidiaries, we are primarily engaged in the non-investment company businesses of these subsidiaries.

We believe that certain of our subsidiaries qualify for an exemption from registration under the 1940 Act as an investment company pursuant to Section 3(c)(5)(C) of the 1940 Act, 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.” This exemption generally requires that at least 55% of such subsidiaries' assets must be comprised of qualifying assets and at least 80% of each of their portfolios

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must be comprised of qualifying assets and real estate-related assets under the 1940 Act. Each of our subsidiaries relying on Section 3(c)(5)(C) relies on guidance published by the SEC staff or on our analyses of guidance published with respect to other types of assets to determine which assets are qualifying real estate assets and real estate-related assets. The SEC staff has not, however, published guidance with respect to the treatment of some of these assets under Section 3(c)(5)(C). To the extent that the SEC staff publishes new or different guidance with respect to these matters, we may be required to adjust our strategy accordingly. In addition, we have been and in the future may be limited in our ability to make certain investments and these limitations could result in the subsidiary holding assets we might wish to sell or selling assets we might wish to hold.

Certain of our subsidiaries may rely on the exemption provided by Section 3(c)(6) to the extent that they hold mortgage assets through majority owned subsidiaries that rely on Section 3(c)(5)(C). The SEC staff has issued little interpretive guidance with respect to Section 3(c)(6) and any guidance published by the staff could require us to adjust our strategy accordingly.

If we or our subsidiaries fail to maintain an exception or exemption from the 1940 Act, we could, among other things, be required either (a) to substantially change the manner in which we conduct our operations to avoid being required to register as an investment company or (b) to register as an investment company under the 1940 Act, either of which could have an adverse effect on us and the market price of our securities. If we were required to register as an investment company under the 1940 Act, we would become subject to substantial regulation with respect to our capital structure (including our ability to use leverage), management, operations, transactions with affiliated persons (as defined in the 1940 Act), portfolio composition, including restrictions with respect to diversification and industry concentration, and other matters.

Qualification for exemption from registration under the 1940 Act limits our ability to make certain investments. For example, these restrictions limit the ability of our subsidiaries that rely on 3(c)(5)(C) to invest directly in mortgage-backed securities ("MBS") that represent less than the entire ownership in a pool of mortgage loans, debt and equity tranches of securitizations and certain asset-backed securities, and real estate companies or in assets not related to real estate.

To the extent that the Staff of the Division of Investment Management of the SEC provides more specific guidance regarding any of the matters bearing upon any exemption, we may be required to adjust our holdings and strategies accordingly. Any additional guidance from the Staff of the Division of Investment Management of the SEC could provide additional flexibility to us, or it could further inhibit our ability to pursue the strategies we have chosen.

### Competition

Our profitability depends, in large part, on our ability to acquire our target assets at attractive prices. We are subject to significant competition in acquiring assets. In particular, we compete with a variety of institutional investors, including other REITs, specialty finance companies, public and private funds, commercial and investment banks, hedge funds, mortgage bankers, commercial finance and insurance companies, governmental bodies and other financial institutions. In addition, there are several REITs with similar investment objectives, including a number that have been recently formed, and others may be organized in the future. These other REITs increase competition for the available supply of commercial mortgage and other real estate-related assets suitable for purchase or origination and single-family homes for purchase. Some of our competitors have greater financial resources, access to lower costs of capital and access to funding sources that may not be available to us, such as funding from the U.S. Government, if we are not eligible to participate in programs established by the U.S. Government. In addition, some of our competitors are not subject to the operating constraints associated with REIT tax compliance or maintenance of an exemption from the 1940 Act. Furthermore, some of our competitors may have higher risk tolerances or different risk assessments, which could allow them to consider a wider variety of investments, or pay higher prices, than we can. Current market conditions may attract more competitors, which may increase the competition for our target assets. An increase in the competition for such assets may increase the price of such assets, which may limit our ability to generate attractive risk-adjusted returns for our stockholders, thereby adversely affecting the market price of our common stock.

### Government Regulations Relating to the Environment

Under various federal, state and local environmental laws, ordinances and regulations, a current or previous owner of real estate (including, in certain circumstances, a secured lender that succeeds to ownership or control of a property)

may become liable for the costs of removal or remediation of certain hazardous or toxic substances at, on, under or in its property. Those laws typically impose cleanup responsibility and liability without regard to whether the owner or control party knew of or was responsible for the release or presence of such hazardous or toxic substances. The costs of investigation, remediation or removal of those substances may be substantial. The owner or control party of a site may be subject to common law claims by third parties based on damages and costs resulting from environmental contamination emanating from a site. Certain environmental laws also impose liability in connection with the handling of or exposure to asbestos-containing materials, pursuant to which third parties may seek recovery from owners of real properties for personal injuries associated with asbestos-containing materials. Absent succeeding to ownership or control of real property, a secured lender is not likely to be subject to any of these forms of environmental liability. We are not currently aware of any environmental issues which could materially affect the Company.

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Federal regulations require building owners and those exercising control over a building's management to identify and warn, via signs and labels, of potential hazards posed by workplace exposure to installed asbestos-containing materials and potentially asbestos-containing materials in the building. The regulations also set forth employee training, record keeping and due diligence requirements pertaining to asbestos-containing materials and potentially asbestos-containing materials. Significant fines can be assessed for violation of these regulations. Building owners and those exercising control over a building's management may be subject to an increased risk of personal injury lawsuits by workers and others exposed to asbestos-containing materials and potentially asbestos-containing materials as a result of these regulations. The regulations may affect the value of a building containing asbestos-containing materials and potentially asbestos-containing materials in which we have invested. Federal, state and local laws and regulations also govern the removal, encapsulation, disturbance, handling and/or disposal of asbestos-containing materials and potentially asbestos-containing materials when such materials are in poor condition or in the event of construction, remodeling, renovation or demolition of a building. Such laws may impose liability for improper handling or a release into the environment of asbestos-containing materials and potentially asbestos-containing materials and may provide for fines to, and for third parties to seek recovery from, owners or operators of real properties for personal injury or improper work exposure associated with asbestos-containing materials and potentially asbestos-containing materials. Prior to closing any property acquisition, we will obtain environmental assessments in a manner we believe prudent in order to attempt to identify potential environmental concerns at such properties. These assessments are carried out in accordance with an appropriate level of due diligence and generally include a physical site inspection, a review of relevant federal, state and local environmental and health agency database records, one or more interviews with appropriate site-related personnel, review of the property's chain of title and review of historic aerial photographs and other information on past uses of the property. We may also conduct limited subsurface investigations and test for substances of concern where the result of the first phase of the environmental assessments or other information indicates possible contamination or where our consultants recommend such procedures.

### Employees

We are externally managed by our Manager pursuant to the management agreement between our Manager and us. All of our officers are employees of our Manager or its affiliates, and we do not have any employees. However, Mr. Tangen is seconded exclusively to us pursuant to a secondment agreement with Colony Capital.

### Available Information; Website Disclosure; Corporate Governance Documents

We make our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy statements and amendments to those reports or statements available free of charge on our website at [www.colonyfinancial.com](http://www.colonyfinancial.com), under "Investor Relations—SEC Filings," as soon as reasonably practicable after we file these materials with, or furnish them to, the SEC. Information contained on our website is not incorporated by reference into this Annual Report and such information should not be considered to be part of this report.

The following documents relating to corporate governance are also available free of charge on our website under "Investor Relations—Corporate Governance" and available in print to any security holder upon request:

• Corporate Governance Guidelines

• Code of Business Conduct and Ethics

• Code of Ethics for Principal Executive Officer and Senior Financial Officers

• Audit Committee Charter

• Nominating & Corporate Governance Committee Charter

• Compensation Committee Charter

You may also request copies of any of these documents by writing to Attention: Investor Relations, Colony Financial, Inc., 2450 Broadway, 6<sup>th</sup> Floor, Santa Monica, CA 90404.

All reports filed with the SEC may also be read and copied at the SEC's public reference room at 100 F Street, N.E., Washington, D.C. 20549. Further information regarding the operation of the public reference room may be obtained by calling 1-800-SEC-0330. In addition, all of our filed reports can be obtained at the SEC's website at [www.sec.gov](http://www.sec.gov).



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### ITEM 1A. Risk Factors.

In addition to the other information contained or incorporated by reference in this Annual Report, readers should carefully consider the following risk factors:

#### Risks Related to Our Management and Our Relationship with Our Manager

We are dependent on our Manager, Colony Capital and their key personnel for our success. We may not find a suitable replacement for our Manager and Colony Capital if the management agreement or the investment advisory agreement is terminated, or for these key personnel if they leave our Manager or Colony Capital or otherwise become unavailable to us, which would materially and adversely affect us.

We are externally advised by our Manager, which is a wholly-owned subsidiary of Colony Capital, and all of our officers are employees of our Manager or its affiliates, including Colony Capital. Pursuant to our management agreement, our Manager is obligated to supply us with substantially all of our senior management team, and Mr. Tangen is seconded exclusively to us pursuant to a secondment agreement with Colony Capital. Subject to investment, leverage and other guidelines or policies adopted by our board of directors, our Manager has significant discretion regarding the implementation of our investment and operating policies and strategies. Accordingly, we believe that our success depends significantly upon the experience, skill, resources, relationships and contacts of the executive officers and key personnel of our Manager and its affiliates. Executive officers and key personnel of our Manager and Colony Capital evaluate, negotiate, close and monitor our investments; therefore, our success depends on their continued service. The departure of any member of our management from Colony Capital, particularly Thomas J. Barrack, Jr., our Executive Chairman, and Richard B. Saltzman, our Chief Executive Officer and President, or such officers or personnel otherwise becoming unavailable to manage our business could have a material adverse effect on our performance.

Neither our Manager nor Colony Capital is obligated to dedicate any specific personnel exclusively to us nor are they or their personnel (other than Mr. Tangen) obligated to dedicate any specific portion of their time to the management of our business. As a result, we cannot provide any assurances regarding the amount of time our Manager or Colony Capital will dedicate to the management of our business. Moreover, each of our officers and non-independent directors is also an employee of our Manager or one of its affiliates, and, other than Mr. Tangen, has significant responsibilities for other investment vehicles currently managed by Colony Capital and its affiliates, and may not always be able to devote sufficient time to the management of our business. Consequently, we may not receive the level of support and assistance that we otherwise might receive if we were internally managed.

In addition, we offer no assurance that our Manager will remain our manager or that we will continue to have access to our Manager's principals and professionals. The initial term of our management agreement with our Manager, and the investment advisory agreement between our Manager and Colony Capital expired on September 29, 2012 (the third anniversary of the completion of the IPO) and automatically renews for one-year terms. The management agreement may be terminated upon at least 180 days' prior written notice to the Manager. If the management agreement or the investment advisory agreement is terminated or not renewed and no suitable replacement is found to manage us, we may not be able to execute our business plan, which could have a material adverse effect on our results of operations and our ability to make distributions to our stockholders.

There are various conflicts of interest in our relationship with Colony Capital and its affiliates, including our Manager, which could result in decisions that are not in the best interests of our stockholders.

We are subject to conflicts of interest arising out of our relationship with Colony Capital and its affiliates, including our Manager. Each of our officers and non-independent directors are employees of Colony Capital and certain of its affiliates, and may have conflicts between their duties to us and their duties to, and interests in, Colony Capital and its other investment funds, including investments in certain of our assets. The activities of other investment funds managed by Colony Capital or its affiliates could restrict our ability to pursue certain asset acquisitions or take other actions related to our business. Further, at times when there are turbulent conditions in the mortgage markets or distress in the credit markets or other times when we will need focused support and assistance from our Manager and its key personnel, Colony Capital's other clients may likewise require greater focus and attention, placing Colony

Capital's resources in high demand. In such situations, we may not receive the level of support and assistance that we may receive if we were internally managed or if our Manager's key personnel did not have investment management responsibilities for other entities. In particular, Colony Capital or its affiliates currently manage funds that may compete with us with respect to our target assets. As a result, there may be certain situations where our officers allocate assets that may be suitable for us to such other funds. There is no assurance that the investment allocation agreement that addresses some of the conflicts relating to our assets will be adequate to address all of the conflicts that may arise.

Our Manager receives substantial base management fees regardless of the performance of our portfolio and, as a result, our Manager might not have an adequate incentive to devote its time and effort to seeking investments that provide attractive

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risk-adjusted returns for our portfolio. Consequently, we may be required to pay our Manager significant base management fees in a particular quarter despite experiencing a net loss or a decline in the value of our portfolio during that quarter. In addition, our Manager has the ability to earn incentive fees each quarter based on our Core Earnings, which may create an incentive for our Manager to invest in assets with higher yield potential, which are generally riskier or more speculative, or sell an asset prematurely for a gain, in an effort to increase our short-term net income and thereby increase the incentive fees to which it is entitled. If our interests and those of our Manager are not aligned, the execution of our business plan and our results of operations could be adversely affected, which could materially and adversely affect our ability to make distributions to our stockholders and the market price of our common stock. Certain current or future private investment funds managed by Colony Capital or its affiliates may have the right to co-invest with us in certain of our target assets, which could adversely affect our ability to invest timely in our target assets, thereby materially and adversely affecting our results of operations and our ability to make distributions to our stockholders.

Certain current or future Co-Investment Funds managed by Colony Capital or its affiliates may have the right to co-invest with us in our target assets, subject to us and each Co-Investment Fund having capital available for investment and the determination by our Manager and the general partner of each Co-Investment Fund (which is or will be an affiliate of Colony Capital) that the proposed investment is suitable for us and such Co-Investment Fund, respectively. Currently, the Co-Investment Funds have the right to co-invest with us under certain circumstances. Depending on the circumstances, we may co-invest in a particular asset with one or any combination of the Co-Investment Funds. To the extent that a Co-Investment Fund has significant available capital, the likelihood that we may co-invest in a particular asset with such fund could increase significantly. We also expect that, in the future, Colony Capital will sponsor other Co-Investment Funds that primarily will invest in our target assets. To the extent that we acquire assets with Co-Investment Funds, our ability to invest our then available capital in revenue-generating assets in the near term may be hindered, which would have a material adverse effect on our results of operations and ability to make distributions to our stockholders.

Many of our investment activities have been structured as co-investments with one or more of the Co-Investment Funds. Accordingly, because affiliates of Colony Capital also manage the Co-Investment Funds and also may participate indirectly in the investments made by such Co-Investment Funds, and because fees payable to such affiliates by the Co-Investment Funds may be more advantageous than fees payable to our Manager, our interests in such investments may conflict with the interests of the Co-Investment Funds, and our Manager or its affiliates may take actions that may not be most favorable to us, including in the event of a default or restructuring of the assets subject to co-investment rights.

In addition, because the Co-Investment Funds are, and in the future likely will be, closed-end funds or other investment vehicles with finite lives, such Co-Investment Funds are expected to dispose of substantially all of the assets in their respective portfolios prior to termination. As a result, prior to such terminations, we may need to sell our interests in certain current or future co-investment assets before we otherwise would in order to avoid a potential conflict. Our decision to sell such interests will depend, among other things, on our ability to sell the interests at favorable prices or at all. It is also possible that our Manager or its affiliates who also manage such Co-Investment Funds may sell such co-investment assets at times or prices that are not in the best interests of us or our stockholders. In addition, to the extent that such Co-Investment Funds dispose of co-investment assets that are qualifying assets, we may be required to purchase additional qualifying assets (subject to the availability of capital at favorable prices or at all) or sell non-qualifying assets at inopportune times or prices in order to maintain our qualification as a REIT and our exemption from registration under the 1940 Act. Even if our interests are not in conflict with those of Co-Investment Funds, we may not realize the full economic benefits of the investment. If any of the foregoing were to occur, our Manager's ability to operate our business in a manner consistent with our business strategy could be hindered materially, which could have a material adverse effect on our results of operations and our ability to make distributions to our stockholders.

Colony Capital and/or our Manager are also subject to certain allocation policies, subject to change in their discretion, in allocating investments among us and other current and future investment funds and vehicles managed by Colony Capital or its affiliates. See "Business—Co-Investment Funds."



The management agreement with our Manager was not negotiated on an arm's length basis and may not be as favorable to us as if it had been negotiated with an unaffiliated third party.

Our executive officers and two of our five directors are executives of Colony Capital. Our management agreement was negotiated between related parties and its terms, including fees payable to our Manager, may not be as favorable to us as if it had been negotiated with an unaffiliated third party. In addition, we may choose not to enforce, or to enforce less vigorously, our rights under the management agreement because of our desire to maintain our ongoing relationship with Colony Capital and its affiliates.

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Termination of our management agreement could be costly and may cause us to be unable to execute our business plan.

Termination of the management agreement with our Manager without cause may be difficult and costly. Our independent directors review our Manager's performance and the fees that may be payable to our Manager annually and the management agreement may be terminated annually upon the affirmative vote of at least two-thirds of our independent directors based upon: (1) our Manager's unsatisfactory performance that is materially detrimental to us; or (2) a determination that the management fees payable to our Manager are not fair, subject to our Manager's right to prevent termination based on unfair fees by accepting a reduction of management fees agreed to by at least two-thirds of our independent directors. Our Manager will be provided 180 days prior written notice of any such a termination. Additionally, upon such a termination without cause, the management agreement provides that we will pay our Manager a termination fee equal to three times the sum of (a) the average annual base management fee and (b) the average annual incentive fee earned by the Manager, in each case during the prior 24-month period immediately preceding such termination, calculated as of the end of the most recently completed fiscal quarter before the date of termination.

The management agreement automatically renews for a one-year term on each anniversary of our IPO; provided, however, that our Manager may terminate the management agreement upon 180 days prior written notice. If the management agreement is terminated and we are unable to identify a suitable replacement to manage us, we may not be able to execute our business plan.

Our Manager manages our portfolio pursuant to very broad investment guidelines, and our board of directors does not approve each investment and financing decision made by our Manager unless required by our investment guidelines. Our Manager is authorized to follow very broad investment guidelines established by our board of directors. Our board of directors periodically reviews our investment guidelines and our portfolio of assets but does not, and is not required to, review all of our proposed investments, except in limited circumstances as set forth in our investment guidelines. In addition, in conducting periodic reviews, our board of directors may rely primarily on information provided to them by our Manager. Furthermore, transactions entered into by our Manager may be costly, difficult or impossible to unwind by the time they are reviewed by our board of directors. Our Manager has great latitude within the broad parameters of our investment guidelines in determining the types and amounts of assets in which to invest on our behalf, including making investments that may result in returns that are substantially below expectations or result in losses, which would materially and adversely affect our business and results of operations, or may otherwise not be in the best interests of our stockholders.

Our Manager's liability is limited under the management agreement and we have agreed to indemnify the Manager against certain liabilities.

Pursuant to the 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. Our Manager maintains a contractual, as opposed to a fiduciary, relationship with us. Under the terms of the management agreement, our Manager, its officers, members, personnel, 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 the management agreement, except those resulting from acts constituting gross negligence, willful misconduct, bad faith or reckless disregard of our Manager's duties under the management agreement. In addition, we have agreed to indemnify our Manager and each of its officers, directors, members, managers and employees from and against any claims or liabilities, including reasonable legal fees and other expenses reasonably incurred, arising out of or in connection with our business and operations or any action taken or omitted on our behalf pursuant to authority granted by the management agreement, except where attributable to gross negligence, willful misconduct, bad faith or reckless disregard of such person's duties under the management agreement.

We do not own the Colony name, but have entered into a license agreement with an affiliate of Colony Capital granting us the right to use the Colony name. Use of the name by other parties or the termination of our license agreement may harm our business.

Concurrently with the closing of our IPO, we entered into a license agreement pursuant to which we have a non-exclusive, royalty-free license to use the name “Colony.” Under this agreement, we have a right to use the “Colony” name as long as Colony Financial Manager, LLC remains our Manager pursuant to the management agreement. Colony Capital retains the right to continue using the “Colony” name. We also are unable to preclude Colony Capital from licensing or transferring the ownership of the “Colony” name to third parties, some of whom may compete against us. Consequently, we will be unable to prevent any damage to goodwill that may occur as a result of the activities of Colony Capital or others. Furthermore, in the event the license agreement is terminated, we will be required to change our name and cease using the “Colony” name. Any of these events could disrupt our recognition in the market place, damage any goodwill we may have generated and otherwise harm our business.

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### Risks Related to Our Business

We may change our business, investment, leverage and financing strategies without stockholder consent.

As the market evolves, we may change our business, investment and financing strategies without a vote of, or notice to, our stockholders, which could result in our making investments and engaging in business activities that are different from, and possibly riskier than, the investments and businesses described in this Annual Report. In particular, a change in our investment strategy, including the manner in which we allocate our resources across our portfolio or the types of assets in which we seek to invest, may increase our exposure to interest rate risk, default risk and real estate market fluctuations. In addition, we may in the future use leverage at times and in amounts deemed prudent by our Manager in its discretion, and such decision would not be subject to stockholder approval. Furthermore, as the market evolves, our board of directors may determine that the commercial real estate market does not offer the potential for attractive risk-adjusted returns for an investment strategy that is consistent with our intention to elect and qualify to be taxed as a REIT and to operate in a manner to maintain our exemption from registration under the 1940 Act. For example, if our board of directors believes it would be advisable for us to be a more active seller of loans and securities, our board of directors may determine that we should conduct such business through a TRS, or that we should cease to maintain our REIT qualification. Changes to our strategies with regards to the foregoing could materially and adversely affect our financial condition, results of operations and our ability to make distributions to our stockholders.

Maintenance of our exemption from registration under the 1940 Act imposes significant limits on our operations, which may have a material adverse effect on our ability to execute our business strategy.

We have conducted, and intend to continue to conduct, our operations so as not to become regulated as an investment company under the 1940 Act. Section 3(a)(1)(A) of the 1940 Act defines an investment company as any issuer that is or holds itself out as being engaged primarily in the business of investing, reinvesting or trading in securities. Section 3(a)(1)(C) of the 1940 Act defines an investment company as any issuer that is engaged or proposes to engage in the business of investing, reinvesting, owning, holding or trading in securities and owns or proposes to acquire investment securities having a value exceeding 40% of the value of the issuer's total assets (exclusive of U.S. Government securities and cash items) on an unconsolidated basis. Excluded from the term "investment securities," among other things, are U.S. Government securities and securities issued by majority-owned subsidiaries that are not themselves investment companies and are not relying on the exception from the definition of investment company set forth in Section 3(c)(1) or Section 3(c)(7) of the 1940 Act. Because we are a holding company that conducts its businesses primarily through wholly-owned or majority-owned subsidiaries, the securities issued by such subsidiaries that are relying on the exception from the definition of "investment company" contained in Section 3(c)(1) or Section 3(c)(7) of the 1940 Act, together with any other investment securities we may own, may not have a combined value in excess of 40% of the value of our total assets on an unconsolidated basis. This requirement limits the types of businesses in which we may engage through our subsidiaries.

Certain of our subsidiaries rely upon the exemption from registration as an investment company under the 1940 Act pursuant to Section 3(c)(5)(C) of the 1940 Act, 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." This exemption generally requires that at least 55% of each such subsidiary's assets must be comprised of qualifying assets and at least 80% of each of their portfolios must be comprised of qualifying assets and real estate-related assets under the 1940 Act. Each of our subsidiaries relying on Section 3(c)(5)(C) relies on guidance published by the SEC staff or on our analyses of guidance published with respect to other types of assets to determine which assets are qualifying real estate assets and real estate-related assets. The SEC staff has not, however, published guidance with respect to the treatment of some of these assets under Section 3(c)(5)(C). To the extent that the SEC staff publishes new or different guidance with respect to these matters, we may be required to adjust our strategy accordingly. In addition, we may be limited in our ability to make certain investments and these limitations could result in the subsidiary holding assets we might wish to sell or selling assets we might wish to hold.

Certain of our subsidiaries may rely on the exemption provided by Section 3(c)(6) to the extent that they hold mortgage assets through majority-owned subsidiaries that rely on Section 3(c)(5)(C). The SEC staff has issued little interpretive guidance with respect to Section 3(c)(6) and any guidance published by the staff could require us to adjust

our strategy accordingly.

The determination of whether an entity is a majority-owned subsidiary of our company is made by us. The 1940 Act defines a majority-owned subsidiary of a person as a company 50% or more of the outstanding voting securities of which are owned by such person, or by another company which is a majority-owned subsidiary of such person. The 1940 Act further defines voting securities as any security presently entitling the owner or holder thereof to vote for the election of directors of a company. We treat companies in which we own at least 50% of the outstanding voting securities as majority-owned subsidiaries for purposes of the 40% test. We have not requested the SEC to approve our treatment of any company as a majority-owned subsidiary and the SEC has not done so. If the SEC were to disagree with our treatment of one or more companies as majority-owned subsidiaries, we would need to adjust our strategy and our assets in order to continue to pass the 40% test. Any such adjustment in our strategy could have a material adverse effect on us.

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There can be no assurance that the laws and regulations governing the 1940 Act status of our company, including the Division of Investment Management of the SEC providing more specific or different guidance regarding these exemptions, will not change in a manner that adversely affects our operations. Our Manager and its affiliates have limited experience managing a portfolio of assets in the manner necessary to maintain our exemption under the 1940 Act. If we or our subsidiaries fail to maintain our exemption, 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, any of which could negatively affect the value of our common stock, the sustainability of our business model, and our ability to make distributions which could have an adverse effect on our business and the market price for our shares of common stock. If we were required to register as an investment company under the 1940 Act, we would become subject to substantial regulation with respect to our capital structure (including our ability to use leverage), management, operations, transactions with affiliated persons (as defined in the 1940 Act), portfolio composition, including restrictions with respect to diversification and industry concentration, and other matters. In addition, if we were required to register as an investment company, but failed to do so, we could be subject to criminal and civil actions. In addition, failure to maintain our 1940 Act exemption would permit our Manager to terminate the management agreement.

Rapid changes in the values of our real estate-related investments may make it more difficult for us to maintain our qualification as a REIT or exemption from the 1940 Act.

If the market value or income potential of real estate-related investments declines as a result of increased interest rates, prepayment rates or other factors, we may need to increase our real estate investments and income and/or liquidate our non-qualifying assets in order to maintain our REIT qualification or exemption from the 1940 Act. Given the illiquid nature of certain real estate investments, we can provide no assurances that we would be able to liquidate our non-qualifying assets at opportune times or prices, if at all, in order to maintain our REIT qualification and 1940 Act exemption. Similarly, we can provide no assurances that we would have sufficient capital or access to capital at favorable prices, if at all, if we were required to increase our qualifying real estate assets in order to maintain our REIT qualification and 1940 Act exemption. If the value of our assets fluctuates dramatically, our ability to maintain compliance may be particularly difficult, which may cause us to make investment decisions that we otherwise would not make absent the REIT and 1940 Act considerations.

Our current and future direct or indirect joint venture investments could be adversely affected by our lack of sole decision-making authority, our reliance on joint venture partners' financial condition and liquidity and disputes between us and our joint venture partners.

We have entered into, and may in the future enter into, joint ventures, including with the Co-Investment Funds, the FDIC or otherwise, to acquire or originate our target assets. Such joint venture investments may involve risks not otherwise present when we acquire our target assets without partners, including the following:

- we do not have exclusive control over the asset or joint venture, which may prevent us from taking actions that are in our best interest;
- joint venture agreements often restrict the transfer of a partner's interest or may otherwise restrict our ability to sell the interest when we desire and/or on advantageous terms;
- any future joint venture agreements may contain buy-sell provisions pursuant to which one partner may initiate procedures requiring the other partner to choose between buying the other partner's interest or selling its interest to that partner;
- we may not be in a position to exercise sole decision-making authority regarding the asset or joint venture, which could create the potential risk of creating impasses on decisions, such as asset acquisitions or dispositions;
- a partner may, at any time, have economic or business interests or goals that are, or that may become, inconsistent with our business interests or goals;
- a partner may be in a position to take action contrary to our instructions, requests, policies or objectives, including our current policy with respect to maintaining our qualification as a REIT and our exemption from registration under the 1940 Act;
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a partner may fail to fund its share of required capital contributions or may become bankrupt, which may mean that we and any other remaining partners generally would remain liable for the joint venture's liabilities; our relationships with our partners are contractual in nature and may be terminated or dissolved under the terms of the applicable joint venture agreements and, in such event, we may not continue to own or operate the interests or assets underlying such relationship or may need to purchase such interests or assets at a premium to the market price to continue ownership;

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disputes between us and a partner may result in litigation or arbitration that would increase our expenses and prevent our officers and directors from focusing their time and efforts on our business and could result in subjecting the assets owned by the joint venture to additional risk; or

we may, in certain circumstances, be liable for the actions of a partner, and the activities of a partner could adversely affect our ability to qualify as a REIT or remain exempt from registration under the 1940 Act, even though we do not control the joint venture.

Any of the above might subject our assets to liabilities in excess of those contemplated and adversely affect the value of our current and future joint venture investments.

We require additional capital to continue to operate and grow our business and portfolio of target assets, and the failure to obtain such financing would have a material adverse effect on our business, financial condition, results of operations and ability to maintain our distributions to our stockholders.

We require capital to fund acquisitions and originations of our target assets, to fund our operations, including overhead costs and the management fee to our Manager, to fund distributions to our stockholders and to repay principal and interest on our borrowings. We expect to meet our capital requirements using cash on hand, cash flow generated from our operations, and principal and interest payments received from our investments. However, because of distribution requirements imposed on us to qualify as a REIT, which generally require that we distribute to our stockholders 90% of our taxable income, our ability to finance our growth must largely be funded by external sources of capital. As a result, we will have to rely on third-party sources of capital, including public and private offerings of securities and debt financings. Financing may not be available to us when needed, on favorable terms, or at all. In the event that we are unable to obtain adequate financing to fund or grow our business, it would have a material adverse effect on our ability to acquire additional assets and make our debt service payments and our financial condition, results of operations and the ability to fund our distributions to our stockholders would be materially adversely affected.

### Risks Related to Our Investments

Our strategy of buying single-family homes for rental to tenants is subject to various risks, any of which could have a material adverse effect on our business and results of operations.

As part of our business strategy, through our investment in CAH OP, we have acquired and expect to continue to acquire interests in single-family homes for the purpose of renting the homes to tenants. To date, we have invested \$550 million in CAH OP. To the extent that we continue to own interests in single-family homes, we will be subject to various risks, including the following:

- our ability to generate revenue from the single-family homes in which we own an interest will be dependent on the ability of tenants to pay rent, and the failure of a significant number of our tenants to pay rent timely or at all or a significant number of lease terminations could have a material adverse effect on our results of operations;

- the single-family homes in which we own an interest will compete with numerous housing alternatives in attracting residents, including other single-family homes and apartment communities, which may reduce occupancy levels and have a material adverse effect on our revenues;

- CAH OP will compete for attractive acquisition opportunities against other sources of capital, including other private investment funds, pension funds and their advisors, individual home buyers, public and private REITs, foreign investors and various types of financial institutions and their affiliates, which could limit suitable investment opportunities or decrease returns and may have a material adverse effect on our revenues;

- the single-family homes in which we own an interest typically are, and homes we acquire in the future likely will be, located in markets that have been particularly susceptible to adverse local and national economic conditions, and there can be no assurances that future economic downturns will not adversely affect our ability to generate revenue from the homes or cause the market value of the homes to decline significantly;

- the rental markets in which the single-family homes are located may remain flat or deteriorate, which could limit the extent to which rental rates can be increased to satisfy increased expenses without having a material adverse effect on occupancy rates;

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the single-family homes in which we hold an interest are illiquid assets. Real estate investments generally cannot be disposed of quickly, especially when market conditions are poor, which could limit CAH OP's ability to vary its portfolio promptly in response to changes in economic or other conditions and its ability to utilize sales proceeds as a source of liquidity, which may have a material adverse effect on our revenues;

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if we are unable to lease or re-lease vacant single-family homes, we will be subject to costs, including mortgage payments, insurance premiums, maintenance and real estate taxes, but will not have a source of revenue to satisfy such costs, which could have a material adverse effect on our results of operations;

we are dependent on the performance of third-party managers to manage the leasing and maintenance of the single-family homes in which we own an interest, and our results of operations could be adversely affected if such third-party managers do not manage the homes in our best interests; and

federal, state and local laws, regulations and ordinances, including landlord/tenant laws and regulations, could exist or be adopted that affect the terms of the leases to which the single-family homes are subject, which could affect our ability to manage the properties in a cost-effective manner.

If any of the foregoing risks were to occur, our business and results of operations could be materially and adversely affected.

CAH OP may not be able to identify and make additional investments that are consistent with its investment objectives, which could have a material adverse effect on our business and results of operations.

We rely on the ability of CAH OP's manager to identify, acquire and manage investments. Because such investments will occur over time, adverse changes in the financial and other relevant markets may reduce the number of investment opportunities available. CAH OP may be unable to find a sufficient number of attractive opportunities to meet its investment objectives. CAH OP's business may also be adversely affected if CAH OP overvalues a property, if it is unable to quickly and efficiently renovate and lease its investment properties and/or if cost estimates for acquiring investment properties prove inaccurate, which could have a material adverse effect on our business and results of operations to the extent that CAH OP's ability to make distributions to us is affected.

Some of the loans in our investment portfolio are in the process of being restructured or may otherwise be at risk, which could result in impairment charges and loan losses.

Some of loans in our investment portfolio are in the process of being restructured or may otherwise be under credit watch or at risk. We make various assumptions and judgments about the collectability of our loan portfolio, including the creditworthiness of our borrowers and the value of the real estate and other assets serving as collateral for the repayment of many of our loans. If we determine that it is probable that we will not be able to collect all amounts due to us under the terms of a particular loan agreement, we could be required to recognize an impairment charge or a loss on the loan unless the loan's observable market price or the value of the collateral securing the loan exceeds the carrying value of the loan. If our assumptions regarding, among other things, the present value of expected future cash flows or the value of the collateral securing our loans are incorrect or general economic and financial conditions cause one or more borrowers to become unable to make payments under their loans, we could be required to recognize impairment charges, which could result in a material reduction in earnings in the period in which the loans are determined to be impaired and may adversely affect, perhaps materially, our financial condition, liquidity and the ability to make distributions to our stockholders.

An economic slowdown, recession or decline in real estate values may cause us to experience losses related to our assets, which may adversely affect our results of operations, the availability and cost of credit and cash available for distribution to our stockholders.

The risks associated with our investments may be more acute during periods of economic slowdown or recession, especially if these periods are accompanied by declining real estate values. Our results of operations are materially affected by conditions in the mortgage market, the commercial real estate markets, the financial markets and the economy generally. In the recent past, concerns about the mortgage market and a declining real estate market, as well as inflation, energy costs, geopolitical issues and the availability and cost of credit, have contributed to increased volatility and diminished expectations for the economy and markets. Furthermore, an economic slowdown may result in continued decreased demand for commercial property, forcing property owners to lower rents on properties with excess supply. To the extent that a property owner has fewer tenants or receives lower rents, such property owners will generate less cash flow on their properties, which increases significantly the likelihood that such property owners will default on their debt service obligations to us. If borrowers default, we may incur losses on our investments with them if the value of any collateral we foreclose upon is insufficient to cover the full amount of such investment, and the funds from such foreclosure may take a significant amount of time to realize. For the foregoing reasons, a weak

economy also may result in the increased likelihood of re-default rates even after we have completed loan modifications. In addition, to the extent that we acquire direct interests in commercial or residential real estate, an economic slowdown could adversely impact, among other things, the ability of our tenants to pay rent on a timely basis, if at all, and could result in tenants terminating their leases, choosing not to renew their existing leases or reducing the amount of space that they rent. A deterioration of the real estate market may result in a decline in the market value of our investments or cause us to experience losses related to our assets, which may adversely affect our results of operations, the availability and cost of credit and our ability to make distributions to our stockholders.

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In addition, an economic slowdown, recession or decline in real estate values may cause lenders and institutional investors to reduce and, in some cases, cease to provide funding to borrowers, including us, which could make it more difficult for us to obtain financing on favorable terms or at all, in the event that we seek to use leverage to acquire our target assets. Our profitability may be adversely affected if we are unable to obtain cost-effective financing for our assets.

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

Our investment in certain assets may decline in value if long-term interest rates increase. Declines in market value may ultimately reduce earnings or result in losses to us, which may negatively affect cash available for distribution to our stockholders. If long-term rates increased significantly, the market value of certain investments may decline, and the duration and weighted average life of these investments may increase. As a result, we could realize a loss if these investments were sold prior to maturity.

In addition, in a period of rising interest rates, our operating results will partially depend on the difference between the income from our assets and financing costs. We anticipate that, in some cases, the income from such assets will respond more slowly to interest rate fluctuations than the cost of our borrowings. Consequently, changes in interest rates, particularly short-term interest rates, may significantly influence our net interest income, which is the difference between the interest income we earn on our interest-earning investments and the interest expense we incur in financing these investments. Increases in these rates could decrease our net income and the market value of our assets. Rising interest rates may also cause our target assets that were issued prior to an interest rate increase to provide yields that are below prevailing market interest rates. If rising interest rates cause us to be unable to acquire a sufficient volume of our target assets with a yield that is above our borrowing cost, our ability to satisfy our investment objectives and to generate income and pay dividends may be materially and adversely affected. An increase in interest rates may cause a decrease in the volume of certain of our target assets, which could adversely affect our ability to acquire target assets that satisfy our investment objectives and to generate income and make distributions to our stockholders.

The relationship between short-term and longer-term interest rates is often referred to as the “yield curve.” Ordinarily, short-term interest rates are lower than longer-term interest rates. If short-term interest rates rise disproportionately relative to longer-term interest rates (a flattening of the yield curve), our borrowing costs may increase more rapidly than the interest income earned on our assets. Because we expect our investments, on average, generally will bear interest based on longer-term rates than our borrowings, a flattening of the yield curve would tend to decrease our net income and the market value of our net assets. Additionally, to the extent cash flows from investments that return scheduled and unscheduled principal are reinvested, the spread between the yields on the new investments and available borrowing rates may decline, which would likely decrease our net income. It is also possible that short-term interest rates may exceed longer-term interest rates (a yield curve inversion), in which event our borrowing costs may exceed our interest income and we could incur operating losses. As a result of the foregoing, significant fluctuations in interest rates could materially and adversely affect our results of operations, financial conditions and our ability to make distributions to our stockholders.

We operate in a highly competitive market for investment opportunities, and competition may limit our ability to continue to acquire attractive investments on favorable terms or at all, which could have a material adverse effect on our business, financial condition and results of operations.

We operate in a highly competitive market for investment opportunities. Our profitability depends, in large part, on our ability to acquire assets, including our target assets, at attractive prices. In acquiring assets, we compete with a variety of institutional investors, including other REITs, specialty finance companies, public and private funds (including other funds managed by Colony Capital), commercial and investment banks, commercial finance and insurance companies and other financial institutions, many of whom are substantially larger and have considerably greater financial, technical, marketing and other resources than we do. Several other REITs have recently raised, and may raise significant amounts of capital in the future, and may have investment objectives that overlap with ours,

which will likely create additional competition for investment opportunities. Some competitors may have a lower cost of funds and access to funding sources that may not be available to us, such as funding from the U.S. Government, if we are not eligible to participate in programs established by the U.S. Government as well as borrowings that are governed by the FDIC. In addition, many of our competitors are not subject to the operating constraints associated with REIT tax compliance or maintenance of an exemption from the 1940 Act. In addition, some of our competitors may have higher risk tolerances or different risk assessments, which could allow them to consider a wider variety of investments and establish more relationships than us. Furthermore, competition for investments may result in an increase in the price of such assets, which may further limit our ability to generate attractive risk-adjusted returns. Moreover, as the conditions in the mortgage market, the financial markets and the economy improve, the availability of commercial mortgage loans that meet our investment objectives and strategies will likely decrease, which will increase competition and may limit us from making investments in our target assets. As a result of such increased competition, we cannot assure you that

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we will be able to identify and make additional investments that are consistent with our investment objectives, which could have a material adverse effect on our business, financial condition and results of operations.

Our real estate assets are subject to risks particular to real property, any of which could reduce our return from an affected property or asset and reduce or eliminate our ability to make distributions to our stockholders.

Our real estate investments, including the real estate investments in which we hold an indirect interest through CAH OP, are subject to various risks, including:

- acts of God, including earthquakes, floods and other natural disasters, which may result in uninsured losses;
- acts of war or terrorism, including the consequences of terrorist attacks, such as those that occurred on September 11, 2001;
- adverse changes in national and local economic and market conditions;
- changes in, and related costs of compliance with, governmental laws and regulations, fiscal policies and zoning ordinances;
- costs of remediation and liabilities associated with environmental conditions such as indoor mold; and
- the potential for uninsured or under-insured property losses.

If any of these or similar events occurs, it may reduce our return from an affected property or asset and reduce or eliminate our ability to make distributions to stockholders.

In addition, under various U.S. federal, state and local laws, an owner or operator of real property may become liable for the costs of removal of certain hazardous substances released on its property. These laws often impose liability without regard to whether the owner or operator knew of, or was responsible for, the release of such hazardous substances. The presence of hazardous substances may adversely affect an owner's ability to sell real estate or borrow using real estate as collateral. To the extent that an owner of a property underlying one of our debt investments becomes liable for removal costs, the ability of the owner to make payments to us may be reduced, which in turn may adversely affect the value of the asset held by us and our ability to make distributions to our stockholders. If we acquire a property through foreclosure or otherwise, the presence of hazardous substances on such property may adversely affect our ability to sell the property and we may incur substantial remediation costs, which could have a material adverse effect on our results of operations, financial condition and our ability to make distributions to our stockholders.

To the extent that we acquire equity interests in real estate either directly, or indirectly through our investment in CAH OP, we will depend on tenants for revenue and, accordingly, lease terminations and/or tenant defaults, particularly by one or more large tenants, could have a material adverse effect on us.

To the extent that we acquire direct or indirect equity interests in commercial or residential real estate including our investment in CAH OP, the success of our investments will depend on the financial stability of our tenants, any of whom may experience a change in their business or economic status at any time. If current economic conditions do not stabilize or worsen, tenants occupying the commercial or residential real estate that we may acquire may delay lease commencements, decline to extend or renew their leases upon expiration, fail to make rental payments when due, or declare bankruptcy. Any of these actions could result in the termination of the tenants' leases, or expiration of existing leases without renewal, and the loss of rental income attributable to the terminated or expired leases. In the event of a tenant default or bankruptcy, we or CAH OP may experience delays in enforcing our rights as a landlord and may incur substantial costs in protecting our investment and re-letting our property. If a significant number of leases, or leases for one or more large tenants, are terminated or defaulted upon, we or CAH OP may be unable to lease the property for the rent previously received or sell the property without incurring a loss. In addition, significant expenditures, such as mortgage payments, real estate taxes and insurance and maintenance costs, are generally fixed and do not decrease when revenues at the related property decrease. If any of the foregoing were to occur, it could have a material adverse effect on our cash flows, results of operations and our ability to make distributions to our stockholders.

A portion of our investments currently are, and in the future may be, in the form of non-performing and sub-performing commercial mortgage loans, or loans that may become non-performing and sub-performing, which are subject to increased risks relative to performing loans.

A portion of our investments currently are, and in the future may be, in the form of whole loan mortgages, including subprime commercial mortgage loans and non-performing and sub-performing commercial mortgage loans, which are subject to increased risks of loss. Such loans may already be, or may become, non-performing or sub-performing for a variety of reasons, including, without limitation, because the underlying property is too highly leveraged or the borrower falls upon financial distress, in either case, resulting in the borrower being unable to meet its debt service obligations to us. Such non-performing or sub-performing loans may require a substantial amount of workout negotiations and/or restructuring, which may divert the attention of our Manager and management from other activities and entail, among other things, a substantial

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reduction in the interest rate, capitalization of interest payments and a substantial write-down of the principal of the loan. However, even if such restructuring were successfully accomplished, a risk exists that the borrower will not be able or willing to maintain the restructured payments or refinance the restructured mortgage upon maturity.

In addition, certain non-performing or sub-performing loans that we acquire may have been originated by financial institutions that are or may become insolvent, suffer from serious financial stress or are no longer in existence. As a result, the standards by which such loans were originated, the recourse to the selling institution, and/or the standards by which such loans are being serviced or operated may be adversely affected. Further, loans on properties operating under the close supervision of a mortgage lender are, in certain circumstances, subject to certain additional potential liabilities that may exceed the value of our investment.

In the future, it is possible that we may find it necessary or desirable to foreclose on some, if not many, of the loans we acquire, and the foreclosure process may be lengthy and expensive. Borrowers or junior lenders may resist mortgage foreclosure actions by asserting numerous claims, counterclaims and defenses against us including, without limitation, numerous lender liability claims and defenses, even when such assertions may have no basis in fact, in an effort to prolong the foreclosure action and force the lender into a modification of the loan or capital structure or a favorable buy-out of the borrower's or junior lender's position. In some states, foreclosure actions can sometimes take several years or more to litigate. At any time prior to or during the foreclosure proceedings, the borrower may file, or a junior lender may cause the borrower to file, for bankruptcy, which would have the effect of staying the foreclosure actions and further delaying the foreclosure process. Foreclosure and associated litigation may create a negative public perception of the related mortgaged property, resulting in a diminution of its value. Even if we are successful in foreclosing on a loan, the liquidation proceeds upon sale of the underlying real estate may not be sufficient to recover our cost basis in the loan, resulting in a loss to us, and the borrower and junior lenders may continue to challenge whether the foreclosure process was commercially reasonable, which could result in additional costs and potential liability. Any costs or delays involved in the effectuation of a foreclosure of the loan or a liquidation of the underlying property, or defending challenges brought after the completion of a foreclosure, will further reduce the proceeds and thus increase the loss. Any such reductions could materially and adversely affect the value of the commercial loans in which we invest.

Whether or not our Manager has participated in the negotiation of the terms of any such mortgages, there can be no assurance as to the adequacy of the protection of the terms of the loan, including the validity or enforceability of the loan and the maintenance of the anticipated priority and perfection of the applicable security interests. Furthermore, claims may be asserted that might interfere with enforcement of our rights. In the event of a foreclosure, we may assume direct ownership of the underlying real estate. The liquidation proceeds upon sale of such real estate may not be sufficient to recover our cost basis in the loan, resulting in a loss to us. Any costs or delays involved in the effectuation of a foreclosure of the loan or a liquidation of the underlying property will further reduce the proceeds and thus increase the loss.

Whole loan mortgages are also subject to "special hazard" risk (property damage caused by hazards, such as earthquakes or environmental hazards, not covered by standard property insurance policies), and to bankruptcy risk (reduction in a borrower's mortgage debt by a bankruptcy court). In addition, claims may be asserted against us on account of our position as mortgage holder or property owner, including responsibility for tax payments, environmental hazards and other liabilities, which could have a material adverse effect on our results of operations, financial condition and our ability to make distributions to our stockholders.

Our ownership of equity interests in an entity that owns a portfolio of hotels subjects us to various risks associated with operating in the lodging industry, any of which could have a material adverse effect on us, including our future results of operations.

We own an indirect interest in a portfolio of 102 limited service hotels. The properties are owned by one of our unconsolidated subsidiaries and leased to another of our unconsolidated subsidiaries that operates the properties. Our indirect ownership and operation of the hotels subjects us to various risks common to the lodging industry that could adversely affect our results of operations, including, among others, the following:

• Lodging assets have different economic characteristics than many other real estate assets. A typical office property, for example, has long-term leases with third-party tenants, which provides a relatively stable long-term stream of



revenue. Hotels, on the other hand, generate revenue from guests that typically stay at the hotel for only a few nights, which causes the room rate and occupancy levels to change every day, and results in earnings that can be highly volatile;

The lodging industry has been adversely affected by the recent economic recession and continued economic uncertainty to a greater extent than many other industries. If the anticipated economic recovery continues to be weak and protracted, or if the U.S. economy falls into another recession, the performance of the hotels could be materially and adversely affected;

To maintain our qualification as a REIT for U.S. federal income tax purposes, we generally cannot operate or manage the hotels.

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Consequently, we will not control the day-to-day operation of the hotels and must rely on the ability of the third-party hotel managers to operate the hotels successfully and in our best interests. As a result, we are subject to the risk that the third-party managers do not perform to our expectations or otherwise do not manage the hotels in our best interests;

The hotels operate under franchise agreements that require maintaining the franchisors' operating standards and satisfying other terms and conditions that could require the expenditure of significant amounts of money. Failure to maintain these standards or satisfy other terms and conditions could result in a franchise license being canceled. The loss of a franchise license could materially and adversely affect the operations or the underlying value of the hotel because of the loss of associated name recognition, marketing support and centralized reservation systems provided by the franchisor, which could adversely affect the financial performance of the hotels;

The lodging industry is highly competitive and other hotel owners may have an operating model that allows them to offer guestrooms at lower rates than those offered at the hotels we own an interest in, which could adversely affect demand for guestrooms and the financial performance of the hotels;

The seasonality of the lodging industry often results in significant fluctuations in occupancy, revenues and operating expenses, which could adversely affect the financial performance of the hotels;

- Restrictive covenants in certain of the hotel management and franchise agreements may limit the ability to sell or refinance a hotel without the consent of the hotel management company or franchisor, which could materially impede our ability to take actions with respect to the hotels that are in the best interests of our stockholders; and

The performance of the hotels may be materially affected by events beyond our control, such as terrorist attacks, travel related health concerns including pandemics and epidemics, imposition of taxes or surcharges by regulatory authorities, travel-related accidents and unusual weather patterns, including natural disasters such as hurricanes and environmental disasters.

Any of the foregoing risks could materially and adversely affect our results of operations, cash flows and ability to make distributions to our stockholders.

The supply of commercial mortgage loans that meet our investment objectives and strategies will likely decrease as the economy improves, which may cause us to adjust our investment strategies.

We believe that there continue to be unique market opportunities to acquire commercial mortgage loans and mortgage-related assets at significant discounts to their unpaid principal balances. However, as conditions in the mortgage market, the financial markets and the economy improve, the availability of commercial mortgage loans that meet our investment objective and strategies will likely decrease, which could prevent us from implementing our business strategies. At such time, we will reevaluate our investment strategies with a view of maximizing the returns from our investment portfolio and identifying other dislocations and opportunities in real estate-related assets, but there can be no assurance that any of our strategies will be successful.

Concerns regarding the European debt crisis and market perceptions concerning the instability of the euro could adversely affect our business, results of operations and financing.

Concerns persist regarding the debt burden of certain Eurozone countries and their ability to meet future financial obligations, the overall stability of the euro and the suitability of the euro as a single currency given the diverse economic and political circumstances in individual Eurozone countries. These concerns could lead to the re-introduction of individual currencies in one or more Eurozone countries, or, in more extreme circumstances, the possible dissolution of the euro currency entirely. Should the euro dissolve entirely, the legal and contractual consequences for holders of euro-denominated obligations would be determined by laws in effect at such time. These potential developments, or market perceptions concerning these and related issues, could materially adversely affect the value of our euro-denominated assets and obligations.

The commercial mortgage loans that we acquire or originate and the mortgage loans underlying our CMBS investments are subject to the ability of the property owner to generate net income from operating the property as well as the risks of delinquency and foreclosure.

The ability of a commercial mortgage borrower to repay a loan secured by an income-producing property, such as a multi-family or commercial 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 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, real estate tax rates

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and other operating expenses, changes in governmental rules, regulations and fiscal policies, including environmental legislation, acts of God, terrorism, social unrest and civil disturbances.

Most commercial mortgage loans underlying CMBS are effectively nonrecourse obligations of the borrower, meaning that there is no recourse against the borrower's assets other than the underlying collateral. In the event of any default under a mortgage 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 (or our ability to realize such value through foreclosure) and the principal and accrued interest of the mortgage loan, which could have a material adverse effect on our results of operations and cash flow from operations and limit amounts available for distribution to our stockholders. In the event of the bankruptcy of a mortgage loan borrower, the mortgage loan to such borrower will be deemed to be secured only to the extent of the value of the underlying collateral at the time of bankruptcy (as determined by the bankruptcy court), and the lien securing the mortgage loan will be subject to the avoidance powers of the bankruptcy trustee or debtor-in-possession to the extent the lien is unenforceable under state law. Foreclosure of a mortgage loan can be an expensive and lengthy process, which could have a substantial negative effect on our anticipated return on the foreclosed mortgage loan.

Our CMBS investments are subject to the risks of the securitization process, as well as all of the risks of the underlying mortgage loans.

CMBS are subject to several risks created through the securitization process, as well as all of the risks of the underlying mortgage loans. Subordinate CMBS are paid interest only to the extent that there are funds available to make payments. In the event of default and the exhaustion of any equity support, reserve fund, letter of credit and any classes of securities junior to those in which we invest, we may not be able to recover all of our investment in the securities we purchase. Furthermore, to the extent the collateral pool includes delinquent loans, there is a risk that interest payments on subordinate CMBS will not be fully paid.

Our investments in non-investment grade rated loans, corporate bank debt and debt securities of commercial real estate operating or finance companies will be subject to the specific risks relating to the particular company and to the general risks of investing in real estate-related loans and securities, which may result in significant losses.

Some of our investments do not conform to conventional loan standards applied by traditional lenders and either will not be rated or will be rated as non-investment grade by the rating agencies. The non-investment grade ratings for these assets typically result from the overall leverage of the loans, the lack of a strong operating history for the properties underlying the loans, the borrowers' credit history, the properties' underlying cash flow or other factors. As a result, these investments have a higher risk of default and loss than investment grade rated assets. We also may invest in corporate bank debt and debt securities of commercial real estate operating or finance companies. These investments will involve special risks relating to the particular company, including its financial condition, liquidity, results of operations, business and prospects. In particular, the debt securities are often non-collateralized and may be subordinated to its other obligations. There are no limits on the percentage of unrated or non-investment grade rated assets we may hold in our investment portfolio.

These investments will also subject us to the risks inherent with real estate-related investments referred to in our Annual Report, including the risks described with respect to commercial properties 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 specific to the type and use of a particular property.

These risks may adversely affect the value of our investments in commercial real estate operating and finance companies and the ability of the issuers thereof to make principal and interest payments in a timely manner, or at all, and could result in significant losses, which could have a material adverse effect on our results of operations and our ability to make distributions to our stockholders.

Our B-Notes may be subject to additional risks related to the privately negotiated structure and terms of the transaction, which may result in losses to us.

We currently hold and may acquire additional B-Notes in the future. A B-Note is a mortgage loan typically (1) secured by a first mortgage on a single large commercial property or group of related properties (and therefore reflect the risks associated with significant concentration) and (2) subordinated to an A-Note secured by the same first mortgage on the same collateral. A privately negotiated intercreditor agreement between the holders of the A- and B-Notes may restrict the rights of the B-Note holders. In particular, the intercreditor agreement may prohibit the B-Note holder from calling the loan, making modifications with respect to the loan or filing a bankruptcy petition without the consent of the A-Note holder. As a result, to the extent that

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we acquire B-Notes, the A-Note holder may take actions that we do not agree with and that are not in our stockholders' best interests.

In addition, because the rights of the B-Note holder are subordinated to the rights of the A-Note holder, the B-Note may be the first to incur loss if the loan does not perform and the collateral value diminishes. As a result, if a borrower defaults, there may not be sufficient funds remaining for B-Note holders after payment to the A-Note holders. If there are insufficient funds after payment to the A-Note holders, we could incur significant losses related to our B-Notes, which would result in operating losses for us and may limit our ability to make distributions to our stockholders. Our existing mezzanine loan assets and those that we may originate or acquire in the future are subject to greater risks of loss than senior loans secured by income-producing properties.

We currently own interests in mezzanine loans and may originate or acquire additional mezzanine loans (or interests in mezzanine loans). Mezzanine loans take the form of subordinated loans secured by junior participations in mortgages or second mortgages on the underlying property, or loans secured by a pledge of the ownership interests of either the entity owning the property or a pledge of the ownership interests of the entity that owns the interest in the entity owning the property. These types of assets involve a higher degree of risk than long-term senior mortgage lending secured by income-producing real property, because the loan may be foreclosed on by the senior lender. 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. 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 paid in full. Where debt senior to our loan exists, the presence of intercreditor arrangements between the holder of the senior mortgage loan and us, as the mezzanine lender, may limit our ability to amend our loan documents, assign our loans, accept prepayments, exercise our remedies and control decisions made in bankruptcy proceedings relating to borrowers. As a result, we may not recover some or all of our investment, which could result in losses. In addition, even if we are able to foreclose on the underlying collateral following a default on a mezzanine loan, we would replace the defaulting borrower and, to the extent income generated on the underlying property is insufficient to meet outstanding debt obligations on the property, we may need to commit substantial additional capital to stabilize the property and prevent additional defaults to lenders with remaining liens on the property. Significant losses related to our current or future mezzanine loans could have a material adverse effect on our results of operations and our ability to make distributions to our stockholders.

The bridge loans that we may originate and/or acquire will involve a greater risk of loss than traditional investment-grade mortgage loans with fully insured borrowers.

We may originate and/or acquire bridge loans secured by first lien mortgages on a property to borrowers who are typically seeking short-term capital to be used in an acquisition, construction or rehabilitation of a property. The typical borrower under a bridge loan has usually identified an undervalued asset that has been under-managed and/or is located in a recovering market. If the market in which the asset is located fails to recover according to the borrower's projections, or if the borrower fails to improve the quality of the asset's management and/or the value of the asset, the borrower may not receive a sufficient return on the asset to satisfy the bridge loan, and we bear the risk that we may not recover some or all of our initial expenditure.

In addition, borrowers usually use the proceeds of a conventional mortgage to repay a bridge loan. Bridge loans therefore are subject to risks of a borrower's inability to obtain permanent financing to repay the bridge loan. Bridge loans are also subject to risks of borrower defaults, bankruptcies, fraud, losses and "special hazard" losses that are not covered by standard hazard insurance. In the event of any default under bridge loans held by us, we bear the risk of loss of principal and non-payment of interest and fees to the extent of any deficiency between the value of the mortgage collateral and the principal amount and unpaid interest of the bridge loan. To the extent we suffer such losses with respect to our bridge loans, the value of our company and the price of our shares of common stock may be adversely affected.

We may acquire non-Agency RMBS collateralized by subprime and Alt A mortgage loans, which are subject to increased risks.

We also may acquire non-Agency RMBS, which are backed by residential real estate property but, in contrast to Agency RMBS, their principal and interest are not guaranteed by federally chartered entities such as the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation, and, in the case of the Government National Mortgage Association, the U.S. Government. We may acquire non-Agency RMBS backed by collateral pools of mortgage loans that have been originated using underwriting standards that are less restrictive than those used in underwriting “prime mortgage loans” and “Alt A mortgage loans.” These lower standards include mortgage loans made to borrowers having imperfect or impaired credit histories, 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 current economic conditions, including fluctuations in interest rates and lower home prices, as well as aggressive lending practices, subprime mortgage loans have in recent periods experienced increased rates of

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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 non-Agency RMBS backed by subprime mortgage loans that we may acquire could be adversely affected, which could materially and adversely impact our results of operations, financial condition and business.

We may invest in derivative instruments, which would subject us to increased risk of loss.

Subject to maintaining our qualification as a REIT, we may invest in derivative instruments. The prices of derivative instruments, including futures and options, are highly volatile. Payments made pursuant to swap agreements may also be highly volatile. Price movements of futures and options contracts and payments pursuant to swap agreements are influenced by, among other things, interest rates, changing supply and demand relationships, trade, fiscal, monetary and exchange control programs and policies of governments, and national and international political and economic events and policies. The value of futures, options and swap agreements also depends upon the value of the assets underlying them. In addition, our assets are also subject to the risk of the failure of any of the exchanges on which our positions trade or of our clearinghouses or counterparties.

We may buy or sell (write) both call options and put options, and when we write options, we may do so on a “covered” or an “uncovered” basis. A call option is “covered” when the writer owns securities of the same class and amount as those to which the call option applies. A put option is covered when the writer has an open short position in securities of the relevant class and amount. Our option transactions may be part of a hedging strategy (i.e., offsetting the risk involved in another securities position) or a form of leverage, in which we will have the right to benefit from price movements in a large number of securities with a small commitment of capital. These activities involve risks that can be substantial, depending on the circumstances.

In general, without taking into account other positions or transactions we may enter into, the principal risks involved in options trading can be described as follows: when we buy an option, a decrease (or inadequate increase) in the price of the underlying security in the case of a call, or an increase (or inadequate decrease) in the price of the underlying security in the case of a put, could result in a total loss of our investment in the option (including commissions). We could mitigate those losses by selling short, or buying puts on, the securities for which we hold call options, or by taking a long position (e.g., by buying the securities or buying calls on them) in securities underlying put options. When we sell (write) an option, the risk can be substantially greater than when we buy an option. The seller of an uncovered call option bears the risk of an increase in the market price of the underlying security above the exercise price. The risk is theoretically unlimited unless the option is “covered,” in which case we would forego the opportunity for profit on the underlying security only to the extent the market price of the security rises above the exercise price. If the price of the underlying security were to drop below the exercise price, the premium received on the option (after transaction costs) would provide profit which, in the case of a covered call, would reduce or offset any loss we might suffer as a result of owning the security. The Commodity Futures Trading Commission and certain commodity exchanges have established limits referred to as speculative position limits or position limits on the maximum net long or net short position which any person or group of persons may hold or control in particular futures and options. Limits on trading in options contracts also have been established by the various options exchanges. It is possible that the trading decisions may have to be modified and that positions held may have to be liquidated in order to avoid exceeding such limits. Such modification or liquidation, if required, could adversely affect our results of operations, financial condition and business.

We may invest in credit default swaps, which may subject us to an increased risk of loss.

Subject to maintaining our qualification as a REIT, we may invest in CDSs. A CDS is a contract between two parties which transfers the risk of loss if a borrower fails to pay principal or interest on time or files for bankruptcy. CDS can be used to hedge a portion of the default risk on a single corporate debt or a portfolio of loans. In addition, CDS can be used to implement our Manager’s view that a particular credit, or group of credits, will experience credit improvement. In the case of expected credit improvement, we may “write” credit default protection in which we receive spread income. We may also “purchase” credit default protection even in the case in which we do not own the



referenced instrument if, in the judgment of our Manager, there is a high likelihood of credit deterioration. The CDS market in high yield securities is comparatively new and rapidly evolving compared to the CDS market for more seasoned and liquid investment grade securities. Swap transactions dependent upon credit events are priced incorporating many variables, including the potential loss upon default. As such, there are many factors upon which market participants may have divergent views.

We may invest in construction loans, which may expose us to an increased risk of loss.

We may invest in construction loans. If we fail to fund our entire commitment on a construction loan or if a borrower otherwise fails to complete the construction of a project, there could be adverse consequences associated with the loan, including: a loss of the value of the property securing the loan, especially if the borrower is unable to raise funds to complete it from other sources; a borrower claim against us for failure to perform under the loan documents; increased costs to the

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borrower that the borrower is unable to pay; a bankruptcy filing by the borrower; and abandonment by the borrower of the collateral for the loan.

Participating interests may not be available and, even if obtained, may not be realized.

In connection with the origination or acquisition of certain structured finance assets, we have obtained, and subject to maintaining our qualification as a REIT, may obtain in the future, participating interests, or equity “kickers,” in the owner of the property that entitle us to payments based upon a development’s cash flow or profits or any increase in the value of the property that would be realized upon a refinancing or sale thereof. Competition for participating interests is dependent to a large degree upon market conditions. Participating interests are more difficult to obtain when real estate financing is available at relatively low interest rates. Participating interests are not insured or guaranteed by any governmental entity and are therefore subject to the general risks inherent in real estate investments. Therefore, there can be no assurance that such interests will result in additional payments to us.

The residential mortgage loans that we may originate and/or acquire, and that underlie the RMBS we may acquire, are subject to risks particular to investments secured by mortgage loans on residential property.

Residential mortgage loans are secured by single-family residential property and are subject to risks of delinquency, foreclosure and loss. The ability of a borrower to repay a loan secured by a residential property typically is dependent upon the income or assets of the borrower. A number of factors, including a general economic downturn, acts of God, terrorism, social unrest and civil disturbances, may impair borrowers’ abilities to repay their loans. In the event of any default under a mortgage 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 principal and accrued interest of the mortgage loan, which could have a material adverse effect on our cash flow from operations. In the event of the bankruptcy of a mortgage loan borrower, the mortgage loan to such borrower will be deemed to be secured only to the extent of the value of the underlying collateral at the time of bankruptcy (as determined by the bankruptcy court), and the lien securing the mortgage loan will be subject to the avoidance powers of the bankruptcy trustee or debtor-in-possession to the extent the lien is unenforceable under state law. In addition, if the federal or a U.S. state government imposes freezes on the ability of lenders to foreclose on residential property or requires lenders to modify loans, we may be precluded from foreclosing on, or exercising other remedies with respect to, the property underlying loans, or may be required to accept modifications not favorable to us.

To the extent that we purchase or originate residential mortgage loans, we may be subject to liability for potential violations of predatory lending laws, which could adversely impact our results of operations, financial condition and business.

Various U.S. federal, state and local laws have been enacted that are designed to discourage predatory lending practices. The federal Home Ownership and Equity Protection Act of 1994 (“HOEPA”), prohibits inclusion of certain provisions in residential mortgage loans that have mortgage rates or origination costs in excess of prescribed levels and requires that borrowers be given certain disclosures prior to origination. Some states have enacted, or may enact, similar laws or regulations, which in some cases impose restrictions and requirements greater than those in the HOEPA. In addition, under the anti-predatory lending laws of some states, the origination of certain residential mortgage loans, including loans that are not classified as “high cost” loans under applicable law, must satisfy a net tangible benefits test with respect to the related borrower. This test may be highly subjective and open to interpretation. As a result, a court may determine that a residential mortgage loan, for example, does not meet the test even if the related originator reasonably believed that the test was satisfied.

To the extent that we originate residential mortgage loans, we would be required to comply with these laws. In addition, if we purchase residential mortgage loans from residential mortgage loan originators or servicers who failed to comply with these laws as an assignee or purchaser to the related residential mortgage loans, we could be subject to monetary penalties and the borrowers could rescind the affected residential mortgage loans. Lawsuits have been brought in various states making claims against assignees or purchasers of high cost loans for violations of state law. Named defendants in these cases have included numerous participants within the secondary mortgage market. If any of our loans are found to have been originated in violation of predatory or abusive lending laws, we could incur losses, which could materially and adversely impact our results of operations, financial condition and business.

We may experience a decline in the fair value of our assets, which could materially and adversely affect our results of operations, financial condition and our ability to make distributions to our stockholders.

A decline in the fair market value of our assets may require us to recognize an “other-than-temporary” impairment against such assets under accounting principles generally accepted in the United States of America (“GAAP”) if we were to determine that, with respect to any assets in unrealized loss positions, we do not have the ability and intent to hold such assets to maturity or for a period of time sufficient to allow for recovery to the amortized cost of such assets. If such a determination were to be made, we would recognize unrealized losses through earnings and write down the amortized cost of such assets to a new cost basis, based on the fair value of such assets on the date they are considered to be other-than-temporarily impaired. Such

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impairment charges reflect non-cash losses at the time of recognition; subsequent disposition or sale of such assets could further affect our future losses or gains, as they are based on the difference between the sale price received and adjusted amortized cost of such assets at the time of sale. If we experience a decline in the fair value of our assets, our results of operations, financial condition and our ability to make distributions to our stockholders could be materially and adversely affected.

Some of our portfolio investments will be recorded at fair value and, as a result, there will be uncertainty as to the value of these investments.

Some of our portfolio investments will be in the form of positions or securities that are not publicly traded. The fair value of securities and other investments that are not publicly traded may not be readily determinable. Depending on whether these securities and other investments are classified as available-for-sale or held-to-maturity, we will value certain of these investments quarterly at fair value, as determined in accordance with GAAP. Because such valuations are subjective, the fair value of certain of our assets may fluctuate over short periods of time and our determinations of fair value may differ materially from the values that would have been used if a ready market for these securities existed. The value of our common stock could be adversely affected if our determinations regarding the fair value of these investments were materially higher than the values that we ultimately realize upon their disposal.

Valuations of certain assets in which we may invest may be difficult to obtain or unreliable. In general, third-party dealers and pricing services heavily disclaim their valuations. Dealers may claim to furnish valuations only as an accommodation and without special compensation, and so they may disclaim any and all liability for any direct, incidental or consequential damages arising out of any inaccuracy or incompleteness in valuations, including any act of negligence or breach of any warranty. Depending on the complexity and illiquidity of an asset, valuations of the same asset can vary substantially from one dealer or pricing service to another. Therefore, conflicts of interest may exist to the extent that our Manager is involved in the determination of the fair value of our investments. Additionally, our results of operations for a given period could be adversely affected if our determinations regarding the fair value of these investments were materially higher than the values that we ultimately realize upon their disposal. During periods of market uncertainty and volatility, the valuation process may be particularly challenging and more unpredictable.

Accounting rules for certain of our investments are highly complex and involve significant judgment and assumptions, and changes in such rules, accounting interpretations or our assumptions could adversely impact our ability to timely and accurately prepare our financial statements.

Accounting rules for mortgage loan sales and securitizations, valuations of financial instruments, investment consolidations and other aspects of our anticipated operations are highly complex and involve significant judgment and assumptions. These complexities could lead to a delay in preparation of financial information and the delivery of this information to our stockholders. Changes in accounting rules, interpretations or our assumptions could undermine our ability to prepare timely and accurate financial statements, which could result in a lack of investor confidence in our publicly filed information and could materially and adversely affect the market price of our common stock.

Prepayment rates may adversely affect the value of our portfolio of assets.

The value of our assets may be affected by prepayment rates on mortgage loans. If we acquire mortgage-related securities or a pool of mortgage securities, we anticipate that the underlying mortgages will prepay at a projected rate generating an expected yield. If we purchase assets at a premium to par value, when borrowers prepay their mortgage loans faster than expected, the corresponding prepayments on the mortgage-related securities may reduce the expected yield on such securities because we will have to amortize the related premium on an accelerated basis. Conversely, if we purchase assets at a discount to par value, when borrowers prepay their mortgage loans slower than expected, the decrease in corresponding prepayments on the mortgage-related securities may reduce the expected yield on such securities because we will not be able to accrete the related discount as quickly as originally anticipated. Prepayment rates on loans may be affected by a number of factors including, but not limited to, the availability of mortgage credit, the relative economic vitality of the area in which the related properties are located, the servicing of the mortgage loans, possible changes in tax laws, other opportunities for investment, and other economic, social, geographic, demographic and legal factors and other factors beyond our control. Consequently, such prepayment rates cannot be

predicted with certainty and no strategy can completely insulate us from prepayment or other such risks. In periods of declining interest rates, prepayment rates on mortgage loans generally increase. If general interest rates decline at the same time, 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, as a result of the risk of prepayment, the market value of the prepaid assets may benefit less than other fixed income securities from declining interest rates. Recent market conditions may make it more difficult for us to analyze potential investment opportunities or our portfolio of assets.

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Our success depends, in part, on our ability to analyze effectively potential investment opportunities in order to assess the level of risk-adjusted returns that we should expect from any particular investment. To estimate the value of a particular asset, our Manager and its affiliates may use historical assumptions that may or may not be appropriate in light of the downturn in the real estate market and general economy in recent years. To the extent that our Manager uses historical assumptions that are inappropriate under current market conditions, we may overpay for an asset or acquire an asset that we otherwise might not acquire, which could have a material adverse effect on our results of operations and our ability to make distributions to our stockholders.

In addition, as part of our overall portfolio risk management, we analyze interest rate changes and prepayment trends separately and collectively to assess their effects on our portfolio of assets. In conducting our analysis, we depend on certain assumptions based upon historical trends with respect to the relationship between interest rates and prepayments under normal market conditions. Dislocations in the mortgage market or other developments may change the way that prepayment trends have historically responded to interest rate changes, which may adversely affect our ability to (1) assess the market value of our portfolio of assets, (2) implement our hedging strategies and (3) implement techniques to reduce our prepayment rate volatility. If our estimates prove to be incorrect or our hedges do not adequately mitigate the impact of changes in interest rates or prepayments, we may incur losses that could materially and adversely affect our financial condition, results of operations and our ability to make distributions to our stockholders.

Many of our investments may be illiquid and we may not be able to vary our portfolio in response to changes in economic and other conditions.

Investments in mortgage-related assets generally experience periods of illiquidity. The lack of liquidity may result from the absence of a willing buyer or an established market for these assets, as well as legal or contractual restrictions on resale or the unavailability of financing for these assets. In addition, certain of our target assets, such as B-Notes, mezzanine loans and bridge and other loans, are also particularly illiquid investments due to their short life, their potential unsuitability for securitization and the greater difficulty of recovery in the event of a borrower's default. Further, we may face other restrictions on our ability to liquidate an investment in a business entity to the extent that we or our Manager has or could be attributed with material, non-public information regarding such business entity. The illiquidity of our investments may make it difficult for us to sell such investments at advantageous times or in a timely manner if the need or desire arises, including, if necessary, to maintain our status as a REIT or to maintain our exemption from the 1940 Act. Moreover, turbulent market conditions, such as those currently in effect, could significantly and negatively affect the liquidity of our assets. As a result, our ability to vary our portfolio in response to changes in economic and other conditions may be relatively limited, which may cause us to incur losses. If we are required to liquidate all or a portion of our portfolio quickly, we may realize significantly less than the value at which we have previously recorded our assets. If and to the extent that we use leverage to finance our investments that are or become liquid, the adverse impact on us related to trying to sell assets in a short period of time for cash could be greatly exacerbated.

If borrowers under our loans or purchasers of our assets pay us in the form of debt or equity securities, a decline in the value of such securities could cause the value of our investment to decrease significantly or we could incur a loss, either of which could have a material adverse effect on our results of operations.

Some of our loans may contain payment-in-kind provisions that permit the borrower to pay us principal and/or interest in the form of debt or equity securities rather than cash. In addition, in connection with the sale of our assets, we may receive debt or equity securities as payment for all or part of the purchase price. To the extent that we receive debt or equity securities as payments-in-kind under our loan agreements or as full or partial consideration for assets that we sell, a decline in the value of such securities could cause the value of our investment to decrease significantly or we could incur a loss, either of which could have a material adverse effect on our results of operations.

Our investments may be concentrated and will be subject to risk of default.

We are not required to observe specific diversification criteria, except as may be set forth in the investment guidelines adopted by our board of directors. Therefore, our investments may at times be concentrated in certain asset types that are subject to a higher risk of non-performance or foreclosure, or secured by a single property, related properties or

properties concentrated in a limited number of geographic locations. To the extent that our portfolio is concentrated in any one region or type of asset, downturns relating generally to such region or type of asset may result in defaults on a number of our investments within a short time period, which may materially and adversely affect our results of operations, the value of our common stock and our ability to pay dividends to our stockholders.

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

Some of our investments may be rated by Moody's Investors Service, Fitch Ratings or Standard & Poor's. Any credit ratings on our investments are subject to ongoing evaluation by credit rating agencies, and we cannot assure you that any such

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ratings will not be changed or withdrawn by a rating agency in the future if, in its judgment, circumstances warrant. If rating agencies assign a lower-than-expected rating or reduce or withdraw, or indicate that they may reduce or withdraw, their ratings of our investments in the future, the value of these investments could significantly decline, which would adversely affect the value of our investment portfolio and could result in losses upon disposition or the failure of borrowers to satisfy their debt service obligations to us.

Our investments in joint ventures that do not use the U.S. dollar as a functional currency subject us to currency rate exposure and the uncertainty of foreign laws and markets.

We have investments in joint ventures that are denominated in Euros, which exposes us to foreign currency risk. A change in foreign currency exchange rates may have an adverse impact on the valuation of our equity investments in foreign joint ventures. Although we generally use collars (consisting of caps and floors) to hedge the foreign currency exposure of our investments, we may not be able to do so successfully and may incur losses on these equity investments as a result of exchange rate fluctuations. In addition, equity investments in foreign countries also subject us to risks of multiple and conflicting tax laws and regulations and political and economic instability abroad, which could adversely affect our receipt of distributions from these investments.

### Risks Related to Our Financing and Hedging Activities

The documents that govern our credit facility restrict our ability to engage in certain activities and require mandatory prepayment in certain circumstances, either of which could materially adversely affect our growth prospects, financial condition and ability to make distributions to our stockholders.

The documents that govern our credit facility contain customary negative covenants and other financial and operating covenants that, among other things may:

- restrict our and our subsidiaries' ability to incur additional indebtedness;
- restrict our and our subsidiaries' ability to make certain investments;
- restrict our and our subsidiaries' ability to merge with another company;
- restrict our and our subsidiaries' ability to create, incur or assume liens;
- restrict our and our subsidiaries' ability to sell, transfer or restructure our assets for any reason;
- restrict our ability to make distributions to our stockholders; and
- require us to maintain certain financial coverage ratios.

In addition, our new credit facility limits the amount of distributions to our stockholders to the greater of (i) 115% of taxable income plus depreciation expense for the applicable fiscal year, and (ii) the greater of (A) the amount necessary for us to maintain our status as a REIT and (B) the amount necessary to avoid income tax and, so long as no default has occurred and is continuing or shall result therefrom, excise tax under the Internal Revenue Code. In addition, during certain events of default resulting from nonpayment under the credit facility or certain bankruptcy events under the documents that govern our credit facility, we are restricted, in certain circumstances, from making any distributions in respect of our equity securities, including distributions to our stockholders necessary to maintain our qualification as a REIT, which could cause us to lose our REIT qualification and become subject to U.S. federal income tax.

Our credit facility permits us to incur significant indebtedness, which could require that we generate significant cash flow to satisfy the payment and other obligations under our credit facility.

We may incur significant indebtedness in connection with draws under our credit facility. This indebtedness may exceed our cash on hand and/or our cash flows from operating activities. Our ability to meet the payment and other obligations under our credit facility depends on our ability to generate sufficient cash flow in the future. Our ability to generate cash flow, to some extent, is subject to general economic, financial, competitive, legislative and regulatory factors, as well as other factors that are beyond our control. We cannot assure you that our business will generate cash flow from operations, or that future borrowings will be available to us, in amounts sufficient to enable us to meet our



payment obligations under our credit facility. If we are not able to generate sufficient cash flow to service our credit facility and other debt obligations, we may need to refinance or restructure our debt, reduce or delay capital investments, or seek to raise additional capital. If we are unable to implement one or more of these alternatives, we may not be able to meet our payment obligations under our credit facility, which could materially and adversely affect our liquidity.

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We expect that the trading price of our Convertible Senior Notes ("Convertible Notes") will be significantly affected by changes in the market price of our common stock, the interest rate environment and our credit quality, each of which could change substantially at any time.

We expect that the trading price of the Convertible Notes will depend on a variety of factors, including, without limitation, the market price of our common stock, the interest rate environment and our credit quality. Each of these factors may be volatile, and may or may not be within our control.

For example, the trading price of the Convertible Notes will increase with the market price and volatility of our common stock. We cannot, however, predict whether the market price of our common stock will rise or fall or whether the volatility of our common stock will continue at its historical level. In addition, general market conditions, including the level of, and fluctuations in, the market price of stocks generally, may affect the market price and the volatility of our common stock. Moreover, we may or may not choose to take actions that could influence the volatility of our common stock.

Likewise, if interest rates, or expected future interest rates, rise during the term of the notes, the yield of the Convertible Notes will likely decrease, but the value of the convertibility option embedded in the notes will likely increase. Because interest rates and interest rate expectations are influenced by a wide variety of factors, many of which are beyond our control, we cannot assure you that changes in interest rates or interest rate expectations will not adversely affect the trading price of the notes.

Furthermore, the trading price of the Convertible Notes will likely be significantly affected by any change in our credit quality. Because our credit quality is influenced by a variety of factors, some of which are beyond our control, we cannot guarantee that we will maintain or improve our credit quality during the term of the Convertible Notes. In addition, because we may choose to take actions that adversely affect our credit quality, such as incurring additional debt, there can be no guarantee that our credit quality will not decline during the term of the Convertible Notes, which would likely negatively impact the trading price of the Convertible Notes.

The claims of holders of our Convertible Notes will be structurally subordinated to claims of creditors of our subsidiaries, because our subsidiaries will not guarantee the Convertible Notes. In addition, we are a holding company with minimal independent operations. Our ability to repay our debt, including the Convertible Notes, depends on the performance of our subsidiaries and their ability to make distributions to us.

The Convertible Notes are not guaranteed by any of our subsidiaries. Accordingly, none of our subsidiaries is currently, and may not become, obligated to pay any amounts due pursuant to the Convertible Notes, or to make any funds available therefor. Consequently, claims of holders of the Convertible Notes will be structurally subordinated to the claims of creditors and preferred stockholders of these subsidiaries, including trade creditors. As a result, in the event of a bankruptcy, liquidation or reorganization of any of our subsidiaries, such subsidiaries will pay the holders of their debt and their trade creditors before they will be able to distribute any of their assets to us.

As a holding company, substantially all of our business is conducted through our subsidiaries, which are separate and distinct legal entities. Therefore, our ability to service our indebtedness, including the Convertible Notes, is dependent on the earnings and the distribution of funds (whether by dividend, distribution or loan) from our subsidiaries. None of our subsidiaries is obligated to make funds available to us for payment on the Convertible Notes. We cannot assure you that the agreements governing the existing and future indebtedness of our subsidiaries will permit our subsidiaries to provide us with sufficient dividends, distributions or loans to fund payments on the notes when due. In addition, any payment of dividends, distributions or loans to us by our subsidiaries could be subject to restrictions on dividends or repatriation of earnings under applicable local law and monetary transfer restrictions in the jurisdictions in which our subsidiaries operate.

If we incur substantial additional debt, these higher levels of debt may affect our ability to pay the principal of and interest on the Convertible Notes.

We and our subsidiaries may be able to incur substantial additional debt in the future, some of which may be secured debt. Neither the base indenture nor the supplemental indentures governing our Convertible Notes restricts our ability to incur additional indebtedness or requires us to maintain financial ratios or specified levels of net worth or liquidity. If we incur substantial additional indebtedness in the future, these higher levels of indebtedness may affect our ability to pay the principal of and interest on the Convertible Notes, or any fundamental change purchase price, and our

creditworthiness generally.

We and our subsidiaries are, and may in the future become, parties to agreements and instruments, which, among other things, may contain financial and other restrictive covenants that will limit our ability to engage in activities that may be in our long-term best interests. For example, under the terms of our revolving credit facility, we are required to satisfy certain financial covenants, including, among others, a minimum consolidated fixed charge coverage ratio of 2.25 to 1.0; a maximum consolidated leverage ratio of 0.5 to 1.0, minimum liquidity not less than \$5,000,000; and a minimum consolidated tangible net worth greater than or equal to the sum of (i) \$1,178,000,000 and (ii) 80% of net cash proceeds received by us from issuances or sales of our common equity. Our failure to comply with those covenants could result in an event of default that, if not cured or waived, could result in the acceleration of all of our debt.

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Servicing the Convertible Notes requires a significant amount of cash, and we may not have sufficient cash flow from our business to pay our debt.

Our ability to make scheduled payments of the principal of, to pay interest on or to refinance our indebtedness, including the Convertible Notes, depends on our future performance, which is subject to economic, financial, competitive and other factors beyond our control. Our business may not continue to generate cash flow from operations in the future sufficient to service our debt and make necessary capital expenditures. If we are unable to generate such cash flow, we may be required to adopt one or more alternatives, such as selling assets, restructuring debt or obtaining additional equity capital on terms that may be onerous or highly dilutive. Our ability to refinance our indebtedness will depend on the capital markets and our financial condition at such time. We may not be able to engage in any of these activities or engage in these activities on desirable terms, which could result in a default on our debt obligations.

Recent regulatory actions may adversely affect the trading price and liquidity of the Convertible Notes.

We expect that many investors in, and potential purchasers of, the Convertible Notes will employ, or seek to employ, a convertible arbitrage strategy with respect to the Convertible Notes. Investors would typically implement this strategy by selling short the common stock underlying the Convertible Notes and dynamically adjusting their short position while they hold the Convertible Notes. Investors may also implement this strategy by entering into swaps on our common stock in lieu of or in addition to short selling the common stock.

The SEC and other regulatory and self-regulatory authorities have implemented various rules and may adopt additional rules in the future that may impact those engaging in short selling activity involving equity securities (including our common stock), including Rule 201 of SEC Regulation SHO, the Financial Industry Regulatory Authority, Inc.'s "Limit Up-Limit Down" program, market-wide circuit breaker systems that halt trading of securities for certain periods following specific market declines, and rules stemming from the enactment and implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act. Past regulatory actions, including emergency actions or regulations have had a significant impact on the trading prices and liquidity of equity-linked instruments. Any governmental action that similarly restricts the ability of investors in, or potential purchasers of, the Convertible Notes to effect short sales of our common stock or enter into swaps on our common stock could similarly adversely affect the trading price and the liquidity of the Convertible Notes.

In addition, if investors and potential purchasers seeking to employ a convertible arbitrage strategy are unable to borrow or enter into swaps on our common stock, in each case on commercially reasonable terms, the trading price and liquidity of the Convertible Notes may be adversely affected.

We may not have the ability to raise funds necessary to purchase the notes upon a fundamental change.

If a "fundamental change" occurs under the indenture or the supplemental indentures governing the Convertible Notes, holders of the Convertible Notes have the right, at their option, to require us to purchase for cash any or all of their Convertible Notes, or any portion of the principal amount thereof such that the principal amount that remains outstanding of each Convertible Note purchased in part equals \$1,000 or an integral multiple of \$1,000 in excess thereof. The fundamental change purchase price will equal 100% of the principal amount of the notes to be purchased, plus accrued and unpaid interest, if any, to, but excluding, the fundamental change purchase date. However, we may not have sufficient funds at the time we are required to purchase the Convertible Notes surrendered therefor and we may not be able to arrange necessary financing on acceptable terms, if at all. In addition, our ability to purchase the Convertible Notes may be limited by law, by regulatory authority or by the agreements governing our other indebtedness outstanding at the time. If we fail to pay the fundamental change purchase price when due, we will be in default under the indenture governing the Convertible Notes. A default under the indenture or the fundamental change itself could also constitute a default under the agreements governing our other existing and future indebtedness which would further restrict our ability to make required payments under the Convertible Notes.

We may issue additional shares of our common stock or instruments convertible into our common stock, including in connection with conversions of Convertible Notes, and thereby materially and adversely affect the price of our common stock, and, in turn, the Convertible Notes.

We are not restricted from issuing additional shares of our common stock or other instruments convertible into our common stock during the life of the Convertible Notes. We cannot predict the size of future issuances or the effect, if

any, that they may have on the market price for our common stock. If we issue additional shares of our common stock or instruments convertible into our common stock, it may materially and adversely affect the price of our common stock and, in turn, the price of the Convertible Notes. Furthermore, the conversion or exercise of some or all of the Convertible Notes may dilute the ownership interests of existing stockholders, and any sales in the public market of shares of our common stock issuable upon any such conversion or exercise could adversely affect prevailing market prices of our common stock or the Convertible Notes. In addition, the anticipated issuance and sale of substantial amounts of common stock or the anticipated conversion or exercise of securities into shares of our common stock could depress the price of our common stock.

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Holders of Convertible Notes will not be entitled to any rights with respect to our common stock, but will be subject to all changes made with respect to our common stock to the extent our conversion obligations include shares of our common stock.

Holders of Convertible Notes will not be entitled to any rights with respect to our common stock (including, without limitation, voting rights and rights to receive any dividends or other distributions on our common stock), until the time at which they become record holders of our common stock upon conversion of the Convertible Notes. For example, if an amendment is proposed to our certificate of incorporation or bylaws requiring stockholder approval and the record date for determining the stockholders of record entitled to vote on the amendment occurs prior to the date a holder of Convertible Notes is deemed to be a record holder of our common stock following a conversion of the Convertible Notes, such holder generally will not be entitled to vote on the amendment, but will nevertheless be subject to any changes affecting our common stock.

Certain provisions in the Convertible Notes and the indenture could delay or prevent an otherwise beneficial takeover or takeover attempt of us and, therefore, the ability of holders to exercise their rights associated with a potential fundamental change or a make-whole fundamental change.

Certain provisions in the Convertible Notes and the indenture could make it more difficult or more expensive for a third party to acquire us. For example, if an acquisition event constitutes a fundamental change under the indenture governing the Convertible Notes, holders of the Convertible Notes will have the right to require us to purchase their Convertible Notes in cash. In addition, if an acquisition event constitutes a “make-whole fundamental change” under the indenture governing the Convertible Notes, we may be required to increase the conversion rate for holders who convert their Convertible Notes in connection with such make-whole fundamental change. Our obligations under the Convertible Notes, the base indenture and the supplemental indentures could increase the cost of acquiring us or otherwise discourage a third party from acquiring us or removing incumbent management.

The Convertible Notes may not be rated or may receive a lower rating than anticipated.

We do not intend to seek a rating on either outstanding series of our Convertible Notes. However, if one or more rating agencies rates either series of our Convertible Notes and assigns the notes a rating lower than the rating expected by investors, or reduces their rating in the future, the trading price of the Convertible Notes and the market price of our common stock could be harmed.

In addition, the trading price of the Convertible Notes is directly affected by market perceptions of our creditworthiness. Consequently, if a credit ratings agency rates any of our debt in the future or downgrades or withdraws any such rating, or puts us on credit watch, the trading price of the Convertible Notes is likely to decline. We may use additional leverage to execute our business strategy, which may adversely affect the return on our assets, reduce cash available for distribution to our stockholders and increase losses when economic conditions are unfavorable.

Subject to market conditions and availability, we may use additional leverage to finance our assets through borrowings from a number of sources, including repurchase agreements, resecuritizations, securitizations, warehouse facilities and bank credit facilities (including draws under our existing credit facility). We may also seek to take advantage of available borrowings, if any, provided by the FDIC in connection with the acquisition of assets from the FDIC or provided under government sponsored debt programs to acquire all types of commercial real estate loans and other real estate-related assets, to the extent such assets are eligible for funding under such programs. Although we are not required to maintain any particular assets-to-equity leverage ratio, the amount of leverage we may deploy for particular assets will depend on our available capital, our ability to access financing arrangements, our Manager’s estimate of the stability of cash flows generated from the asset in our portfolio and our Manager’s assessment of the risk-adjusted returns associated with those assets. The percentage of leverage will vary over time depending on our ability to enter into repurchase agreements, resecuritizations, securitizations, warehouse facilities and additional bank credit facilities (including term loans and revolving facilities), our ability to participate in and obtain funding under programs established by the U.S. government, available credit limits and financing rates, type and/or amount of collateral required to be pledged and our assessment of the appropriate amount of leverage for the particular assets we are funding. We may use leverage at times and in amounts deemed appropriate by our Manager without approval of our board of directors or our stockholders.

To the extent that we use leverage to finance our assets, our financing costs will reduce cash available for distributions to stockholders. We may not be able to meet our financing obligations and, to the extent that we cannot, we risk the loss of some or all of our assets to liquidation or sale to satisfy the obligations. We may leverage certain of our assets through repurchase agreements. A decrease in the value of these assets may lead to margin calls, which may require us to sell assets at significantly depressed prices due to market conditions or otherwise, and cause us to incur losses. The satisfaction of such margin calls also may reduce cash flow available for distribution to our stockholders. Any reduction in distributions to our stockholders may cause the value of our common stock to decline.

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Our outstanding indebtedness and indebtedness to be incurred in the future could subject us to increased risk of loss, which could have a material adverse effect on our results of operations and our ability to make distributions to our stockholders.

As deemed appropriate by our Manager in its discretion, we may incur indebtedness, which, together with our existing indebtedness, could subject us to several risks, including, among others, that:

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

Any repurchase agreements that we use to finance our assets may require us to provide additional collateral or pay down debt.

We are a party to a \$150 million master repurchase agreement, and we may enter into additional repurchase agreements in the future. Our repurchase agreement and any future repurchase agreements involve the risk that the market value of the loans pledged or sold by us to the repurchase agreement counterparty may decline in value, in which case the counterparty may require us to provide additional collateral or to repay all or a portion of the funds advanced. We may not have the funds available to repay our debt at that time, which would likely result in defaults unless we are able to raise the funds from alternative sources, which we may not be able to achieve on favorable terms or at all. Posting additional collateral would reduce our liquidity and limit our ability to leverage our assets. If we cannot meet these requirements, the counterparty could accelerate our indebtedness, increase the interest rate on advanced funds and terminate our ability to borrow funds from them, which could materially and adversely affect our financial condition and ability to implement our business plan. In addition, in the event that the counterparty files for bankruptcy or becomes insolvent, our loans may become subject to bankruptcy or insolvency proceedings, thus depriving us, at least temporarily, of the benefit of these assets. Such an event could restrict our access to bank credit facilities and increase our cost of capital. Counterparties to these transactions may also require us to maintain a certain amount of cash or set aside assets sufficient to maintain a specified liquidity position that would allow us to satisfy our collateral obligations. As a result, we may not be able to leverage our assets as fully as we would choose which could reduce our return on assets. In the event that we are unable to meet these collateral obligations, our financial condition and prospects could deteriorate rapidly.

The utilization of any of our repurchase facilities is subject to the pre-approval of the lender.

We utilize repurchase agreements to finance certain investments. In order to borrow funds under a repurchase agreement, the lender has the right to review the potential assets for which we are seeking financing and approve such asset in its sole discretion. Accordingly, we may be unable to obtain the consent of a lender to finance an investment and alternate sources of financing for such asset may not exist.

A failure to comply with restrictive covenants in our repurchase agreements could have a material adverse effect on us.

We are subject to various restrictive covenants contained in our existing financing arrangements, including our existing repurchase agreement, and may become subject to additional covenants in connection with future financings. Our master repurchase agreement requires us to maintain compliance with various financial covenants, including a



minimum tangible net worth and cash liquidity, and specified financial ratios. These covenants may limit our flexibility to pursue certain investments or incur additional debt. If we fail to meet or satisfy any of these covenants, we would be in default under these agreements, and our lenders could elect to declare outstanding amounts due and payable, terminate their commitments, require the posting of additional collateral and enforce their interests against existing collateral. We may also be subject to cross-default and acceleration rights and, with respect to collateralized debt, the posting of additional collateral and foreclosure rights upon

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default. Further, this could also make it difficult for us to satisfy the distribution requirements necessary to maintain our status as a REIT for U.S. federal income tax purposes.

Our access to private sources of financing may be limited and thus our ability to maximize our returns may be adversely affected.

Even if we choose to use leverage to finance the acquisition of our target assets, our access to such sources of financing will depend upon a number of factors over which we have little or no control, including:

- general market conditions;
- the market's view of the quality of our assets;
- the market's perception of our growth potential;
- our eligibility to participate in and access capital from programs established by the U.S. Government;
- our current and potential future earnings and cash distributions; and
- the market price of our common stock.

Continued weaknesses in the capital and credit markets could adversely affect one or more private lenders and could cause one or more lenders to be unwilling or unable to provide us with financing or to increase the costs of such financing. In addition, several banks and other institutions that historically have been reliable sources of financing have gone out of business in recent years, which has reduced the number of lending institutions and the availability of credit. Moreover, the return on our assets and cash available for distribution to our stockholders may be reduced to the extent that market conditions prevent us from leveraging our assets or cause the cost of our financing to increase relative to the income that can be derived from the assets acquired. If we are unable to obtain financing on favorable terms or at all, we may have to curtail our investment activities, which could limit our growth prospects, and we may be forced to dispose of assets at inopportune times in order to maintain our REIT qualification and 1940 Act exemption.

As market conditions improve, structured financing alternatives are becoming more available, in addition to borrowings under warehouse and repurchase agreements, although these financing markets are still not functioning at normalized levels. Consequently, depending on market conditions at the relevant time, we may have to rely more heavily on additional equity issuances, which may be dilutive to our stockholders, or on less efficient forms of debt financing that require a larger portion of our cash flow from operations, thereby reducing funds available for our operations, future business opportunities, cash distributions to our stockholders and other purposes. We cannot assure you that we will have access to such equity or debt capital on favorable terms at the desired times, or at all, which may cause us to curtail our investment activities and/or to dispose of assets at inopportune times, and could adversely affect our results of operations and growth prospects.

We may seek to utilize non-recourse long-term securitizations in the future, and such structures may expose us to risks, which could result in losses to us.

In the future, we may seek to utilize non-recourse long-term securitizations of our investments in mortgage loans, especially loan originations, if and when they become available and to the extent consistent with the maintenance of our REIT qualification and exemption from the 1940 Act in order to generate cash for funding new investments. This would involve conveying a pool of assets to a special purpose vehicle (or the issuing entity) which would issue one or more classes of non-recourse notes pursuant to the terms of an indenture. The notes would be secured by the pool of assets. In exchange for the transfer of assets to the issuing entity, we would receive the cash proceeds on the sale of non-recourse notes and a 100% interest in the equity of the issuing entity. The securitization of our portfolio investments might magnify our exposure to losses on those portfolio investments because any equity interest we retain in the issuing entity would be subordinate to the notes issued to investors and we would, therefore, absorb all of the losses sustained with respect to a securitized pool of assets before the owners of the notes experience any losses. Moreover, we cannot be assured that we will be able to access the securitization market, or be able to do so at favorable rates. The inability to consummate securitizations of our portfolio to finance our investments on a long-term basis could require us to seek other forms of potentially less attractive financing or to liquidate assets at an inopportune time or price, which could adversely affect our performance and our ability to grow our business.

To the extent that we obtain additional debt financing, we expect that certain of our financing facilities may contain restrictive covenants relating to our operations, which could have a material adverse effect on our business, results of operations, ability to make distributions to our stockholders and the market value of our common stock.

If or when we obtain additional debt financing, lenders (especially in the case of bank credit facilities) may impose restrictions on us that would affect our ability to incur additional debt, make certain investments or acquisitions, reduce liquidity below certain levels, make distributions to our stockholders, redeem debt or equity securities and impact our flexibility to determine our operating policies and investment strategies. For example, the documents that govern our existing credit facility contain customary negative covenants and other financial and operating covenants that limit, among other things, our ability to incur additional indebtedness, make certain investments, merge with another company, and make distributions to our

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stockholders. If or when we seek to obtain additional debt financing, we could be required to agree to similar or more burdensome restrictions on our operations. Furthermore, if we fail to meet or satisfy any of these covenants, we would be in default under these agreements, and our lenders could elect to declare outstanding amounts due and payable, terminate their commitments, require the posting of additional collateral and enforce their respective interests against existing collateral. We also may be subject to cross-default and acceleration rights and, with respect to collateralized debt, the posting of additional collateral and foreclosure rights upon default. Further, this could also make it difficult for us to satisfy the qualification requirements necessary to maintain our status as a REIT for U.S. federal income tax purposes. A default also could limit significantly our financing alternatives, which could cause us to curtail our investment activities and/or dispose of assets.

Any warehouse facilities that we may obtain in the future may limit our ability to acquire assets, and we may incur losses if the collateral is liquidated.

In the event that securitization financings become available, we may utilize, if available, warehouse facilities pursuant to which we would accumulate mortgage loans in anticipation of a securitization financing, which assets would be pledged as collateral for such facilities until the securitization transaction is consummated. In order to borrow funds to acquire assets under any future warehouse facilities, we expect that our lenders thereunder would have the right to review the potential assets for which we are seeking financing. We may be unable to obtain the consent of a lender to acquire assets that we believe would be beneficial to us and we may be unable to obtain alternate financing for such assets. In addition, no assurance can be given that a securitization structure would be consummated with respect to the assets being warehoused. If the securitization is not consummated, the lender could liquidate the warehoused collateral and we would then have to pay any amount by which the original purchase price of the collateral assets exceeds its sale price, subject to negotiated caps, if any, on our exposure. In addition, regardless of whether the securitization is consummated, if any of the warehoused collateral is sold before the consummation, we would have to bear any resulting loss on the sale. Currently, we have no warehouse facilities in place, and no assurance can be given that we will be able to obtain one or more warehouse facilities on favorable terms, or at all.

Our ability to transfer assets purchased in structured transactions with the FDIC is restricted, which could have a material adverse effect on our results of operations and our ability to make distributions to our stockholders.

With respect to the loan portfolios acquired in structured transactions with the FDIC, we are restricted from conducting a sale or disposition to a single buyer of two or more assets; selling or otherwise transferring any assets to any affiliate; financing the sale of any asset; selling any asset in a transaction that provides for any recourse; or making distributions until the FDIC debt obligation has been satisfied. As a result of these restrictions, we may be unable to take actions that would otherwise be in our and our stockholders' best interests, including, among other things, selling certain assets in order to maintain our REIT qualification and/or our exemption from registration under the 1940 Act, which could have a material adverse effect on our results of operations and our ability to make distributions to our stockholders.

Our investments in international real estate-related assets are subject to special risks that we may not manage effectively, which would have a material adverse effect on our results of operations and our ability to make distributions to our stockholders.

We have invested in assets outside of the United States and, from time to time, may make additional such investments if our Manager deems the investments appropriate in its discretion. Our investments in non-domestic real estate-related assets are subject to certain risks associated with international investments generally, including, among others:

- economic fluctuations in the international locations in which we invest;
- the availability of capital to purchase assets located outside the United States may be unavailable on favorable terms or at all, or may be subject to non-customary covenants that hinder our operations;
- the burdens of complying with international regulatory requirements and prohibitions that differ between jurisdictions;
- social, political and economic changes and disruptions;
- tariffs and other trade barriers or restrictions;

potentially adverse tax consequences;  
difficulty enforcing contractual rights;  
governmental currency controls; and  
currency exchange rate fluctuations.

If any of the foregoing risks were to materialize, our results of operations and our ability to make distributions to our stockholders could be materially and adversely affected.

We may enter into hedging transactions that could expose us to contingent liabilities in the future.

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Subject to maintaining our qualification as a REIT and our exemption from the 1940 Act, part of our strategy may involve entering into hedging transactions that could require us to fund cash payments in certain circumstances (e.g., the early termination of the hedging instrument caused by an event of default or other early termination event, or the decision by a counterparty to request margin securities it is contractually owed under the terms of the hedging instrument). The amount due would be equal to the unrealized loss of the open swap positions with the respective counterparty and could also include other fees and charges. These economic losses will be reflected in our results of operations, and our ability to fund these obligations will depend on the liquidity of our assets and access to capital at the time, and the need to fund these obligations could adversely affect our financial condition.

Hedging against interest rate exposure may adversely affect our results of operations, which could reduce our cash available for distribution to our stockholders.

Subject to maintaining our qualification as a REIT and our exemption from the 1940 Act, we may pursue various hedging strategies to seek to reduce our exposure to adverse changes in interest rates. Our hedging activity will vary in scope based on the level and volatility of interest rates, the type of assets held and other changing market conditions. Interest rate hedging may fail to protect or could adversely affect us because, among other things:

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

Our hedging transactions, which are intended to limit losses, may actually adversely affect our results of operations and our ability to make distributions to our stockholders.

In addition, hedging instruments involve risk since they often are not traded on regulated exchanges, guaranteed by an exchange or its clearing house, or regulated by any U.S. or foreign governmental authorities. Consequently, there are no requirements with respect to record keeping, financial responsibility or segregation of customer funds and positions. Furthermore, the enforceability of agreements underlying hedging transactions may depend on compliance with applicable statutory and commodity and other regulatory requirements and, depending on the identity of the counterparty, applicable international requirements. The business failure of a hedging counterparty with whom we enter into a hedging transaction will most likely result in its default. Default by a party with whom we enter into a hedging transaction may result in the loss of unrealized profits and force us to cover our commitments, if any, at the then current market price. Although generally we will seek to reserve the right to terminate our hedging positions, it may not always be possible to dispose of or close out a hedging position without the consent of the hedging counterparty and we may not be able to enter into an offsetting contract in order to cover our risk. We cannot assure you that a liquid secondary market will exist for hedging instruments purchased or sold, and we may be required to maintain a position until exercise or expiration, which could result in losses.

We may fail to qualify for, or not elect, hedge accounting treatment, which could have a material adverse effect on our results of operations.

Changes in application of relevant accounting standards could materially increase earnings volatility. We are subject to earnings volatility because of our use of derivatives and accounting for those derivatives. This earnings volatility may be caused by hedge ineffectiveness, which is the difference in the amounts recognized in our earnings for the changes in fair value of a derivative and the related hedged item, and by the changes in the fair values of derivatives that do not qualify for hedge accounting (referred to as economic hedges where the change in fair value of the derivative is not offset by any change in fair value on a hedged item). If we did not apply hedge accounting or fail to qualify for hedge accounting treatment for a number of reasons, including if we use instruments that do not meet the definition of a derivative (such as short sales), we fail to satisfy hedge documentation and hedge effectiveness assessment requirements or our instruments are not highly effective, the result could be an increase in volatility of our

earnings from period to period. Furthermore, if we fail to qualify for hedge accounting treatment, the losses on the derivatives that we enter into may not be offset by a change in the fair value of the related hedged transaction, which may have a material adverse effect on our results of operations.

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### Risks Related to Our Organization and Structure

Certain provisions of Maryland law could inhibit changes in control.

Certain provisions of the Maryland General Corporation Law (“MGCL”) may have the effect of deterring a third party from making a proposal to acquire us or of impeding a change in control under circumstances that otherwise could provide the holders of our common stock with the opportunity to realize a premium over the then-prevailing market price of our common stock. Our board of directors may elect to become subject to the “business combination” provisions of the MGCL that, subject to limitations, prohibit certain business combinations (including a merger, consolidation, share exchange, or, in circumstances specified in the statute, an asset transfer or issuance or reclassification of equity securities) between us and an “interested stockholder” (defined generally as any person who beneficially owns 10% or more of our then outstanding voting capital stock or an affiliate or associate of ours who, at any time within the two-year period prior to the date in question, was the beneficial owner of 10% or more of our then outstanding voting capital stock) or an affiliate thereof for five years after the most recent date on which the stockholder becomes an interested stockholder. After the five-year prohibition, any business combination between us and an interested stockholder generally must be recommended by our board of directors and approved by the affirmative vote of at least (1) 80% of the votes entitled to be cast by holders of outstanding shares of our voting capital stock; and (2) two-thirds of the votes entitled to be cast by holders of voting capital 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. These super-majority vote requirements do not apply if our common stockholders receive a minimum price, as defined under Maryland law, for their shares in the form of cash or other consideration in the same form as previously paid by the interested stockholder for its shares. These provisions of the MGCL do not apply, however, to business combinations that are approved or exempted by a board of directors prior to the time that the interested stockholder becomes an interested stockholder.

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

Certain provisions of the MGCL permit our board of directors, without stockholder approval and regardless of what is currently provided in our charter or bylaws, to adopt certain mechanisms, some of which (for example, a classified board) we do not yet have. These provisions may have the effect of limiting or precluding a third party from making an acquisition proposal for us or of delaying, deferring or preventing a change in control of us under circumstances that otherwise could provide the holders of shares of our common stock with the opportunity to realize a premium over the then current market price. We have elected to be subject to the provisions of Title 3, Subtitle 8 of the MGCL relating to the filling of vacancies on our board of directors.

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

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

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



Under Maryland law generally, a director is required to perform his or her duties in good faith, in a manner he or she reasonably believes to be in our best interests and with the care that an ordinarily prudent person in a like position would use under similar circumstances. Under Maryland law, directors are presumed to have acted with this standard of care. In addition, our charter limits the liability of our directors and officers to us and our stockholders for money damages, except for liability resulting from:

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

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Our charter obligates us to indemnify our directors and officers for actions taken by them in those capacities to the maximum extent permitted by Maryland law. Our bylaws require us to indemnify each director or officer, to the maximum extent permitted by Maryland law, in the defense of any proceeding to which he or she is made, or threatened to be made, a party by reason of his or her service to us. In addition, we may be obligated to advance the defense costs incurred by our directors and officers. As a result, we and our stockholders may have more limited rights against our directors and officers than might otherwise exist absent the current provisions in our charter and bylaws or that might exist with other companies.

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

Our charter provides that a director may only be removed for cause upon the affirmative vote of holders of two-thirds of the votes entitled to be cast in the election of directors. Vacancies may be filled only by a majority of the remaining directors in office, even if less than a quorum. These requirements make it more difficult to change our management by removing and replacing directors and may prevent a change in control of our company that is in the best interests of our stockholders.

The stock ownership limit imposed by the Internal Revenue Code for REITs and our charter may restrict our business combination opportunities.

In order for us to maintain our qualification as a REIT under the Internal Revenue 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 Internal Revenue Code to include certain entities) at any time during the last half of each taxable year following 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 9.8%, by value or by number of shares, whichever is more restrictive, of the aggregate of the outstanding shares of our common stock or more than 9.8%, by value or by number of shares, whichever is more restrictive, of the aggregate of the outstanding shares of such series or class of our preferred stock. Our board may, in its sole discretion, grant, and has in certain circumstances granted, an exemption to the stock ownership limits, subject to such conditions and the receipt by our board of certain representations and undertakings. Our charter also prohibits any person from (a) beneficially or constructively owning, as determined by applying certain attribution rules of the Internal Revenue Code, our stock that would result in us being “closely held” under Section 856(h) of the Internal Revenue Code or that would otherwise cause us to fail to qualify as a REIT or to have significant non-qualifying income from “related” parties or (b) transferring stock if such transfer would result in our stock being owned by fewer than 100 persons. The ownership limits imposed under the Internal Revenue Code are based upon direct or indirect ownership by “individuals,” but only during the last half of a tax year. The ownership limits contained in our charter key off of the ownership at any time by any “person,” which term includes entities. These ownership limitations in our charter are common in REIT charters and are intended to provide added assurance of compliance with the tax law requirements, and to minimize administrative burdens. However, the ownership limit on our common stock might also delay or prevent a transaction or a change in our control that might involve a premium price for our common stock or otherwise be in the best interest of our stockholders.

### Risks Related to Our Taxation as a REIT

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

Qualification as a REIT involves the application of highly technical and complex Internal Revenue Code provisions for which only limited judicial and administrative authorities exist. Even a technical or inadvertent violation could jeopardize our REIT qualification. Our qualification as a REIT will depend on our satisfaction of certain asset, income, organizational, distribution, stockholder ownership and other requirements on a continuing basis. We own direct or indirect interests in one or more REITs (each, a “Subsidiary REIT”) that have elected to be taxed as REITs under the U.S. federal income tax laws. Each Subsidiary REIT is subject to the various REIT qualification requirements and other limitations described herein that are applicable to us. If a Subsidiary REIT were to fail to qualify as a REIT, then (i) that Subsidiary REIT would become subject to U.S. federal income tax, (ii) our ownership

of shares in such Subsidiary REIT would cease to be a qualifying asset for purposes of the asset tests applicable to REITs, and (iii) it is possible that we would fail certain of the asset tests applicable to REITs, in which event we would fail to qualify as a REIT unless we could avail ourselves of certain relief provisions. New legislation, court decisions or administrative guidance, in each case possibly with retroactive effect, may make it more difficult or impossible for us to qualify as a REIT. Certain rules applicable to REITs are particularly difficult to interpret or to apply in the case of REITs investing in real estate mortgage loans that are acquired at a discount, subject to work-outs or modifications, or reasonably expected to be in default at the time of acquisition. In addition, our ability to satisfy the requirements to qualify as a REIT depends in part on the actions of third parties over which we have no control or only limited influence, including in cases where we own an equity interest in an entity that is classified as a partnership for U.S. federal income tax purposes.

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If we do not qualify as a REIT or fail to remain qualified as a REIT, we will be subject to U.S. federal income tax and potentially to additional state and local taxes which would reduce the amount of cash available for distribution to our stockholders.

We have been organized and have operated and intend to continue to operate in a manner that will enable us to qualify as a REIT for U.S. federal income tax purposes. We do not intend to request a ruling from the Internal Revenue Service (the “IRS”) as to 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.

To qualify as a REIT, we are required to satisfy certain gross income and asset tests. Our ability to satisfy the gross income and asset tests depends upon our analysis of the characterization and fair market values of our assets, some of which are not susceptible to a precise determination, and for which we will not obtain independent appraisals. Our compliance with the REIT income and quarterly asset requirements also depends upon our ability to successfully manage the composition of our income and assets on an ongoing basis (which, based on the types of assets we own, can fluctuate rapidly, significantly and unpredictably). Moreover, the proper classification of an instrument as debt or equity for U.S. federal income tax purposes may be uncertain in some circumstances, which could affect the application of the REIT qualification requirements as described below. In addition, we will be required to make estimates of or otherwise determine the value of real property that is collateral for our mortgage loan assets. In some cases, the real property will be under construction or the subject of significant improvements, making such collateral even more difficult to value. There can be no assurance that the IRS would not challenge our valuations or valuation estimates of this collateral. Accordingly, there can be no assurance that the IRS will not contend that our interests in subsidiaries or in securities of other issuers will not cause a violation of the REIT requirements.

If we were to fail to qualify as a REIT in any taxable year, we would be subject to U.S. federal income tax, including any applicable alternative minimum tax, on our taxable income at regular corporate rates, and dividends paid to our stockholders would not be deductible by us in computing our taxable income. Any resulting corporate tax liability could be substantial and would reduce the amount of cash available for distribution to our stockholders, which in turn could have an adverse impact on the value of our common stock. In addition, we would no longer be required to make distributions to stockholders. Unless we were entitled to relief under certain Internal Revenue Code provisions, we also would be disqualified from taxation as a REIT for the four taxable years following the year in which we failed to qualify as a REIT.

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

Dividends payable by REITs generally are not eligible for the preferential tax rates on qualified dividend income. Although this does not adversely affect the taxation of REITs or dividends payable by REITs, to the extent that the preferential rates continue to apply to regular corporate qualified dividends, 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.

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

We generally must distribute annually at least 90% of our REIT taxable income, subject to certain adjustments and excluding any net capital gain, in order for U.S. federal corporate income tax not to apply to earnings that we distribute. To the extent that we satisfy this distribution requirement, but distribute less than 100% of our taxable income, we will be subject to U.S. federal corporate income tax on our undistributed taxable income. In addition, we will be subject to a 4% nondeductible excise tax if the actual amount that we pay out to our stockholders in a calendar year is less than a minimum amount specified under U.S. federal tax laws. We intend to make distributions to our stockholders to comply with the REIT requirements of the Internal Revenue Code.

From time to time, we may generate taxable income greater than our income for financial reporting purposes prepared in accordance with GAAP, or differences in timing between the recognition of taxable income and the actual receipt of cash may occur. For example, we may be required to accrue income from mortgage loans, MBS, and other types of debt securities or interests in debt securities before we receive any payments of interest or principal on such assets. We may also acquire distressed debt investments that are subsequently modified by agreement with the borrower. If the amendments to the outstanding debt are “significant modifications” under the applicable U.S. Treasury regulations, the

modified debt may be considered to have been reissued to us at a gain in a debt-for-debt exchange with the borrower, with gain recognized by us to the extent that the principal amount of the modified debt exceeds our cost of purchasing it prior to modification.

As a result, we may find it difficult or impossible to meet distribution requirements in certain circumstances. In particular, where we experience differences in timing between the recognition of taxable income and the actual receipt of cash, the requirement to distribute a substantial portion of our 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 a taxable distribution of our shares of common stock as part of a distribution in which stockholders may elect to receive shares of common stock or (subject to a limit measured as a percentage of the total distribution) cash, in order to comply with REIT requirements. These alternatives could increase our costs or reduce

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our equity. Thus, compliance with the REIT requirements may hinder our ability to grow, which could adversely affect the value of our common stock.

Even if we continue to qualify as a REIT, we may face other tax liabilities that reduce our cash flow.

Even if we continue to qualify for taxation as a REIT, we may be subject to certain U.S. federal, state and local taxes on our income and assets, including taxes on any undistributed income, tax on income from some activities conducted as a result of a foreclosure, and state or local income, property and transfer taxes, such as mortgage recording taxes. In addition, we could, in certain circumstances, be required to pay an excise or penalty tax (which could be significant in amount) in order to utilize one or more relief provisions under the Internal Revenue Code to maintain our qualification as a REIT. We are subject to U.S. federal and state income tax (and any applicable non-U.S. taxes) on the net income earned by our taxable REIT subsidiaries. Due to the nature of the assets in which we invest, we expect our taxable REIT subsidiaries will have a material amount of assets and net taxable income. Our TRS may have tax liability with respect to “phantom income” if it is treated as a “dealer” for U.S. federal income tax purposes which would require the TRS to mark to market its assets at the end of each taxable year. Any of these taxes would decrease cash available for distribution to our stockholders.

Complying with REIT requirements may force us to forgo and/or liquidate otherwise attractive investment opportunities.

To qualify as a REIT, we must ensure that we meet the REIT gross income tests annually and that at the end of each calendar quarter, at least 75% of the value of our assets consists of cash, cash items, government securities and qualified REIT real estate assets, including certain mortgage loans and certain kinds of MBS. The remainder of our investment in securities (other than government securities and qualified real estate assets) generally cannot include more than 10% of the outstanding voting securities of any one issuer or more than 10% of the total value of the outstanding securities of any one issuer. In addition, in general, no more than 5% of the value of our assets (other than government securities and qualified real estate assets) can consist of the securities of any one issuer, and no more than 25% of the value of our total securities can be represented by securities of one or more TRSs. If we fail to comply with these requirements at the end of any calendar quarter, we must correct the failure within 30 days after the end of the calendar quarter or qualify for certain statutory relief provisions to avoid losing our REIT qualification and suffering adverse tax consequences. As a result, we may be required to liquidate from our portfolio, or contribute to a TRS, otherwise attractive investments in order to maintain our qualification as a REIT. These actions could have the effect of reducing our income, increasing our income tax liability, and reducing amounts available for distribution to our stockholders. In addition, we may be required to make distributions to stockholders at disadvantageous times or when we do not have funds readily available for distribution, and may be unable to pursue investments (or, in some cases, forego the sale of such investments) that would be otherwise advantageous to us in order to satisfy the source-of-income or asset-diversification requirements for qualifying as a REIT. Thus, compliance with the REIT requirements may hinder our ability to make, and, in certain cases, maintain ownership of certain attractive investments.

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 entered into and may in the future enter into additional financing arrangements that are structured as sale and repurchase agreements pursuant to which we would 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 which are secured by the assets sold pursuant thereto. We believe that we would be treated for REIT asset and income test purposes as the owner of the assets that are the subject of any such sale and repurchase agreement notwithstanding that such 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 could 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 have acquired and may continue to 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 U.S. federal income tax purposes. Accrued market discount is reported as income when, and to the extent that, any payment of principal of the debt instrument is made, unless we elect to include accrued market discount in income as it accrues. Principal payments on certain loans are made monthly, and consequently accrued market discount may have to be included in income each month as if the debt instrument were assured of ultimately being collected in full. 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.

Similarly, some of the MBS that we acquire may have been issued with original issue discount. We will be required to report such original issue discount based on a constant yield method and will be taxed based on the assumption that all future

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projected payments due on such MBS will be made. If such MBS turns out not to be fully collectible, an offsetting loss deduction will become available only in the later year that uncollectability is provable.

In the event that any debt instruments or MBS 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 as it accrues, despite doubt as to its ultimate collectability. Similarly, we may be required to accrue interest income with respect to subordinate MBS at its stated rate regardless of whether corresponding cash payments are received or are ultimately collectable. In each case, while we would in general ultimately have an offsetting loss deduction available to us when such interest was determined to be uncollectible, the utility of that deduction could depend on our having taxable income in that later year or thereafter.

Finally, we or our TRSs may recognize taxable “phantom income” as a result of modifications, pursuant to agreements with borrowers, of debt instruments that we acquire if the amendments to the outstanding debt are “significant modifications” under the applicable Treasury regulations. In addition, our TRSs may be treated as a “dealer” for U.S. federal income tax purposes, in which case the TRS would be required to mark to market its assets at the end of each taxable year and recognize taxable gain or loss on those assets even though there has been no actual sale of those assets.

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

Securitizations by us or our subsidiaries could result in the creation of taxable mortgage pools for U.S. federal income tax purposes. As a result, we could have “excess inclusion income.” Certain categories of stockholders, such as non-U.S. 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 any such excess inclusion income. In addition, to the extent that our common stock is owned by tax-exempt “disqualified organizations,” such as certain government-related entities and charitable remainder trusts that are not subject to tax on unrelated business income, we may incur a corporate level tax on a portion of any excess inclusion income. In that case, we may reduce the amount of our distributions to any disqualified organization whose stock ownership gave rise to the tax. Moreover, we could face limitations in selling equity interests in these securitizations to outside investors, or selling any debt securities issued in connection with these securitizations that might be considered to be equity interests for tax purposes. These limitations may prevent us from using certain techniques to maximize our returns from securitization transactions.

The tax on prohibited transactions will limit our ability to engage in transactions, including certain methods of securitizing mortgage loans, which would be treated as sales for U.S. federal income tax purposes.

A REIT’s net income from prohibited transactions is subject to a 100% tax. In general, prohibited transactions are sales or other dispositions of property, other than foreclosure property, but including mortgage loans, held primarily for sale to customers in the ordinary course of business. We might be subject to this tax if we were to dispose of or securitize loans in a manner that was treated as a sale of the loans for U.S. federal income tax purposes. Therefore, in order to avoid the prohibited transactions tax, we may choose not to engage in certain sales of loans 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. We sell loans or other assets from time to time and those sales could be treated as prohibited transactions. We cannot make any assurance that we will not be subject to the prohibited transactions tax on some income we earn.

The failure of a mezzanine loan to qualify as a real estate asset could adversely affect our ability to qualify as a REIT. We may acquire mezzanine loans for which the IRS has provided a safe harbor but not rules of substantive law. In Revenue Procedure 2003-65, the IRS provided a safe harbor pursuant to which a mezzanine loan, if it meets certain requirements, will be treated by the IRS as a real estate asset for purposes of the REIT asset tests, and interest derived from the mezzanine loan will be treated as qualifying mortgage interest for purposes of the REIT 75% gross income test. We may acquire mezzanine loans that do not meet all of the requirements of this safe harbor. In the event we own a mezzanine loan that does not meet the safe harbor, the IRS could challenge such loan’s treatment as a real estate asset for purposes of the REIT asset and gross income tests and, if such a challenge were sustained, we could fail to qualify



as a REIT.

Our ownership of TRSs has been and will continue to be limited and our transactions with our TRSs will cause us to be subject to a 100% penalty tax on certain income or deductions if those transactions are not conducted on arm's length terms.

A REIT may own up to 100% of the stock of one or more TRSs. A TRS may hold assets and earn income that would not be qualifying assets or income if held or earned directly by a REIT. Both the subsidiary and the REIT must jointly elect to treat the subsidiary as a TRS. A corporation of which a TRS directly or indirectly owns more than 35% of the voting power or value of the stock will automatically be treated as a TRS. Overall, no more than 25% of the value of a REIT's assets may consist of stock or securities of one or more TRSs. In addition, the TRS rules limit the deductibility of interest paid or accrued by a TRS

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to its parent REIT to assure that the TRS is subject to an appropriate level of corporate taxation. The rules also impose a 100% excise tax on certain transactions between a TRS and its parent REIT that are not conducted on an arm's length basis.

TRSs that we have formed have paid and will continue to pay U.S. federal, state and local income tax on their taxable income, and their after-tax net income is available for distribution to us but is not required to be distributed by such domestic TRSs to us. We believe that the aggregate value of the stock and securities of our TRSs has been and we anticipate that the aggregate value will continue to be less than 25% of the value of our total assets (including our TRS stock and securities). Furthermore, we have monitored and will continue to monitor the value of our respective investments in our TRSs for the purpose of ensuring compliance with TRS ownership limitations. In addition, we have scrutinized and will continue to scrutinize all of our transactions with TRSs to ensure that they are entered into on arm's length terms to avoid incurring the 100% excise tax described above. There can be no assurance, however, that we will be able to comply with the 25% limitation discussed above or to avoid application of the 100% excise tax discussed above.

Complying with REIT requirements may limit our ability to hedge effectively and may cause us to incur tax liabilities. The REIT provisions of the Internal Revenue Code substantially limit our ability to hedge our liabilities. Any income from a hedging transaction we enter into to manage risk of interest rate changes with respect to borrowings made or to be made to acquire or carry real estate assets does not constitute "gross income" for purposes of the 75% or 95% gross income tests. To the extent that we enter into other types of hedging transactions, the income from those transactions is likely to be treated as non-qualifying income for purposes of both of the gross income tests. As a result of these rules, we intend to limit our use of advantageous hedging techniques or implement those hedges through a TRS. This could increase the cost of our hedging activities because our TRS would be subject to tax on gains or expose us to greater risks associated with changes in interest rates than we would otherwise want to bear. In addition, losses in our TRS will generally not provide any tax benefit, except for being carried forward against future taxable income in the TRS.

Our ability to qualify as a REIT could be adversely affected by our ownership of equity interests in an entity that owns a portfolio of hotels if our leases with these hotels are not respected as true leases for U.S. federal income tax purposes, if our TRS fails to qualify as a "taxable REIT subsidiary" under the Internal Revenue Code, if our hotel manager does not qualify as an "eligible independent contractor," or if our hotels are not "qualified lodging facilities." We lease hotels to a TRS. If the leases with our TRS are not respected as true leases for U.S. federal income tax purposes, we may fail to qualify as a REIT. For the rent paid pursuant to the hotel leases with our TRS to qualify for purposes of the gross income tests, the leases must be respected as a true lease for U.S. federal income tax purposes and must not be treated as a service contract, joint venture or some other type of arrangement. We structured our leases so that the lease will be respected as a true lease for U.S. federal income tax purposes, but there can be no assurance that the IRS will agree with this characterization.

- If our TRS fails to qualify as a "taxable REIT subsidiary" under the Internal Revenue Code, we could fail to qualify as a REIT. Rent paid by a lessee that is a "related party tenant" of ours is not qualifying income for purposes of the two gross income tests applicable to REITs. So long as the TRS lessee qualifies as a TRS, it will not be treated as a "related party tenant" with respect to our properties that are managed by a qualifying independent hotel management company. We believe that our TRS qualifies to be treated as a TRS for U.S. federal income tax purposes, but there can be no assurance that the IRS will not challenge the status of our TRS for U.S. federal income tax purposes or that a court would not sustain such a challenge.

If our hotel manager does not qualify as an "eligible independent contractor" or if our hotels are not "qualified lodging facilities," we could fail to qualify as a REIT. Each property with respect to which our TRS lessee pays rent must be a "qualified lodging facility." As of the date hereof, we believe that all of the hotels leased to or owned by our TRS are qualified lodging facilities. The REIT provisions of the Internal Revenue Code provide only limited guidance for making determinations under the requirements for qualified lodging facilities, and there can be no assurance that these requirements will be satisfied in all cases. The hotel management company that entered into a management contract with our TRS must qualify as an "eligible independent contractor" under the REIT rules in order for the rent paid to us by our TRS to be qualifying income for our REIT income test requirements. Complex ownership attribution rules

apply for purposes of these ownership thresholds. Although we intend to monitor ownership of our stock by our hotel manager and its owners, and certain provisions of our charter are designed to prevent ownership of our stock in violation of these rules, there can be no assurance that these ownership levels will not be exceeded.

ITEM 1B. Unresolved Staff Comments.

None

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## ITEM 2. Properties.

Our executive and administrative office is located at 2450 Broadway, 6th Floor, Santa Monica, CA 90404. Pursuant to the management agreement between us and our Manager, our Manager is responsible for providing offices necessary for all operations and, accordingly, all lease responsibilities belong to our Manager.

## Investment Properties

Single-Family Homes—We invest in single-family residential properties for rental through our equity investment in CAH OP (see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Our Investments." The following table presents certain information related to single-family residential properties held for investment by CAH OP at December 31, 2013:

State	Number of Homes <sup>(1)</sup>	Estimated Total Cost Basis (in thousands) <sup>(2)</sup>	Estimated Average Cost Per Home (in thousands)	Average Home Size (Square Feet)	Estimated Average Cost Per Square Foot
Properties wholly-owned by CAH OP:					
Arizona	1,131	\$151,615	\$134	1,706	\$79
California	2,898	800,321	276	1,665	166
Colorado	674	110,531	164	1,708	96
Delaware	97	15,089	156	1,473	106
Florida	3,105	534,421	172	1,854	93
Georgia	3,464	445,074	128	1,994	64
Nevada	1,180	220,015	186	1,965	95
Pennsylvania	3	408	136	1,113	122
Texas	1,323	153,927	116	1,787	65
	13,875	\$2,431,401	\$175	1,831	\$96
Jointly-owned properties <sup>(3)</sup>	1,025				
	14,900				

Represents total housing units, which are leased separately from any other housing units. No property with a single (1) deed has more than four housing units, and less than 1% of our wholly owned properties have more than one housing unit.

(2) Includes acquisition and renovation costs plus estimated renovation costs for homes currently in construction or not yet started incurred through December 31, 2013.

(3) Jointly-owned properties are owned through a joint venture with Fannie Mae in which CAH OP acquired its managing member interest for an aggregate payment of \$35.1 million.

Hotel Properties—We and a Co-Investment Fund, through a joint venture, collectively own an approximate 94% interest in 102 limited service hotels that we acquired through foreclosure. Our effective ownership interest in each of the hotels, based upon our percentage interest in the joint venture, is 31%. The hotel operations are managed by a minority equity partner. The following table presents certain information related to our hotel properties at December 31, 2013:

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State	Number of Properties	Number of Rooms
Alabama	18	967
Florida	6	390
Georgia	21	1,198
Illinois	1	115
Indiana	8	871
Kentucky	3	305
Louisiana	3	213
Mississippi	6	349
North Carolina	12	601
South Carolina	10	575
Tennessee	12	780
Virginia	2	122
	102	6,486

For the year ended December 31, 2013, the average occupancy rate and average daily rate (ADR) of occupied rooms were 57% and \$59, respectively.

**Commercial Real Estate Property**—We and a strategic partner with a 0.75% noncontrolling interest together acquired and own an office campus in Minnesota. The property includes two buildings with approximately 502,000 total square feet that are fully occupied by a single-A rated tenant under a triple net lease expiring in September 2020.

**Multifamily Properties**—We and a minority unaffiliated investor, through a venture, own a preferred equity interest in 20 apartment communities composed of approximately 7,600 units across three states. The combined preferred equity contributed represents 75% of total equity capitalization in the properties. The remaining 25% common equity interest owned by the sponsor is subordinate to the preferred equity interest. Based on our 83.3% interest in the preferred equity venture, our current indirect interest in the apartment communities is 62.5%. See more detailed description of this investment at "Management's Discussion and Analysis of Financial Condition and Results of Operations—Our Investments—Multifamily Portfolio Preferred Equity."

The following table presents certain information related to the properties at December 31, 2013:

State	Number of Properties	Number of Units	Average Unit Size (Square Feet)	Occupancy <sup>(1)</sup>
Florida	4	1,956	941	81%
Georgia	7	2,609	1,016	84%
Texas	9	3,006	944	88%
	20	7,571	968	85%

(1) At December 31, 2013, 15 of the 20 properties were undergoing planned unit upgrade renovations. The average occupancy of the five not undergoing renovations was 91%.

### ITEM 3. Legal Proceedings.

As of December 31, 2013, we were not involved in any material legal proceedings.

### ITEM 4. Mine Safety Disclosures.

Not applicable.

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## PART II

## ITEM 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

Our common stock is traded on the New York Stock Exchange ("NYSE") under the symbol "CLNY." The following table illustrates the high, low and closing prices as reported on the NYSE and cash dividends declared by quarter during 2013 and 2012.

Quarter Ended	High	Low	Close	Cash Dividends Declared Per Share of Common Stock	
March 31, 2012	\$17.38	\$15.64	\$16.38	\$ 0.34	
June 30, 2012	17.41	16.16	17.30	0.35	
September 30, 2012	20.10	17.22	19.48	0.35	
December 31, 2012	20.28	18.40	19.50	0.40	(1)
March 31, 2013	23.48	19.75	22.20	0.35	
June 30, 2013	23.73	19.13	19.89	0.35	
September 30, 2013	21.39	19.03	19.98	0.35	
December 31, 2013	21.12	19.55	20.29	0.35	

(1) Reflects our quarterly dividend of \$0.35 per common share and a special dividend of \$0.05 per common share. On February 25, 2014, the last reported sale price of our common stock on the NYSE was \$23.11 and there were 49 holders of record of our common stock.

Holders of our common stock are entitled to receive distributions if and when the board of directors authorizes and declares distributions. The board of directors has not established any minimum distribution level. In order to maintain our qualification as a REIT, we intend to pay dividends to our stockholders that, on an annual basis, will represent at least 90% of our taxable income (which may not necessarily equal net income as calculated in accordance with GAAP), determined without regard to the deduction for dividends paid and excluding any net capital gains. In addition, our credit facility limits the amount of distributions. See "Item 7. Management Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources—Dividends."

See Note 15 to our consolidated financial statements included in this Annual Report for information regarding our 2009 Non-Executive Director Stock Plan and our 2011 Equity Incentive Plan.

## Performance Graph

The following graph compares the cumulative total return on our common stock from September 24, 2009 (the date on which our common stock began trading on the NYSE) to the NYSE closing price per share on December 31, 2013 with the cumulative total returns on the Standard & Poor's 500 Composite Stock Price Index (the "S&P 500 Index") and the FTSE National Association of Real Estate Investment Trusts Mortgage REIT Index (the "FTSE NAREIT MREIT Index"). The graph assumes the investment of \$100 in our common stock and each of the indices on September 24, 2009 and the reinvestment of all dividends. The return shown on the graph is not necessarily indicative of future performance.

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## ITEM 6. Selected Financial Data.

The following selected financial data are derived from our audited financial statements and should be read in conjunction with the more detailed information contained in the financial statements and accompanying notes included in Item 15 of this Annual Report and “Management’s Discussion and Analysis of Financial Condition and Results of Operations.”

We commenced operations upon completion of our IPO on September 29, 2009 and have been actively investing in our target assets. Due to our ongoing capital raising and investment activities, the selected financial data presented below do not reflect comparable year over year results, nor are they indicative of future financial condition or results of operations.

	Year Ended December 31,				Period from June 23, 2009 (Date of Inception) to December 31,
(In thousands, except share and per share data)	2013	2012	2011	2010	2009
Statements of Operations Data:					
Total income	\$180,239	\$107,155	\$65,469	\$27,425	\$1,091
Total expenses	58,191	36,553	20,061	9,882	1,489
Net income (loss)	125,923	68,205	43,364	17,754	(398 )
Net income (loss) attributable to Colony Financial, Inc.	101,765	62,011	42,260	17,731	(400 )
Net income (loss) attributable to common stockholders	80,345	48,096	42,260	17,731	(400 )
Share Data:					
Net income (loss) per share attributable to common stockholders—basic	\$1.20	\$1.33	\$1.47	\$1.20	\$(0.06 )
Net income (loss) per share attributable to common stockholders—diluted	\$1.20	\$1.32	\$1.46	\$1.18	\$(0.06 )
Dividends per common share	\$1.40	\$1.44	\$1.31	\$0.97	\$0.07
Weighted average number of common shares outstanding—basic	66,181,700	35,925,600	28,732,200	14,716,200	6,963,000
Weighted average number of common shares outstanding—diluted	66,181,700	35,943,200	28,993,700	15,003,700	6,963,000

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	Year Ended December 31,				Period from June 23, 2009 (Date of Inception) to December 31, 2009
(In thousands, except share and per share data)	2013	2012	2011	2010	
Balance Sheet Data—At Period End:					
Investments in unconsolidated joint ventures	\$1,369,529	\$877,081	\$443,500	\$248,750	\$129,087
Loans held for investment, net	1,028,654	333,569	232,619	69,929	—
Real estates assets, net	112,468	—	—	—	—
Beneficial interests in debt securities, available-for-sale, at fair value	30,834	32,055	32,427	—	—
Total assets	2,628,552	1,435,567	727,519	390,457	287,529
Total debt	616,107	108,167	82,845	34,000	—
Total liabilities	674,325	152,537	114,029	57,178	14,112
Total stockholders' equity	1,684,310	1,223,331	602,976	333,039	273,377
Total equity	1,954,227	1,283,030	613,490	333,279	273,417
Other Data:					
Core Earnings (Loss) <sup>(1)</sup>	\$96,638	\$59,762	\$43,243	\$17,798	\$(385 )
Cash flows provided by (used in):					
Operating activities	125,289	70,218	24,417	9,857	(385 )
Investing activities	(1,313,220 )	(425,169 )	(366,433 )	(178,660 )	(129,329 )
Financing activities	1,060,738	521,278	279,646	77,716	287,044

Core Earnings is a non-GAAP financial measure more fully described under “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Non-GAAP Supplemental Financial Measure: Core Earnings.” We believe that Core Earnings is a useful supplemental measure of our operating performance. The exclusion from Core Earnings of certain items allows investors and analysts to readily identify the operating results of the assets that form the core of our activity and assists in comparing those operating results between periods. Core Earnings is also the basis upon which the incentive fee to our Manager is calculated. Also, as some of our competitors use a similar supplemental measure, it facilitates comparisons of operating performance to other similar REITs. However, other REITs may use different methodologies to calculate Core Earnings, and accordingly, our calculation of Core Earnings may not be comparable to other similar REITs that present similar supplemental measures. Core Earnings does not represent cash flow from operations as defined by GAAP, should not be considered as an alternative to net income as defined by GAAP and is not indicative of cash available to fund all cash flow needs. For a description of Core Earnings and a reconciliation of our GAAP net income (loss) available for common stockholders to Core Earnings, see “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Non-GAAP Supplemental Financial Measure: Core Earnings.”

## ITEM 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion should be read in conjunction with our financial statements and accompanying notes included in Item 15 of this Annual Report.

## Overview

We are an externally managed real estate investment and finance company that was organized in June 2009 primarily to acquire, originate and manage a diversified portfolio of real estate-related debt and equity investments at attractive



risk-adjusted returns. Our investment portfolio and target assets are primarily composed of interests in: (i) real estate and real estate-related debt, including loans acquired at a discount to par in the secondary market and new originations; and (ii) real estate equity, including single-family homes held as rental investment properties.

Our objective is to provide attractive risk-adjusted returns to our investors through a diversified portfolio of real estate-related debt and equity investments, including single-family homes to be rented to tenants. The total return profile of our investments is composed of both current yield, which is distributed through regular-way dividends, and capital appreciation potential, which is distributed through regular-way and/or special dividends. Our investments typically fall within two broad categories:

• Real estate debt investments, including loan acquisitions and originations:

• Loan acquisitions include the purchase of performing, sub-performing and/or non-performing commercial real estate debt (including loan-to-own strategies), often at significant discounts to par

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- Originations include structured senior and subordinate debt secured by mortgages and/or equity interests in commercial real estate with a bias towards current yield

Real estate equity, which includes:

- Single-family homes for rent held through our investment in CAH OP, which is externally managed by an affiliate of our Manager; and

- Other real estate equity, which include real estate acquired in settlement of loans, common equity in real estate or related companies, and certain preferred equity investments with profit participation meeting certain risk or return profiles.

We also may pursue other real estate-related special situation investments including CMBS, sale/leasebacks, triple net lease investments and minority equity interests in banks. Our investments are diversified across a wide spectrum of commercial real estate property types – office, industrial, retail, multifamily, hospitality and single-family residential – and geographically, with investments across North America and Europe. See “Business—Our Target Assets” in Item 1 of this Annual Report for additional information about our target assets.

### Business Outlook

Significant dislocation occurred in global real estate credit markets during the financial downturn, and while these markets are in various stages of recovery, we continue to find opportunities to acquire financial and real estate assets that we believe are mispriced relative to intrinsic value of the underlying collateral. U.S. markets are now in a later stage of recovery which is producing an increasing number of loan origination and property acquisition opportunities, as commercial real estate fundamentals continue to stabilize and commercial real estate assets are refinanced or acquired with new capital based on revised underwriting, valuation and operating metrics. On the other hand, European markets are in an earlier stage of recovery and producing many loan acquisition opportunities as financial institutions continue to deleverage and divest of troubled assets. We believe that we are well positioned to capitalize on such opportunities sourcing transactions globally through the numerous relationships enjoyed by our Manager through its two decade history in the real estate investment business. We also believe that our Manager’s in-depth understanding of commercial real estate and real estate-related investments (including our target assets), and in-house underwriting and asset management capabilities, enable us to acquire assets with attractive risk-adjusted return profiles and the potential for meaningful capital appreciation.

### 2013 Developments

#### Investment Activities

The following are highlights of our 2013 investment activities:

- Invested or committed \$885 million of capital in 18 new real estate debt investments, including \$95 million in the Transitional CRE Lending Platform;

- Invested or committed \$250 million in two real estate equity investments, including \$123 million in our first triple net-leased office property acquisition;

- Invested \$295 million in CAH OP and \$8.4 million in three other existing investments;

- Fully realized seven real estate debt investments and two real estate equity investments, including the sale of the remaining 615,932 shares of common stock in First Republic Bank;

- Obtained financing on six of our loan portfolios and one real estate equity investment, for net proceeds of \$250 million to us, or 63% of our original equity on a blended basis;

- Fully repaid or defeased the purchase money notes on four of our loan portfolios acquired from the FDIC. To date, we have fully paid off or defeased the purchase money notes on all eight FDIC-financed loan portfolios.

See “—Our Investments” and “—Results of Operations” for more detailed information about our recent investment activities and financial results.

#### Financing Activities

During the year ended December 31, 2013, we completed two equity offerings of an aggregate 21.5 million shares of our common stock for net proceeds of approximately \$434 million and also sold approximately 1.9 million shares of our common stock in our at-the-market equity offering for net proceeds of approximately \$41 million.

In April 2013, we issued \$200 million aggregate principal amount of our 5% convertible senior notes due April 15, 2023 for net proceeds of approximately \$194 million. In January 2014, we issued \$230 million aggregate principal

amount of our 3.875% convertible senior notes due January 15, 2021 for net proceeds of approximately \$224 million.

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In August 2013, we obtained a new secured revolving credit facility to replace our previous credit facility. The new credit facility currently provides up to \$420 million of available credit and an option to increase the amount to up to \$600 million, subject to certain lender approvals and other customary conditions.

In February 2014, we entered into a \$150 million master repurchase agreement with a commercial bank to partially finance loans within our Transitional CRE Lending Platform.

See the financial statements in Item 15 of this Annual Report and “—Liquidity and Capital Resources” for more detailed information.

**Our Investments**

The following tables summarize the carrying and fair values of our net invested equity in our investment portfolio by target asset type, shown net of investment-specific financing and amounts attributable to noncontrolling interests. Fair values presented below have been determined in accordance with GAAP, assuming we had elected the fair value option for all of our investments. Many of our investments have been structured as joint ventures with one or more Co-Investment Funds and are held through unconsolidated joint ventures. For more information about our investment allocation agreement and conflicts of interest that may arise in connection with these co-investments, see “Business—Co-Investment Funds” and “Risk Factors—Risks Related to Our Management and Our Relationship with Our Manager.”

(Amounts in thousands)	December 31, 2013			
	Carrying Value		Fair Value	
	Amount	Percentage of Portfolio	Amount	Percentage of Portfolio
Target Asset Type				
Acquisitions	\$660,328	33 %	\$691,515	32 %
Originations <sup>(1)</sup>	605,727	30 %	613,271	28 %
Single-family residential rentals	530,007	26 %	643,400	29 %
Other real estate equity investments <sup>(2)</sup>	230,973	11 %	244,055	11 %
Total investments <sup>(3)</sup>	\$2,027,035	100 %	\$2,192,241	100 %

(Amounts in thousands)	December 31, 2012			
	Carrying Value		Fair Value	
	Amount	Percentage of Portfolio	Amount	Percentage of Portfolio
Target Asset Type				
Acquisitions	\$524,572	48 %	\$562,466	49 %
Originations <sup>(1)</sup>	234,988	22 %	236,252	21 %
Single-family residential rentals	251,501	23 %	262,000	23 %
Other real estate equity investments <sup>(2)</sup>	70,959	7 %	77,250	7 %
Total investments <sup>(3)</sup>	\$1,082,020	100 %	\$1,137,968	100 %

(1) Originations include preferred equity investments earning a fixed return.

Other real estate equity investments include interests in real estate properties, equity interests obtained through

(2) foreclosures or deed-in-lieu of foreclosure on the collateral of target assets originally acquired or originated as debt instruments, and preferred equity earning a fixed return plus equity participation.

(3) The following table provides a reconciliation of total investments presented above to the amounts included in our consolidated financial statements and the accompanying notes in Item 15 of this Annual Report:

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(Amounts in thousands)	December 31, 2013		December 31, 2012	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Investments in unconsolidated joint ventures	\$1,369,529	\$1,530,574	\$877,081	\$931,117
Loans receivable, net	1,028,654	1,034,600	333,569	335,734
Real estate assets, net	112,468	112,468	—	—
Beneficial interests in debt securities, available-for-sale	30,834	30,834	32,055	32,055
Other assets, net of other liabilities	36,026	36,026	11,079	11,079
Less: Embedded derivative liability associated with beneficial interests in debt securities	(2,952 )	(2,952 )	(3,898 )	(3,898 )
Less: Secured financing	(277,607 )	(277,600 )	(108,167 )	(108,090 )
Less: Noncontrolling interests	(269,917 )	(271,709 )	(59,699 )	(60,029 )
Total investments	\$2,027,035	\$2,192,241	\$1,082,020	\$1,137,968
At December 31, 2013 and 2012, our net invested equity in European investments amounted to approximately \$197.4 million and \$41.3 million, respectively.				

Additional details and recent developments about our individual investments are provided in the following table and discussion:

(Amounts in millions)		Balance at December 31, 2013		Investment Description/ Status at December 31, 2013
Our Investments	Date of Initial Investment	Investment Carrying Value <sup>(1)</sup>	Committed Equity <sup>(2)</sup>	
Real Estate Debt—Acquisitions				
Spanish CRE Loan Portfolio I	Nov-13	\$147.9	\$—	3 sub-performing, first mortgage loans secured by two office properties and one retail property in Spain
Freddie Mac Portfolio <sup>(3)</sup>	Oct-13	49.7		27 performing acquired loans secured mostly by first mortgage, commercial real estate
German Loan Portfolio IV	Jul-11	36.1	—	1 non-performing commercial real estate loan and 2 REO properties
Luxury Destination Club Recourse Loan II <sup>(3)</sup>	May-12	34.6	—	First mortgage loan collateralized by 243 high-end units at 26 resorts in the US and various international destinations
CRE FDIC Portfolio	Aug-11	34.3	—	410 performing and non-performing loans acquired in a structured transaction with the FDIC, secured mostly by commercial real estate, and 22 REO properties
U.S. Life Insurance Loan Portfolio	Dec-09	33.7	—	15 performing acquired first mortgages secured by commercial real estate
Bulls Loan Portfolio <sup>(3)</sup>	Jun-11	30.3	—	354 performing and non-performing acquired loans consisting of substantially all first mortgage recourse commercial real estate loans and 14 REO properties
Multifamily Tax-Exempt Bonds	Jun-11	27.9	—	Senior interest in tax-exempt bonds secured by a multifamily residential property located in Atlanta, GA
DB FDIC Portfolio	Jan-10	26.3	1.7	

Ashford Notes	Feb-12	24.8	—	452 performing and non-performing loans acquired in a structured transaction with the FDIC, secured mostly by commercial real estate and 117 REO properties
Florida Retail First Mortgage	Feb-13	23.3	—	2 most junior mortgage participation interests secured by 5 full-service hotels
Class A Manhattan Office Loan Participation	Mar-10	19.1	—	Performing acquired senior mortgage loan secured by a retail property in Florida
Project London Loan Portfolio <sup>(3)</sup>	Sep-12	18.1	—	First mortgage pari-passu participation interest secured by Class A midtown Manhattan office building
ADC FDIC Portfolio II <sup>(3)</sup>	Dec-12	16.8	—	8 performing and non-performing acquired loans secured by commercial real estate
				383 performing and non-performing loans acquired in a structured transaction with the FDIC, mostly secured by commercial real estate and 5 REO properties

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(Amounts in millions)		Balance at December 31, 2013		
Our Investments	Date of Initial Investment	Investment Carrying Value <sup>(1)</sup>	Committed Equity <sup>(2)</sup>	Investment Description/ Status at December 31, 2013
Other acquisitions <sup>(3)</sup>	Various	137.4	0.7	19 investments, each with less than \$15 million of current investment balance
Total acquisitions		660.3	2.4	
Real Estate Debt—Originations				
National Hotel Portfolio Mezzanine Loan	May-13	174.8	—	Mezzanine loan origination secured by equity interests in an entity owning a diversified portfolio of 152 full service, limited service, and extended stay hotels located throughout the U.S.
Lifestyle Athletic Club Mortgage Participation	Mar-13	89.8	8.3	First mortgage loan origination secured by 11 athletic lifestyle clubs located in California
Transitional CRE Lending Platform	Various	86.1	9.0	6 first mortgage loan originations secured by retail, multifamily, office and hospitality properties
One Court Square Preferred Equity	Jul-12	49.1	—	Preferred equity investment in an entity that acquired a Class A office tower located in Long Island City, New York
Luxury Destination Club Recourse Loan I	Sep-11	25.5	—	Performing first mortgage secured by 39 properties located primarily in Manhattan, NY and Maui
New York Student Housing Loan <sup>(3)</sup>	Aug-13	22.3	—	First mortgage loan secured by a student housing community in New York
Boca Raton Multifamily Land Loan	Jan-13	21.1	—	First mortgage loan origination secured by a multifamily development parcel located in Florida
Mexico Luxury Resort Junior Mortgage Participation	Aug-13	20.1	—	Participation in junior first mortgage interest secured by a luxury beach resort in Mexico
St. Barths Hotel and Villa Mortgage Loan	Sep-13	16.6	—	First mortgage loans secured by a partially constructed hotel and residential development project located in the Caribbean
Southern California Land Loan	May-11	16.1	—	First mortgage loan secured by a Southern California master planned development and equity participation rights
American Coastal Properties Loan	Jul-13	15.3	—	First mortgage loan to finance the acquisition and redevelopment of high-end, single family residential properties in infill, coastal southern California markets
Other originations <sup>(3)</sup>	Various	68.9	2.7	7 investments, each with less than \$15 million of current investment balance
Total originations		605.7	20.0	

Real Estate Equity—Single-Family Residential Rentals <sup>(3)</sup>	Mar-12	530.0	—	Investment in CAH OP, an investment vehicle created for the purpose of acquiring and renting single-family homes
Real Estate Equity—Other				
Multifamily Portfolio Preferred Equity	Mar-13	123.9	3.4	Preferred equity investment in an entity that acquired a multifamily portfolio composed of approximately 7,600 units located in Georgia, Florida and Texas
Midwest NNN Office Campus <sup>(3)</sup>	Dec-13	35.3		Equity interests in a credit tenant lease office campus in the Midwest
Hotel Portfolio <sup>(3)</sup>	Apr-10	31.5	—	Equity interests in and senior mezzanine loan receivable from entities owning a portfolio of 102 limited service hotels
Phoenix Corporate Tower	Dec-12	18.4	—	Equity interest in a high-rise office tower located in Phoenix, Arizona
California Master Planned Communities	May-12	15.9	—	Equity interests acquired through deed-in-lieu in 2 partially developed master planned communities located in California
Other Equity Investments	Dec-09	6.0	—	1 investment with less than \$15 million of current investment balance
Total other real estate equity		231.0	3.4	
Total investments		\$2,027.0	\$25.8	



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Amounts represent the carrying value of our investment at December 31, 2013, net of investment-specific (1) financing and amounts attributable to noncontrolling interests. Amounts reflect our investments and our share of income less amounts distributed and realized since the inception of the investment.

Amounts represent our share of additional funding commitments for future investments, unfunded lending (2) commitments, ordinary operating costs, guaranties or other commitments of each investment as of December 31, 2013, as described in Note 17 to our consolidated financial statements included in Item 15 of this Annual Report. (3) Investments with non-recourse financing.

### Real Estate Debt—Acquisitions

**Spanish CRE Loan Portfolio I.** In November 2013, we invested \$143 million, prior to potential financing, in a joint venture with certain Co-Investment Funds to acquire 100% participation interests in three sub-performing first mortgages at a substantial discount to the unpaid principal balance ("UPB"). The mortgages are secured by two office properties and one retail property in Spain. Our share of this investment is approximately 83%. In January 2014, we acquired the loans using Spanish securitization trusts, triggering transfer taxes payable by the trusts. We expect to record an expense of approximately \$4.6 million in the first quarter of 2014, or \$3.8 million net of the amount attributable to noncontrolling interests, related to the transaction costs associated with this transfer.

**Freddie Mac Portfolio.** In October 2013, we invested \$130 million in a joint venture with certain Co-Investment Funds that acquired a portfolio of loans secured by multifamily and senior housing assets. The portfolio included 27 loans, all of which were performing at acquisition, with an aggregate UPB of approximately \$194 million. The aggregate purchase price for the portfolio was approximately \$177 million, representing 91% of the portfolio's UPB. In December 2013, we obtained financing in the amount of \$115 million secured by the loans in this portfolio, representing 63% of our initial invested equity. In connection with the financing, we obtained a 2.5% London Interbank Offered Rate ("LIBOR") cap on 50% of the financing proceeds. Our share of this investment is 73%.

**Florida Retail First Mortgage.** In February 2013, we invested \$23 million in a joint venture with Co-Investment Funds that acquired a performing \$59 million senior mortgage loan secured by a retail mall in Florida. The loan was acquired for \$46 million, or 78% of the unpaid principal balance. The loan bears a 6.0% fixed interest rate with a 30-year amortization schedule and matures in May 2021. The current yield is approximately 9% based on purchase price. Our share of this investment is 50%.

### Other Real Estate Debt Acquisitions with Current Investment Balance Less Than \$15 Million:

**FDIC CRE 2013—**In October 2013, we invested \$13 million in a joint venture with certain Co-Investment Funds that consummated a structured transaction with the FDIC. The joint venture acquired an initial 20% managing member equity interest in a newly formed limited liability company created to hold a portfolio of acquired loans, with the FDIC retaining the other 80% equity interest. Additionally, upon return of capital to all parties, the joint venture will receive a 40% equity interest in the entity, with the FDIC retaining the other 60% equity interest. The portfolio included 415 performing and non-performing loans with an aggregate UPB of \$199 million, consisting of substantially all first mortgage recourse commercial real estate and acquisition, development and construction loans. The portfolio was effectively acquired for a purchase price of \$112.6 million, representing 57% of the portfolio's UPB. Our share of this investment is 50%.

**California First Mortgage Portfolio I—**In April 2013, we invested \$27 million in a joint venture with certain Co-Investment Funds that acquired a portfolio of loans secured by commercial and residential real estate. The portfolio included 52 loans, of which 83% were performing at acquisition, with an aggregate UPB of approximately \$72.3 million. The aggregate purchase price for the portfolio was approximately \$54 million, representing 75% of the portfolio's UPB. Our share of this investment is 50%. In July 2013, the portfolio obtained financing from a commercial bank and returned \$14.6 million, representing 53% of our initial invested equity. The financing bears interest at 1-month LIBOR plus a spread of 3.75%. In connection with the financing, we obtained a 2.5% LIBOR cap on 50% of the financing proceeds.

**California First Mortgage Portfolio II—**In June 2013, we invested \$23 million in a joint venture with certain Co-Investment Funds that acquired a portfolio of loans secured by commercial and residential real estate. The portfolio included 41 loans, of which 100% were performing at acquisition, with an aggregate UPB of approximately \$54.5 million. The aggregate purchase price for the portfolio was approximately \$45 million, representing 83% of the

portfolio's UPB. Our share of this investment is 50%. In September 2013, the portfolio obtained financing from a commercial bank and returned \$13.6 million, representing 59% of our initial invested equity. The financing bears interest at 1-month LIBOR plus a spread of 3.25%. In connection with the financing, we obtained a 2.5% LIBOR cap on 50% of the financing proceeds.

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**MF5 Loan Portfolio (formerly, MF5 CMBS)**—In February 2012, we invested \$25 million in a joint venture with certain Co-Investment Funds that acquired the most senior bond and the interest-only certificate in a CMBS trust. The senior bond has a coupon of 5.1% and is secured by approximately 270 first mortgage loans, of which 89% were performing, collateralized primarily by multifamily properties. The aggregate purchase price for the senior bond and interest-only certificate was approximately \$226.1 million, representing a discount of 27.4% to par value of the senior bond. In February 2013, the joint venture completed a desecuritization of the CMBS trust and sold a 40% participation interest in each of the assets previously held in the trust and recognized a gain on sale of \$25.8 million. Our share of the gain, based on our 11% interest in the joint venture, was \$2.8 million.

### **Real Estate Debt—Originations**

**National Hotel Portfolio Mezzanine Loan.** In May 2013, we and certain Co-Investment Funds participated in the origination of \$560.0 million of mezzanine debt, consisting of senior and junior tranches, secured by the equity interests in an entity owning a diversified portfolio of 152 full service, limited service, and extended stay hotels located throughout the U.S. We and the Co-Investment Funds funded \$327.6 million at closing, net of a 1% origination fee, of which our share was \$173.3 million. The senior and junior tranches bear interest at a blended rate of 1-month LIBOR plus 10.8% and are subordinate to a \$775.0 million first mortgage. Both loans have an initial maturity date of June 2016 and can be extended for a maximum of 24 months, subject to payment of extension fees and satisfaction of debt yield requirements.

**Lifestyle Athletic Club Mortgage Participation.** In March 2013, we participated in a recently originated \$375 million first mortgage loan secured by 11 upscale athletic clubs located in California. The loan bears an 8.0% fixed interest rate with a 25-year amortization schedule and has a five year term. The loan may be increased to \$400 million based on the achievement of certain performance metrics by the borrower. Our share of this investment was \$123 million with a future funding obligation of \$8.25 million. In July 2013, we split the first mortgage loan into a \$32.8 million A-note and \$90.1 million B-note, and sold the A-note to an unrelated party at par. The remaining B-note bears a fixed interest rate of 9.3%.

**Transitional CRE Lending Platform.** From May 2013 to December 31, 2013, we originated six first mortgage loans with an aggregate UPB of \$87 million and unfunded commitments of \$9 million within our Transitional CRE Lending Platform. These loans are earmarked for a potential floating rate securitization. The loans bear interest, on a weighted average basis, at 1-month LIBOR plus 6.5%, and have initial terms of 2 to 3 years. The loans feature one to three 12-month extension options subject to payment of extension fees and satisfaction of certain performance metrics. The underlying collateral includes retail, multifamily, office and hospitality properties. We recently obtained a warehouse credit facility to finance these loans on a short-term basis while we aggregate a sufficient pool able to be ultimately financed in a matched term, non-recourse, floating rate securitization.

**New York Student Housing Loan.** In August 2013, we invested \$20 million with a third party joint venture partner to originate a \$70 million senior mortgage bridge loan secured by a newly constructed 385-unit off campus student housing property in Upstate New York. The initial funding was \$63 million with a \$7 million future funding obligation subject to the property achieving certain operating metrics. The \$7 million additional funding was advanced to the borrower in October 2013 as the property achieved the threshold operating metrics. The loan bears interest at 1-month LIBOR plus 5% with a 0.5% LIBOR floor and matures in September 2015. The loan was funded via a \$46 million non-recourse, matched term loan and \$24 million from the joint venture. Our share of this investment is 90%.

**Boca Raton Multifamily Land Loan.** In January 2013, we invested \$20 million in a joint venture with a Co-Investment Fund and a strategic partner that funded a \$41 million first mortgage loan secured by a 7 acre multifamily development parcel located in Florida. The loan bears an interest rate of 12%, of which 3.5% may be paid in-kind, and is subject to a 1.5% origination fee and a 1% exit fee. The initial term of the loan is three years. Our share of the investment is 49.5%. In January 2014, the borrower paid down the outstanding balance by \$18.6 million, in exchange for a partial release of the site, of which our share was \$9.2 million.

**Mexico Luxury Resort Junior Mortgage Participation.** In August 2013, we invested \$20 million in a joint venture with certain Co-Investment Funds that originated a \$40 million junior first mortgage interest secured by a luxury beach resort in Mexico. The loan bears interest at a fixed rate of 11.5%, of which 3% may be paid in-kind and is subject to

certain other fees and yield maintenance features. The loan matures in January 2019. Our share of this investment is 50%.

St. Barths Hotel and Villa Mortgage Loan. In September 2013, we invested \$16 million in a joint venture with certain Co-Investment Funds that originated two U.S. dollar denominated first mortgage loans with a combined UPB of \$57 million to recapitalize a partially constructed hotel and residential development project located in St Barths, French West Indies. One loan secured by the hotel portion of the property has an initial term of five years and bears interest at 1-month LIBOR plus 12.25%. The other loan secured by the residential portion of the property has an initial term of two years and bears interest

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at 1-month LIBOR plus 10.25%. The loans are subject to certain cross collateralization and cross default features, a 1% origination fee, a 1% exit fee and yield maintenance. Our share of this investment is 33.3%.

**American Coastal Properties Loan.** In July 2013, we and a Co-Investment Fund originated a \$30 million first mortgage loan, with an option to fund an additional \$40 million, to finance the acquisition and redevelopment of high-end, single family residential properties in infill coastal Southern California markets. The loan bears a fixed interest rate of 15%, of which 7% may be paid in-kind, and is subject to certain other fees including a 1% origination fee and 0.5% exit fee. The term of the loan is four years. Our share of the investment is 50%.

**Other Real Estate Debt Originations with Current Investment Balance Less Than \$15 Million:**

**Marin Land Development Loan—**In March 2013, we invested \$10 million (with a future funding obligation of \$3.4 million) in a joint venture with a Co-Investment Fund that originated a \$26.8 million loan for the land acquisition and predevelopment costs for a mixed use development in San Rafael, CA. We and the Co-Investment Fund funded \$20 million at closing for the acquisition and funded the remaining \$6.8 million upon completion of various items in September 2013. The loan bears an interest rate of 10.0% current and 5.0% paid in-kind, with a 1.0% origination fee, and matures in March 2018. Our share of this investment is 50%.

**Texas Master Planned Community Land Loan—**In May 2013, we invested in a joint venture with certain Co-Investment Funds that originated a \$23.4 million loan to finance the development of a master planned residential community near Austin, TX. The loan matures in May 2018 and bears an interest rate of 14% paid in-kind, with a 1.0% origination fee, plus profit participation. Our share of this investment is 50%, or \$12 million.

**Multifamily Lending Platform—**In August 2013, we entered into a joint venture with unaffiliated investors to form a platform to originate short-term, first mortgage loans on multifamily properties. This lending platform was formed in part to take advantage of the void expected to be left by the recently announced multifamily lending curtailment by Government Sponsored Enterprises (“GSEs”). In October 2013, the lending platform originated a \$44.2 million first mortgage loan to finance the acquisition and redevelopment of a 560-unit multifamily property located in Nashville, Tennessee. The loan bears interest at 1-month LIBOR plus 4.65% with a 2.5% LIBOR cap and matures in October 2015. The loan was funded via a \$28.7 million non-recourse, matched term loan provided by a warehouse facility and \$15.5 million from the joint venture. The warehouse facility provides up to \$150 million of credit at 1-month LIBOR plus 2.0% and matures in October 2016 with an option to extend as a term loan for 3 additional years. Our share of this investment is 47.5%.

**Extended Stay Mezzanine B&C Loans.** In September 2013, we sold our \$37.5 million participation interest in these loans, which was originated in December 2012, to an unrelated third party for a \$1.1 million gain.

**Centro Mezzanine Loans.** In August 2013, we received full payoff of the \$60 million loans originated in June 2011. **2100 Grand B-Note.** In May 2013, upon sale of the collateral property, the borrower paid off the entire loan and accrued interest thereon, including a yield maintenance premium of \$3.6 million. Our share of the gain on payoff was approximately \$3.2 million, after the promote payment due to the sponsor.

**Luxury Destination Resort Loans.** In May 2013, we received full payoff of this \$15 million mezzanine loan originated in November 2011, including a prepayment premium. Our 50% share of the gain on payoff was approximately \$0.9 million.

**Florida Residential Development Loan.** In January 2013, we invested \$10 million in a joint venture with a Co-Investment Fund that originated a \$22 million first mortgage loan secured by a waterfront development parcel located in Florida. The loan bore an interest rate of 14%, with a 1% origination fee and a 1% exit fee. In June 2013, the borrower repaid the entire amount due under the loan agreement, including \$5.5 million in yield maintenance and fees. Our share of this investment was 50%.

**Real Estate Equity—Single-Family Residential Rentals**

During the year ended December 31, 2013, we invested an additional \$295 million in CAH OP. To date, we have invested \$550 million in CAH OP and have no further capital commitments at this time.

In September 2013, CAH OP obtained a \$500 million credit facility with J.P. Morgan, which was subsequently increased to \$1.2 billion. CAH OP has also begun originating loans under a new lending program to other owners of single family homes for rent. This loan portfolio, once scaled, as well as CAH OP's broader owned homes portfolio, may be financed with securitizations in the future.

At December 31, 2013, CAH OP owned 14,900 housing units located in nine states across the United States with an estimated cost basis of approximately \$2.6 billion, including units owned in a joint venture with Fannie Mae. The following table provides an overview of the portfolio at December 31, 2013:

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State	Number of Homes <sup>(1)</sup>	Estimated Total Cost Basis (in thousands) <sup>(2)</sup>	Estimated Average Cost Per Home (in thousands)	Average Home Size (Square Feet)	Estimated Average Cost Per Square Foot
Properties wholly-owned by CAH OP:					
Arizona	1,131	\$151,615	\$134	1,706	\$79
California	2,898	800,321	276	1,665	166
Colorado	674	110,531	164	1,708	96
Delaware	97	15,089	156	1,473	106
Florida	3,105	534,421	172	1,854	93
Georgia	3,464	445,074	128	1,994	64
Nevada	1,180	220,015	186	1,965	95
Pennsylvania	3	408	136	1,113	122
Texas	1,323	153,927	116	1,787	65
	13,875	\$2,431,401	\$175	1,831	\$96
Jointly-owned properties <sup>(3)</sup>	1,025				
	14,900				

Represents total housing units, which are leased separately from any other housing units. No property with a single (1) deed has more than four housing units, and less than 1% of our wholly owned properties have more than one housing unit.

(2) Includes acquisition and renovation costs plus estimated renovation costs for homes currently in construction or not yet started incurred through December 31, 2013.

(3) Jointly-owned properties are owned through a joint venture with Fannie Mae in which CAH OP acquired its managing member interest for an aggregate payment of \$35.1 million.

### Real Estate Equity—Other

**Multifamily Portfolio Preferred Equity.** In March 2013, we entered into a joint venture with a minority unaffiliated investor and a separate agreement with a third party sponsor to provide participating preferred equity to an entity investing in multifamily properties. At the March 2013 closing, we and the minority investor funded preferred equity of \$34 million and \$7 million, respectively, and the sponsor funded \$14 million of common equity. Subsequent to the initial closing, we and the minority investor funded an additional \$90 million and \$18 million, respectively, of preferred equity and the sponsor funded \$36 million of common equity. The common and preferred equity proceeds were used along with mortgage financing proceeds to acquire multifamily properties comprising approximately 7,600 units within 20 apartment communities in Georgia, Texas and Florida. Our cumulative preferred equity of \$124 million to-date provides a 12% preferred return, 1% issuance fee and a 30% profit participation after the joint venture first, and the sponsor, second, have each attained a 12% internal rate of return. Our share of this participating preferred equity interest in the investment entity is 83%.

**Midwest NNN Office Campus.** In December 2013, we acquired an office campus in the Midwestern United States fully occupied by a single-A rated tenant. The acquisition cost, including closing costs, was \$123 million. We financed this acquisition with a 10-year term, non-recourse, fixed rate loan resulting in an initial cash-on-cash yield of approximately 13%. The acquisition was completed with a strategic partner with a 0.75% noncontrolling interest. The strategic partner is entitled to certain promoted interests after a 12% preferred return to us.

### Other Real Estate Equity with Current Investment Balance Less Than \$15 Million:

**WLH Stock—**We indirectly owned approximately 2.4 million shares of Class A common stock of William Lyon Homes (“WLH”), which we acquired in connection with the sale of residential lots to WLH in June 2012. In May 2013, WLH completed its initial public offering at a price of \$25 per share, after giving effect to a 1-for-8.25 share reverse stock split. After giving effect to the reverse stock split, we indirectly owned approximately 291,000 shares of WLH Class A common stock at a cost basis of \$8.66 per share. In December 2013, we sold 23,000 shares at a weighted average

price per share of \$19.63 for cumulative proceeds of \$444,000, and realized a gain of \$247,000. In January 2014, we sold all our remaining shares at a weighted average price per share of \$23.05 for cumulative proceeds of \$6.2 million, and realized a gain of \$3.9 million.

First Republic Bank. During the year ended December 31, 2013, we sold our remaining 615,932 shares of common stock in First Republic Bank for combined net cash proceeds of \$23.8 million, and realized a combined gain of \$10.7 million. After giving effect to this sale, we have sold all of our original 1,600,000 shares acquired in June 2010, for cumulative



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proceeds of \$52.4 million, or approximately 2.2 times our original invested amount of \$24 million.

### Investment Activity Subsequent to December 31, 2013

**Hawaii Luxury Resort**—A joint venture between us, a Co-Investment Fund and an unaffiliated investor acquired an REO property consisting of a five-diamond resort hotel on a 55-acre coastal site located in Hawaii. The hotel received an extensive \$180 million renovation in 2006 and 2007, is branded by a renowned luxury hotel operator and includes 73 unsold condos. The property was acquired from a former lender who had foreclosed following a loan default by the previous owners. The total initial capitalization of the investment is approximately \$160 million, including an initial funding of \$85 million via a first mortgage at the closing of the acquisition. We and the Co-Investment Fund are expected to own a \$45 million mezzanine loan and \$15 million, or 50%, of the equity, with the remainder of the equity owned by the unaffiliated investor. The mezzanine loan has a term of five years and bears a fixed interest rate of 11% which may be paid-in-kind. Our share of the joint venture with the Co-Investment Fund that owns 100% of the mezzanine loan and 50% of the equity is 83%.

**Transitional CRE Lending Platform**—Subsequent to December 31, 2013, we originated four first mortgage loans and one related mezzanine loan with an aggregate UPB of \$70 million within our Transitional CRE Lending Platform.

The loans bear interest, on a weighted average basis, at 1-month LIBOR plus 6.9% and have initial terms of 2 to 3 years. The loans feature one to two 12-month extension options subject to payment of extension fees and satisfaction of certain performance metrics. The underlying collateral includes hospitality, multifamily and office properties.

**UK Retail Borrower Recapitalization**—As a part of a borrower recapitalization transaction, a joint venture between us and a Co-Investment Fund expects to originate a £140 million (approximately \$233 million) loan that is primarily collateralized by a first mortgage on a large U.K. shopping center. The loan proceeds will be used to refinance an existing loan at a significant discount to par despite there having been no monetary default. The investment will include: (i) the loan which bears a cash pay interest rate of 10% per annum, has a term of seven years, and has springing recourse to an individual guarantor under certain conditions; and (ii) an equity participation in the shopping center of 35%. Subsequent to the closing of our financing, it is expected that the borrower will secure a new first mortgage which will partially pay down our loan and leave our joint venture with a subordinated loan position secured by a second ranking mortgage on the shopping center. There will be an additional exit fee of between £3 million and £4 million (approximately \$5 million and \$6.7 million, respectively) depending on the timing of this subsequent pay down. Under certain circumstances, the loan may be increased by up to €10 million, or approximately \$13.7 million.

Our share of the joint venture with the Co-Investment Fund providing the loan will be 96%. We have not yet originated this loan, and there can be no assurance that we will be successful in originating this loan on these terms, or at all.

### Critical Accounting Policies and Estimates

Our financial statements are prepared in accordance with GAAP, which requires the use of estimates and assumptions that involve the exercise of judgment and that affect the reported amounts of assets, liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period.

Certain accounting policies are considered to be critical accounting policies. Critical accounting policies are those that are most important to the portrayal of our financial condition and results of operations and require management's most difficult, subjective and complex judgments, and for which the impact of changes in estimates and assumptions could have a material effect on our financial statements. The following discussion addresses the accounting policies that we believe are critical based on the nature of our operations, and applies to both the Company and our unconsolidated joint ventures. We believe that all of the decisions and assessments upon which our financial statements are based were reasonable at the time made, based upon information available to us at that time. This discussion is intended to supplement the description of our significant accounting policies in Note 2 to our consolidated financial statements included in this Annual Report.

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### Investments in Unconsolidated Joint Ventures

Many of our investments have been structured as joint ventures with one or more Co-Investment Funds pursuant to an investment allocation agreement (see “Business—Co-Investment Funds”). The joint ventures are generally capitalized through equity contributions from the members, although certain investments are leveraged through various financing arrangements. Our exposure to the joint ventures is limited to amounts invested or committed to the joint ventures at inception, and neither we nor the other investors are required to provide financial or other support in excess of their capital commitments.

In some cases these joint ventures are considered to be variable interest entities (“VIEs”). Generally, a VIE is an entity with one or more of the following characteristics: (a) the total equity investment at risk is not sufficient to permit the entity to finance its activities without additional subordinated financial support; (b) as a group, the holders of the equity investment at risk lack (i) the power, through voting rights or similar rights, to direct the activities of the entity that most significantly impact its financial performance, (ii) the obligation to absorb the expected losses of the entity, or (iii) the right to receive the expected residual returns of the entity; or (c) the equity investors have voting rights that are not proportional to their economic interests and substantially all of the entity’s activities either involve, or are conducted on behalf of, an investor (including its related parties) that has disproportionately few voting rights.

In certain circumstances, we hold 50% of the voting rights to elect the board of directors of the joint venture, but own varying economic interests, which currently range from 4.5% to 90%. In other cases, our voting rights are proportional to our economic interests, however the joint ventures are subject to management or other contracts that create VIEs. GAAP requires a VIE to be consolidated in the financial statements of the entity that is determined to be the primary beneficiary of the VIE. The primary beneficiary generally is the entity that has both the following characteristics: (i) the power to direct the activities of the VIE that most significantly impact its economic performance; and (ii) the obligation to absorb expected losses of, or the right to receive benefits from, the VIE that could potentially be significant to the VIE.

We have analyzed each of the joint ventures and determined that either: (1) they are not VIEs and we do not have a controlling financial interest; or (2) they are VIEs but we are not the primary beneficiary. In determining whether we are the primary beneficiary of a VIE, we consider qualitative and quantitative factors, including, but not limited to: the amount and characteristics of our investment; the obligation or likelihood that we or other investors will be required to provide financial support; our and the other investors’ ability to control or significantly influence key decisions for the VIE; and the similarity and significance of the VIE’s business activities to our and the other investors’ business activities. Significant judgments related to these determinations include estimates about the current and future fair values and performance of assets held by the VIEs and general market conditions.

Since we do not consolidate the joint ventures but have significant influence over their operating and financial policies, we account for our investments in joint ventures using the equity method. Under the equity method, we initially record investments in unconsolidated joint ventures at cost and adjust for our proportionate share of net earnings or losses, cash contributions made and distributions received, and other adjustments, as appropriate.

Distributions of operating profit from joint ventures are reported as part of operating cash flows on our statement of cash flows. Distributions related to a capital transaction, such as a refinancing transaction or sale, are reported as investing activities on our statement of cash flows.

We perform a quarterly evaluation of our investments in unconsolidated joint ventures to determine whether the fair value of our interest in each joint venture is less than the carrying value, and, if such decrease in value is deemed to be other-than-temporary, we write down our investment to fair value.

### Loans Receivable and Interest Income Recognition

We originate and purchase loans receivable. Originated loans are recorded at amortized cost, or the UPB less net deferred loan fees. Net deferred loan fees include unamortized origination and other fees charged to the borrower less direct incremental loan origination costs we incurred. Purchased loans are recorded at amortized cost, or the UPB less unamortized purchase discount. Costs to purchase loans are expensed as incurred. Interest income is recognized based upon the contractual rate and the outstanding principal balance of the loans. Purchase discount or net deferred loan fees are amortized over the expected life of the loans using the effective yield method except on revolving loans, for which the straight-line method is used. When a loan is prepaid, prepayment fees and any excess of proceeds over the

carrying amount of the loan are recognized as a gain. Loans that we have the intent and ability to hold for the foreseeable future are classified as held-for-investment.

**Loans Held for Sale**—Loans held for sale are loans that we intend to sell or liquidate in the foreseeable future and are carried at the lower of amortized cost or fair value.

**Past Due Loans**—We place loans on nonaccrual status when any portion of principal or interest is more than 90 days past due, or earlier when concern exists as to the ultimate collection of principal or interest. When we place a loan on nonaccrual status, we reverse the accrual for unpaid interest and do not recognize interest income until we receive cash and the loan returns

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to accrual status. Generally, a loan may be returned to accrual status when all delinquent principal and interest are brought current in accordance with the terms of the loan agreement and the borrower has met certain performance criteria.

**Impairment and Allowance for Loan Losses**—We regularly analyze the extent and effect of any credit migration from underwriting and the initial investment review associated with a loan’s performance and/or value of underlying collateral as well as the financial and operating capability of the borrower/sponsor. Specifically, a property’s operating results and any cash reserves are analyzed and used to assess (i) whether cash from operations are sufficient to cover the debt service requirements currently and into the future, (ii) the ability of the borrower to refinance the loan, and/or (iii) the property’s liquidation value. Where applicable, we also evaluate the financial wherewithal of any loan guarantors as well as the borrower’s competency in managing and operating the properties. Such analysis is performed at least quarterly, or more often as needed when impairment indicators are present. We do not utilize a statistical credit rating system to monitor and assess the credit risk and investment quality of our acquired or originated loans. Given the diversity of our investment portfolio, management believes there is no consistent method of assigning a numerical rating to a particular loan that captures all of the various credit metrics and their relative importance. Therefore, we evaluate impairment and allowance for loan loss on an individual loan basis.

A loan is considered to be impaired when it is probable that we will not be able to collect all amounts due according to the contractual terms of the loan agreement. A loan is also considered to be impaired if it has been restructured in a troubled debt restructuring (“TDR”) involving a modification of terms as a concession resulting from the debtor’s financial difficulties. We measure impairment based on the present value of expected future cash flows discounted at the loan’s effective interest rate, the loan’s observable market price, or the fair value of the collateral if the loan is collateral dependent. If the loan valuation is less than the recorded investment in the loan, a valuation allowance is established with a corresponding charge to allowance for loan loss.

**Purchased Credit-Impaired (“PCI”) Loans**—PCI loans are acquired loans with evidence of credit quality deterioration since origination for which it is probable at acquisition that we will collect less than the contractually required payments. PCI loans are recorded at the initial investment in the loans and accreted to the estimated cash flows expected to be collected measured at acquisition date. The excess of cash flows expected to be collected measured at acquisition date over the initial investment (“accretable yield”) is recognized in interest income over the remaining life of the loan using the effective interest method. The excess of contractually required payments at the acquisition date over expected cash flows (“nonaccretable difference”) is not recognized as an adjustment of yield, loss accrual or valuation allowance. We evaluate estimated future cash flows on a quarterly basis, starting with the first full quarter after acquisition, or earlier if conditions indicating impairment are present. Subsequent increases in cash flows expected to be collected are recognized prospectively through an adjustment to the loan’s accretable yield over its remaining life, which may result in a reclassification from nonaccretable difference to accretable yield. Subsequent decreases in cash flows expected to be collected are evaluated to determine whether a provision for loan loss should be established. If decreases in expected cash flows result in a decrease in the estimated fair value of the loan below its amortized cost, we will record a provision for loan losses calculated as the difference between the loan’s amortized cost and the revised cash flows, discounted at the loan’s effective yield.

PCI loans may be aggregated into pools based upon common risk characteristics, such as loan performance, collateral type and/or geographic location of the collateral. Once a loan pool is identified, a composite yield and estimate of cash flows expected to be collected (including expected prepayments) are used to recognize interest income. A loan resolution within a loan pool, which may involve the sale of the loan or foreclosure on the underlying collateral, results in the removal of an allocated carrying amount. A loan modified within a loan pool remains in the loan pool, with the effect of the modification incorporated into the expected future cash flows.

### **Investment in Real Estate**

**Real Estate Acquisitions**—Real estate acquisitions are recorded at the fair values of the acquired components at the time of acquisition, allocated among land, building, improvements, equipment, lease-related tangible and identifiable intangible assets, such as tenant improvements, deferred leasing costs, in-place lease values, above- and below-market lease values. We evaluate each purchase transaction to determine whether the acquired assets meet the definition of a business. Transaction costs related to acquisitions that are not deemed to be businesses are included in the cost basis

of the acquired assets, while transaction costs related to acquisitions that are deemed to be businesses are expensed as incurred. Net cash paid to acquire an operating property is classified as investing activities on our statements of cash flows.

The fair value of acquired land is derived from recent comparable sales of land and listings within the same local region based on available market data. The fair value of acquired buildings and building improvements is derived from comparable sales, discounted cash flow analysis using market-based assumptions, or replacement cost, as appropriate. The fair value of site and tenant improvements is estimated based upon current market replacement costs and other relevant market rate information.

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In-place leases generate value over and above the tangible real estate because a property that is occupied with leased space is typically worth more than a vacant building without an operating lease contract in place. The fair value of acquired in-place leases is derived based on management's assessment of lost rental income and tenant reimbursements that would be incurred to lease a hypothetically vacant building to its actual existing occupancy level on the valuation date. The net amount recorded for acquired in-place leases is included in other assets on our balance sheets and amortized on a straight-line basis as an increase to depreciation and amortization expense over the remaining term of the applicable leases.

The fair value of the above- or below-market component of an acquired in-place operating lease represents the present value of the difference between contractual rents of acquired leases and market rents at the time of the acquisition, discounted for tenant credit risks. Above- or below-market lease values are amortized on a straight-line basis as a decrease or increase to rental income, respectively, over the applicable lease terms.

Deferred leasing costs represent management's estimation of the avoided leasing commissions and legal fees associated with an existing in-place lease. The net amount is included in other assets on our balance sheets and amortized on a straight-line basis as an increase to depreciation and amortization expense over the remaining term of the applicable lease.

Fair values of these components generally rely on Level 2 or Level 3 inputs of the fair value hierarchy (see —Fair Value Measurement).

**Depreciation—**Depreciation is computed on the straight-line basis over the estimated useful lives of the assets, which generally range from 10 to 40 years for buildings and improvements and 5 to 15 years for furniture, fixtures and equipment. Tenant improvements are amortized over the shorter of the remaining lease term or the estimated useful life.

Expenditures for ordinary repairs and maintenance are expensed as incurred, while expenditures for significant renovations that improve or extend the useful life of the asset are capitalized and depreciated over their estimated useful lives.

**Real Estate Acquired in Settlement of Loans—**Real estate acquired in full or partial settlement of loans (REO) is measured at fair value less estimated costs to sell at the acquisition date if the property meets the GAAP definition of a held for sale property. REO property that is classified as held for sale is not depreciated during the holding period. If we intend to operate the property, the fair value is allocated among the acquired assets (see —Real Estate Acquisitions). The difference between the carrying value of the loan and the fair value of the foreclosed asset is recognized in the statement of operations, after reversing any previously recognized provision on the loan. The fair value of REO is generally based on a third party appraisal or on a combination of appraised value, broker price opinions and comparable sales.

**Real Estate Impairment—**We evaluate our investments in real estate for impairment periodically or whenever events or changes in circumstances indicate that the carrying amounts may not be recoverable. We evaluate cash flows and determine impairments on an individual property basis. In making this determination, we review, among other things, current and estimated future cash flows associated with each property, market information for each sub-market, including, where applicable, competition levels, foreclosure levels, leasing trends, occupancy trends, lease or room rates, and the market prices of similar properties recently sold or currently being offered for sale, and other quantitative and qualitative factors. If an impairment indicator exists, We compare the expected future undiscounted cash flows to the carrying amount of the asset to evaluate whether the carrying value is recoverable. If the sum of the estimated undiscounted cash flows is less than the carrying amount of the asset, we would record an impairment loss for the difference between the estimated fair value and the carrying amount of the asset.

### **Rental Income and Tenant Reimbursements**

Rental income is recognized on a straight-line basis over the term of the related lease. Residential leases generally have one-year terms while commercial leases generally have longer terms. Rents received in advance are deferred. In net lease arrangements, costs reimbursable from tenants for real estate taxes, property insurance and other recoverable costs are recognized as revenue in the period the recoverable costs are incurred. When we are the primary obligor with respect to purchasing goods and services for property operations and have discretion in selecting the supplier and retain credit risk, tenant reimbursement revenue and property operating expenses are presented on a gross

basis in our statement of operations. For certain triple net leases where the lessee self-manages the property, hires its own service providers and retains credit risk for routine maintenance contracts, no reimbursement revenue and expense are recognized.

#### Fair Value Measurement

We determine the estimated fair value of financial assets and liabilities using the three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. The three levels of inputs that may be used to measure fair value are as follows:

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

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Level 2—Prices are determined using other significant observable inputs. Observable inputs are inputs that other market participants would use in pricing a security. These may include quoted prices for similar securities, interest rates, prepayment speeds, credit risk and others.

Level 3—Prices are determined using significant unobservable inputs. In situations where quoted prices or observable inputs are unavailable (for example, when there is little or no market activity for an investment at the end of the period), unobservable inputs may be used.

We record certain financial instruments at fair value on a recurring basis when required by GAAP. Examples of financial instruments we own that are required by GAAP to be carried at fair value are derivative instruments and debt securities designated as available-for-sale. We have not elected the fair value option for financial instruments not required to be carried at fair value by GAAP. We carry those financial instruments at amortized cost and separately disclose the fair value on a quarterly basis. These instruments are recorded at fair value only if they are impaired. In cases where quoted market prices are not available, fair values are estimated using inputs such as discounted cash flow projections, market comparables, dealer quotes and other quantitative and qualitative factors. The fair values of foreign exchange contracts are determined by discounting the expected cash flow of each instrument based on forecast foreign exchange rates. This analysis reflects the contractual terms of the derivatives, observable market-based inputs, and credit valuation adjustments to appropriately reflect the non-performance risk for both the Company and the respective counterparty. The fair value of debt securities and loans are generally determined by discounting the expected cash flows using observable current and forward rates of applicable published indices. Fair values of our investments in unconsolidated joint ventures are primarily derived by applying our ownership interest to the fair value of the underlying assets and liabilities of each joint venture. Our proportionate share of each joint venture's fair value approximates our fair value of the investment as the timing of cash flows of the joint venture does not deviate materially from the timing of cash flows we receive from the joint venture. Considerable judgment is necessary to interpret market data and develop estimated fair value. The use of different assumptions or methodologies could have a material effect on the estimated fair value amounts.

### Income Taxes and REIT Compliance

We elected to be taxed as a REIT, commencing with our initial taxable year ended December 31, 2009. A REIT is generally not subject to corporate level federal and state income tax on net income it distributes to its stockholders. To qualify as a REIT, we must meet a number of organizational and operational requirements, including a requirement to distribute at least 90% of our taxable income to our stockholders. If we fail to qualify as a REIT in any taxable year, we will be subject to federal and state income taxes at regular corporate rates (including any applicable alternative minimum tax) and may not be able to qualify as a REIT for four subsequent taxable years. Even if we qualify as a REIT, we may be subject to certain federal, state, local and foreign taxes on our income and property and to federal income and excise taxes on our undistributed taxable income.

We have elected or may elect to treat certain of our subsidiaries as TRSs. In general, a TRS of a REIT may perform non-customary services for tenants of the REIT, hold assets that the REIT cannot hold directly and, subject to certain exceptions related to hotels and healthcare properties, may engage in any real estate or non-real estate related business. A TRS is treated as a regular corporation and is subject to federal, state, local, and foreign taxes on its income and property.

### Recent Accounting Updates

Recent accounting updates are included in Note 2 to our consolidated financial statements in Item 15 of this Annual Report.

### Results of Operations

We commenced operations upon completion of our IPO on September 29, 2009 and continue to actively invest in our target assets. In general, period-over-period increases in our results of operations reflect our ongoing investment activities and capital-raising efforts. At December 31, 2013, we had 58 active investments representing \$2.0 billion of invested equity, compared to 47 investments and \$1.1 billion at December 31, 2012. Due to the overall growth and increased number of investments in nearly every category, the results of operations presented below for each period



are not directly comparable and are not necessarily indicative of future financial condition or results of operations. We operate in three reportable segments: real estate debt investments, SFR rentals and other real estate equity investments. The real estate debt investments segment includes our investments in originated and acquired commercial real estate debt, mortgage-backed securities, and other debt-related investments. The SFR rental segment represents our investment in CAH OP. The other real estate equity investments segment includes real estate acquired in settlement of loans, common equity in real estate or related companies, and certain preferred equity investments with profit participation meeting certain risk or return profiles.

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## Income from Our Investments

Our largest source of income is our real estate debt investments, which we hold either directly or through our investments in unconsolidated joint ventures. We have been continually investing in our target assets throughout 2011, 2012 and 2013, and therefore, income from some investments may reflect less than a full year's results of operations. We have also sold or received early payoffs on some of our debt investments, sometimes at substantial gains, which affect period over period comparability.

Income (loss) from our investments by type of investment is summarized below. We have recently re-categorized some of our investments, as described in Note 2 to our consolidated financial statements included in this Annual Report. Certain amounts for the years ended December 31, 2012 and 2011 have been reclassified to conform to the current period presentation:

(In thousands)	Year Ended December 31, 2013			
	Income (Loss)	Less: Expenses, Other (Income) Loss and Income Tax Provision	Less: Net Income Attributable to Noncontrolling Interests	Net Income (Loss) Attributable to Colony Financial, Inc.
Amounts allocated to investment segments:				
Real estate debt investments				
Acquisitions:				
Single loans—first mortgages	\$28,487	\$5,068	\$ 5,935	\$17,484
Single loans—subordinated debt	6,290	18	805	5,467
Loan portfolios	52,581	2,747	1,137	48,697
CMBS/bonds	8,360	123	798	7,439
Total acquisitions	95,718	7,956	8,675	79,087
Originations:				
Senior & whole mortgage loans	23,420	665	1,478	21,277
Subordinated debt <sup>(1)</sup>	53,453	353	12,739	40,361
Total originations	76,873	1,018	14,217	61,638
Total real estate debt investments	172,591	8,974	22,892	140,725
Single-family residential rentals	(8,013 )	—	—	(8,013 )
Other real estate equity investments <sup>(2)</sup>	19,957	1,357	1,266	17,334
Total investments	184,535	10,331	24,158	150,046
Amounts not allocated to investment segments	282	48,563	—	(48,281 )
	\$184,817	\$58,894	\$ 24,158	\$101,765

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(In thousands)	Year Ended December 31, 2012			
	Income (Loss)	Less: Expenses, Other (Income) Loss and Income Tax Provision	Less: Net Income Attributable to Noncontrolling Interests	Net Income (Loss) Attributable to Colony Financial, Inc.
Amounts allocated to investment segments:				
Real estate debt investments				
Acquisitions:				
Single loans—first mortgages	\$ 19,221	\$ 3,866	\$ 4,209	\$ 11,146
Single loans—subordinated debt	4,392	179	869	3,344
Loan portfolios	31,438	2,141	—	29,297
CMBS/bonds	5,467	748	38	4,681
Total acquisitions	60,518	6,934	5,116	48,468
Originations:				
Senior & whole mortgage loans	20,395	218	972	19,205
Subordinated debt <sup>(1)</sup>	18,456	754	106	17,596
Total originations	38,851	972	1,078	36,801
Total real estate debt investments	99,369	7,906	6,194	85,269
Single-family residential rentals	(2,126 )	—	—	(2,126 )
Other real estate equity investments <sup>(2)</sup>	10,550	22	—	10,528
Total investments	107,793	7,928	6,194	93,671
Amounts not allocated to investment segments	170	31,830	—	(31,660 )
	\$ 107,963	\$ 39,758	\$ 6,194	\$ 62,011
(In thousands)	Year Ended December 31, 2011			
	Income (Loss)	Less: Expenses, Other (Income) Loss and Income Tax Provision	Less: Net Income Attributable to Noncontrolling Interests	Net Income (Loss) Attributable to Colony Financial, Inc.
Amounts allocated to investment segments:				
Real estate debt investments				
Acquisitions:				
Single loans—first mortgages	\$ 7,158	\$ 7	\$ 888	\$ 6,263
Single loans—subordinated debt	1,360	125	—	1,235
Loan portfolios	22,906	1,976	—	20,930
CMBS/bonds	3,023	595	207	2,221
Total acquisitions	34,447	2,703	1,095	30,649
Originations:				
Senior & whole mortgage loans	13,293	170	—	13,123
Subordinated debt <sup>(1)</sup>	9,299	799	9	8,491
Total originations	22,592	969	9	21,614
Total real estate debt investments	57,039	3,672	1,104	52,263
Single-family residential rentals	—	—	—	—
Other real estate equity investments <sup>(2)</sup>	8,118	—	—	8,118

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Total investments	65,157	3,672	1,104	60,381
Amounts not allocated to investment segments	312	18,433	—	(18,121 )
	\$65,469	\$22,105	\$ 1,104	\$42,260

(1) Subordinated debt includes B-notes, mezzanine loans, and preferred equity earning a fixed return.

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Other real estate equity investments include interests in real estate properties, equity interests obtained through (2) foreclosures or deed-in-lieu of foreclosure on the collateral of target assets originally acquired or originated as debt instruments, and preferred equity earning a fixed return plus equity participation.

### Net Income from Real Estate Debt Investments

Net income from acquired first mortgage loans for the year ended December 31, 2013 increased \$6.3 million, or 57%, compared to the year ended December 31, 2012. The increase primarily reflects income from the Florida Retail First Mortgage, Phoenix Corporate Tower Loan and Luxury Destination Club Recourse Loan II acquired in February 2013, December 2012 and May 2012, respectively. We recognized a \$2.5 million gain on foreclosure of the Phoenix Corporate Tower Loan in September 2013. Expenses on acquired first mortgage loans for the years ended December 31, 2013 and 2012 include the interest expense and servicing costs on Luxury Destination Club Recourse Loan II, where we obtained seller-provided financing. All contractual interest due for the term of the financing was pre-funded by the borrower. Net income from acquired first mortgage loans for the year ended December 31, 2012 increased \$4.9 million, or 78%, compared to the year ended December 31, 2011, primarily reflecting income from the Luxury Destination Club Recourse Loan II acquired in May 2012.

Net income from acquired subordinated debt for the year ended December 31, 2013 increased \$2.1 million, or 63%, compared to the year ended December 31, 2012. The increase primarily reflects a full year's effect of income from the Ashford Notes acquired in February 2012 and the Manhattan Landmark Buildings Loan B-note retained subsequent to the A-note sale in April 2012. Net income from acquired subordinated debt for the year ended December 31, 2012 increased \$2.1 million, or 171%, compared to the year ended December 31, 2011. The increase primarily reflects net income from the Ashford Notes and the reclassification of net income from the Manhattan Landmark Buildings Loan from acquired first mortgage loan to subordinated debt after the A-note sale. This increase was partially offset by the reclassification of net income generated from the Hotel Portfolio to other real estate equity investments effective January 2012 upon the foreclosure on the collateral.

Net income from loan portfolios include income from loan portfolios acquired in structured transactions with the FDIC as well as from commercial banks. For the year ended December 31, 2013, net income from loan portfolios increased \$19.4 million, or 66%, compared to the year ended December 31, 2012. The drivers of the overall increase are: additional income from 10 loan portfolios acquired throughout 2012 and 2013, lower notional interest expense on FDIC purchase money notes resulting from principal payments, an \$11 million gain on foreclosure of an REO property in the German Loan Portfolio IV, and favorable changes in expected accretable yields on some of our existing portfolios. These increases are partially offset by decreases due to ongoing loan resolutions and a combined impairment of \$6.6 million on certain loan pools within 13 of our loan portfolios, including impairment on REO properties held for sale. Net income from loan portfolios for the year ended December 31, 2012 increased \$8.4 million, or 40%, compared to the year ended December 31, 2011. The increase primarily reflects 11 loan portfolios acquired throughout 2011 and 2012. Two of our FDIC portfolios acquired in late 2010 are managed by asset management companies that are wholly-owned by us. We charge a fee of 50 basis points on each portfolio's UPB per annum, payable monthly, which is included in income from loan portfolios. Expenses on loan portfolios reflect asset management, servicing fees and interest expense incurred by the asset management companies and our consolidated loan portfolios.

Net income from CMBS/bonds for the year ended December 31, 2013 increased \$2.8 million, or 59%, compared to the year ended December 31, 2012. The increase primarily reflects a \$1.2 million gain from the sale of a senior bond in a CMBS-resecuritization acquired in May 2010 and interest income from the MF5 Loan Portfolio following the desecuritization of the trust in February 2013. Net income from CMBS/bonds for the year ended December 31, 2012 increased \$2.5 million, or 111%, compared to the year ended December 31, 2011, reflecting net income generated from MF5 CMBS acquired in February 2012, prior to the desecuritization.

Net income from originated senior and whole mortgage loans for the year ended December 31, 2013 increased \$2.1 million, or 11%, compared to the year ended December 31, 2012. The increase primarily reflects \$14.3 million of net income generated from eight new originated loans in 2013 plus six loans within the Transitional CRE Lending Platform, a full year's effect of one loan originated in late 2012, and a \$2.8 million gain recognized from an early payoff of the Florida Residential Development Loan which was acquired and resolved within 2013. The increases are

partially offset by the reduction in income following the November 2012 payoff of WLH Secured Loan, which had generated \$12.6 million of net income in 2012. Net income from originated senior and whole mortgage loans for the year ended December 31, 2012 increased \$6.1 million, or 46%, compared to the year ended December 31, 2011. The increase primarily reflects a \$5.5 million gain recognized from the early payoff of the WLH Secured Loan and a full year's effect of net income generated from the Luxury Destination Club Recourse Loan I originated in September 2011.

Net income from originated subordinated debt for the year ended December 31, 2013 increased \$22.8 million, or 129%, compared to the year ended December 31, 2012. The increase primarily reflects income from new originations including One Court Square Preferred Equity originated in July 2012, National Hotel Portfolio Mezzanine Loan originated in May 2013, and Mexico Luxury Resort Junior Mortgage Participation and New York Student Housing Loan originated in August 2013, among

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others. The increase also reflects income from the Lifestyle Athletic Club Mortgage Participation originated in March 2013 following the sale of an A-note in July 2013, a \$3.2 million gain recognized from the payoff of 2100 Grand B-Note in May 2013 and a \$1.1 million gain recognized from the sale of our pro-rata share of the Extended Stay Mezzanine B&C Loans in September 2013. The increases are partially offset by the reduction in income resulting from the payoff of Centro Mezzanine Loans, the sale of Extended Stay Mezzanine B&C Loans, as well as the May 2013 prepayment of Luxury Destination Resort Loan, a loan we originated in 2011. Net income from originated subordinated debt for the year ended December 31, 2012 increased \$9.1 million, or 107%, compared to the year ended December 31, 2011. The increase primarily reflects net income from new 2012 originations and a full year's effect of 2011 originations, including Centro Mezzanine Loans and Luxury Destination Resort Loan originated in the second half of 2011 and One Court Square Preferred Equity and New England Hotel Portfolio Mezzanine Loan originated in 2012.

Net income from our European real estate debt investments for the three years ended December 31, 2013, 2012 and 2011 was \$14.0 million, \$3.7 million and \$3.1 million, respectively.

### Loss from Single-Family Residential Rentals

Our investment in single-family residential rentals through CAH OP generated a loss of \$8.0 million and \$2.1 million during the years ended December 31, 2013 and 2012, respectively, including approximately \$8.0 million and \$1.2 million, respectively, that represent our share of depreciation expense. Loss for the year ended December 31, 2013 also reflects our share of expense related to the June 2013 Colony American Homes initial public offering attempt. The SFR rental business was started in March 2012 and the business has grown rapidly; therefore, prior year results do not provide meaningful comparisons to the current year results. As of December 31, 2013, CAH OP owned 14,900 units in nine states, including units operated in a joint venture with Fannie Mae, compared to 5,405 units as of December 31, 2012. The overall portfolio was 61% occupied as of December 31, 2013, up from 57% occupied as of December 31, 2012. The improvement in portfolio occupancy is the result of a recent strategy to slow acquisition activity in order to focus on improved operational performance including higher renovation and leasing productivity. During the year ended December 31, 2013, CAH OP averaged approximately 750 renovations and 700 new leases per month.

### Net income from Other Real Estate Equity Investments

Net income from other real estate equity investments increased by \$6.8 million, or 65%, from 2012 to 2013 and \$2.4 million, or 30%, from 2011 to 2012. Net income from other real estate equity investments for the year ended December 31, 2013 includes a \$10.7 million gain recognized from the sale of our remaining 615,932 shares of common stock in First Republic Bank, net income from the operations of our Hotel Portfolio, \$6.3 million of income from the Multifamily Portfolio Preferred Equity, which we closed in March 2013 and in which we have made additional investments since March 2013. Net income from other real estate equity investments for the year ended December 31, 2012 reflects income from our investment in First Republic Bank, including a \$5.4 million gain recognized from the sale of 543,760 shares of its common stock, a \$1.8 million gain on sale of residential development projects to WLH in June 2012 and net income from the operations of our Hotel Portfolio following the foreclosure on the collateral in January 2012. Net income from other real estate equity investments for the year ended December 31, 2011 primarily represents income from our investment in First Republic Bank, including a \$4.1 million gain recognized from the sale of 325,126 shares of its common stock.

### Concentration

Certain investments individually generated greater than 10% of our total income for the periods presented. For the years ended December 31, 2013 and 2012, Luxury Destination Club Recourse Loan I and II, which share the same corporate guarantor, generated 14% and 18% of total income, respectively. After deducting investment-specific interest and other expenses, and amounts attributable to noncontrolling interests, Luxury Destination Club Recourse Loan I and II represent 12% and 16% of our net income attributable to stockholders, respectively. National Hotel Portfolio Mezzanine Loan generated 13% of our total income for the year ended December 31, 2013. After deducting investment-specific expenses and amounts attributable to noncontrolling interests, the National Hotel Portfolio Mezzanine Loan represents 12% of our net income attributable to stockholders for the same period. For the year ended December 31, 2012, WLH Secured Loan generated 12% of total income. For the year ended December 31, 2011,

WLH Secured Loan and our investment in First Republic Bank each generated 12% of our total income.

Amounts Not Allocated to Investments

Certain non-investment-specific income and expense amounts not allocated to segments are summarized below.



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	Year Ended December 31,		
(in thousands)	2013	2012	2011
Interest income from cash	\$282	\$170	\$312
Expenses:			
Management fees	\$26,263	\$18,982	\$8,477
Unconsummated deal expenses	955	498	676
Interest expense	13,316	3,839	2,309
Administrative expense	7,370	6,346	5,780
Income tax provision	659	2,165	1,191
Total expenses	\$48,563	\$31,830	\$18,433

Management Fees—Management fees include the following:

	Year Ended December 31,		
(in thousands)	2013	2012	2011
Base management fees	\$22,265	\$12,332	\$8,128
Share-based compensation	3,998	5,714	—
Incentive fees	—	936	349
	\$26,263	\$18,982	\$8,477

Base management fees have increased by approximately \$9.9 million from 2012 to 2013 and \$4.2 million from 2011 to 2012 due to an increase in our fee base, as defined in our management agreement with the Manager. The increases in our fee base are largely attributable to net proceeds from our equity offerings. The increases resulted from two common stock offerings and our issuance of common stock under our at-the-market stock offering program ("ATM Program") during 2013, with combined net proceeds of approximately \$475 million; and two common stock offerings and two preferred stock offerings during 2012, with combined net proceeds of approximately \$616 million.

Share-based compensation represents expense recognized on restricted shares awarded to our Manager, certain of our executive officers and certain employees of our Manager and its affiliates in 2012. Based upon the vesting schedule of shares awarded and the fair value as of each measurement date, share-based compensation could fluctuate significantly. Incentive fees are based upon our Core Earnings, further described at "—Non-GAAP Supplemental Financial Measure: Core Earnings," and are payable to our Manager in shares of our common stock.

Interest Expense—For the years ended December 31, 2013, 2012 and 2011, we incurred non-segment interest expense of \$13.3 million, \$3.8 million and \$2.3 million, respectively, primarily on our credit facility and convertible senior notes. Interest expense for 2013 was significantly higher as our convertible senior notes were issued in April 2013 and due to higher average outstanding borrowings to temporarily finance our investments during the period. We do not attribute borrowings on our credit facility or proceeds from issuance of convertible notes to specific investments.

Administrative Expenses—Administrative expenses are summarized below:

	Year Ended December 31,		
(In thousands)	2013	2012	2011
Reimbursements to Colony Capital:			
Compensation pursuant to secondment agreement	\$1,286	\$1,207	\$1,248
Allocated overhead and direct administrative expenses	1,787	1,253	344
Total reimbursements to Colony Capital	3,073	2,460	1,592
Professional fees	2,590	2,082	2,767
Other	1,707	1,804	1,421
	\$7,370	\$6,346	\$5,780

Total administrative expenses increased by \$1.0 million, or 16%, from 2012 to 2013 and \$0.6 million, or 10%, from 2011 to 2012 reflecting the added administrative burden associated with the growth of our business.

Income Tax Provision—Our TRSs, which directly or indirectly hold certain of our investments, are subject to corporate level federal, state, foreign and local income taxes. For the years ended December 31, 2013, 2012 and 2011, we incurred income tax expense of \$0.7 million, \$2.2 million and \$1.2 million, respectively. Our current primary sources of income



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subject to taxation at the TRSs are income from loan resolutions in some of our loan portfolios, income from our interests in asset management companies which manage some of our loan portfolios, and hotel operations from our Hotel Portfolio. Income tax provision for 2013 was lower than 2012 as a result of the tax benefit recognized from net operating losses from our Hotel Portfolio which partially offset the income tax expenses on other taxable activities. The increase in income tax provision for 2012 compared to 2011 reflects higher taxable income from loan resolutions held by our TRSs.

## Information About Our Real Estate Debt Portfolio

The following tables summarize certain characteristics of the loans and beneficial interests in securities held by the Company and the joint ventures and our proportionate share:

		December 31, 2013								
(\$ in thousands)		Total Portfolio		Company's Proportionate Share						
Collateral Type	Unpaid Principal Balance	Amortized Cost <sup>(1)</sup>	Unpaid Principal Balance	Amortized Cost <sup>(1)(2)</sup>	% of Amortized Cost	Weighted Average Coupon	Current Interest Yield on Cost	Weighted Average Maturity in Years		
Originated performing loans										
Retail	\$43,850	\$43,400	\$43,850	\$43,400	3.2	% 6.5	% 6.6	% 2.3		
Office	21,725	21,548	21,725	21,548	1.6	% 6.9	% 7.0	% 2.4		
Hospitality	493,242	490,168	253,057	251,350	18.4	% 11.2	% 11.3	% 2.8		
Multifamily	123,700	123,555	93,495	93,382	6.8	% 5.4	% 5.4	% 2.0		
Other commercial	103,823	103,112	102,521	101,810	7.4	% 9.1	% 9.2	% 3.8		
Residential	100,260	99,577	46,618	46,320	3.4	% 13.5	% 13.7	% 3.6		
Land	96,257	92,341	47,919	45,961	3.4	% 12.5	% 13.3	% 2.7		
Total originated performing loans	982,857	973,701	609,185	603,771	44.2	% 9.8	% 9.9	% 2.9		
Acquired loans and beneficial interests in bonds										
Performing:										
Retail	576,529	389,345	264,464	175,766	12.9	% 3.2	% 5.0	% 3.3		
Office	325,986	228,305	138,550	91,176	6.7	% 2.6	% 4.1	% 4.0		
Industrial	204,280	151,883	43,372	31,716	2.3	% 6.3	% 8.7	% 7.8		
Hospitality	285,531	237,885	127,282	109,083	8.0	% 8.4	% 10.7	% 0.9		
Multifamily	522,513	428,340	233,778	205,660	15.0	% 5.0	% 5.7	% 9.0		
Other commercial	283,426	191,045	45,440	33,739	2.5	% 9.4	% 12.2	% 3.7		
Residential	56,039	36,748	17,058	12,649	0.9	% 4.2	% 5.9	% 17.2		
Land	107,830	44,628	14,538	6,382	0.5	% 5.7	% 10.7	% 1.4		
Total acquired performing	2,362,134	1,708,179	884,482	666,171	48.8	% 4.9	% 6.6	% 5.1		
Non-performing:										
Retail	238,841	90,366	41,453	17,970	1.3	%				
Office	108,128	53,801	20,811	11,133	0.8	%				
Industrial	137,125	61,481	29,003	15,141	1.1	%				
Hospitality	58,781	29,101	7,801	3,821	0.3	%				
Multifamily	123,576	52,832	29,890	13,066	1.0	%				
Other commercial	334,197	119,562	44,702	15,507	1.1	%				
Residential	131,315	40,316	19,315	7,453	0.5	%				
Land	619,410	125,227	59,971	12,078	0.9	%				
Total acquired non-performing	1,751,373	572,686	252,946	96,169	7.0	%				

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Total acquired loans	4,113,507	2,280,865	1,137,428	762,340	55.8	%
Total portfolio	\$5,096,364	\$3,254,566	\$1,746,613	\$1,366,111	100.0	%

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Collateral Type	December 31, 2012		Company's Proportionate Share						
	Unpaid Principal Balance	Amortized Cost <sup>(1)</sup>	Unpaid Principal Balance	Amortized Cost <sup>(1)(2)</sup>	% of Amortized Cost	Weighted Average Coupon	Current Interest Yield on Cost	Weighted Average Maturity in Years	
Originated performing loans									
Retail	\$60,000	\$60,000	\$60,000	\$60,000	8.1	% 9.8	% 9.8	% 3.5	
Office	20,258	20,223	20,056	20,021	2.7	% 8.0	% 8.0	% 2.9	
Hospitality	133,285	132,515	82,937	82,472	11.2	% 11.4	% 11.5	% 5.3	
Other commercial	6,109	6,109	3,054	3,054	0.4	% 12.2	% 12.2	% 1.8	
Residential	82,196	79,840	34,960	33,860	4.6	% 12.2	% 12.8	% 3.3	
Total originated performing loans	301,848	298,687	201,007	199,407	27.0	% 10.7	% 10.9	% 4.1	
Acquired loans and beneficial interests in bonds									
Performing:									
Retail	415,149	293,227	92,534	69,409	9.4	% 5.7	% 7.6	% 4.0	
Office	307,008	211,378	77,266	52,032	7.1	% 5.4	% 8.3	% 4.9	
Industrial	244,140	182,908	49,032	36,085	4.9	% 6.3	% 8.7	% 7.2	
Hospitality	300,291	247,002	139,883	118,080	16.0	% 8.6	% 10.3	% 1.9	
Multifamily	478,674	370,053	104,569	87,722	11.9	% 5.0	% 6.0	% 10.9	
Other commercial	358,800	233,877	43,971	28,872	3.9	% 9.6	% 13.9	% 3.3	
Residential	58,077	28,128	8,881	4,781	0.6	% 5.6	% 10.3	% 7.6	
Land	159,611	67,642	17,228	6,968	0.9	% 5.6	% 14.3	% 1.8	
Total acquired performing	2,321,750	1,634,215	533,364	403,949	54.7	% 6.6	% 8.9	% 5.1	
Non-performing:									
Retail	322,592	145,863	50,130	23,371	3.1	%			
Office	422,423	106,487	114,910	24,724	3.4	%			
Industrial	181,647	86,819	35,338	17,946	2.4	%			
Hospitality	74,334	40,046	9,159	4,902	0.7	%			
Multifamily	200,119	91,772	41,704	17,618	2.4	%			
Other commercial	401,434	138,128	55,406	18,189	2.5	%			
Residential	182,411	58,319	29,431	11,847	1.6	%			
Land	856,417	164,897	80,024	15,953	2.2	%			
Total acquired non-performing	2,641,377	832,331	416,102	134,550	18.3	%			
Total acquired loans	4,963,127	2,466,546	949,466	538,499	73.0	%			
Total portfolio	\$5,264,975	\$2,765,233	\$1,150,473	\$737,906	100.0	%			

(1) The following table summarizes the amortized cost of the total portfolio and the Company's proportionate share included in the table above:

(Amounts in thousands)	December 31, 2013		December 31, 2012	
	Total Portfolio	Company's Proportionate Share	Total Portfolio	Company's Proportionate Share
Loans receivable, net, on the Company's consolidated balance sheet	\$1,028,654	\$ 730,204	\$333,569	\$ 240,914
	30,834	30,680	32,055	31,895

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Beneficial interests in debt securities on the  
Company's consolidated balance sheet

Loans receivable, net, held by unconsolidated joint ventures	2,171,943	593,660	2,383,748	457,166
ADC loans held by unconsolidated joint ventures <sup>(a)</sup>	23,135	11,567	15,861	7,931
	\$3,254,566	\$ 1,366,111	\$2,765,233	\$ 737,906

(a) Certain acquisition, development and construction loans are accounted for under the equity method depending upon their characteristics.

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- (2) Our proportionate share of amortized cost is calculated as our share of the loans and debt securities based upon our ownership interest in each respective investment entity.

As of December 31, 2013, our and our joint ventures' performing loan portfolio comprised fixed rate loans bearing interest rates ranging from 2.0% to 20.9% (weighted average of 7.6%) with an aggregate UPB of \$1.43 billion and variable rate loans bearing interest rates ranging from 1.1% to 12.5% (weighted average of 6.3%) with an aggregate UPB of \$1.91 billion. Maturity dates of performing loans range from January 2014 to February 2049. Scheduled maturities based on UPB of performing loans as of December 31, 2013 are as follows:

(In thousands)

One year or less	\$792,923
Greater than one year and less than five years	1,873,349
Greater than or equal to five years	678,719
Total	\$3,344,991

### Liquidity and Capital Resources

Our current primary uses of liquidity are to fund:

- acquisitions of our target assets and related ongoing commitments;
- our operations, including overhead costs and the management fee to our Manager;
- distributions to our stockholders; and
- principal and interest payments on our borrowings, including interest obligation on our convertible debt.

Our current primary sources of liquidity are:

- cash on hand;
- our credit facility;
- cash flow generated from our investments, both from operations and return of capital;
- proceeds from full or partial realization of investments;
- investment-level financing; and
- proceeds from public or private equity and debt offerings.

We believe that our capital resources are sufficient to meet our short-term and long-term capital requirements.

However, because of distribution requirements imposed on us to qualify as a REIT, which generally require that we distribute to our stockholders 90% of our taxable income, our ability to finance our growth must largely be funded by external sources of capital. As a result, in order to continue investing in our target assets and sustain our growth, we will have to rely on third-party sources of capital, including public and private offerings of securities and debt financings, which may or may not be available on favorable terms, or at all.

### Contractual Obligations and Commitments

The following table summarizes our known contractual obligations and commitments on an undiscounted basis as of December 31, 2013 and in future periods in which we expect to settle such obligations. The table does not reflect the effects of actual repayments or draws on our credit facility or new financing obtained subsequent to year end.

(In thousands)	Payments Due by Period				
	Total	Less Than 1 Year	1-3 Years	3-5 Years	More Than 5 Years
Contractual Obligations					
Principal payments—credit facility	\$138,500	\$—	\$138,500	\$—	\$—
Interest and fees—credit facility	16,136	5,623	10,513	—	—
Convertible senior notes—principal and interest <sup>(2)</sup>	295,000	10,000	20,000	20,000	245,000
Secured financing—principal and interest <sup>(3)</sup>	327,079	104,296	100,038	18,647	104,098
Total	\$776,715	\$119,919	\$269,051	\$38,647	\$349,098

As of December 31, 2013, we had outstanding borrowings on our credit facility of \$138.5 million bearing interest (1) at 1-month LIBOR plus 2.75%. We have estimated the future interest payments based on the 1-month LIBOR forward rates as of December 31, 2013 and



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unused commitment fees calculated at 0.5% assuming the principal amount is repaid on August 5, 2016, the contractual maturity date of our credit facility.

As of December 31, 2013, we had outstanding \$200 million in convertible senior notes which bear interest at 5% (2)per annum. We have assumed the entire principal amount to be repaid on April 15, 2023, the contractual maturity date of the notes.

Amounts include minimum principal and fixed-rate interest obligations through the original maturity date of the secured financing related to our Luxury Destination Club Recourse Loan II and Midwest NNN Office Campus. For the secured financing related to our Freddie Mac Portfolio which is indexed to the 1-month LIBOR, we have estimated future interest payments using the 1-month LIBOR forward rates through the original maturity date of (3)the financing. The Freddie Mac Portfolio financing requires monthly interest payments and principal curtailment based upon the ratio of principal outstanding to collateral cost basis. The initial principal curtailment requirement is 70% of all excess cash flow from the underlying loan portfolio, after payment of certain loan servicing fees and monthly interest, but may increase or decrease in the future. We have estimated the timing of future principal payments based on estimated future cash flows of the underlying loan portfolio used during underwriting. The table does not reflect amounts due under our management agreement, as described below, or derivative instruments as those contracts do not have fixed and determinable payments.

Pursuant to the operating agreements of certain unconsolidated joint ventures, the joint venture partners may be required to fund additional amounts for future investments, unfunded lending commitments, ordinary operating costs, guaranties or commitments of the joint ventures. As of December 31, 2013, our share of those commitments was \$8.5 million.

We may be required to fund additional amounts to borrowers pursuant to certain loan agreements. As of December 31, 2013, We had combined unfunded lending commitments of \$17.3 million.

### Our Management Agreement

Our management agreement automatically renews for a one-year term on each anniversary of our IPO. The management agreement may be terminated upon at least 180 days' prior written notice to the Manager.

**Base Management Fee**—We pay our Manager a base management fee in an amount equal to 1.5% of our stockholders' equity, as defined in the management agreement, per annum, calculated and payable quarterly in arrears in cash.

**Incentive Fee**—We also pay our Manager an incentive fee based upon our Core Earnings, as defined in "—Non-GAAP Supplemental Financial Measure: Core Earnings." The incentive fee payable, with respect to each calendar quarter, is an amount not less than zero, equal to the difference between (1) the product of (x) 20% and (y) the difference between (i) Core Earnings, on a rolling four-quarter basis and before the incentive fee for the current quarter, and (ii) the product of (A) the weighted average of the issue price per share of common stock in all of our offerings multiplied by the weighted average number of shares of common stock outstanding (including any restricted shares of common stock and any other shares of common stock underlying awards granted under our equity incentive plans, if any) in such four-quarter period and (B) 8%, and (2) the sum of any incentive fee paid to the Manager with respect to the first three calendar quarters of such previous four quarters; provided, however, that no incentive fee is payable with respect to any calendar quarter unless Core Earnings is greater than zero for the most recently completed 12 calendar quarters.

The incentive fee is payable to the Manager quarterly in arrears in shares of our common stock subject to certain ownership and NYSE limitations. The number of shares to be issued to the Manager is equal to the dollar amount of the portion of the quarterly installment of the incentive fee payable in shares divided by the average of the closing prices of our common stock on the NYSE for the five trading days prior to the date on which such quarterly installment is paid.

**Reimbursement of Expenses**—We are required to reimburse our Manager for expenditures incurred by the Manager on our behalf (except those specifically required to be borne by our Manager under the management agreement), including legal, accounting, financial, due diligence and other services, in amounts which are no greater than those which would be payable to third parties negotiated on an arm's length basis. In addition, pursuant to a secondment agreement with Colony Capital, we are responsible for Colony Capital's expenses incurred in employing Mr. Tangen. As a result, we are responsible for reimbursing Colony Capital for the cost of Mr. Tangen's base salary, bonus to the

extent approved by the compensation committee of our board of directors, benefits and related payroll costs and taxes. We also reimburse Colony Capital for our pro rata portion of overhead expenses incurred by Colony Capital and its affiliates, including our Manager, based upon the ratio of our assets to all Colony Capital-managed assets.

**Off-Balance Sheet Arrangements**

Several of our unconsolidated joint ventures have financing that is not reflected on our balance sheet. For some of the financing arrangements, Company provided customary non-recourse carve-out guaranties. The Company believes that the likelihood of making any payments under the guaranties is remote. See Note 3 to our consolidated financial statements included in this Annual Report and "—Investment-Level Financing" for additional information.

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## Dividends

U.S. federal income tax law generally requires that a REIT distribute annually at least 90% of its REIT taxable income, without regard to the deduction for dividends paid and excluding net capital gains, and that it pay tax at regular corporate rates to the extent that it annually distributes less than 100% of its net taxable income. We intend to pay regular quarterly dividends to our stockholders in an amount equal to our net taxable income, if and to the extent authorized by our board of directors. Before we pay any dividend, whether for U.S. federal income tax purposes or otherwise, we must first meet both our operating requirements and debt service, if any. In addition, our new credit facility limits the amount of distributions as follows: (1) for the year ended December 31, 2013, the greater of (i) 110% of taxable income plus depreciation expense and (ii) 140% of Core Earnings as defined below, and (2) thereafter, 115% of taxable income plus depreciation expense. If our cash available for distribution is less than our net taxable income, we could be required to sell assets or borrow funds to make cash distributions or we may make a portion of the required distribution in the form of a taxable stock distribution or distribution of debt securities.

Common Stock—Our board of directors declared the following dividends in 2013:

Quarter Ended	Dividends Declared per Share	Date Paid
March 31, 2013	\$ 0.35	April 15, 2013
June 30, 2013	0.35	July 15, 2013
September 30, 2013	0.35	October 15, 2013
December 31, 2013	0.35	January 15, 2014

Preferred Stock—We are required to make quarterly cash distributions on the 10,080,000 outstanding shares of our 8.5% Series A Preferred Stock. The aggregate quarterly amount of \$5.4 million, or \$0.53125 per share, is payable on or about the 15th of each January, April, July and October.

## Cash and Cash Flows

As of February 25, 2014, we had approximately \$57 million of cash on hand.

The following table summarizes our cash flow activity for the periods presented:

	Year Ended December 31,		
(In thousands)	2013	2012	2011
Net cash provided by operating activities	\$ 125,289	\$ 70,218	\$ 24,417
Net cash used in investing activities	(1,313,220 )	(425,169 )	(366,433 )
Net cash provided by financing activities	1,060,738	521,278	279,646

## Operating Activities

For the year ended December 31, 2013, cash flows from operating activities increased \$55.1 million, or 78%, compared to 2012. For the year ended December 31, 2012, cash flows from operating activities increased \$45.8 million, or 188%, compared to 2011. The increases reflect the substantial increase in the number of investments in our portfolio. Cash flows from operating activities are primarily distributions of earnings from unconsolidated joint ventures and interest received from our investments in loans, partially offset by payment of operating expenses.

## Investing Activities

Net cash used in investing activities for all periods presented reflect our investing activity. Cash outlays for our contributions to unconsolidated joint ventures and for investments in loans and real estate assets during the periods are partially offset by distributions of capital from unconsolidated joint ventures resulting from principal repayments, loan resolutions and financing activities. Cash provided by investing activities also include principal repayments of loans held for investment. We invested approximately \$1.7 billion, \$641 million and \$387 million, primarily in new investments, during the years ended December 31, 2013, 2012 and 2011.

## Financing Activities

Net cash provided by financing activities for the year ended December 31, 2013 reflects net proceeds of \$475 million from our common stock offerings, \$194 million from issuance of convertible senior notes, \$138.5 million net borrowings on our credit facility, \$169.4 million net borrowings on secured financing, and contributions from noncontrolling interests of \$256.6 million primarily related to National Hotel Portfolio Mezzanine Loan, Freddie Mac Portfolio and Multifamily Portfolio Preferred Equity. These amounts were offset by \$111.3 million payment of

dividends and \$52.7 million distributions to

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noncontrolling interests. Net cash provided by financing activities for the year ended December 31, 2012 reflects net proceeds of \$246.6 million from the two preferred stock offerings, \$371 million from the two common stock offerings and contributions from noncontrolling interests of \$55 million related to Luxury Destination Club Recourse Loans I and II as well as Extended Stay Mezzanine B&C Loans. These amounts were offset by \$57.7 million payment of dividends, net repayments of \$69 million on our credit facility and \$9.2 million on secured financing, and distributions to noncontrolling interests of \$12 million.

### Cash from Investments

Our investments generate cash, either from operations or as a return of our invested capital. We receive monthly or quarterly distributions from some of our unconsolidated joint ventures from earnings, principal receipts or capital transactions such as financing transactions or full or partial loan sales. We also receive interest and principal on our loans held for investment. As loans reach their maturity we may receive all or a portion of the outstanding principal balance. Certain loans held for investment require minimum principal payments, including partial paydowns of principal in the event of a sale of the underlying collateral. We may also, from time to time, fully or partially realize our investments through sale and expect to continue to resolve loans in our loan pools to generate cash, particularly those in acquired credit-distressed portfolios. We may also pursue opportunities to sell whole or partial positions in our originated loan investments or obtain financing (see “—Investment-Level Financing” and “—Leverage Policies”) to generate cash and improve the return on our investments.

For the year ended December 31, 2013, our investments generated \$636 million of cash from various sources as follows:

- Acquired loans—We received approximately \$319.7 million from our acquired single loans and loan portfolios from various sources, such as interest and fees, loan sales and principal receipts including payoffs, and distributed \$38.4 million of this amount to noncontrolling interests. Approximately \$239.6 million of cash received was capital in nature. The major contributors to capital returned were \$162.3 million from investment-level financing on six loan portfolios, \$10.4 million from MF5 CMBS from the partial sale of participation interest, \$9.5 million from the Bulls Loan Portfolio from loan resolutions, and \$21.0 million of principal receipts on the Luxury Destination Club Recourse Loan II.

Originated loans—We received approximately \$239.1 million from our originated loans and distributed \$13.2 million to noncontrolling interests. Approximately \$178.8 million of cash received was capital in nature including \$101 million from the early payoff of four loans and \$71.3 million from loan sales. The remainder of the cash generated from originated loans consists of current interest and required principal payments received.

Single-family residential rentals—We received approximately \$8.5 million from our investments in the single-family residential rentals, which was entirely a return of capital.

Other real estate equity investments—We received approximately \$121.3 million from our other real estate equity investments of which \$87.4 million was from the Midwest NNN Office Campus financing, \$23.8 million was from the sale of 615,932 shares of common stock in First Republic Bank and \$6.2 million from the Multifamily Portfolio Preferred Equity investment. We distributed \$1 million of this amount to noncontrolling interests.

### Credit Facility

On August 6, 2013, we entered into a new credit agreement (the “JPM Credit Agreement”) with JPMorgan Chase Bank, N.A. as administrative agent, and certain lenders, which provides a credit facility in the initial maximum principal amount of \$360 million which may be increased to \$600 million, subject to certain conditions, including each lender or substitute lender agreeing to provide commitments for such increased amount. In November 2013, the maximum principal amount was increased by \$20 million to \$380 million when one of the lenders increased its share of commitments. The maximum principal amount was again increased in January 2014 to \$420 million.

The maximum amount available to borrow under the JPM Credit Agreement at any time is limited by a borrowing base of certain investment assets, with the valuation of such investment assets generally determined according to a percentage of net book value or a multiple of Core Earnings (as further described under “—Non-GAAP Supplemental Financial Measure: Core Earnings”). As of February 27, 2014, the borrowing base valuation was sufficient to permit borrowings of up to the entire \$420 million commitment, of which \$209 million was drawn in anticipation of an investment funding expected to occur shortly.

The JPM Credit Agreement contains covenants and restrictions requiring us to meet certain financial ratios and reporting requirements. At December 31, 2013, we were in compliance with all debt covenants. The following table summarizes the key financial covenants and our actual results as of and for the three months ended December 31, 2013:

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(\$ in thousands)	Covenant Level	Actual Level December 31, 2013
Financial covenant as defined in the Credit Agreement:		
Consolidated Tangible Net Worth	Minimum \$1,352,880	\$1,663,062
Consolidated Fixed Charge Coverage Ratio	Minimum 2.25 to 1.0	4.13 to 1.0
Consolidated Leverage Ratio	Maximum 0.5 to 1.0	0.33 to 1.0
Liquidity	Minimum \$5,000	\$284,423

**Warehouse Facility**

In February 2014, we entered into a master repurchase agreement with a commercial bank to partially finance loans within our Transitional CRE Lending Platform. The repurchase facility provides up to \$150 million of financing for eligible assets within the Transitional CRE Lending Platform and has an initial term of two years, plus a one-year extension option. Advances under the repurchase agreement will bear interest ranging from LIBOR plus a spread of 2.25% to 2.5%, with a maximum loan-to-value ratio on advances of 40% to 60% depending on the type of borrowing.

**Investment-Level Financing**

The structured transactions with the FDIC were consummated in part with leverage provided by the FDIC with zero-coupon financing and terms ranging from two to seven years. As of December 31, 2013, seven of eight FDIC-financed portfolios had fully repaid or defeased the purchase money notes and are making distributions to investors. In February 2014, the last remaining FDIC-financed portfolio fully repaid its purchase money note. The notes are not guaranteed by the managing member entities in which we have ownership interests and are non-recourse to us. In addition to FDIC financing, we have various forms of investment-level financing from commercial banks on several of our investments, including several loan portfolios, Midwest NNN Office Campus, the Hotel Portfolio and CAH OP. The Hotel Portfolio we acquired through foreclosure is subject to an existing mortgage loan.

We may attempt to secure other investment-level financing in the future, if available, including term loans, securitizations, warehouse facilities, repurchase agreements and the issuance of debt and equity securities. We also expect to continue to invest in a number of our assets through co-investments with other investment vehicles managed by affiliates of our Manager and/or other third parties, which may allow us to pool capital to access larger transactions and diversify investment exposure.

**Convertible Notes**

In April 2013, we issued \$200 million of our 5% convertible notes due on April 15, 2023. The net offering proceeds, after deducting underwriting discounts and offering costs payable by us, were approximately \$193.7 million. These convertible notes bear interest at 5% per annum which is payable semiannually in arrears on April 15 and October 15 of each year. The first interest payment was made on October 15, 2013. The holders of the convertible notes may convert their convertible notes into shares of our common stock, at their option, at any time prior to the close of business on the second scheduled trading day immediately preceding the maturity date, subject to certain limitations as described in the indenture, at the applicable conversion rate in effect on the conversion date. The conversion rate is initially set to equal 42.3819 shares of common stock per \$1,000 principal amount of convertible notes (equivalent to a conversion price of approximately \$23.60 per share of common stock), subject to adjustment upon the occurrence of certain events. We may redeem the convertible notes at our option at any time on or after April 22, 2020 if the last reported sale price of our common stock has been at least 130% of the conversion price of the convertible notes then in effect for at least 20 trading days (whether or not consecutive) during any 30 consecutive trading day period ending on, and including, the trading day immediately preceding the date on which we provide notice of redemption, at a redemption price equal to 100% of the principal amount of the convertible notes to be redeemed, plus accrued and unpaid interest to, but excluding, the redemption date. We used the proceeds from the convertible notes offering to acquire our target assets and for working capital and general corporate purposes.

In January 2014, we issued \$230 million of our 3.875% convertible senior notes due on January 15, 2021. The net offering proceeds, after deducting underwriting discounts and offering costs payable by us, were approximately \$223.9 million. These convertible notes bear interest at a rate equal to 3.875% per annum payable semiannually in arrears on January 15 and July 15 of each year, beginning on July 15, 2014. The holders of the convertible notes may

convert their convertible notes into shares of our common stock, at their option, at any time prior to the close of business on the second scheduled trading day immediately preceding the maturity date, subject to certain limitations as described in the indenture, at the applicable conversion rate in effect on the conversion date. The conversion rate is initially set to equal 40.2941 shares of common stock per \$1,000 principal amount of convertible notes (equivalent to a conversion price of approximately \$24.82 per share of common stock), subject to adjustment upon the occurrence of certain events. We may redeem the convertible notes at our



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option at any time on or after January 22, 2019 if the last reported sale price of our common stock has been at least 130% of the conversion price of the convertible notes then in effect for at least 20 trading days (whether or not consecutive) during any 30 consecutive trading day period ending on, and including, the trading day immediately preceding the date on which we provide notice of redemption, at a redemption price equal to 100% of the principal amount of the convertible notes to be redeemed, plus accrued and unpaid interest to, but excluding, the redemption date. We used a portion of the net proceeds to repay amounts outstanding under our secured revolving credit facility, and intend to use the remainder to acquire our target assets and for general corporate purposes.

Equity Offerings

The following table summarizes our common stock offerings for the year ended December 31, 2013:

	Number of Shares	Average Price per Share	Net Proceeds (in thousands) (1)
January 2013	11,500,000	20.20	232,020
November 2013	10,000,000	20.21	201,758
At-the-market sales in 2013	1,901,755	21.65	40,765

(1) Net of underwriting discounts and commissions and offering costs payable by us

We used the net proceeds from the offerings to make additional investments in CAH OP, to repay amounts outstanding under the line of credit at the time of the offering, fund acquisitions of target assets in a manner consistent with our investment strategies and guidelines, and for working capital and general corporate purposes.

We may in the future offer and sell various types of debt and equity securities under our current shelf registration statement filed with the SEC. These securities may be issued from time to time at our discretion based on our needs and depending upon market conditions and available pricing.

Non-GAAP Supplemental Financial Measure: Core Earnings

Core Earnings is a non-GAAP measure and is defined as GAAP net income (loss) excluding non-cash equity compensation expense, incentive fees, real estate depreciation and amortization and any unrealized gains or losses from mark-to-market valuation changes (other than permanent impairment) that are included in net income. The amount is adjusted to exclude one-time events pursuant to changes in GAAP and certain other non-cash items after discussions between the Manager and our independent directors and after approval by a majority of our independent directors.

We believe that Core Earnings is a useful supplemental measure of our operating performance. The exclusion from Core Earnings of the items specified above allows investors and analysts to readily identify the operating results of the assets that form the core of our activity and assists in comparing those operating results between periods. Core Earnings is also the basis upon which the incentive fee to our Manager is calculated. Also, since some of our competitors use a similar supplemental measure, it facilitates comparisons of operating performance to other similar REITs. However, other REITs may use different methodologies to calculate Core Earnings, and accordingly, our calculation of Core Earnings may not be comparable to other similar REITs that present similar supplemental measures.

Core Earnings does not represent cash flow from operations as defined by GAAP, should not be considered as an alternative to net income as defined by GAAP and is not indicative of cash available to fund all cash flow needs. Portions of adjustments to GAAP net income to reconcile to Core Earnings represent our proportionate share of such items incurred by our unconsolidated joint ventures. A reconciliation of our GAAP net income attributable to common stockholders to Core Earnings is presented below:

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(In thousands)	Year Ended December 31,		
	2013	2012	2011
GAAP net income attributable to common stockholders	\$80,345	\$48,096	\$42,260
Adjustments to GAAP net income attributable to common stockholders to reconcile to Core Earnings:			
Noncash equity compensation expense	4,283	6,133	116
Incentive fee	—	936	349
Depreciation expense	12,290	4,478	—
Net unrealized (gain) loss on derivatives	(280	) 119	518
Core Earnings	\$96,638	\$59,762	\$43,243

## ITEM 7A. Quantitative and Qualitative Disclosures About Market Risk

Market risk includes the exposure to loss resulting from changes in interest rates, credit curve spreads, foreign currency exchange rates, commodity prices, equity prices and credit risk in our underlying investments. The primary market risks to which the Company is exposed, either directly or indirectly through its investments in unconsolidated joint ventures, are credit risk, interest rate risk, credit curve spread risk and foreign currency risk.

## Credit Risk

Our joint venture investments and loans receivable are subject to a high degree of credit risk. Credit risk is the exposure to loss from loan defaults. Default rates are subject to a wide variety of factors, including, but not limited to, borrower financial condition, property performance, property management, supply/demand factors, construction trends, consumer behavior, regional economics, interest rates, the strength of the U.S. economy, and other factors beyond our control. All loans are subject to a certain probability of default. We manage credit risk through the underwriting process, acquiring our investments at the appropriate discount to face value, if any, and establishing loss assumptions. We also carefully monitor the performance of the loans, including those held by the joint ventures, as well as external factors that may affect their value. For more information, see “Business—Risk Management.”

## Interest Rate and Credit Curve Spread Risk

Interest rate risk relates to the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Interest rate risk is highly sensitive to many factors, including governmental, monetary and tax policies, domestic and international economic and political considerations and other factors beyond our control. Credit curve spread risk is highly sensitive to the dynamics of the markets for commercial real estate loans and securities we hold. Excessive supply of these assets combined with reduced demand will cause the market to require a higher yield. This demand for higher yield will cause the market to use a higher spread over the U.S. Treasury securities yield curve, or other benchmark interest rates, to value these assets. As U.S. Treasury securities are priced to a higher yield and/or the spread to U.S. Treasuries used to price the assets increases, the price at which we could sell some of our fixed rate financial assets may decline. Conversely, as U.S. Treasury securities are priced to a lower yield and/or the spread to U.S. Treasuries used to price the assets decreases, the value of our fixed rate loans may increase. Fluctuations in LIBOR may affect the amount of interest income we earn on our floating rate loans and interest expense we incur on borrowings indexed to LIBOR, including those under our credit facility and certain investment-level financing.

The interest rate sensitivity table below illustrates the projected impact of changes in interest rates in 1% increments on our net income for twelve months, assuming no changes in our interest-bearing assets and liabilities mix as it stood at December 31, 2013. The maximum decrease in LIBOR is assumed to be 0.17%, the actual rate at December 31, 2013.

(Amounts in thousands)	+2.00%	+1.00%	-0.17%
Affected Line Item in the Consolidated Statement of Operations			
Equity in income of unconsolidated joint ventures	\$(3,344	) \$(1,672	) \$416
Interest income	9,132	4,566	(763
Interest expense	(5,070	) (2,535	) 424
Net income	718	359	77

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Net income attributable to noncontrolling interests	2,710	1,354	(226	)
Net income attributable to Colony Financial, Inc.	\$(1,992	) \$(995	) \$303	

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We utilize a variety of financial instruments on some of our investments, including interest rate swaps, caps, floors and other interest rate exchange contracts, in order to limit the effects of fluctuations in interest rates on our operations. The use of these types of derivatives to hedge interest-earning assets and/or interest-bearing liabilities carries certain risks, including the risk that losses on a hedge position will reduce the funds available for distribution and that such losses may exceed the amount invested in such instruments. A hedge may not perform its intended purpose of offsetting losses of rising interest rates. Moreover, with respect to certain of the instruments used as hedges, we are exposed to the risk that the counterparties with which we trade may cease making markets and quoting prices in such instruments, which may render us unable to enter into an offsetting transaction with respect to an open position. If we anticipate that the income from any such hedging transaction will not be qualifying income for REIT income purposes, we may conduct all or part of our hedging activities through a to-be-formed corporate subsidiary that is fully subject to federal corporate income taxation. Our profitability may be adversely affected during any period as a result of changing interest rates.

### Currency Risk

We have foreign currency rate exposures related to our Euro-denominated investments. Changes in currency rates can adversely affect the fair values and earnings of our non-U.S. holdings. As of December 31, 2013, we had approximately €166.2 million, or \$228.4 million, in European investments. A 1% change in the exchange rate would result in a \$2.3 million increase or decrease in translation gain or loss on our investments in unconsolidated joint ventures and loan investments. We mitigate this risk by utilizing currency instruments to hedge the capital portion of our foreign currency risk. The types of hedging instrument that we employed on our European investments were forwards and costless collars (buying a protective put while writing an out-of-the-money covered call with a strike price at which the premium received is equal to the premium of the protective put purchased) which involved no initial capital outlay. The puts were structured with strike prices approximately 10% lower than our cost basis in such investments, thereby limiting any Euro related foreign exchange related fluctuations to approximately 10% of the original capital invested in the deal. At December 31, 2013, net tax-effected accumulated foreign exchange loss on the European investments was approximately \$1.3 million, net of effect of hedging.

At December 31, 2013, the total notional amount of the collars was approximately €75.5 million, with termination dates ranging from July 2014 to December 2017, and the total notional amount of forward exchange contracts was €50 million, with a termination date of June 2014. The maturity dates of such instruments approximate the projected dates of related cash flows for specific investments. Termination or maturity of currency hedging instruments may result in an obligation for payment to or from the counterparty to the hedging agreement. We are exposed to credit loss in the event of non-performance by counterparties for these contracts. To manage this risk, we select major international banks and financial institutions as counterparties and perform a quarterly review of the financial health and stability of our trading counterparties. Based on our review as of December 31, 2013, we do not expect any counterparty to default on its obligations.

### Inflation

Virtually all of our assets and liabilities are interest rate sensitive in nature. As a result, interest rates and other factors influence 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.

### ITEM 8. Financial Statements and Supplementary Data

The financial statements and the supplementary financial data required by this item appear in Item 15: Exhibits and Financial Statement Schedules.

### ITEM 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

ITEM 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) of the Exchange Act) that are designed to ensure that information required to be disclosed in our reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time period specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding disclosure. In designing and evaluating the disclosure controls

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and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives.

As required by Rule 13a-15(b) of the Exchange Act, we have evaluated, under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer, the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Annual Report. Based upon our evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective at December 31, 2013.

### Changes in Internal Control over Financial Reporting

There have been no changes in our internal control over financial reporting (as defined in Rule 13a-15(f) and 15d-15(f) of the Exchange Act) during the fourth quarter ended December 31, 2013 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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

Management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in 13a-15(f) and 15d-15(f) of the Exchange Act). Our internal control over financial reporting includes policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of our assets; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP, and that receipts and expenditures are being made only in accordance with authorizations of our management and directors; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of assets that could have a material effect on our financial statements.

Under the supervision and with the participation of our management, we evaluated the effectiveness of our internal control over financial reporting using the criteria set forth in the Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in 1992. Based on our evaluation, our management concluded that our internal control over financial reporting was effective as of December 31, 2013.

Our internal control system was designed to provide reasonable assurance to management and our board of directors regarding the preparation and fair presentation of published financial statements. All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

Ernst & Young LLP, our independent registered accounting firm, has audited our financial statements included in this Annual Report and has issued an attestation report on the effectiveness of our internal control over financial reporting, which is included herein.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders of  
Colony Financial, Inc.

We have audited Colony Financial, Inc.'s (the "Company") internal control over financial reporting as of December 31, 2013, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (1992 framework) (the COSO criteria). Colony Financial, Inc.'s management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Annual Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed 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. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Colony Financial, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2013, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Colony Financial, Inc. as of December 31, 2013 and 2012, and the related consolidated statements of operations, comprehensive income, equity and cash flows for each of the three years in the period ended December 31, 2013, and our report dated February 27, 2014 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Los Angeles, California  
February 27, 2014

ITEM 9B. Other Information

None.





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PART III

ITEM 10. Directors, Executive Officers and Corporate Governance.

The information required by Item 10 is hereby incorporated by reference to the definitive proxy statement to be filed with the SEC pursuant to Regulation 14A within 120 days after December 31, 2013.

ITEM 11. Executive Compensation.

The information required by Item 11 is hereby incorporated by reference to the definitive proxy statement to be filed with the SEC pursuant to Regulation 14A within 120 days after December 31, 2013.

ITEM 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

The information required by Item 12 is hereby incorporated by reference to the definitive proxy statement to be filed with the SEC pursuant to Regulation 14A within 120 days after December 31, 2013.

ITEM 13. Certain Relationships and Related Transactions, and Director Independence.

The information required by Item 13 is hereby incorporated by reference to the definitive proxy statement to be filed with the SEC pursuant to Regulation 14A within 120 days after December 31, 2013.

ITEM 14. Principal Accountant Fees and Services.

The information required by Item 14 is hereby incorporated by reference to the definitive proxy statement to be filed with the SEC pursuant to Regulation 14A within 120 days after December 31, 2013.

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PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) and (c) Financial Statements and Schedules

Financial Statements of Colony Financial, Inc.

Report of Independent Registered Public Accounting Firm F-2

Consolidated Balance Sheets as of December 31, 2013 and 2012 F-3

Consolidated Statements of Operations for the Years Ended December 31, 2013, 2012 and 2011 F-4

Consolidated Statements of Comprehensive Income for the Years Ended December 31, 2013, 2012 and 2011 F-5

Consolidated Statements of Equity for the Years Ended December 31, 2013, 2012 and 2011 F-6

Consolidated Statements of Cash Flows for the Years Ended December 31, 2013, 2012 and 2011 F-7

Notes to Consolidated Financial Statements F-9

Schedule IV—Mortgage Loans on Real Estate as of December 31, 2013 F-40

All other schedules are omitted because they are not applicable, or the required information is included in the consolidated financial statements or notes thereto.

(b) Exhibits

The Exhibit Index attached hereto is incorporated by reference under this item.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders of  
Colony Financial, Inc.

We have audited the accompanying consolidated balance sheets of Colony Financial, Inc. (the Company) as of December 31, 2013 and 2012, and the related consolidated statements of operations, comprehensive income, equity, and cash flows for each the three years in the period ended December 31, 2013. Our audits also included the financial statement schedule listed in the Index at Item 15. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Colony Financial, Inc. at December 31, 2013 and 2012, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2013, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Colony Financial, Inc.'s internal control over financial reporting as of December 31, 2013, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (1992 framework) and our report dated February 27, 2014 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Los Angeles, California  
February 27, 2014

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## COLONY FINANCIAL, INC.

## CONSOLIDATED BALANCE SHEETS

(In thousands, except share and per share data)

	December 31,	
	2013	2012
<b>ASSETS</b>		
Cash	\$43,167	\$170,199
Investments in unconsolidated joint ventures	1,369,529	877,081
Loans held for investment, net	1,028,654	333,569
Real estate assets, net	112,468	—
Beneficial interests in debt securities, available-for-sale, at fair value	30,834	32,055
Other assets	43,900	22,663
Total assets	\$2,628,552	\$1,435,567
<b>LIABILITIES AND EQUITY</b>		
Liabilities:		
Line of credit	\$138,500	\$—
Secured financing	277,607	108,167
Accrued and other liabilities	18,105	12,944
Due to affiliates	7,986	4,984
Dividends payable	32,127	26,442
Convertible senior notes	200,000	—
Total liabilities	674,325	152,537
Commitments and contingencies (Note 17)		
Equity:		
Stockholders' equity:		
Preferred stock, \$0.01 par value, 8.5% Series A Cumulative Redeemable Perpetual, liquidation preference of \$25 per share, 50,000,000 shares authorized, 10,080,000 shares issued and outstanding	101	101
Common stock, \$0.01 par value, 450,000,000 shares authorized, 76,492,225 and 53,091,623 shares issued and outstanding, respectively	765	531
Additional paid-in capital	1,701,274	1,222,682
Distributions in excess of earnings	(20,423)	(5,167)
Accumulated other comprehensive income	2,593	5,184
Total stockholders' equity	1,684,310	1,223,331
Noncontrolling interests	269,917	59,699
Total equity	1,954,227	1,283,030
Total liabilities and equity	\$2,628,552	\$1,435,567

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

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## COLONY FINANCIAL, INC.

## CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except share and per share data)

	Year Ended December 31,		
	2013	2012	2011
Income			
Equity in income of unconsolidated joint ventures	\$ 100,708	\$68,737	\$46,720
Interest income	77,475	36,445	16,775
Rental income and tenant reimbursements	789	—	—
Other income from affiliates	1,267	1,973	1,974
Total income	180,239	107,155	65,469
Expenses			
Management fees (including \$3,998, \$5,714 and \$0 of share-based compensation, respectively)	26,263	18,982	8,477
Investment and servicing expenses (including \$1,771, \$1,657 and \$1,719 reimbursable to affiliates, respectively)	3,228	2,977	2,793
Interest expense	18,838	8,248	3,011
Property operating expenses	197	—	—
Administrative expenses (including \$3,073, \$2,460 and \$1,592 reimbursable to affiliates, respectively)	7,548	6,346	5,780
Depreciation and amortization	310	—	—
Transaction costs	1,807	—	—
Total expenses	58,191	36,553	20,061
Realized gain on resolution of loans receivable	4,578	808	—
Other loss, net	(44	) (1,040	) (853
Income before income taxes	126,582	70,370	44,555
Income tax provision	659	2,165	1,191
Net income	125,923	68,205	43,364
Net income attributable to noncontrolling interests	24,158	6,194	1,104
Net income attributable to Colony Financial, Inc.	101,765	62,011	42,260
Preferred dividends	21,420	13,915	—
Net income attributable to common stockholders	\$80,345	\$48,096	\$42,260
Net income per common share:			
Basic	\$ 1.20	\$ 1.33	\$ 1.47
Diluted	\$ 1.20	\$ 1.32	\$ 1.46
Weighted average number of common shares outstanding:			
Basic	66,181,700	35,925,600	28,732,200
Diluted	66,181,700	35,943,200	28,993,700

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

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## COLONY FINANCIAL, INC.

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands)

	Year Ended December 31,		
	2013	2012	2011
Net income	\$125,923	\$68,205	\$43,364
Other comprehensive income (loss), net of tax:			
Equity in other comprehensive (loss) income of unconsolidated joint ventures, net	(3,107	) 7,144	(1,853 )
Unrealized (loss) gain on beneficial interests in debt securities	(554	) 267	614
Net change in fair value of cash flow hedge	(27	) —	—
Foreign currency translation adjustments:			
Foreign currency translation adjustment gain (loss)	5,599	1,261	(3,253 )
Change in fair value of net investment hedges	(3,828	) (1,149	) 1,192
Net foreign currency translation adjustments	1,771	112	(2,061 )
Other comprehensive (loss) income	(1,917	) 7,523	(3,300 )
Comprehensive income	124,006	75,728	40,064
Comprehensive income attributable to noncontrolling interests	24,832	6,203	1,070
Comprehensive income attributable to stockholders	\$99,174	\$69,525	\$38,994

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

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COLONY FINANCIAL, INC.  
CONSOLIDATED STATEMENTS OF EQUITY  
(In thousands, except share and per share data)

	Preferred Stock		Common Stock		Additional	Retained	Accumulated	Total		Noncontrolling	Total Equity
	Shares	Amount	Shares	Amount	Paid-in Capital	(Distribution of) Earnings	Other Comprehensive Income (Loss)	Stockholders' Equity		Interests	
Balance at December 31, 2010	—	\$—	17,384,000	\$174	\$330,777	\$1,152	\$936	\$333,039	\$240		\$333,279
Net income	—	—	—	—	—	42,260	—	42,260	1,104		43,364
Other comprehensive loss	—	—	—	—	—	—	(3,266 )	(3,266 )	(34 )		(3,300 )
Common stock offering	—	—	15,350,000	153	283,822	—	—	283,975	—		283,975
Underwriting and offering costs	—	—	—	—	(12,268 )	—	—	(12,268 )	—		(12,268 )
Issuance of common stock in connection with:											
Anti-dilution purchase price adjustment	—	—	175,000	2	(164 )	—	—	(162 )	—		(162 )
Reimbursement of deferred underwriting discounts and commissions to Manager	—	—	287,500	3	5,747	—	—	5,750	—		5,750
Payment of incentive fees	—	—	5,989	—	88	—	—	88	—		88
Common stock repurchases	—	—	(580,600 )	(6 )	(8,648 )	—	—	(8,654 )	—		(8,654 )
Share-based payments	—	—	3,000	—	116	—	—	116	—		116
Contributions from noncontrolling interests	—	—	—	—	—	—	—	—	10,140		10,140
Distributions to noncontrolling interests	—	—	—	—	—	—	—	—	(936 )		(936 )
Common stock dividends declared (\$1.31)	—	—	—	—	—	(37,902 )	—	(37,902 )	—		(37,902 )

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per share)										
Balance at										
December 31, 2011	—	—	32,624,889	326	599,470	5,510	(2,330 )	602,976	10,514	613,490
Net income	—	—	—	—	—	62,011	—	62,011	6,194	68,205
Other comprehensive income	—	—	—	—	—	—	7,514	7,514	9	7,523
Issuance of 8.5% Series A Cumulative Redeemable Perpetual Preferred Stock	10,080,000	101	—	—	254,477	—	—	254,578	—	254,578
Common stock offering	—	—	19,550,000	196	370,806	—	—	371,002	—	371,002
Underwriting and offering costs	—	—	—	—	(9,392 )	—	—	(9,392 )	—	(9,392 )
Issuance of common stock for incentive fees	—	—	65,703	1	1,196	—	—	1,197	—	1,197
Share-based payments	—	—	851,031	8	6,125	—	—	6,133	—	6,133
Contributions from noncontrolling interests	—	—	—	—	—	—	—	—	54,963	54,963
Distributions to noncontrolling interests	—	—	—	—	—	—	—	—	(11,981 )	(11,981 )
Preferred stock dividends	—	—	—	—	—	(14,328 )	—	(14,328 )	—	(14,328 )
Common stock dividends declared (\$1.44 per share)	—	—	—	—	—	(58,360 )	—	(58,360 )	—	(58,360 )
Balance at										
December 31, 2012	10,080,000	101	53,091,623	531	1,222,682	(5,167 )	5,184	1,223,331	59,699	1,283,030
Net income	—	—	—	—	—	101,765	—	101,765	24,158	125,923
Other comprehensive (loss) income	—	—	—	—	—	—	(2,591 )	(2,591 )	674	(1,917 )
Common stock offerings	—	—	23,401,755	234	475,368	—	—	475,602	—	475,602
Underwriting and offering costs	—	—	—	—	(1,059 )	—	—	(1,059 )	—	(1,059 )
	—	—	(1,153 )	—	4,283	—	—	4,283	—	4,283



Share-based payments										
Contributions from noncontrolling interests	—	—	—	—	—	—	—	—	256,589	256,589
Distributions to noncontrolling interests	—	—	—	—	—	—	—	—	(71,203 )	(71,203 )
Preferred stock dividends	—	—	—	—	—	(21,420 )	—	(21,420 )	—	(21,420 )
Common stock dividends declared (\$1.40 per share)	—	—	—	—	—	(95,601 )	—	(95,601 )	—	(95,601 )
Balance at December 31, 2013	10,080,000	\$101	76,492,225	\$765	\$1,701,274	\$(20,423)	\$2,593	\$1,684,310	\$269,917	\$1,954,227

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

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COLONY FINANCIAL, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(In thousands)

	Year Ended December 31,		
	2013	2012	2011
Cash Flows from Operating Activities			
Net income	\$ 125,923	\$ 68,205	\$ 43,364
Adjustments to reconcile net income to net cash provided by operating activities:			
Amortization of discount and net origination fees on purchased and originated loans	(9,509)	(3,656)	(1,332)
Paid-in-kind interest added to loan principal	(218)	(851)	(608)
Amortization of deferred financing costs	3,017	2,152	1,109
Equity in income of unconsolidated joint ventures	(100,708)	(68,737)	(46,720)
Distributions of income from unconsolidated joint ventures	101,874	64,839	25,959
Depreciation and amortization	310	—	—
Share-based payments	4,283	7,330	204
Realized gain on resolution of loans receivable	(4,578)	(808)	—
Changes in operating assets and liabilities:			
Increase in other assets	(6,917)	(2,914)	(1,802)
Increase in accrued and other liabilities	8,049	2,148	1,759
Increase in due to affiliates	3,002	1,196	1,574
Other adjustments, net	761	1,314	910
Net cash provided by operating activities	125,289	70,218	24,417
Cash Flows from Investing Activities			
Contributions to unconsolidated joint ventures	(672,338)	(528,347)	(199,340)
Distributions from unconsolidated joint ventures	177,287	136,496	20,394
Investments in purchased loans receivable, net of seller financing	(340,563)	(56,427)	(53,507)
Repayments of principal on loans receivable	109,643	48,892	—
Net disbursements on originated loans	(535,940)	(56,000)	(105,804)
Proceeds from sales of loans receivable	71,298	30,159	—
Acquisition of real estate assets, net	(122,750)	—	—
Acquisition of beneficial interests in debt securities	—	—	(28,000)
Other investing activities, net	143	58	(176)
Net cash used in investing activities	(1,313,220)	(425,169)	(366,433)
Cash Flows from Financing Activities			
Proceeds from issuance of preferred stock, net	—	246,559	—
Proceeds from issuance of common stock, net	475,190	371,002	272,261
Dividends paid to preferred stockholders	(21,420)	(9,326)	—
Dividends paid to common stockholders	(89,916)	(48,367)	(32,894)
Common stock repurchases	—	—	(8,654)
Line of credit borrowings	514,000	133,500	73,000
Line of credit repayments	(375,500)	(202,500)	(24,000)
Proceeds from secured financing	203,000	—	—
Secured financing repayments	(33,560)	(9,202)	(155)
Net proceeds from issuance of convertible senior notes	194,000	—	—
Payment of deferred financing costs	(6,011)	(1,772)	(2,204)
Payment of offering costs	(944)	(922)	(554)
Payment of deferred underwriting discounts and commissions	—	—	(5,750)

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Contributions from noncontrolling interests	256,589	54,963	10,140
Distributions to noncontrolling interests	(52,703 )	(11,981 )	(936 )
Other financing activities, net	(1,987 )	(676 )	(608 )
Net cash provided by financing activities	1,060,738	521,278	279,646
Effect of exchange rates on cash	161	—	(3 )
Net (decrease) increase in cash	(127,032 )	166,327	(62,373 )
Cash, beginning of period	170,199	3,872	66,245
Cash, end of period	\$43,167	\$170,199	\$3,872

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## COLONY FINANCIAL, INC.

## CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)

(In thousands)

	Year Ended December 31,		
	2013	2012	2011
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:			
Cash paid for interest	\$13,558	\$5,667	\$1,568
Cash paid for income taxes	\$2,294	\$4,930	\$337
SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING AND FINANCING ACTIVITIES:			
Dividends payable	\$32,127	\$26,442	\$11,092
Offering costs included in accrued and other liabilities	\$—	\$297	\$—
Deferred financing costs deducted from convertible debt issuance proceeds	\$6,000	\$—	\$—
Noncash distribution of loan receivable to a noncontrolling interest	\$18,500	\$—	\$—
Proceeds from settlement of a derivative instrument in other assets	\$1,736	\$—	\$—
Seller-provided secured financing on purchased loan	\$—	\$103,524	\$—
Interest reserve for seller financing funded by borrower of purchased loan (Note 9)	\$—	\$9,984	\$—
Assignment of loans receivable and related liabilities to investment in unconsolidated joint ventures	\$—	\$29,427	\$—
Derivative liability assumed for beneficial interests in securities	\$—	\$—	\$4,122
Investments in loans receivable in accrued and other liabilities	\$—	\$—	\$1,669
Deferred payment on investment in unconsolidated joint venture	\$—	\$—	\$150

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

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COLONY FINANCIAL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2013

1. Organization

Colony Financial, Inc. (the “Company”) was organized on June 23, 2009 as a Maryland corporation. The Company acquires, originates and manages a diversified portfolio of real estate-related debt and equity investments primarily composed of acquired and originated loans and real estate equity, including interests in single-family residential rental properties through its investment in CAH Operating Partnership, L.P. (“CAH OP”). The Company is externally managed and advised by Colony Financial Manager, LLC (the “Manager”), a wholly-owned subsidiary of Colony Capital, LLC (“Colony Capital”), a privately held global real estate investment firm. The Company elected to be taxed as a real estate investment trust (“REIT”) under the Internal Revenue Code commencing with its first taxable year ended December 31, 2009.

2. Significant Accounting Policies

The significant accounting policies of the Company are described below. The accounting policies of the Company's unconsolidated joint ventures are substantially similar to those of the Company.

Principles of Consolidation and Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”). The accompanying consolidated financial statements include the accounts of the Company and its majority-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated. The portions of the equity, net income and other comprehensive income of consolidated subsidiaries that are not attributable to the parent are presented separately as amounts attributable to noncontrolling interests in the consolidated financial statements. A substantial portion of noncontrolling interests represent interests held by private investment funds or other investment vehicles managed by Colony Capital or its affiliates (“Co-Investment Funds”).

The Company consolidates entities in which it retains a controlling financial interest or entities that meet the definition of a variable interest entity (“VIE”) for which the Company is deemed to be the primary beneficiary. In performing its analysis of whether it is the primary beneficiary, at initial investment and at each quarterly reporting period, the Company considers whether it individually has the power to direct the activities of the VIE that most significantly affect the entity’s performance and also has the obligation to absorb losses or the right to receive benefits of the VIE that could potentially be significant to the VIE. The Company also considers whether it is a member of a related party group that collectively meets the power and benefits criteria and, if so, whether the Company is most closely associated with the VIE. In making that determination, the Company considers both qualitative and quantitative factors, including, but not limited to: the amount and characteristics of its investment relative to other investors; the obligation or likelihood for the Company or other investors to fund operating losses of the VIE; the Company’s and the other investors’ ability to control or significantly influence key decisions for the VIE, and the similarity and significance of the VIE’s business activities to those of the Company and the other investors. The determination of whether an entity is a VIE, and whether the Company is the primary beneficiary, involves significant judgments, including the determination of which activities most significantly affect the entities’ performance, estimates about the current and future fair values and performance of assets held by the VIE and/or general market conditions.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents

For purposes of reporting cash flows, the Company considers short-term, highly liquid investments with original maturities of three months or less to be cash equivalents. The Company did not have any cash equivalents at December 31, 2013 and 2012. The Company maintains its cash accounts in a number of commercial banks. At various

times during the year, the Company had deposits in excess of federally insured limits.

**Investments in Unconsolidated Joint Ventures**

The Company holds ownership interests in certain joint ventures. The Company evaluates its interest in these entities to determine whether they meet the definition of a VIE and whether the Company should consolidate these entities. In each case,

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the Company has determined that (1) the entity is not a VIE and the Company does not have a controlling financial interest, or (2) the entity is a VIE but the Company is not the primary beneficiary. Since the Company may not consolidate these entities but has significant influence over operating and financial policies, it accounts for its investments in joint ventures using the equity method. Under the equity method, the Company initially records its investments at cost and adjusts for the Company's proportionate share of net earnings or losses and other comprehensive income or loss, cash contributions made and distributions received, and other adjustments, as appropriate. Distributions of operating profit from the joint ventures are reported as part of operating cash flows. Distributions related to a capital transaction, such as a refinancing transaction or sale, are reported as investing activities.

The Company performs a quarterly evaluation of its investments in unconsolidated joint ventures to determine whether the fair value of each investment is less than the carrying value, and, if such decrease in value is deemed to be other-than-temporary, writes down the investment to fair value.

### Loans Receivable

The Company originates and purchases loans receivable. Originated loans are recorded at amortized cost, or the outstanding unpaid principal balance ("UPB") less net deferred loan fees. Net deferred loan fees include unamortized origination and other fees charged to the borrower less direct incremental loan origination costs incurred by the Company. Purchased loans are recorded at amortized cost, or the UPB less unamortized purchase discount. Costs to purchase loans are expensed as incurred. Interest income is recognized based upon the contractual rate and the outstanding principal balance of the loans. Purchase discount or net deferred loan fees are amortized over the expected life of the loans using the effective yield method except on revolving loans, for which the straight-line method is used. When a loan is prepaid, prepayment fees and any excess of proceeds over the carrying amount of the loan are recognized as a gain. Loans that the Company has the intent and ability to hold for the foreseeable future are classified as held-for-investment.

**Loans Held for Sale**—Loans held for sale are loans that the Company intends to sell or liquidate in the foreseeable future and are carried at the lower of amortized cost or fair value.

**Past Due Loans**—The Company places loans on nonaccrual status when any portion of principal or interest is more than 90 days past due, or earlier when concern exists as to the ultimate collection of principal or interest. When a loan is placed on nonaccrual status, the Company reverses the accrual for unpaid interest and does not recognize interest income until the cash is received and the loan returns to accrual status. Generally, a loan may be returned to accrual status when all delinquent principal and interest are brought current in accordance with the terms of the loan agreement and the borrower has met certain performance criteria.

**Impairment and Allowance for Loan Losses**—The Company regularly analyzes the extent and effect of any credit migration from underwriting and the initial investment review associated with a loan's performance and/or value of underlying collateral as well as the financial and operating capability of the borrower/sponsor. Specifically, a property's operating results and any cash reserves are analyzed and used to assess (i) whether cash from operations are sufficient to cover the debt service requirements currently and into the future, (ii) the ability of the borrower to refinance the loan, and/or (iii) the property's liquidation value. Where applicable, the Company also evaluates the financial wherewithal of any loan guarantors as well as the borrower's competency in managing and operating the properties. Such analysis is performed at least quarterly, or more often as needed when impairment indicators are present. The Company does not utilize a statistical credit rating system to monitor and assess the credit risk and investment quality of its acquired or originated loans. Given the diversity of the Company's portfolio, management believes there is no consistent method of assigning a numerical rating to a particular loan that captures all of the various credit metrics and their relative importance. Therefore, the Company evaluates impairment and allowance for loan loss on an individual loan basis.

A loan is considered to be impaired when it is probable that the Company will not be able to collect all amounts due according to the contractual terms of the loan agreement. A loan is also considered to be impaired if it has been restructured in a troubled debt restructuring ("TDR") involving a modification of terms as a concession resulting from the debtor's financial difficulties. The Company measures impairment based on the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's observable market price, or the fair value of the

collateral if the loan is collateral dependent. If the loan valuation is less than the recorded investment in the loan, a valuation allowance is established with a corresponding charge to allowance for loan loss.

**Purchased Credit-Impaired ("PCI") Loans**—PCI loans are acquired loans with evidence of credit quality deterioration since origination for which it is probable at acquisition that the Company will collect less than the contractually required payments. PCI loans are recorded at the initial investment in the loans and accreted to the estimated cash flows expected to be collected measured at acquisition date. The excess of cash flows expected to be collected measured at acquisition date over the initial investment ("accretable yield") is recognized in interest income over the remaining life of the loan using the effective interest method. The excess of contractually required payments at the acquisition date over expected cash flows

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(“nonaccretable difference”) is not recognized as an adjustment of yield, loss accrual or valuation allowance. The Company evaluates estimated future cash flows on a quarterly basis, starting with the first full quarter after acquisition, or earlier if conditions indicating impairment are present. Subsequent increases in cash flows expected to be collected are recognized prospectively through an adjustment to the loan’s accretable yield over its remaining life, which may result in a reclassification from nonaccretable difference to accretable yield. Subsequent decreases in cash flows expected to be collected are evaluated to determine whether a provision for loan loss should be established. If decreases in expected cash flows result in a decrease in the estimated fair value of the loan below its amortized cost, the Company will record a provision for loan losses calculated as the difference between the loan’s amortized cost and the revised cash flows, discounted at the loan’s effective yield.

PCI loans may be aggregated into pools based upon common risk characteristics, such as loan performance, collateral type and/or geographic location of the collateral. Once a loan pool is identified, a composite yield and estimate of cash flows expected to be collected (including expected prepayments) are used to recognize interest income. A loan resolution within a loan pool, which may involve the sale of the loan or foreclosure on the underlying collateral, results in the removal of an allocated carrying amount. A loan modified within a loan pool remains in the loan pool, with the effect of the modification incorporated into the expected future cash flows.

### Investments in Debt and Equity Securities

The Company designates debt and equity securities as held-to-maturity, available-for-sale, or trading depending upon its intent at the time of acquisition. The Company’s beneficial interests in debt securities are designated as available-for-sale and are presented at fair value. Unrealized gains or losses are included as a component of other comprehensive income or loss. Premiums or discounts on acquired debt securities are amortized or accreted into income using the effective interest method over the expected lives of the individual securities. The Company performs a quarterly assessment of its debt and equity securities to determine whether a decline in fair value below amortized cost is other than temporary. Other-than-temporary impairment exists when it is probable that the Company will be unable to recover the entire amortized cost basis of the security. If the decline in fair value is deemed to be other than temporary, the security is written down to fair value which becomes the new cost basis and an impairment loss is recognized.

### Investment in Real Estate

**Real Estate Acquisitions**—Real estate acquisitions are recorded at the fair values of the acquired components at the time of acquisition, allocated among land, building, improvements, equipment, lease-related tangible and identifiable intangible assets, such as tenant improvements, deferred leasing costs, in-place lease values, above- and below-market lease values. The Company evaluates each purchase transaction to determine whether the acquired assets meet the definition of a business. Transaction costs related to acquisitions that are not deemed to be businesses are included in the cost basis of the acquired assets, while transaction costs related to acquisitions that are deemed to be businesses are expensed as incurred. Net cash paid to acquire an operating property is classified as investing activities on the accompanying statements of cash flows.

The fair value of acquired land is derived from recent comparable sales of land and listings within the same local region based on available market data. The fair value of acquired buildings and building improvements is derived from comparable sales, discounted cash flow analysis using market-based assumptions, or replacement cost, as appropriate. The fair value of site and tenant improvements is estimated based upon current market replacement costs and other relevant market rate information.

In-place leases generate value over and above the tangible real estate because a property that is occupied with leased space is typically worth more than a vacant building without an operating lease contract in place. The fair value of acquired in-place leases is derived based on management’s assessment of lost rental income and tenant reimbursements that would be incurred to lease a hypothetically vacant building to its actual existing occupancy level on the valuation date. The net amount recorded for acquired in-place leases is included in other assets on the accompanying balance sheets and amortized on a straight-line basis as an increase to depreciation and amortization expense over the remaining term of the applicable leases.

The fair value of the above- or below-market component of an acquired in-place operating lease represents the present value of the difference between contractual rents of acquired leases and market rents at the time of the acquisition,

discounted for tenant credit risks. Above- or below-market lease values are amortized on a straight-line basis as a decrease or increase to rental income, respectively, over the applicable lease terms. The Company did not have any above- or below-market lease values at December 31, 2013 or 2012.

Deferred leasing costs represent management's estimation of the avoided leasing commissions and legal fees associated with an existing in-place lease. The net amount is included in other assets on the accompanying balance sheets and amortized on a straight-line basis as an increase to depreciation and amortization expense over the remaining term of the applicable lease.

Fair values of these components generally rely on Level 2 or Level 3 inputs of the fair value hierarchy (see —Fair Value Measurement).

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**Depreciation**—Depreciation is computed on the straight-line basis over the estimated useful lives of the assets, which generally range from 10 to 40 years for buildings and improvements and 5 to 15 years for furniture, fixtures and equipment. Tenant improvements are amortized over the shorter of the remaining lease term or the estimated useful life.

Expenditures for ordinary repairs and maintenance are expensed as incurred, while expenditures for significant renovations that improve or extend the useful life of the asset are capitalized and depreciated over their estimated useful lives.

**Real Estate Acquired in Settlement of Loans**—Real estate acquired in full or partial settlement of loans ("real estate owned," or "REO") is measured at fair value less estimated costs to sell at the acquisition date if the property meets the GAAP definition of a held for sale property. REO property that is classified as held for sale is not depreciated during the holding period. If the Company intends to operate the property, the fair value is allocated among the acquired assets (see —Real Estate Acquisitions). The difference between the carrying value of the loan and the fair value of the foreclosed asset is recognized in the statement of operations, after reversing any previously recognized provision on the loan. The fair value of REO is generally based on a third party appraisal or on a combination of appraised value, broker price opinions and comparable sales.

**Real Estate Impairment**—The Company evaluates its investments in real estate for impairment periodically or whenever events or changes in circumstances indicate that the carrying amounts may not be recoverable. The Company evaluates cash flows and determines impairments on an individual property basis. In making this determination, the Company reviews, among other things, current and estimated future cash flows associated with each property, market information for each sub-market, including, where applicable, competition levels, foreclosure levels, leasing trends, occupancy trends, lease or room rates, and the market prices of similar properties recently sold or currently being offered for sale, and other quantitative and qualitative factors. If an impairment indicator exists, the Company compares the expected future undiscounted cash flows to the carrying amount of the asset to evaluate whether the carrying value is recoverable. If the sum of the estimated undiscounted cash flows is less than the carrying amount of the asset, the Company would record an impairment loss for the difference between the estimated fair value and the carrying amount of the asset.

### **Other Assets**

Other assets include the fair value of derivative instruments, deferred financing costs, acquired intangible assets, restricted cash, deferred tax assets, interest receivable and prepaid expenses.

**Deferred Financing Costs**—Costs incurred in connection with the Company's financing arrangements are recorded as deferred financing costs and included in other assets on the accompanying balance sheets. Deferred financing costs associated with the credit facility are amortized using the straight-line method over the expected term of the credit facility. Deferred financing costs associated with convertible senior notes, secured financing and mortgage loans are amortized using the effective interest method over the respective term of the financing.

**Restricted Cash**—Restricted cash primarily includes escrow deposits from borrowers for various purposes, including property taxes, insurance, replacement reserves and interest reserves, with a corresponding liability included in accrued and other liabilities.

**Acquired Intangible Assets**—Intangible assets consist of acquired in-place leases and deferred leasing costs associated with acquiring an operating property with existing leases. In-place leases and deferred leasing costs are recorded at their respective fair value as of the acquisition date, net of straight-line amortization over the applicable lease terms.

### **Transfers of Financial Assets**

Transfers of financial assets are accounted for as sales when control over the assets has been surrendered. Control over a transferred financial asset is deemed to be surrendered when (1) the asset has been legally isolated; (2) the transferee has the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred asset; and (3) the Company does not maintain effective control over the transferred asset through either (a) an agreement that entitles and obligates the Company to repurchase or redeem it before its maturity or (b) an agreement that provides the Company with both the unilateral ability to cause the holder to return specific assets and a more than trivial benefit attributable to that ability. The difference between the net proceeds received and the carrying amount of the financial assets being sold is recognized as a gain or loss on sale. Transfers of financial assets that do

not meet these requirements are accounted for as financing transactions.

Debt

The Company's debt balance includes a mortgage loan, loan-on-loan secured financing arrangements and transfers of financial assets that are accounted for as financing transactions as they did not meet the criteria for treatment as sales.

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### Rental Income and Tenant Reimbursements

Rental income is recognized on a straight-line basis over the term of the related lease. Residential leases generally have one-year terms while commercial leases generally have longer terms. Rents received in advance are deferred. In net lease arrangements, costs reimbursable from tenants for real estate taxes, property insurance and other recoverable costs are recognized as revenue in the period the recoverable costs are incurred. When the Company is the primary obligor with respect to purchasing goods and services for property operations and has discretion in selecting the supplier and retains credit risk, tenant reimbursement revenue and property operating expenses are presented on a gross basis in the Company's statement of operations. For certain triple net leases where the lessee self-manages the property, hires its own service providers and retains credit risk for routine maintenance contracts, no reimbursement revenue and expense are recognized.

### Foreign Currency Translation

The Company translates the assets and liabilities of its non-U.S. dollar functional currency investments and subsidiaries into U.S. dollars using exchange rates in effect at the balance sheet date. Income and expenses from these investments and subsidiaries are translated at the average rate of exchange prevailing during the period such income was earned or expenses were incurred. Translation adjustments resulting from changes in exchange rates are recorded as other comprehensive income or loss. Foreign currency transaction gains and losses are recognized when the Company receives distributions from non-U.S. dollar currency investments and subsidiaries, and are included in other gain or loss in the accompanying statements of operations.

### Other Income from Affiliates

Other income primarily includes asset management fees earned by two wholly-owned subsidiaries of the Company that provide asset management services for two of the Company's unconsolidated joint ventures that invested in loan portfolios. Asset management fees are recognized as earned.

### Derivative Instruments and Hedging Activities

The Company uses derivative instruments to manage its foreign currency risk and interest rate risk.

**Foreign Currency Risk**—The Company has entered into currency collars (consisting of caps and floors) and forwards to hedge the foreign currency exposure of its net investments in foreign entities. The Company has entered into various foreign exchange contracts with notional amounts and termination dates based upon the anticipated return of capital from the investments.

**Interest Rate Risk**—The Company uses interest rate swaps and caps to hedge against the risk of interest rate fluctuations on its future cash flows from investments. These derivative instruments are designed to mitigate the interest rate risk for certain floating rate debt investments and liabilities.

All derivative instruments are recorded at their fair values and included in other assets or other liabilities on the accompanying balance sheets on a gross basis. To the extent they are effective, fair value adjustments on derivative instruments designated as hedging instruments are reported as other comprehensive income and included in stockholders' equity until the hedged item is realized. Ineffective portions and settlement gains and losses, if any, are included in earnings. Fair value adjustments on derivative instruments that are not designated as hedging instruments are reported in other gain or loss on the accompanying statements of operations. The Company does not enter into derivative transactions for speculative or trading purposes.

### Fair Value Measurement

The Company determines the estimated fair value of financial assets and liabilities using the three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. The three levels of inputs that may be used to measure fair value are as follows:

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

**Level 2**—Prices are determined using other significant observable inputs. Observable inputs are inputs that other market participants would use in pricing a security. These may include quoted prices for similar securities, interest rates, prepayment speeds, credit risk and others.

**Level 3**—Prices are determined using significant unobservable inputs. In situations where quoted prices or observable inputs are unavailable (for example, when there is little or no market activity for an investment at the end of the period), unobservable inputs may be used.



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The Company records certain financial instruments at fair value on a recurring basis when required by GAAP. The Company has not elected the fair value option for any other financial instruments. Such financial instruments are carried at cost while fair value is separately disclosed (see Note 11).

### Share-Based Payments

The Company recognizes the cost of share-based awards based upon their fair values on a straight-line basis over the requisite service period, which is generally the vesting period of the awards. For awards to the Company's employees, including its independent directors, the fair value is determined as the grant date stock price. For share-based awards to non-employees, including the Manager and employees of the Manager, the fair value is based upon the vesting date stock price, which requires the amount of related expense to be remeasured at the end of each reporting period until the award has vested.

For awards with periodic vesting, the Company recognizes the related expense on a straight-line basis over the requisite service period for the entire award, subject to periodic adjustments to ensure that the cumulative amount of expense recognized through the end of any reporting period is at least equal to the fair value of the portion of the award that has vested through that date. Share-based payments are reflected in the same expense category as would be appropriate if the payments had been made in cash.

### Net Earnings Per Share

The Company calculates basic earnings per share using the two-class method which defines unvested share-based payment awards that contain nonforfeitable rights to dividends as participating securities. The two-class method is an allocation formula that determines earnings per share for each share of common stock and participating securities according to dividends declared and participation rights in undistributed earnings. Under this method, all earnings (distributed and undistributed) are allocated to common shares and participating securities based on their respective rights to receive dividends. Earnings per common share is calculated by dividing earnings allocated to common shareholders by the weighted-average number of common shares outstanding during the period.

Diluted earnings per common share is computed by dividing income allocated to common stockholders by the weighted average common shares outstanding plus the dilutive effect, if any, of share-based payments and the assumed conversion of convertible notes to common shares.

### Income Taxes

The Company elected to be taxed as a REIT, commencing with the Company's initial taxable year ended December 31, 2009. A REIT is generally not subject to corporate level federal and state income tax on net income it distributes to its stockholders. To qualify as a REIT, the Company must meet a number of organizational and operational requirements, including a requirement to distribute at least 90% of its REIT taxable income to its stockholders. If the Company fails to qualify as a REIT in any taxable year, it will be subject to federal and state income taxes at regular corporate rates (including any applicable alternative minimum tax) and may not be able to qualify as a REIT for four subsequent taxable years. Even if the Company qualifies for taxation as a REIT, it and its subsidiaries may be subject to certain federal, state, local and foreign taxes on its income and property and to federal income and excise taxes on its undistributed taxable income.

The Company has elected or may elect to treat certain of its existing or newly created corporate subsidiaries as taxable REIT subsidiaries (each a "TRS"). In general, a TRS of a REIT may perform non-customary services for tenants of the REIT, hold assets that the REIT cannot hold directly and, subject to certain exceptions related to hotels and healthcare properties, may engage in any real estate or non-real estate related business. A TRS is treated as a regular corporation and is subject to federal, state, local and foreign taxes on its income and property.

Deferred tax assets and liabilities are recognized for the expected future tax consequences of events that have been included in the financial statements or tax returns. Under this method, deferred tax assets and liabilities are determined based on the differences between the financial reporting and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. The deferred tax assets and liabilities of the TRSs relate primarily to temporary differences in the book and tax income of TRSs and operating loss carryforwards for federal and state income tax purposes, as well as the tax effect of accumulated other comprehensive income of TRSs. A valuation allowance for deferred tax assets is provided if the Company believes it is more likely than not that all or some portion of the deferred tax assets will not be realized. Realization of deferred tax assets is dependent on the

Company generating sufficient taxable income in future periods.

The Company periodically evaluates its tax positions to determine whether it is more likely than not that such positions would be sustained upon examination by a tax authority for all open tax years, as defined by the statute of limitations, based on their technical merits. As of December 31, 2013 and 2012, the Company has not established a liability for uncertain tax positions.

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## Segment Reporting

The Company currently operates in three reportable segments: (1) real estate debt investments, which include originated and acquired commercial real estate debt, mortgage-backed securities, and other debt-related investments, (2) single-family residential rentals through its investment in CAH OP, and (3) other real estate equity investments, which include real estate acquired in settlement of loans or from acquisition of operating properties, common equity in real estate or related companies, and certain preferred equity investments with profit participation meeting certain risk or return profiles.

Prior to the third quarter of 2013, the Company had two reportable segments, real estate debt investments and single-family residential rentals. During the third quarter of 2013, the Company reevaluated its operating and reportable segments in light of the increasing significance of its real estate equity investments. As a result of this evaluation, the Company created a third reportable segment which represents its investments in other real estate equity, which was previously included in the real estate debt investments segment. Prior to 2012, there was only one reportable segment, real estate debt investments.

## Reclassification

Certain amounts in the statement of cash flows for the year ended December 31, 2012 have been reclassified for consistency with the current year presentation. The reclassification did not have a material effect on the Company's financial position or results of operations.

## Recent Accounting Updates

**Comprehensive Income**—In February 2013, the FASB issued ASU No. 2013-02, Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income. Under ASU No. 2013-02, an entity is required to provide information about the amounts reclassified out of accumulated other comprehensive income ("AOCI") by component. In addition, an entity is required to present, either on the face of the income statement or in the notes, significant amounts reclassified from AOCI by the respective line items of the income statement. ASU No. 2013-02 did not change the current requirements for reporting net income or other comprehensive income in the financial statements. The adoption of the new presentation requirements of ASU No. 2013-02 in the first quarter of 2013 did not have a significant effect on the Company's consolidated financial position, results of operations or cash flows.

## 3. Investments in Unconsolidated Joint Ventures

Pursuant to an investment allocation agreement among the Company, the Manager and Colony Capital, many of the Company's investments have been structured as joint ventures with one or more Co-Investment Funds. The joint ventures are generally capitalized through equity contributions from the members, although certain investments are leveraged through various financing arrangements. The Company's exposure to the joint ventures is limited to amounts invested or committed to the joint ventures at inception, and neither the Company nor the other investors are required to provide financial or other support in excess of their capital commitments.

The Company's investments in unconsolidated joint ventures are summarized below:

(Amounts in thousands)		Ownership Percentage	Carrying Value	
Joint Ventures	Investment Status at December 31, 2013	at December 31, 2013 (1)	December 31, 2013	December 31, 2012
CAH Operating Partnership, L.P.	Investment in CAH OP, an investment vehicle created for the purpose of acquiring and renting single-family homes	24.3	% \$530,007	\$ 251,501
Portfolio 8 Investors, LLC <sup>(2)</sup>	Preferred equity investment in an entity that acquired a multifamily portfolio composed of approximately 7,600 units located in Georgia, Florida and Texas	75.0	% 148,683	—
		50.0	% 49,103	46,188

ColFin Court Square Funding, LLC	Preferred equity investment in an entity that acquired a Class A office tower located in Long Island City, New York				
ColFin Hunt Holdco A, LLC and ColFin Hunt Holdco B, LLC	1 non-performing commercial real estate loan and 2 REO properties	37.9	%	36,133	26,963
ColFin 2011 CRE Holdco, LLC and Colony AMC 2011 CRE, LLC	410 performing and non-performing loans acquired in a structured transaction with the FDIC, secured mostly by commercial real estate, and 22 REO properties	44.4	%	34,298	38,220

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(Amounts in thousands)		Ownership Percentage	Carrying Value	
Joint Ventures	Investment Status at December 31, 2013	at December 31, 2013 <sup>(1)</sup>	December 31, 2013	December 31, 2012
ColFin NW Funding, LLC	15 performing acquired first mortgages secured by commercial real estate	37.9 %	33,682	32,676
ColFin JIH Holdco, LLC, ColFin JIH Mezzco A, LLC and ColFin JIH Opco, LLC	Equity interests in and senior mezzanine loan receivable from entities owning a portfolio of 102 limited service hotels	33.3 %	31,559	32,320
ColFin Bulls Funding A, LLC and ColFin Bulls Funding B, LLC	354 performing and non-performing acquired loans consisting of substantially all first mortgage recourse commercial real estate loans and 14 REO properties	32.5 %	30,309	39,662
ColFin DB Guarantor, LLC and Colony AMC DB, LLC	452 performing and non-performing loans acquired in a structured transaction with the FDIC, secured mostly by commercial real estate and 117 REO properties	33.3 %	26,293	39,317
ColFin Ash Funding, LLC	2 most junior mortgage participation interests secured by 5 full-service hotels	50.0 %	24,765	24,365
ColFin STC Funding, LLC	Acquired performing senior mortgage loan secured by a retail property in Florida	50.0 %	23,299	—
W&D Interim Lender, LLC <sup>(3)</sup>	First mortgage loan secured by a student housing community in New York	90.0 %	22,309	—
ColFin Mizner Funding, LLC	First mortgage loan origination secured by a multifamily development parcel located in Florida	50.0 %	21,130	—
ColFin Cabo Palm Funding, LLC	Participation in junior first mortgage interest secured by a luxury beach resort in Mexico	50.0 %	20,072	—
ColFin 666 Funding, LLC	First mortgage pari-passu participation interest secured by Class A midtown Manhattan office building	33.3 %	19,096	17,595
ColFin PHX Tower Funding, LLC	Equity interest in a high-rise office tower located in Phoenix, Arizona	50.0 %	18,408	16,454
ColFin London Funding, LLC	8 performing and non-performing acquired loans secured by commercial real estate	50.0 %	18,138	37,427
ColFin 2012 CRE ADC Holdco, LLC and Colony AMC 2012 CRE ADC, LLC	383 performing and non-performing loans acquired in a structured transaction with the FDIC, mostly secured by commercial real estate and 5 REO properties	50.0 %	16,795	15,370
ColFin Grand Cul Funding, LLC	First mortgage loans secured by a partially constructed hotel and residential development project located in the Caribbean	33.3 %	16,595	—
ColFin Inland Funding, LLC and ColFin Inland Investor, LLC	First mortgage loan secured by a Southern California master planned development and equity participation rights	50.0 %	16,068	15,086
ColFin FCDC Funding, LLC	Equity interests acquired through deed-in-lieu in 2 partially developed master planned communities located in California	50.0 %	15,894	15,422

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ColFin ARP Funding, LLC	First mortgage loan to finance the acquisition and redevelopment of high-end, single family residential properties in infill, coastal southern California markets	50.0	%	15,350	—
Other unconsolidated joint ventures	26 investments with less than \$15 million carrying value at December 31, 2013	4.5% to 50.0%		201,543	228,515
				\$1,369,529	\$ 877,081

(1) The Company's ownership percentage represents capital contributed to date and may not be reflective of the Company's economic interest in the entity because of provisions in operating agreements governing various matters, such as classes of partner or member interests, allocations of profits and losses, preferential returns and guaranty of debt. Each unconsolidated joint venture has been determined to be either a VIE for which the Company was not deemed to be the primary beneficiary or a voting interest entity in which the Company does not have a controlling financial interest.

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While the Company has a majority ownership interest in Portfolio 8 Investors, LLC, the minority member has (2) control over the day-to-day operations of the entity. Accordingly, the Company accounts for its investment using the equity method.

The Company has determined that W&D Interim Lender, LLC is a VIE for which the Company is not the primary (3) beneficiary because the power to direct the activities that most significantly impact the VIE is shared equally between its members but the other member has the obligation to absorb losses of the VIE that potentially could be significant to the VIE. Accordingly, the Company accounts for its investment using the equity method.

Activity in the Company's investments in unconsolidated joint ventures is summarized below:

(In thousands)	2013	2012
Balance at January 1	\$877,081	\$443,500
Contributions	672,338	528,347
Assignment of loans receivable and related liabilities	—	29,427
Distributions	(279,161 )	(201,335 )
Equity in net income	100,708	68,737
Equity in other comprehensive income	9,827	7,144
Equity in realized gain reclassified from accumulated other comprehensive income	(12,935 )	—
Foreign currency translation gain	1,671	1,261
Balance at December 31	\$1,369,529	\$877,081

During the year ended December 31, 2013, the Company invested a combined \$369 million in 14 new unconsolidated joint ventures representing 10 originations and four loan acquisitions, and \$295 million in CAH OP. Six investments in unconsolidated joint ventures were fully resolved during the year.

During the year ended December 31, 2012, the Company invested a combined \$528 million in 15 new unconsolidated joint ventures representing four originations, 10 loan acquisitions, and \$255 million in CAH OP. Three investments in unconsolidated joint ventures were fully resolved during the year.

To-date, the Company has invested cumulative \$550 million in CAH OP. As of December 31, 2013, the Company had no further capital commitments to CAH OP.

Combined condensed balance sheets and statements of operations for all unconsolidated joint ventures are presented below:

### Combined Condensed Balance Sheets of Unconsolidated Joint Ventures

(In thousands)	December 31, 2013	2012
Assets:		
Cash and cash equivalents	\$321,183	\$156,704
Loans receivable, net	2,171,943	2,383,748
Investments in real estate	3,658,940	990,105
Investments in unconsolidated joint ventures	459,010	436,188
Debt and equity securities, available-for-sale, at fair value	24,753	247,963
Other assets	345,196	825,804
Total assets	\$6,981,025	\$5,040,512
Liabilities:		
Debt	\$1,515,188	\$1,018,865
Other liabilities	140,509	65,193
Total liabilities	1,655,697	1,084,058
Owners' equity	4,465,363	2,997,533
Noncontrolling interests	859,965	958,921
Total liabilities and equity	\$6,981,025	\$5,040,512
Company's share of equity	\$1,369,529	\$877,081



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## Combined Condensed Statements of Operations of Unconsolidated Joint Ventures

(In thousands)	Year Ended December 31,		
	2013	2012	2011
Income:			
Interest income	\$362,163	\$372,958	\$320,409
Property operating income	206,848	96,897	5,998
Equity in income of unconsolidated joint ventures	26,410	53,110	75,953
Other income	25,221	29,325	14,962
Total income	620,642	552,290	417,322
Expenses:			
Interest expense	31,012	37,185	26,950
Property operating expenses	152,154	73,770	9,695
Depreciation and amortization	59,902	12,850	953
Other expenses	90,547	88,662	61,682
Total expenses	333,615	212,467	99,280
Other income:			
Realized and unrealized gain on investments, net	194,372	145,258	71,651
Net income	481,399	485,081	389,693
Net income attributable to noncontrolling interests	102,431	84,806	81,439
Net income attributable to members	\$378,968	\$400,275	\$308,254
Company's equity in net income	\$100,708	\$68,737	\$46,720

The Company's investments in CAH OP represented 20% and 18% of the Company's total assets as of December 31, 2013 and December 31, 2012, respectively. No other single investment represented greater than 10% of total assets. For the year ended December 31, 2012, ColFin WLH Funding, LLC generated greater than 10% of total income of the Company. For the year ended December 31, 2011, ColFin FRB Investor, LLC and ColFin WLH Funding, LLC individually generated greater than 10% of total income. On a combined basis, these investments generated 12% and 24% of total income for the years ended December 31, 2012 and 2011, respectively. No single investment in an unconsolidated joint venture generated greater than 10% of total income for the year ended December 31, 2013.

**Related Party Transactions of Unconsolidated Joint Ventures**—The Company has equity ownership interests in certain unconsolidated asset management companies (each an “AMC”) that provide management services to certain of its unconsolidated joint ventures. The AMCs earn annual management fees equal to 50 to 75 basis points times the outstanding UPB of each loan portfolio and are responsible for the payment of allocations of compensation, overhead and direct costs incurred by an affiliate of the Manager pursuant to a cost allocation arrangement (see Note 14). Certain unconsolidated joint ventures reimburse Colony Capital and its affiliates for costs incurred on their behalf, including costs of property management personnel. The joint ventures, including AMCs, were allocated approximately \$26.7 million, \$12.9 million and \$7.7 million in costs from such affiliates of the Manager for the years ended December 31, 2013, 2012 and 2011, respectively. Such costs are included in property operating and other expenses in the combined condensed statements of operations of unconsolidated joint ventures above. The Company's proportionate share, based upon its percentage interests in the joint ventures, was \$7.3 million, \$3.8 million and \$1.6 million for the years ended December 31, 2013, 2012 and 2011, respectively.

Until October 16, 2013, an affiliate of CAH OP's manager provided construction and rehabilitation services on the single-family rental homes held through CAH OP. CAH OP reimbursed approximately \$66.5 million and \$5.4 million for the years ended December 31, 2013 and 2012, respectively, to the affiliate for third party costs and overhead, which have been capitalized or expensed, as appropriate, in accordance with the capitalization policy of CAH OP. Pursuant to a distribution agreement dated as of October 16, 2013, the affiliate relationship between CAH OP's manager and the provider of such construction and rehabilitation services ended.





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## 4. Loans Receivable

The following table summarizes the Company's loans held for investment by class of receivable:

(Amounts in thousands)	December 31, 2013					December 31, 2012				
	Principal	Carrying Amount	Weighted Average Coupon	Weighted Average Maturity in Years	Number of Loans	Principal	Carrying Amount	Weighted Average Coupon	Weighted Average Maturity in Years	Number of Loans
Non-PCI Loans:										
Mortgage loans	\$463,552	\$423,078	7.1 %	3.9	33	\$233,003	\$203,098	8.9 %	2.1	3
B-note	104,068	103,458	10.9 %	3.8	2	14,558	14,471	20.9 %	3.3	1
Mezzanine loans	330,909	328,185	11.0 %	2.4	2	116,000	116,000	10.1 %	5.2	3
	898,529	854,721			37	363,561	333,569			7
Purchased Credit-Impaired Loans:										
Mortgage loans	299,235	173,933			5	—	—			—
	\$1,197,764	\$1,028,654			42	\$363,561	\$333,569			7

The following table summarizes the Company's investments in non-PCI loans with variable interest rates:

(Amounts in thousands)	Index	Weighted Average Spread	Weighted Average Rate	Principal	Carrying Amount	Number of Loans
December 31, 2013						
Mortgage loans	1-Month LIBOR	(1) 4.85%	7.71%	(3) \$246,478	\$220,111	9
Mortgage loan	1-Month Reference Bills	(2) 4.65%	4.66%	30,064	27,595	3
Mezzanine loans	1-Month LIBOR	10.80%	10.97%	330,909	328,185	2
				\$607,451	\$575,891	14
December 31, 2012						
Mortgage loan	1-Month LIBOR	4.00%	8.57%	\$171,961	\$142,575	1

(1)LIBOR = London Interbank Offered Rate

(2)Reference Bills = Freddie Mac Reference Bill index

(3)Certain loans are subject to a LIBOR floor which is higher than the actual LIBOR at December 31, 2013.

Activity in loans held for investment is summarized below:

(In thousands)	2013	2012	2011
Balance at January 1	\$333,569	\$232,619	\$69,929
Loan acquisitions and originations	876,503	204,298	160,980
Paid-in-kind interest added to loan principal	218	851	608
Discount and net loan fee amortization	10,053	3,656	1,332
Carrying value of loans sold	(70,280)	(30,159)	—
Assignment of loans receivable to investment in unconsolidated joint ventures	—	(29,612)	—
Noncash distribution of loan receivable to a noncontrolling interest	(18,500)	—	—
Principal repayments	(106,083)	(48,084)	(230)
Payments received from PCI loans	(544)	—	—
Effect of foreign exchange rates	3,718	—	—

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Balance at December 31	\$1,028,654	\$333,569	\$232,619
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During the year ended December 31, 2013, the Company invested \$877 million in the origination or acquisition of loans as follows:

- \$122 million to participate in the origination of a first mortgage loan secured by 11 athletic clubs located in California;

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\$328 million to participate in the origination of mezzanine loans secured by equity interests in an entity owning a portfolio of hotels located throughout the United States, including \$154 million by noncontrolling interests; \$177 million to acquire a portfolio of 27 loans secured by multifamily and senior housing properties located throughout the United States, including \$48 million by noncontrolling interests. Two of the loans in the portfolio are PCI loans;

\$164 million to acquire a portfolio of three PCI loans secured by office and retail properties in Spain, including \$28 million by a noncontrolling interest; and

\$86 million, net of origination fees, to originate 6 loans within the Company's Transitional CRE Lending Platform. These loans are earmarked for a potential floating rate securitization. The loans bear interest, on a weighted average basis, at 1-month LIBOR plus 6.5%, and have initial terms of 2 to 3 years. The underlying collateral includes retail, multifamily, office and hospitality properties.

During the year ended December 31, 2013, the Company resolved certain loans as follows:

The borrowers of a first mortgage loan originated in December 2010 and mezzanine loans originated in June 2011 paid off the entire loan balances and accrued interest thereon, including a yield maintenance premium of \$3.6 million for the first mortgage loan (see Note 9);

The Company split an originated first mortgage loan into a \$32.8 million A-note and \$90.1 million B-note, and sold the A-note to an unrelated party at par; and

The Company sold its pro-rata share of its investment in two performing hotel portfolio mezzanine loans resulting in a realized gain of approximately \$1.1 million.

A mezzanine loan partially owned by noncontrolling interests and secured by hotel properties represented 12% of the Company's total assets as of December 31, 2013. The same loan generated 13% of total income for the year ended December 31, 2013. No single loan receivable represented greater than 10% of total assets as of December 31, 2012. Two first mortgage loans, which share the same corporate guarantor and partially owned by noncontrolling interests, generated 14% and 18% of total income for the years ended December 31, 2013 and 2012, respectively. No single loan generated greater than 10% of total income for the year ended December 31, 2011.

As of December 31, 2013 and 2012, all loans were current and performing in accordance with their contractual terms. There were no troubled debt restructurings during the years ended December 31, 2013, 2012 and 2011.

Minimum scheduled principal payments required under the loan agreements, excluding PCI loans, as of December 31, 2013 are as follows:

Year Ending December 31,	(In thousands)
2014	\$ 150,835 <sup>(1)</sup>
2015	68,582
2016	452,380
2017	111,941
2018	7,360
2019 and after	95,931
Total	\$ 887,029

(1) Net of \$11.5 million credit available to borrower upon full payoff.

#### Purchased Credit-Impaired Loans

In October 2013, the Company and a 27% noncontrolling interest acquired a portfolio of 27 loans secured by multifamily and senior housing assets, all of which were performing at acquisition. Two of the 27 loans are considered PCI loans for which the Company expects to collect less than the contractually required amounts. In November 2013, the Company and a 17% noncontrolling interest acquired participation interests in three PCI loans secured by office and retail properties in Spain.

The excess of cash flows expected to be collected, as measured at acquisition date, over the initial investment is referred to as the accretable yield. This amount is not reported in the accompanying consolidated balance sheets, but is recognized as interest income over the estimated life of the acquired loans using the effective interest method.

The following table summarizes the accretable yield and nonaccretable difference at acquisition for PCI loans acquired during the year ended December 31, 2013:

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(In thousands)

Contractually required payments including interest	\$315,939
Less: cash flows not expected to be collected (nonaccretable difference)	17,253
Total cash flows expected to be collected	298,686
Less: accretable yield	131,037
Fair value of loans at acquisition	\$167,649

The expected cash flows were determined based on the estimated performance over the remaining life of the underlying loans. Fair value of the acquired loans include credit losses expected to be incurred over the life of the loans, if any.

Changes in the accretable yield for the PCI loans were as follows:

(In thousands)	2013
Accretable yield at January 1	\$—
Additions	131,037
Accretion	(3,108)
Effect of foreign exchange rates	2,894
Accretable yield at December 31	\$130,823

The factors that most significantly affect estimates of cash flows expected to be collected, and accordingly the accretable yield, include: (i) estimate of the remaining life of acquired loans which may change the amount of future interest income; (ii) changes to prepayment assumptions; (iii) changes to collateral value assumptions for loans expected to foreclose; and (iv) changes in interest rates on variable rate loans. During the year ended December 31, 2013, there were no changes to estimates of cash flows expected to be collected on PCI loans, as all PCI loans were acquired during the fourth quarter of 2013 and there were no significant changes to the factors described above since their acquisition.

## 5. Acquisition of Real Estate

On December 9, 2013, the Company acquired an office campus in Minnesota from an unrelated third party. The property includes two buildings with approximately 502,000 total rentable square feet (unaudited) and fully occupied by a single-A rated tenant under a triple net lease. The acquisition cost, including closing costs of \$0.6 million, was approximately \$123.4 million. The acquisition was subsequently financed with a \$88 million 10-year term, non-recourse, fixed-rate mortgage loan from a financial institution (see Note 9). The acquisition was completed with a strategic partner with a 0.75% ownership interest.

The related assets, liabilities, and results of operations of the acquired property are included in the consolidated financial statements as of the date of acquisition. The following table summarizes the estimated fair values of the assets at the acquisition date:

(Amounts in thousands)	Purchase Consideration	Estimated Useful Life (in years)	
Real estate assets:			
Land	\$8,319	n/a	
Buildings and improvements	97,011	(1) 10 - 40	
Tenant improvements	7,356	6.8	(3)
Identifiable intangible assets:			
In-place lease value	7,845	(2) 6.8	(3)
Deferred leasing costs	2,219	(2) 6.8	(3)
Total assets acquired	\$122,750		

(1) Buildings and improvements consist of two office buildings, two parking garages and non-building site improvements including paving, site lights, landscaping and others. Since the in-place lease represents a separate fair value component from the tangible real estate in an income-producing property subject to lease, the buildings

were valued as if they were vacant and available to lease at market terms on the purchase date.

- (2) The net amount recorded for acquired identifiable intangible assets was included in other assets on the accompanying balance sheet as of December 31, 2013.

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(3) The lease-related tangible and intangible assets are amortized on a straight-line basis as an increase to depreciation and amortization expense over the remaining term of the applicable leases.

The following table summarizes the results of operations of the acquired properties for the period from December 9, 2013, the date of acquisition, to December 31, 2013:

	(In thousands)
Rental income and tenant reimbursements	\$ 789
Net loss	(542 )

The following table summarizes information regarding the components of real estate assets held for investment as of December 31, 2013:

	(In thousands)
Land	\$8,319
Buildings and improvements	97,011
Tenant improvements	7,356
	112,686 (1)
Accumulated depreciation	(218 )
Net carrying amount	\$ 112,468

(1) The aggregate gross cost of property for federal income tax purposes was approximately \$121.1 million as of December 31, 2013.

Depreciation expense for the year ended December 31, 2013 was \$218,000.

#### Acquired Intangible Assets

The following table summarizes acquisition-related intangible assets as of December 31, 2013:

(In thousands)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
In-place lease	7,845	(72 )	7,773
Deferred leasing costs	2,219	(20 )	2,199
	10,064	(92 )	9,972

Amortization expense for the year ended December 31, 2013 was \$92,000.

Expected amortization expense for acquisition-related intangible assets for each of the next five years and thereafter is as follows as of December 31, 2013:

(In thousands)		In-Place Leases	Deferred Leasing Costs
Year Ending December 31,			
2014		\$ 1,152	\$ 326
2015		1,152	326
2016		1,152	326
2017		1,152	326
2018		1,152	326
2019 and after		2,013	569
Total		\$ 7,773	\$ 2,199

#### Future Minimum Rent

The in-place leases on the acquired operating properties expire in September 2020 with an option to renew and are subject to scheduled rent increases. The leases also provide for additional rents based on real estate taxes, utilities, insurance and certain operating expenses. The tenant elected to self-manage the office properties pursuant to the lease agreements.

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Future contractual minimum rental payments under noncancelable operating leases as of December 31, 2013 are as follows:

Year Ending December 31,	(In thousands)
2014	\$9,195
2015	9,195
2016	9,365
2017	9,654
2018	9,820
2019 and after	17,380
Total	\$64,609

## Unaudited Pro Forma Results

The following table presents pro forma results of the Company as if the acquisition had been consummated on January 1, 2012. The pro forma results for the year ended December 31, 2013 were adjusted to exclude acquisition-related expenses of approximately \$597,000 and the pro forma results for the year ended December 31, 2012 were adjusted to include these expenses. The unaudited pro forma results are not necessarily indicative of future operating results.

(Amounts in thousands, except per share data)	Year Ended December 31,	
	2013	2012
Total income	\$192,095	\$119,800
Net income attributable to common stockholders	\$80,952	\$47,563
Net income attributable to common stockholders per share—basic	\$1.21	\$1.31
Net income attributable to common stockholders per share—diluted	\$1.21	\$1.31

## 6. Beneficial Interests in Debt Securities

On June 30, 2011, the Company, through a 99%-owned joint venture with a strategic partner, acquired \$28 million in beneficial interests in a series of tax-exempt bonds with an aggregate principal amount of \$40.4 million. The bonds are secured by a multifamily property located in Georgia. At closing, the bonds financed the acquisition of the property by an institutional real estate firm. The \$28 million in beneficial interests, in the form of senior certificates, were acquired at par but had an estimated fair value of \$32.1 million at acquisition. The bonds have a six-year term, bear interest at a fixed rate of 7.125%, require semi-annual interest payments each December and June, and may be prepaid, subject to the payment of certain fees. The beneficial interests in debt securities are classified as available-for-sale and stated at estimated fair value, with changes in fair value reflected in other comprehensive income or loss. The Company's beneficial interests in debt securities are summarized below:

(In thousands)	December 31,	
	2013	2012
Principal	\$28,000	\$28,000
Unamortized premium	2,507	3,174
Amortized cost	30,507	31,174
Unrealized gain included in accumulated other comprehensive income	327	881
Fair value	\$30,834	\$32,055

Concurrently with the acquisition of beneficial interests in debt securities, the Company's strategic partner entered into an interest rate swap agreement with the borrower (see Note 10).

## 7. Other Assets

The following table summarizes the Company's other assets, net:



(In thousands)	December 31,		
	2013	2012	
Restricted cash	\$7,898	(1) \$13,866	(1)
Deferred financing costs, net	11,275	(2) 2,281	(2)
In-place lease value, net	7,773	(3) —	
Deferred leasing costs, net	2,199	(4) —	
Receivables	8,277	3,414	
Derivative assets, net of tax effect	3,108	760	
Deferred tax assets, net of allowances	2,391	(5) 1,176	
Other	979	1,166	
Total other assets	\$43,900	\$22,663	

(1) Restricted cash includes borrower escrow accounts and an interest reserve account to service secured financing.

(2) Deferred financing costs are shown net of accumulated amortization of \$6.5 million and \$3.5 million as of December 31, 2013 and 2012, respectively.

(3) In-place lease value is shown net of accumulated amortization of \$72,000 as of December 31, 2013.

(4) Deferred leasing costs are shown net of accumulated amortization of \$20,000 as of December 31, 2013.

(5) Deferred tax assets are shown net of allowances of \$356,000 and \$300,000 as of December 31, 2013 and 2012.

#### 8. Line of Credit

On August 6, 2013, the Company entered into a credit agreement (the "JPM Credit Agreement") with JPMorgan Chase Bank, N.A. as administrative agent, and certain lenders. The JPM Credit Agreement provided a credit facility in the initial maximum principal amount of \$360 million which may be increased to \$600 million, subject to certain conditions, including each lender or substitute lender agreeing to provide commitments for such increased amount. In November 2013, the maximum principal amount was increased by \$20 million to \$380 million when one of the lenders increased its share of commitments. The maximum principal amount was again increased in January 2014 to \$420 million.

The JPM Credit Agreement replaces the previous credit agreement (the "BofA Credit Agreement"), dated as of September 1, 2011, with Bank of America, N.A. and certain lenders, which provided \$175 million of credit availability. Borrowings under the JPM Credit Agreement were used by the Company to repay all obligations due under the BofA Credit Agreement, pay closing costs associated with the JPM Credit Agreement and finance investments in target assets, as well as for general corporate purposes.

The maximum amount available to borrow under the JPM Credit Agreement at any time is limited by a borrowing base of certain investment assets, with the valuation of such investment assets generally determined according to a percentage of net book value or a multiple of Core Earnings (as defined in the management agreement between the Company and the Manager). As of December 31, 2013, the borrowing base valuation was sufficient to permit borrowings of up to the entire \$380 million commitment, of which \$241.5 million remained available.

Advances under the JPM Credit Agreement accrue interest at a per annum rate equal to the sum of LIBOR plus 2.75% or 3.00%, depending upon the leverage ratio as defined in the JPM Credit Agreement. At December 31, 2013, the applicable spread was 2.75% and the Company had outstanding borrowings bearing weighted average interest at 2.92%. The Company also pays a commitment fee of 0.5% or 0.4% of the unused amount (0.5% at December 31, 2013), depending upon usage.

The initial maturity date of the JPM Credit Agreement is August 5, 2016, and any amounts outstanding upon maturity will convert automatically to a fully amortizing 2-year term loan payable in quarterly installments. In the event of such conversions, the term loan will continue to bear interest at the same rate as the revolving loans from which it was converted.

Some of the Company's subsidiaries guaranty the obligations of the Company under the JPM Credit Agreement. As security for the advances under the JPM Credit Agreement, the Company and some of its affiliates pledged their equity interests in certain subsidiaries through which the Company directly or indirectly owns substantially all of its assets.

The JPM Credit Agreement contains various affirmative and negative covenants, including financial covenants that require the Company to maintain minimum tangible net worth and liquidity levels and financial ratios, as defined in the JPM Credit Agreement. At December 31, 2013, the Company was in compliance with all of these financial covenants.

The JPM Credit Agreement also includes customary events of default, in certain cases subject to reasonable and customary periods to cure, including but not limited to: failure to make payments when due; breach of covenants; breach of representations and warranties; insolvency proceedings; cross default to material indebtedness or material judgment defaults;

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certain judgments and attachments; and certain change of control events. The occurrence of an event of default may result in the termination of the credit facility, accelerate the Company's repayment obligations, in certain cases limit the Company's ability to make distributions, and allow the lenders to exercise all rights and remedies available to them with respect to the collateral. There have been no events of default since the inception of the credit facility.

### 9. Debt

#### Secured Financing

The following table summarizes certain information about the Company's secured debt:

				Outstanding Balance	
(Amounts in thousands)				December 31,	
Type	Collateral	Interest Rate	Maturity Date	2013	2012
Secured financing <sup>(1)</sup>	Portfolio of 25 first mortgage loans and 2 subordinated loans	1-month LIBOR+2.85%	December 2017	\$115,000	\$—
Secured financing <sup>(2)</sup>	Participation interest in first mortgage loan	5% fixed	July 2014	74,607	94,499
Secured financing <sup>(3)</sup>	N/A	4.85% fixed	January 2016	—	13,668
First mortgage loan <sup>(4)</sup>	Office property in Minnesota	4.84% fixed	January 2024	88,000	—
Total				\$277,607	\$108,167

The financing is secured by a loan portfolio acquired in October 2013. The financing requires monthly interest payments and principal curtailment based upon the ratio of principal outstanding to collateral cost basis. The initial principal curtailment requirement is 70% of all excess cash flow from the underlying loan portfolio, after payment of certain loan servicing fees and monthly interest, but may increase or decrease in the future.

In connection with the acquisition of a \$181 million participation interest in a first mortgage loan in May 2012, the seller provided concurrent non-recourse financing for \$103.5 million, or 65% of the purchase price. Concurrently with the loan acquisition, the borrower funded, on behalf of the Company, an interest reserve account in an amount sufficient to service the interest for the term of the secured financing. The interest reserve account is controlled by the secured financing lender and is included in other assets in the accompanying balance sheets. The financing has an initial maturity of July 2014 and can be extended to January 2017, subject to an extension fee. Upon exercise of the extension option, the borrower of the first mortgage loan will again be required to fund the interest reserve account on behalf of the Company to service the interest for the extended term of the secured financing.

On December 23, 2010, the Company assigned a \$20.75 million first mortgage it originated to a third party in exchange for \$14 million in proceeds, and retained a \$6.75 million subordinated B-note participation. The Company accounted for the assignment as a financing transaction, as the Company retained effective control over the original first mortgage loan and, accordingly, it did not meet the criteria of a loan sale. In April 2013, as a result of a default by the borrower, the Company exercised its option to repurchase the A-note at par from the third party. The loan requires monthly interest payments until January 2016, then principal and interest payments based on a 30-year amortization period. The loan agreement requires rent receipts from the collateral property to be initially deposited into a lockbox account controlled by the lender. The excess of monthly rent receipts over monthly debt service is remitted to the Company.

The financing agreements require minimum scheduled principal payments or payments that depend upon the net cash flows from the collateral assets and the ratio of principal outstanding to collateral. The following table summarizes such minimum principal payments and estimated principal payments based upon reasonable expectations of cash flows from the underlying collateral assets as of December 31, 2013:

Year Ending December 31,	(In thousands)
2014	\$94,920
2015	83,677

2016	4,684
2017	8,825
2018	1,403
2019 and after	84,098
Total	\$277,607

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### Convertible Senior Notes

On April 10, 2013, the Company issued \$200 million of its 5.00% Convertible Senior Notes due on April 15, 2023 (the "Convertible Notes"). The Convertible Notes were sold to the underwriters at a discount of 3%, resulting in net proceeds of \$194 million to the Company. The Convertible Notes bear interest at 5.00% per annum payable semiannually in arrears on April 15 and October 15 of each year. The first interest payment in the amount of \$5.1 million was made on October 15, 2013.

The Convertible Notes are convertible, at the holders' option, into shares of the Company's common stock at any time prior to the close of business on the second scheduled trading day immediately preceding the maturity date, subject to certain limitations as described in the indenture, at the applicable conversion rate in effect on the conversion date. The conversion rate is initially set to equal 42.3819 shares of common stock per \$1,000 principal amount of Convertible Notes (equivalent to a conversion price of approximately \$23.60 per share of common stock), subject to adjustment upon the occurrence of certain events. The Company may redeem the Convertible Notes at its option at any time on or after April 22, 2020 if the last reported sale price of its common stock has been at least 130% of the conversion price of the Convertible Notes then in effect for at least 20 trading days (whether or not consecutive) during any 30 consecutive trading day period ending on, and including, the trading day immediately preceding the date on which the Company provides notice of redemption, at a redemption price equal to 100% of the principal amount of the Convertible Notes to be redeemed, plus accrued and unpaid interest to, but excluding, the redemption date.

### 10. Derivatives and Hedging

#### Net Investment Hedges

The Company has investments in unconsolidated joint ventures and loans denominated in Euro that expose the Company to foreign currency risk. At December 31, 2013 and 2012, the Company's combined net investments in such joint ventures and loans receivable totaled approximately €166.2 million, or \$228.4 million, and €31.3 million, or \$41.3 million, respectively. The Company uses forwards and collars (consisting of caps and floors) without upfront premium costs to hedge the foreign currency exposure of its net investments. At December 31, 2013, the total notional amount of the collars was approximately €75.5 million, with termination dates ranging from July 2014 to December 2017, and the total notional amount of forward exchange contracts was €50 million, with a termination date of June 2014.

#### Cash Flow Hedge

In December 2013, the Company entered into an interest rate cap designated as a cash flow hedge to limit the exposure of increases in interest rates on one of the Company's LIBOR-indexed secured debt. The cap has a notional amount of \$57.5 million and a 2.5% strike on one-month LIBOR and expires in November 2015.

#### Non-Designated Hedges

Non-designated hedges are derivatives that do not meet the criteria for hedge accounting or for which the Company did not elect to designate as hedges. The Company does not enter into derivative transactions for speculative or trading purposes, but may enter into derivatives to manage the economic risk of changes in foreign exchange rates or interest rates. The Company may also assume existing derivative instruments in connection with investment transactions. Changes in the fair value of derivatives not designated as hedges are recorded in other income or loss in the accompanying statements of operations.

In connection with the acquisition of three PCI loans during November 2013 (see Note 4), the Company acquired two interest rate swaps with a combined notional of €79.5 million whereby it receives fixed coupons ranging from 4.10% to 4.24% of the notional amount and pays Euro Interbank Offered Rate ("Euribor"). The Company acquired the swaps at a cost of \$2.8 million. These swaps effectively convert the acquired floating rate loans to fixed rate loans. One of the interest rate swaps terminated in December 2013 with a net settlement of \$1.7 million to the Company. For the year ended December 31, 2013, an \$18,000 gain was included in other loss, net in the accompanying statement of operations.

Concurrently with the acquisition of beneficial interests in debt securities in June 2011 (see Note 6), the Company's strategic partner entered into an interest rate swap agreement with the borrower which, in conjunction with a special contribution/distribution arrangement with the joint venture, will result in a net current yield to the joint venture of the Securities Industry and Financial Markets Association ("SIFMA") Municipal Swap Index plus 3.25% per annum (3.31%

at December 31, 2013). The Company determined that the special contribution/distribution arrangement is an embedded derivative that meets the criteria for bifurcation and recorded a derivative liability. The bifurcated derivative does not qualify as a hedging instrument, so changes in the estimated fair value of the derivative are recognized in income. For the years ended December 31, 2013, 2012 and 2011, unrealized losses of \$112,000, \$734,000 and \$682,000, respectively, are included in other loss, net in the accompanying statements of operations.

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The fair values of derivative instruments included in the Company's consolidated balance sheets are as follows:

	December 31,	
(In thousands)	2013	2012
<b>Assets</b>		
Foreign exchange contracts designated as hedging instruments	\$2,126	\$760
Interest rate cap designated as a hedging instrument	11	—
Interest rate swaps not designated as hedging instruments	971	—
Total derivatives included in other assets	\$3,108	\$760
<b>Liabilities</b>		
Foreign exchange contracts designated as hedging instruments	\$5,504	\$293
Embedded derivative liability not designated as a hedging instrument	2,952	3,898
Total derivatives included in accrued and other liabilities	\$8,456	\$4,191

Certain counterparties to the derivative instruments require the Company to deposit cash or other eligible collateral for derivative financial liabilities exceeding \$100,000. As of December 31, 2013, the Company had no amounts on deposit related to these agreements.

# 11. Fair Value Measurements

## Financial Instruments Reported at Fair Value

The Company has certain assets and liabilities that are required to be recorded at fair value on a recurring basis. The following table summarizes the fair values of those assets and liabilities:

	December 31,	
(In thousands)	2013	2012
<b>Assets</b>		
Beneficial interests in debt securities	\$30,834	\$32,055
Foreign currency derivative contracts	2,126	760
Interest rate derivative contracts	982	—
	\$33,942	\$32,815
<b>Liabilities</b>		
Foreign currency derivative contracts	\$5,504	\$293
Embedded derivative liability associated with beneficial interests in debt securities	2,952	3,898
	\$8,456	\$4,191

All of the fair values in the table above fall within Level 2 of the fair value hierarchy which rely on significant observable inputs, other than quoted market prices for identical assets or liabilities, including quoted prices for similar securities, interest rates, prepayment speeds, credit risk and others.

The fair value of the beneficial interests in debt securities and the associated embedded derivative liability were determined by discounting the expected cash flows using observable current and forward rates of widely used indices that closely follow the SIFMA Municipal Swap Index. The fair values of foreign currency and interest rate derivative contracts are determined by discounting the expected cash flow of each derivative instrument based on forecast foreign exchange rates or interest rates. This analysis reflects the contractual terms of the derivatives, observable market-based inputs, and credit valuation adjustments to appropriately reflect the non-performance risk for both the Company and the respective counterparty. Although credit valuation adjustments, such as the risk of default, rely on Level 3 inputs, the Company has determined that these inputs are not significant to the overall valuation of its derivatives. As a result, derivative valuations in their entirety are classified in Level 2 of the fair value hierarchy.

## Fair Value Disclosure of Financial Instruments Reported at Cost

The following tables present the estimated fair values and carrying values of the Company's financial instruments carried at cost, aggregated by the level in the fair value hierarchy:





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(In thousands)	Fair Value Measurements Using			Total Fair Value	Carrying Value
	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)		
December 31, 2013					
Assets					
Investments in unconsolidated joint ventures	\$—	\$5,953	\$ 1,524,621	\$1,530,574	\$1,369,529
Loans held for investment	—	—	1,034,600	1,034,600	1,028,654
Liabilities					
Line of credit	\$—	\$138,500	\$ —	\$138,500	\$138,500
Secured financing	—	—	277,600	277,600	277,607
Convertible senior notes	208,000	—	—	208,000	200,000
December 31, 2012					
Assets					
Investments in unconsolidated joint ventures	\$—	\$20,667	\$ 910,450	\$931,117	\$877,081
Loans held for investment	—	—	335,734	335,734	333,569
Liabilities					
Line of credit	\$—	\$—	\$ —	\$—	\$—
Secured financing	—	—	108,090	108,090	108,167

The Company estimates the fair value of financial instruments carried at historical cost on a quarterly basis. These instruments are recorded at fair value only if they are impaired. No impairment was recognized during the years ended December 31, 2013, 2012 and 2011.

Fair values of loans receivable are estimated using inputs such as discounted cash flow projections, interest rates available for borrowers with similar credit metrics, market comparables, dealer quotes, and other quantitative and qualitative factors. Fair values of investments in unconsolidated joint ventures are primarily derived by applying the Company's ownership interest to the fair value of the underlying assets and liabilities of each joint venture. The Company's proportionate share of each joint venture's fair value approximates the Company's fair value of the investment, as the timing of cash flows of the joint venture does not deviate materially from the timing of cash flows the Company receives from the joint venture.

The fair values of the Company's secured financing and line of credit at December 31, 2013 and 2012 were estimated by discounting expected future cash outlays at current interest rates available for similar instruments. The fair value of convertible senior notes was determined using the last trade price in active markets on the balance sheet date.

The carrying values of interest receivable and accrued and other liabilities approximate their fair values due to their short term nature. Considerable judgment is necessary to interpret market data and develop estimated fair value. The use of different assumptions or methodologies could have a material effect on the estimated fair value amounts.

## 12. Stockholders' Equity

The Company's authorized capital stock consists of 50,000,000 shares of preferred stock, \$0.01 par value per share, and 450,000,000 shares of common stock, \$0.01 par value per share.

### Series A Preferred Stock

As of December 31, 2013 and 2012, the Company had 10,080,000 shares of its 8.5% Series A Cumulative Redeemable Perpetual Preferred Stock, par value \$0.01 per share ("Series A Preferred Stock"), issued and outstanding. In March 2012, the Company completed an underwritten public offering of 5,800,000 shares of its Series A Preferred Stock. The net offering proceeds, after deducting underwriting discounts and commissions and offering costs payable by the Company, were approximately \$140 million.

In July 2012, the Company completed an underwritten public offering of 4,280,000 shares of Series A Preferred Stock at a premium to par that translated to a strip yield of 8.3%. The net offering proceeds, after deducting underwriting discounts and commissions and offering costs payable by the Company, were approximately \$106 million. The Company used a portion of the net proceeds from both offerings to repay amounts outstanding under the line of credit at the time of each offering and the remaining proceeds to fund acquisitions of target assets.

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The Series A Preferred Stock must be paid a dividend at a rate of 8.5% per year on the \$25.00 liquidation preference before the common stock is entitled to receive any dividends. The Series A Preferred Stock is redeemable at \$25.00 per share plus accrued and unpaid dividends (whether or not declared) exclusively at the Company's option commencing on March 20, 2017 (subject to the Company's right under limited circumstances to redeem the Series A Preferred Stock earlier in order to preserve its qualification as a REIT or upon the occurrence of a change of control (as defined in the articles supplementary relating to the Series A Preferred Stock)). The Series A Preferred Stock is senior to the Company's common stock with respect to dividends and distributions, including distributions upon liquidation, dissolution or winding up. The Series A Preferred Stock generally does not have any voting rights, except if the Company fails to pay dividends on the Series A Preferred Stock for six or more quarterly periods (whether or not consecutive). Under such circumstances, the Series A Preferred Stock will be entitled to vote to elect two additional directors to the Company's board of directors, until all unpaid dividends have been paid or declared and set aside for payment. In addition, certain changes to the terms of the Series A Preferred Stock cannot be made without the affirmative vote of holders of at least two-thirds of the outstanding shares of Series A Preferred Stock voting separately as a class.

**Common Stock Offerings**

The following table summarizes the sales of the Company's common stock for the years ended December 31, 2013, 2012 and 2011:

	Number of Shares	Average Price per Share	Net Proceeds (in thousands) (1)
April 2011	15,350,000	\$18.50	\$271,707
September 2012	8,050,000	18.53	148,969
December 2012	11,500,000	19.29	221,348
January 2013	11,500,000	20.20	232,020
November 2013	10,000,000	20.21	201,758
At-the-market sales in 2013	1,901,755	21.65	40,765

(1) Net of underwriting discounts and commissions and offering costs payable by the Company

The Company used the net proceeds from the offerings to repay amounts outstanding under the line of credit at the time of the offering, fund acquisitions of target assets and for working capital and general corporate purposes.

**At-The-Market Stock Offering Program ("ATM Program")**

In May 2013, the Company entered into separate "at-the-market" equity distribution agreements with certain sales agents to offer and sell, from time to time, shares of its common stock having an aggregate offering price of up to \$200 million. Sales of the shares may be made in negotiated transactions and/or transactions that are deemed to be "at the market" offerings, including sales made by means of ordinary brokers' transactions, including directly on the New York Stock Exchange ("NYSE"), or sales made to or through a market maker other than on an exchange. The Company is required to pay each sales agent a commission not to exceed 2% of the gross sales proceeds for any common stock sold through such agent.

**2010 Private Placement**

In December 2010, the Company sold 2,750,000 shares of its common stock at a price per share of \$20.25 to certain institutional investors (the "Investors") in a private placement ("2010 Private Placement"), resulting in total proceeds of \$55.7 million. In connection with the 2010 Private Placement, the Investors were granted a right to participate in offerings of the Company's common stock or common stock equivalents that occurred on or before December 20, 2011, the one-year anniversary of the closing of the 2010 Private Placement (the "Participation Period"), subject to such Investors continuing to own the shares acquired in the 2010 Private Placement. The participation right allowed the Investors to maintain their percentage ownership interest in the Company calculated immediately prior to such offerings (subject to certain limitations). In addition, if any such offering during the Participation Period was for a per share price less than the then-prevailing adjusted purchase price (which was to be adjusted from time to time as a result of, among other things, special dividends, stock splits and other similar events), the Company was required to

make a payment to any Investors who continued to own shares acquired in the 2010 Private Placement to reduce the aggregate purchase price of the 2010 Private Placement to the subsequent offering price (“Anti-Dilution Purchase Price Adjustment”). The Anti-Dilution Purchase Price Adjustment was accounted for as a component of stockholders' equity, as it was not legally detachable or separately exercisable from the common stock sold in the private placement and met the criteria for equity classification.

As a result of the Company offering shares of its common stock in April 2011 at a per share price of \$18.50, the Company issued 175,000 shares of its common stock valued at \$18.50 per share and made an aggregate cash payment of \$162,500 to certain Investors for a total Anti-Dilution Purchase Price Adjustment of \$3.4 million. The increase in additional

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paid-in capital resulting from the issuance of 175,000 shares of common stock was fully offset by a corresponding decrease in additional paid-in capital related to the 2010 Private Placement.

**Shares Issued to Manager**

In November 2011, the Company issued 287,500 shares of its common stock to the Manager as reimbursement of its partial payment of initial underwriting discounts and commissions in connection with the Company's initial public offering ("IPO") in 2009. During the years ended December 31, 2012 and 2011, the Company issued 65,703 and 5,989 shares of its common stock, respectively, to the Manager in full payment of the incentive fees earned by the Manager (see Note 14).

**Dividend Reinvestment and Direct Stock Purchase Plan**

The Company's Dividend Reinvestment and Direct Stock Purchase Plan (the "DRIP Plan") provides existing common stockholders and other investors the opportunity to purchase shares (or additional shares, as applicable) of the Company's common stock by reinvesting some or all of the cash dividends received on their shares of the Company's common stock or making optional cash purchases within specified parameters. The DRIP Plan acquires shares either in the open market, directly from the Company as newly issued common stock, or in privately negotiated transactions with third parties. As of December 31, 2013, no shares had been acquired under the DRIP Plan from the Company in the form of new issuances.

**Common Stock Repurchases**

In August 2011, the board of directors authorized a common stock repurchase program pursuant to which the Company was authorized to repurchase up to \$50 million of its outstanding shares of common stock over a twelve-month period. During the year ended December 31, 2011, the Company repurchased 580,600 shares of its common stock at an aggregate cost of \$8.7 million including commissions, or a weighted-average cost of \$14.90 per share, in the open market. The program expired in August 2012. Repurchases of common stock reduce the common stock account for the par value and additional paid-in capital for the excess of cost over par value.

**Accumulated Other Comprehensive Income**

The following tables present the changes in each component of accumulated other comprehensive income attributable to the stockholders, net of immaterial tax effect:

(In thousands)	Equity in AOCI of Unconsolidated Joint Ventures	Unrealized Gain on Beneficial Interests in Debt Securities	Unrealized Gain on Fair Value of Cash Flow Hedge	Foreign Currency Translation Gain/Loss	Unrealized Gain/Loss on Fair Value of Net Investment Hedges	Total
Balance at December 31, 2010	\$ 1,410	\$—	\$—	\$(1,075 )	\$601	\$936
Other comprehensive (loss) income before reclassifications	(1,010 )	611	—	(3,159 )	1,192	(2,366 )
Amounts reclassified from accumulated other comprehensive income	(806 )	—	—	(94 )	—	(900 )
Net other comprehensive (loss) income	(1,816 )	611	—	(3,253 )	1,192	(3,266 )
Balance at December 31, 2011	(406 )	611	—	(4,328 )	1,793	(2,330 )
Other comprehensive income (loss) before reclassifications	7,135	266	—	905	(1,176 )	7,130
Amounts reclassified from accumulated other comprehensive income	—	—	—	356	28	384
Net other comprehensive income (loss)	7,135	266	—	1,261	(1,148 )	7,514

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Balance at December 31, 2012	6,729	877	—	(3,067	) 645	5,184
Other comprehensive income (loss) before reclassifications	9,787	(552	) (19	) 4,983	(3,846	) 10,353
Amounts reclassified from accumulated other comprehensive income	(12,895	) —	—	(67	) 18	(12,944 )
Net other comprehensive (loss) income	(3,108	) (552	) (19	) 4,916	(3,828	) (2,591 )
Balance at December 31, 2013	\$ 3,621	\$325	\$(19	) \$1,849	\$(3,183	) \$2,593

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Information about amounts reclassified out of accumulated other comprehensive income by component is presented below:

(In thousands)	Year Ended December 31,			Affected Line Item in the Consolidated Statements of Operations
Component of Accumulated Other Comprehensive Income	2013	2012	2011	
Equity in realized gain on sale of marketable securities of unconsolidated joint ventures	\$ 12,895	\$—	\$ 806	Equity in income of unconsolidated joint ventures
Net settlement loss on derivative instruments designated as net investment hedges	(18	) (28	) —	Other loss, net
Realized foreign exchange gain (loss)	67	(356	) 94	Other gain (loss), net

### 13. Earnings per Share

The following table provides the basic and diluted earnings per common share computations:

(In thousands, except share and per share data)	Year Ended December 31,		
	2013	2012	2011
Numerator:			
Net income	\$ 125,923	\$ 68,205	\$ 43,364
Net income attributable to noncontrolling interest	(24,158	) (6,194	) (1,104
Net income attributable to Colony Financial, Inc.	101,765	62,011	42,260
Preferred dividends	(21,420	) (13,915	) —
Net income attributable to common stockholders	80,345	48,096	42,260
Net income allocated to participating securities (nonvested shares)	(725	) (476	) (8
Numerator for basic net income allocated to common stockholders	79,620	47,620	42,252
Interest expense attributable to convertible senior notes	—	—	—
Numerator for diluted net income allocated to common stockholders	\$ 79,620	\$ 47,620	\$ 42,252
Denominator:			
Basic weighted average number of common shares outstanding	66,181,700	35,925,600	28,732,200
Weighted average effect of dilutive shares <sup>(1)</sup>	—	17,600	261,500
Diluted weighted average number of common shares outstanding	66,181,700	35,943,200	28,993,700
Earnings per share:			
Net income attributable to common stockholders per share—basic	\$ 1.20	\$ 1.33	\$ 1.47
Net income attributable to common stockholders per share—diluted	\$ 1.20	\$ 1.32	\$ 1.46

For the year ended December 31, 2013, excluded from the calculation of diluted income per share are 6,154,100 weighted average dilutive common share equivalents which represent the assumed dilutive effect of the Convertible Senior Notes as the effect of their inclusion would be antidilutive. For the years ended December 31, (1)2012 and 2011, weighted average dilutive shares represent the effect of shares of common stock issuable to the Manager for incentive fees due for the period. For the year ended December 31, 2011, weighted average dilutive shares also include the effect of shares of common stock issuable for reimbursement of the Manager's partial payment of underwriting discounts and commissions incurred in connection with the Company's IPO (see Note 12).

### 14. Related Party Transactions

#### Management Agreement

The Manager provides the day-to-day management of the Company's operations pursuant to a management agreement. The Manager is responsible for (1) selecting, purchasing and selling the Company's portfolio investments, (2) the

Company's financing activities and (3) providing investment advisory services. The management agreement requires the Manager to manage the Company's business affairs in conformity with the Company's investment guidelines and other policies that are approved and monitored by the Company's board of directors. The Manager's role is under the supervision and direction of the Company's board of directors. The initial term of the management agreement expired on September 29, 2012 (the third anniversary of the completion of the IPO) and automatically renews for one-year terms. The management agreement may be terminated upon at least 180 days' prior written notice to the Manager.

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**Base Management Fee**—The Manager earns a base management fee of 1.5% of stockholders’ equity, per annum. For purposes of calculating the base management fee, stockholders’ equity means: (a) the sum of (1) the net proceeds from all issuances of equity securities since inception (allocated on a pro rata basis for such issuances during the fiscal quarter of any such issuance), plus (2) retained earnings at the end of the most recently completed calendar quarter (as determined in accordance with GAAP, adjusted to exclude any non-cash equity compensation expense incurred in current or prior periods), less (b) any amount paid to repurchase the Company’s common stock since inception. The definition of stockholders’ equity also excludes (1) any unrealized gains or losses from mark-to-market valuation changes (other than permanent impairment) that have impacted stockholders’ equity as reported in the financial statements prepared in accordance with GAAP, (2) the effect of any gains or losses from one-time events pursuant to changes in GAAP, (3) non-cash items which in the judgment of management should not be included in Core Earnings (as defined below) and (4) the portion of the net proceeds of the IPO and the concurrent private placement that have not yet been initially invested in the Company’s target assets. For items (2) and (3), such exclusions shall only be applied after discussions between the Manager and the independent directors and after approval by a majority of the independent directors. As a result, stockholders’ equity, for purposes of calculating the management fee, could be greater or less than the amount of stockholders’ equity shown in the Company’s financial statements.

**Incentive Fees**—The Manager is entitled to an incentive fee with respect to each calendar quarter that the management agreement is in effect, in an amount not less than zero, equal to the difference between (1) the product of (x) 20% and (y) the difference between (i) Core Earnings (as defined below), on a rolling four-quarter basis and before the incentive fee for the current quarter, and (ii) the product of (A) the weighted average of the issue price per share of common stock in all of the Company’s offerings multiplied by the weighted average number of shares of common stock outstanding (including any restricted shares of common stock and any other shares of common stock underlying awards granted under our equity incentive plans, if any) in such four-quarter period and (B) 8%, and (2) the sum of any incentive fee paid to the Manager with respect to the first three calendar quarters of such previous four quarters; provided, however, that no incentive fee is payable with respect to any calendar quarter unless Core Earnings is greater than zero for the most recently completed 12 calendar quarters.

**Core Earnings** is a non-GAAP measure and is defined as GAAP net income (loss) excluding non-cash equity compensation expense, incentive fees, real estate depreciation and amortization and any unrealized gains or losses from mark-to-market valuation changes (other than permanent impairment) that are included in net income. The amount is adjusted to exclude one-time events pursuant to changes in GAAP and certain other non-cash items after discussions between the Manager and the Company’s independent directors and after approval by a majority of the Company’s independent directors.

The incentive fee is payable to the Manager quarterly in arrears in shares of the Company’s common stock, subject to certain ownership and NYSE limitations. The number of shares to be issued to the Manager is equal to the dollar amount of the portion of the quarterly installment of the incentive fee payable in shares divided by the average of the closing prices of the Company’s common stock on the NYSE for the five trading days prior to the date on which such quarterly installment is settled. The Company issued 65,703 and 5,989 shares of its common stock during the years ended December 31, 2012 and 2011, respectively, for incentive fees. No such shares were issued during the year ended December 31, 2013.

**Reimbursement of Expenditures**—Pursuant to the management agreement, the Company is required to reimburse the Manager for expenditures incurred by the Manager on behalf of the Company, including legal, accounting, financial, due diligence and other services, in amounts which are no greater than those which would be payable to third parties negotiated on an arm’s length basis. In addition, pursuant to a secondment agreement between the Company and Colony Capital, the Company is responsible for Colony Capital’s expenses incurred in employing the Company’s chief financial officer/chief operating officer. The Company also reimburses Colony Capital for its pro rata portion of overhead expenses incurred by Colony Capital and its affiliates, including the Manager, based upon the ratio of the Company’s assets to all Colony Capital-managed assets.

**Cost Reimbursement for Asset Management Services**

Colony AMC Milestone West, LLC (“AMC Milestone West”) and Colony AMC Milestone North, LLC (“AMC Milestone North”), each a wholly-owned subsidiary of the Company, provide asset management services to two joint

ventures with the FDIC (“FDIC Ventures”) for which certain of our unconsolidated joint ventures are managing members. The FDIC Ventures pay an annual 50-basis point asset management fee calculated on the aggregate UPB of each respective loan portfolio. In addition, one of the unconsolidated joint ventures reimburses AMC Milestone North for any expenses not covered by the 50-basis point fee. Asset management fees and expense reimbursements were \$1.3 million, \$2.0 million and \$2.0 million for the years ended December 31, 2013, 2012 and 2011, respectively. Pursuant to a cost allocation arrangement, the Company reimburses an affiliate of the Manager for compensation, overhead and direct costs incurred by the affiliate related to providing asset management services. The Company reimbursed the affiliate \$0.8 million, \$1.1 million and \$1.2 million for the years ended December 31, 2013, 2012 and 2011, respectively.

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### Reimbursement of Manager's Partial Payment of Initial Underwriting Discounts and Commissions

In connection with the IPO and the underwriters' exercise of the overallotment option, the underwriters deferred \$5.75 million of underwriting discounts and commissions and the Manager paid the underwriters \$5.75 million of underwriting discounts and commissions on the Company's behalf. Pursuant to the underwriting agreement entered into in connection with the IPO, the Company was required to pay the underwriters the deferred underwriting discounts and commissions in cash if, during any full four calendar quarter period during the 24 full calendar quarters after the consummation of the IPO, the Company's Core Earnings (as defined above) for any such four-quarter period exceeded the product of (1) the weighted average of the issue price per share of common stock in all offerings multiplied by the weighted average number of shares of common stock outstanding (including any restricted shares of common stock and any other shares of common stock underlying awards granted under equity incentive plans, if any) in such four-quarter period and (2) 8%. Additionally, pursuant to the management agreement, the Company was required to reimburse the Manager for its partial payment of initial underwriting discounts and commissions if the same 8% performance threshold was met. At the time of the IPO, the Company had recorded a deferred liability and a reduction of additional paid-in capital as the Company determined the likelihood of payment of both amounts to be probable.

For the four calendar quarter period ended September 30, 2011, the Company's Core Earnings exceeded the 8% performance threshold. In November 2011, the Company settled both deferred amounts with a cash payment of \$5.75 million to the underwriters and, pursuant to the management agreement, payment in the form of 287,500 shares of the Company's common stock (the reimbursement amount divided by the initial public offering price per share) to the Manager.

### Investment Allocation Agreement

The Company, the Manager and Colony Capital entered into an investment allocation agreement which provides for the Company to co-invest with certain current or future private investment funds or other investment vehicles managed by Colony Capital or its affiliates to make investments in the Company's target assets. Under the investment allocation agreement, the Company is entitled (but not obligated) to contribute (subject to the Company's investment guidelines, its availability of capital and maintaining its qualification as a REIT for U.S. federal income tax purposes and its exemption from registration under the Investment Company Act of 1940) at least one-half the capital to be funded by co-investment vehicles in assets secured by U.S. collateral (or at least one-third for assets secured by non-U.S. collateral). In the event that the Company does not have sufficient capital to contribute its full entitlement of the capital required for any proposed investment by such investment vehicles, the investment allocation agreement provides for a fair and equitable allocation of investment opportunities among all such vehicles and the Company, in each case, taking into account the suitability of each investment opportunity for the particular vehicle and the Company and each such vehicle's and the Company's availability of capital for investment.

The Company does not incur any additional fees payable to Colony Capital, the Manager or any of their affiliates in connection with investments made pursuant to the investment allocation agreement. The Company is required to pay its pro rata portion (based upon percentage of equity) of transaction and other investment-level expenses incurred in connection with such co-investments.

The following table summarizes the amounts incurred by the Company and payable to the Manager or its affiliates for the periods presented:

(In thousands)	Year Ended December 31,		
	2013	2012	2011
Base management fees	\$22,265	\$12,332	\$8,128
Incentive fees	—	936	349
Compensation pursuant to secondment agreement	1,286	1,207	1,248
Allocated and direct investment-related expenses	1,771	1,657	1,719
Allocated and direct administrative expenses	1,787	1,253	344
	\$27,109	\$17,385	\$11,788

The following table summarizes the amounts due to the Manager or its affiliates as of each balance sheet date:

December 31,

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(In thousands)	2013	2012
Base management fees	\$6,045	\$3,932
Secondment reimbursement	895	844
Reimbursement of direct and allocated administrative and investment costs	1,046	208
	\$7,986	\$4,984

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### 15. Share-Based Payments

#### Director Stock Plan

The Company's 2009 Non-Executive Director Stock Plan (the "Director Stock Plan") provides for the grant of restricted stock, restricted stock units and other stock-based awards to its non-executive directors. The maximum number of shares of stock reserved under the Director Stock Plan is 100,000. The individual share awards generally vest 1 year from the date of grant.

#### Equity Incentive Plan

The Company's 2011 Equity Incentive Plan (the "Equity Incentive Plan") provides for the grant of options to purchase shares of common stock, share awards (including restricted stock and stock units), stock appreciation rights, performance awards and annual incentive awards, dividend equivalent rights, long-term incentive units, cash and other equity-based awards. Certain named executive officers of the Company, other eligible employees, directors and service providers, including the Manager and employees of the Manager, are eligible to receive awards under the Equity Incentive Plan. The Company has reserved a total of 1,600,000 shares of common stock for issuance pursuant to the Equity Incentive Plan, subject to certain adjustments set forth in the plan. The share awards granted under this plan generally vest over a 3-year period from the date of grant.

A summary of the Company's vested and nonvested shares under the Director Stock Plan and Equity Incentive Plan for the year ended December 31, 2013 is presented below:

	Restricted Stock Grants to Non-Executive Directors	Restricted Stock Grants to Employee	Restricted Stock Grants to the Manager or Manager's Employees	Total	Weighted Average Grant Date Fair Value
Nonvested shares at December 31, 2012	8,274	17,172	496,749	522,195	18.17
Granted	6,837	—	—	6,837	21.94
Vested	(8,274 )	—	—	(8,274 )	16.32
Forfeited	—	—	(7,990 )	(7,990 )	16.16
Nonvested shares at December 31, 2013	6,837	17,172	488,759	512,768	18.28
Weighted average grant date fair value per share for shares granted during the year ended December 31, 2013	\$ 21.94	n/a	n/a		

The following table summarizes the components of share-based compensation included in the consolidated statements of operations:

	Year Ended December 31,		
(In thousands, except per share amounts)	2013	2012	2011
Share-based compensation included in management fees	\$3,998	\$5,714	\$—
Share-based compensation included in administrative expenses	285	419	116
Total fair value of shares vested <sup>(1)</sup>	182	6,079	82
Weighted average grant date fair value per share for shares granted during the period <sup>(1)</sup>	21.94	17.79	17.26

<sup>(1)</sup> Based on the quoted closing share price of the Company's common stock on the NYSE on grant date or vesting date.

As of December 31, 2013, aggregate unrecognized compensation cost related to restricted stock granted under the Director Stock Plan and Equity Incentive Plan was approximately \$6.1 million. That cost is expected to be fully recognized over a weighted-average period of 20 months.

### 16. Income Taxes

The Company's TRSs are subject to corporate level federal, state, foreign and local income taxes. The following is a summary of the Company's income tax provision:

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(In thousands)	Year Ended December 31,		
	2013	2012	2011
Current			
Federal	\$1,470	\$2,242	\$1,444
State	671	669	252
Total current tax provision	2,141	2,911	1,696
Deferred			
Federal	(1,115)	(661)	(431)
State	(367)	(85)	(74)
Total deferred tax (benefit) provision	(1,482)	(746)	(505)
Total income tax provision	\$659	\$2,165	\$1,191

Deferred tax assets of \$2.4 million and \$1.2 million are included in other assets as of December 31, 2013 and 2012, respectively. Deferred tax assets and liabilities arise from temporary differences in income recognition for GAAP and tax purposes and the tax effect of net foreign currency translation gains and losses on certain investments in unconsolidated joint ventures held in TRSs.

The following table summarizes the income tax treatment of dividends declared for the years ended December 31, 2013, 2012 and 2011:

	Year Ended December 31,		
	2013	2012	2011
Common Stock:			
Ordinary income per share	\$0.98	\$0.83	\$1.00
Long-term capital gains per share	0.42	0.61	0.31
Total dividends declared per share	\$1.40	\$1.44	\$1.31
Series A Preferred Stock:			
Ordinary income per share	\$1.48	\$1.01	\$—
Long-term capital gains per share	0.65	0.74	—
Total dividends declared per share	\$2.13	\$1.75	\$—

## 17. Commitments and Contingencies

Pursuant to the operating agreements of certain unconsolidated joint ventures, the joint venture partners may be required to fund additional amounts for future investments, unfunded lending commitments, ordinary operating costs, guaranties or commitments of the joint ventures. As of December 31, 2013, the Company's share of those commitments was \$8.5 million.

The Company may be required to fund additional amounts to borrowers pursuant to certain loan agreements. As of December 31, 2013, the Company had combined unfunded lending commitments of \$17.3 million.

In connection with financing arrangements for certain unconsolidated joint ventures, the Company provided customary non-recourse carve-out guaranties. The Company believes that the likelihood of making any payments under the guaranties is remote, and has not accrued for a guaranty liability as of December 31, 2013.

In the ordinary course of business, the Company may be involved in litigation which may result in legal costs and liability that could have a material effect on the Company's financial position and results of operations. At December 31, 2013, the Company was not involved in such litigation.

## 18. Segment Information

The Company's chief operating decision maker reviews various key financial measures to assess the performance and financial condition of each segment. Segment profit or loss is evaluated based upon income before income taxes, which includes equity in income of unconsolidated joint ventures, interest income and other income, less investment-specific expenses, including interest and asset management costs, as well as other gains or losses. Non-investment-specific income and expenses, such as interest income on cash and cash equivalents, management

fees, interest expense on the line of credit and administrative expenses, are not allocated to specific segments. There is no intersegment activity. The Company's segment

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disclosures present the measures used by the chief operating decision maker for purposes of assessing each segment's performance.

The operating results for each of the reportable segments are summarized below, including the reclassification of operating results of the other real estate equity segment for prior periods to conform to the current period presentation:

(In thousands)	Real Estate Debt Investments	Single-Family Residential Rentals	Other Real Estate Equity Investments	Amounts Not Allocated to Segments	Total
Year Ended December 31, 2013					
Income:					
Equity in income (loss) of unconsolidated joint ventures	\$ 89,553	\$ (8,013 )	\$ 19,168	\$ —	\$ 100,708
Interest income	77,193	—	—	282	77,475
Rental income and tenant reimbursements	—	—	789	—	789
Other income from affiliates	1,267	—	—	—	1,267
Total income	168,013	(8,013 )	19,957	282	180,239
Expenses:					
Management fees	—	—	—	26,263	26,263
Investment and servicing expenses	2,247	—	26	955	3,228
Interest expense	5,295	—	227	13,316	18,838
Property operating expenses	—	—	197	—	197
Administrative expenses	178	—	—	7,370	7,548
Depreciation and amortization	—	—	310	—	310
Transaction costs	1,210	—	597	—	1,807
Total expenses	8,930	—	1,357	47,904	58,191
Realized gain on resolution of loans receivable	4,578	—	—	—	4,578
Other loss, net	(44 )	—	—	—	(44 )
Income (loss) before income taxes	163,617	(8,013 )	18,600	(47,622 )	126,582
Income tax provision	—	—	—	659	659
Net income (loss)	163,617	(8,013 )	18,600	(48,281 )	125,923
Net income attributable to noncontrolling interests	22,892	—	1,266	—	24,158
Net income (loss) attributable to Colony Financial, Inc.	\$ 140,725	\$ (8,013 )	\$ 17,334	\$ (48,281 )	\$ 101,765

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(In thousands)	Real Estate Debt Investments	Single-Family Residential Rentals	Other Real Estate Equity Investments	Amounts Not Allocated to Segments	Total
Year Ended December 31, 2012					
Income:					
Equity in income (loss) of unconsolidated joint ventures	\$ 60,313	\$ (2,126 )	\$ 10,550	\$ —	\$ 68,737
Interest income	36,275	—	—	170	36,445
Other income from affiliates	1,973	—	—	—	1,973
Total income	98,561	(2,126 )	10,550	170	107,155
Expenses:					
Management fees	—	—	—	18,982	18,982
Investment and servicing expenses	2,457	—	22	498	2,977
Interest expense	4,409	—	—	3,839	8,248
Administrative expenses	—	—	—	6,346	6,346
Total expenses	6,866	—	22	29,665	36,553
Realized gain on resolution of loans receivable	808	—	—	—	808
Other loss, net	(1,040 )	—	—	—	(1,040 )
Income (loss) before income taxes	91,463	(2,126 )	10,528	(29,495 )	70,370
Income tax provision	—	—	—	2,165	2,165
Net income (loss)	91,463	(2,126 )	10,528	(31,660 )	68,205
Net income attributable to noncontrolling interests	6,194	—	—	—	6,194
Net income (loss) attributable to Colony Financial, Inc.	\$ 85,269	\$ (2,126 )	\$ 10,528	\$ (31,660 )	\$ 62,011
(In thousands)	Real Estate Debt Investments	Single-Family Residential Rentals	Other Real Estate Equity Investments	Amounts Not Allocated to Segments	Total
Year Ended December 31, 2011					
Income:					
Equity in income (loss) of unconsolidated joint ventures	\$ 38,602	\$ —	\$ 8,118	\$ —	\$ 46,720
Interest income	16,463	—	—	312	16,775
Other income from affiliates	1,974	—	—	—	1,974
Total income	57,039	—	8,118	312	65,469
Expenses:					
Management fees	—	—	—	8,477	8,477
Investment and servicing expenses	2,117	—	—	676	2,793
Interest expense	702	—	—	2,309	3,011
Administrative expenses	—	—	—	5,780	5,780
Total expenses	2,819	—	—	17,242	20,061
Other loss, net	(853 )	—	—	—	(853 )
Income (loss) before income taxes	53,367	—	8,118	(16,930 )	44,555
Income tax provision	—	—	—	1,191	1,191
Net income (loss)	53,367	—	8,118	(18,121 )	43,364
Net income attributable to noncontrolling interests	1,104	—	—	—	1,104

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Net income (loss) attributable to Colony Financial, Inc.	\$52,263	\$ —	\$ 8,118	\$ (18,121 )	\$42,260
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The net investments in each of the reportable segments are summarized as follows:

(In thousands)	December 31, 2013	December 31, 2012
Assets:		
Real estate debt investments	\$1,707,228	\$939,448
Single-family residential rentals	530,007	251,501
Other real estate equity investments	344,244	70,496
Other assets not allocated to segments	47,073	174,122
Total consolidated assets	\$2,628,552	\$1,435,567

## 19. Selected Quarterly Financial Information (Unaudited)

The following is a summary of quarterly results of operations for the years ended December 31, 2013 and 2012:

(In thousands, except per share data)	2013 Quarter Ended				2012 Quarter Ended			
	Dec 31	Sep 30	Jun 30	Mar 31	Dec 31	Sep 30	Jun 30	Mar 31
Equity in income of unconsolidated joint ventures	\$30,862	\$25,052	\$22,992	\$21,802	\$21,464	\$15,838	\$15,994	\$15,441
Interest income	26,486	22,122	17,455	11,412	10,752	10,816	9,051	5,826
Rental income and tenant reimbursements	789	—	—	—	—	—	—	—
Other income from affiliates	283	296	317	371	458	396	569	550
Total income	58,420	47,470	40,764	33,585	32,674	27,050	25,614	21,817
Management fees	6,951	6,520	6,422	6,370	6,706	3,812	3,944	4,520
Other expenses	12,167	7,861	7,094	4,806	4,662	4,583	4,398	3,928
Total expenses	19,118	14,381	13,516	11,176	11,368	8,395	8,342	8,448
Other (loss) gain, net	(19 )	860	3,756	(63 )	603	(331 )	(276 )	(228 )
Income tax provision (benefit)	79	(14 )	242	352	764	596	441	364
Net income	39,204	33,963	30,762	21,994	21,145	17,728	16,555	12,777
Net income attributable to noncontrolling interest	8,946	7,514	5,111	2,587	2,261	2,170	1,454	309
Net income attributable to Colony Financial, Inc.	30,258	26,449	25,651	19,407	18,884	15,558	15,101	12,468
Preferred dividends	5,355	5,355	5,355	5,355	5,355	5,102	3,082	376
Net income attributable to common stockholders	\$24,903	\$21,094	\$20,296	\$14,052	\$13,529	\$10,456	\$12,019	\$12,092
Net income per common share—basic	\$0.34	\$0.32	\$0.31	\$0.22	\$0.31	\$0.30	\$0.36	\$0.37
Net income per common share—diluted	\$0.34	\$0.32	\$0.31	\$0.22	\$0.31	\$0.30	\$0.36	\$0.37

## 20. Subsequent Events

On January 28, 2014, the Company issued \$230.0 million of its convertible senior notes due on January 15, 2021, resulting in net proceeds of approximately \$223.9 million to the Company after deducting underwriting discounts and commissions and estimated offering expenses payable by the Company. The convertible notes bear interest at a rate equal to 3.875% per annum payable semiannually in arrears on January 15 and July 15 of each year, beginning on July 15, 2014. The Company used a portion of the net proceeds to repay amounts outstanding under its secured revolving credit facility, and intends to use the remainder to acquire its target assets and for general corporate purposes.

Subsequent to the year end, the Company sold 405,899 shares of its common stock under the ATM Program for net offering proceeds of \$8.5 million after deducting commissions.

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In January 2014, the Company awarded 500,000 restricted shares of its common stock to the Manager under the Equity Incentive Plan. The award vests over a 3-year period as follows: 25% on grant date and 25% on each of the three anniversaries of the grant date.

In February 2014, the Company entered into a master repurchase agreement with a commercial bank to partially finance loans within its Transitional CRE Lending Platform. The repurchase facility provides up to \$150 million of financing for eligible assets within the Transitional CRE Lending Platform and has an initial term of two years, plus a one-year extension option. Advances under the repurchase agreement will bear interest ranging from LIBOR plus a spread of 2.25% to 2.5%.

Subsequent to the year end, the Company invested \$45.8 million in one new investment and a combined \$69.1 million in four new loan originations in the Transitional CRE Lending Platform.

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Colony Financial, Inc.

Schedule IV—Mortgage Loans on Real Estate

December 31, 2013

(Amounts in thousands)

Loan / Collateral Description / Location	Prior Liens <sup>(1)</sup>	Payment Terms <sup>(2)</sup>	Principal	Carrying Amount	Interest Rate	Maturity Date
First mortgages:						
Assisted Living - Dallas, TX	\$—	P&I	\$3,207	\$3,002	6.03 %	November 2024
Assisted Living - Kennewick, WA	—	P&I	10,875	9,973	6.07 %	January 2017
Hospitality - HI/NY	—	I/O	38,097	37,785	10.75 %	September 2016
Hospitality - North America	—	P&I	150,867	(3) 126,288	8.57 %	July 2014
Independent Living - Florissant, MO	—	P&I	9,277	8,655	5.95 %	June 2016
Multifamily - Phoenix, AZ	—	P&I	6,858	6,590	4.88 %	September 2014
Multifamily - Tucson, AZ	—	I/O	29,700	26,504	5.98 %	May 2037
Multifamily - Tucson, AZ	—	I/O	3,100	2,166	6.09 %	December 2032
Multifamily - El Cajon, CA	—	P&I	4,574	4,092	3.09 %	December 2015
Multifamily - Riverside, CA	—	P&I	7,677	7,189	5.58 %	December 2015
Multifamily - Branford, CT	—	P&I	18,000	16,416	4.16 %	January 2019
Multifamily - Gainesville, FL	—	P&I	7,101	6,680	5.90 %	June 2019
Multifamily - Jacksonville, FL	—	P&I	5,543	5,232	6.08 %	December 2015
Multifamily - Stockbridge, GA	—	P&I	6,360	6,074	5.43 %	April 2015
Multifamily - Niles, MI	—	P&I	1,224	1,198	8.05 %	November 2015
Multifamily - Gulfport, MS	—	I/O	9,500	9,417	6.17 %	January 2016
Multifamily - City Of Keene, NH	—	P&I	2,582	2,464	6.63 %	November 2023
Multifamily - Orange, NJ	—	P&I	3,087	3,004	6.40 %	July 2034
Multifamily - Las Vegas, NV	—	P&I	8,683	8,266	5.60 %	December 2020
Multifamily - Bronx, NY	—	I/O	1,399	1,343	5.19 %	January 2015
Multifamily - Columbus, OH	—	P&I	5,599	4,943	6.11 %	August 2018
Multifamily - Collegeville, PA	—	I/O	11,000	9,949	4.20 %	September 2022
Multifamily - Charleston, SC	—	P&I	1,540	1,453	6.11 %	December 2020
Multifamily - Houston, TX	—	P&I	7,901	7,418	5.20 %	September 2015
Multifamily - Houston, TX	—	P&I	2,762	2,377	4.66 %	July 2017
Multifamily - Gillette, WY	—	P&I	18,166	16,916	5.26 %	April 2019
Office - Ann Arbor, MI	—	I/O	10,425	10,338	7.17 %	November 2015
Office - Madrid, Spain <sup>(5)</sup>	—	P&I	91,972	55,979	1.14 %	August 2017
Office - Madrid, Spain <sup>(5)</sup>	—	P&I	17,782	8,623	1.67 % <sup>(4)</sup>	February 2015
Office - Chattanooga, TN	—	I/O	11,300	11,211	6.67 %	January 2017
Other - Elkridge, MD	—	I/O	11,550	11,444	7.42 %	October 2016
Retail - Jonesboro, AR	—	I/O	11,200	11,110	7.42 %	November 2015
Retail - Leominster, MA	—	I/O	32,650	32,290	6.17 %	June 2016
Retail - Murcia, Spain <sup>(5)</sup>	—	P&I	183,727	105,397	1.39 %	August 2016
Student Housing - Georgetown , MI	—	P&I	4,412	3,921	3.49 %	March 2016
Student Housing - Beaumont, TX	—	P&I	9,135	8,302	3.46 %	October 2015
Subordinated debt and mezzanine:						
Healthcare - CA	32,607	P&I	89,669	89,064	9.32 %	December 2017

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Hospitality - USA	770,000	I/O	330,909	328,185	10.97	% <sup>(4)</sup>	June 2016
Mixed use - New York, NY	25,252	P&I	14,400	14,394	20.92	%	March 2016
Multifamily - Phoenix, AZ	—	P&I	2,654	1,767	5.60	%	September 2014
Multifamily - City of Keene, NH	—	P&I	1,300	1,235	6.43	%	November 2023
	\$827,859		\$1,197,764	\$1,028,654			

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- (1) Prior liens represent loan amounts owned by third parties that are senior to the Company's subordinated or mezzanine positions and are approximate.
- (2) P&I = principal and interest; I/O = interest only
- (3) Includes \$11.5 million credit available to borrower upon full payoff
- (4) The loan is composed of multiple promissory notes. The interest rate is a blended weighted average rate calculated based upon the outstanding principal and interest rate on each note.
- (5) Loans denominated in Euro are translated at the spot rate of exchange as of December 31, 2013.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

COLONY FINANCIAL, INC.

Dated: February 27, 2014

By: /S/ DARREN J. TANGEN  
Darren J. Tangen  
Chief Operating Officer, Chief Financial Officer and  
Treasurer  
(Principal Financial Officer and Principal Accounting  
Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/S/ THOMAS J. BARRACK, JR. Thomas J. Barrack, Jr.	Executive Chairman of the Board of Directors	February 27, 2014
/S/ RICHARD B. SALTZMAN Richard B. Saltzman	Chief Executive Officer and President and Director (Principal Executive Officer)	February 27, 2014
/S/ DARREN J. TANGEN Darren J. Tangen	Chief Operating Officer, Chief Financial Officer and Treasurer (Principal Financial Officer and Principal Accounting Officer)	February 27, 2014
/S/ GEORGE G. C. PARKER George G. C. Parker	Director	February 27, 2014
/S/ JOHN A. SOMERS John A. Somers	Director	February 27, 2014
/S/ JOHN L. STEFFENS John L. Steffens	Director	February 27, 2014

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EXHIBIT INDEX

Exhibit Number	Description
3.1	Articles of Amendment and Restatement of Colony Financial, Inc. (incorporated by reference to Exhibit 3.1 to Amendment No. 5 to the Company's Registration Statement on Form S-11 (No. 333-160323) filed on September 23, 2009)
3.2	Articles Supplementary designating Colony Financial, Inc.'s 8.50% Series A Cumulative Redeemable Perpetual Preferred Stock, liquidation preference \$25.00 per share, par value \$0.01 per share (incorporated by reference to Exhibit 3.2 to the Company's Form 8-A filed on March 20, 2012)
3.3	Articles Supplementary Establishing Additional Shares of 8.50% Series A Cumulative Redeemable Perpetual Preferred Stock (incorporated by reference to Exhibit 3.1 to the Company's Current Report on Form 8-K filed on July 16, 2012)
3.4	Second Amended and Restated Bylaws of Colony Financial, Inc. (incorporated by reference to Exhibit 3.1 to the Company's Current Report on Form 8-K filed on March 8, 2013)
4.1	Specimen Common Stock Certificate of Colony Financial, Inc. (incorporated by reference to Exhibit 4.1 to Amendment No. 4 to the Company's Registration Statement on Form S-11 (No. 333-160323) filed on September 18, 2009)
4.2	Form of stock certificate evidencing the 8.50% Series A Cumulative Redeemable Perpetual Preferred Stock, liquidation preference \$25.00 per share, par value \$0.01 per share (incorporated by reference to Exhibit 4.1 to the Company's Form 8-A filed on March 20, 2012)
4.3	Indenture, dated as of April 10, 2013, between the Company and the Bank of New York Mellon, as trustee (incorporated by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K filed on April 10, 2013)
4.4	First Supplemental Indenture to the Indenture dated as of April 10, 2013 between the Company and the Bank of New York Mellon, as trustee (incorporated by reference to Exhibit 4.2 to the Company's Current Report on Form 8-K filed on April 10, 2013)
4.5	Second Supplemental Indenture, dated as of January 28, 2014, between the Company and The Bank of New York Mellon, as trustee (incorporated by reference to Exhibit 4.2 to the Company's Current Report on Form 8-K filed on January 23, 2014)
10.1	Private Placement Purchase Agreement between the Company and the persons listed on Schedule A thereto (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q filed on November 12, 2009)
10.2	Registration Rights Agreement by and among the Company and the persons listed on Schedule A thereto (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q filed on November 12, 2009)
10.3	Investment Allocation Agreement among Colony Financial, Inc., Colony Capital, LLC and Colony Financial Manager, LLC (incorporated by reference to Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q filed on November 12, 2009)
10.4	License Agreement between Colony Financial, Inc. and New Colony Investors, LLC regarding use of the Colony name (incorporated by reference to Exhibit 10.5 to the Company's Quarterly Report on Form 10-Q filed on November 12, 2009)
10.5*	Indemnification Agreement by and between Colony Financial, Inc. and Thomas J. Barrack, Jr. (incorporated by reference to Exhibit 10.7 to the Company's Quarterly Report on Form 10-Q filed on November 12, 2009)
10.6*	Indemnification Agreement by and between Colony Financial, Inc. and Richard B. Saltzman (incorporated by reference to Exhibit 10.8 to the Company's Quarterly Report on Form 10-Q filed on November 12, 2009)
10.7*	Indemnification Agreement by and between Colony Financial, Inc. and Darren J. Tange (incorporated by reference to Exhibit 10.9 to the Company's Quarterly Report on Form 10-Q filed on November 12, 2009)
10.8*	

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- Indemnification Agreement by and between Colony Financial, Inc. and Kevin P. Traenkle (incorporated by reference to Exhibit 10.10 to the Company's Quarterly Report on Form 10-Q filed on November 12, 2009)
- 10.9\* Indemnification Agreement by and between Colony Financial, Inc. and Ronald M. Sanders (incorporated by reference to Exhibit 10.11 to the Company's Quarterly Report on Form 10-Q filed on November 12, 2009)
- 10.10\* Indemnification Agreement by and between Colony Financial, Inc. and Mark M. Hedstrom (incorporated by reference to Exhibit 10.12 to the Company's Quarterly Report on Form 10-Q filed on November 12, 2009)
- 10.11\* Indemnification Agreement by and between Colony Financial, Inc. and George G. C. Parker (incorporated by reference to Exhibit 10.13 to the Company's Quarterly Report on Form 10-Q filed on November 12, 2009)
- 10.12\* Indemnification Agreement by and between Colony Financial, Inc. and John A. Somers (incorporated by reference to Exhibit 10.14 to the Company's Quarterly Report on Form 10-Q filed on November 12, 2009)
- 10.13\* Indemnification Agreement by and between Colony Financial, Inc. and John L. Steffens (incorporated by reference to Exhibit 10.15 to the Company's Quarterly Report on Form 10-Q filed on November 12, 2009)
- 10.14\* 2009 Non-Executive Director Stock Plan of Colony Financial, Inc. (incorporated by reference to Exhibit 10.1 to the Company's Registration Statement on Form S-8 filed on September 29, 2009)
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Exhibit Number	Description
10.15*	Form of Restricted Stock Award Agreement for Non-Executive Directors (incorporated by reference to Exhibit 10.9 to Amendment No. 5 to the Company's Registration Statement on Form S-11 (No. 333-160323) filed on September 23, 2009)
10.16*	Form of Stock Option Award Agreement for Non-Executive Directors (incorporated by reference to Exhibit 10.13 to Amendment No. 4 to the Company's Registration Statement on Form S-11 (No. 333-160323) filed on September 18, 2009)
10.17	Securities Purchase Agreement, dated December 20, 2010, among Colony Financial, Inc. and the Investors named therein (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed on December 21, 2010)
10.18	Registration Rights Agreement, dated December 20, 2010, among Colony Financial, Inc. and the Investors named therein (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K filed on December 21, 2010)
10.19	Credit Agreement, dated as of August 6, 2013, among Colony Financial, Inc., the several banks and other financial institutions or entities from time to time parties thereto and JPMorgan Chase Bank, N.A., as administrative agent (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed on August 8, 2013)
10.20*	Form of Restricted Stock Award Agreement under the Colony Financial, Inc. 2011 Equity Incentive Plan (incorporated by reference to Exhibit 10.5 to the Company's Quarterly Report on Form 10-Q filed on November 9, 2011)
10.21*	Form of Non-Qualified Stock Option Award Agreement under the Colony Financial, Inc. 2011 Equity Incentive Plan (incorporated by reference to Exhibit 10.6 to the Company's Quarterly Report on Form 10-Q filed on November 9, 2011)
10.22	Second Amended and Restated Management Agreement, dated as of March 6, 2013, by and among Colony Financial, Inc., Colony Financial TRS, LLC and Colony Financial Manager, LLC (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed on March 8, 2013)
10.23*	Amended and Restated Secondment Agreement by and between Colony Financial, Inc. and Colony Capital, LLC (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed on March 26, 2012)
10.24*	Amended and Restated 2011 Equity Incentive Plan (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q filed on May 8, 2012)
10.25	Partnership Subscription Agreement for Purchase of An Associate General Partnership Interest in CSFR Operating Partnership, L.P. dated as of July 31, 2012 (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q filed on November 9, 2012)
10.26	Uncommitted Master Repurchase Agreement, dated as of February 5, 2014, between CMC Loan Funding A, LLC, as seller, and JPMorgan Chase Bank, National Association, as buyer (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed on February 10, 2014)
10.27	Guarantee Agreement, dated as of February 5, 2014, made by Colony Financial, Inc., as guarantor, in favor of JPMorgan Chase Bank, National Association, as buyer (incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K filed on February 10, 2014)
12.1**	Computation of Ratio of Earnings to Fixed Charges and to Combined Fixed Charges and Preferred Dividends
21.1**	List of Subsidiaries of Colony Financial, Inc.
23.1**	Consent of Ernst & Young LLP
31.1**	Certification of Richard B. Saltzman, President and Chief Executive Officer, pursuant to Rule 13a-14(a)/15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2**	Certification of Darren J. Tangen, Chief Operating officer, Chief Financial Officer and Treasurer, pursuant to Rule 13a-14(a)/15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1**	

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Certification of Richard B. Saltzman, President and 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 Darren J. Tangen, Chief Operating officer, Chief Financial Officer and Treasurer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Financial statements from the Annual Report on Form 10-K of Colony Financial, Inc. for the year ended December 31, 2013, formatted in XBRL (eXtensible Business Reporting Language): (1) Consolidated

101\*\* Balance Sheets, (2) Consolidated Statements of Operations, (3) Consolidated Statements of Comprehensive Income, (4) Consolidated Statements of Equity, (5) Consolidated Statements of Cash Flows and (6) Notes to Consolidated Financial Statements.

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\* Denotes a management contract or compensatory, plan contract or arrangement.

\*\* Filed herewith