CHIMERA INVESTMENT CORP
Form 10-K
March 08, 2013

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-K

(MARK ONE)

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

FOR THE FISCAL YEAR ENDED: DECEMBER 31, 2011

OR

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

FOR THE TRANSITION PERIOD FROM TO

COMMISSION FILE NUMBER: 1-33796

CHIMERA INVESTMENT CORPORATION
(Exact Name of Registrant as Specified in its Charter)

MARYLAND (State or other jurisdiction of incorporation of organization)	26-0630461 (I.R.S. Employer Identification Number)
1211 Avenue of the Americas, Suite 2902 New York, New York (Address of Principal Executive Offices)	10036 (Zip Code)

(646) 454-3759
(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, par value $.01 per share	New York Stock Exchange

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

None.

Indicate by check mark whether the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No X

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

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 X

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes____ No_X___

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. x

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 "accelerated filer, large accelerated filer and smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one): Large accelerated filer X Accelerated filer __ Non-accelerated filer __ 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 X .

At June 30, 2012, the aggregate market value of the voting stock held by non-affiliates of the Registrant was $2,321,709,293 based on the closing sale price on the New York Stock Exchange on that date.

The number of shares of the Registrant's Common Stock outstanding on December 31, 2012 was 1,027,597,458.

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Explanatory Note

Restatement Overview

In this Annual Report on Form 10-K for the year ended December 31, 2011 (the "2011 Form 10-K"), Chimera Investment Corporation is restating its previously issued (i) consolidated statement of financial condition included in its Annual Report on Form 10-K as of December 31, 2010 and (ii) consolidated statements of operations and comprehensive income (loss), consolidated statements of changes in stockholders' equity, and consolidated statements of cash flows for the years ending December 31, 2010 and 2009, including the cumulative effect of the restatement on retained earnings (accumulated deficit) as of the earliest period presented (the "Restatement"). We do not plan to file an amended version of any previously filed reports on Forms 10-K or 10-Q in connection with the Restatement.

The Restatement also impacted each of the quarters for the periods beginning with the Company's inception in November 2007 through the quarter ended September 30, 2011. The interim periods for the years ended December 31, 2008 and 2007 are not included in this Form 10-K.

In this 2011 Form 10-K, the annual and interim periods from the Company's inception in 2007 through the quarter ended September 30, 2011 are collectively referred to as the "Restatement Period." References to the "Company," "Chimera," "we," "our" and "us" in this 2011 Form 10-K refer to Chimera Investment Corporation together, in each case, with our subsidiaries unless the context suggests otherwise.

The impact of the Restatement is included in this 2011 Form 10-K, and is more specifically described below in this Explanatory Note and in Notes 16 and 17 of the Notes to the Consolidated Financial Statements, "Item 6 – Selected Financial Data" and "Item 7 – Management's Discussion and Analysis of Financial Condition and Results of Operations." All references to prior periods included below in the Management's Discussion and Analysis of Financial Condition and Results of Operations have been revised to reflect the effects of the Restatement.

From the Company's inception in 2007 through the second quarter of 2011, we applied the U.S. generally accepted accounting principles ("GAAP") guidance in the Financial Accounting Standards Board's ("FASB") Accounting Standards Codification ("ASC" or the "Codification") Subtopic 320-10, Investments – Debt and Equity Securities ("ASC 320-10"), and ASC Subtopic 310-20, Nonrefundable Fees and Other Costs (ASC 310-20) as the basis for recognizing interest income and other-than-temporary impairment ("OTTI") for our investments in Non-Agency residential mortgage-backed securities ("Non-Agency RMBS"). We should have also applied the guidance in ASC Subtopic 325-40, Investments – Other – Beneficial Interests in Securitized Financial Assets ("ASC 325-40") for securities not of high credit quality, and ASC Subtopic 310-30, Receivables – Loans and Debt Securities Acquired with Deteriorated Credit Quality ("ASC 310-30"), for certain of our investments in Non-Agency RMBS with deteriorated credit quality. Specifically, we determined that we had incorrectly recognized interest income and OTTI on certain Non-Agency RMBS since the Company's inception. We have determined that these errors were material therefore requiring this Restatement.

The Restatement has no material effect on the Company's previously reported book value per share, the net increase (decrease) in cash and cash equivalents as presented in our historical Consolidated Statements of Cash Flows, nor any effect on taxable income, which is the basis for the Company's dividend distributions.

The Company has corrected other errors, some of which had been previously identified or were identified in connection with the Restatement. These items include i) changes in the presentation of interest rate swaps from Interest expense to Realized gains (losses) on interest rate swaps, ii) changes in the presentation of the amortization of debt issue costs in the Consolidated Statements of Cash Flows from payments on securitized debt borrowings, RMBS transferred to consolidated VIEs (financing activities), to Amortization of debt issue costs of securitized debt (operating activities), iii) changes in the fair value of interest-only RMBS have been recognized in the Company's Consolidated Statements of Operations and Comprehensive Income (Loss), and iv) an increase in the allowance for loan losses related to securitized loans held for investment. In connection with the Restatement, we also reevaluated the classification of our Non-Agency RMBS securities in the fair value hierarchy as required by ASC 820, Fair Value Measurement. We have restated the 2010 amounts previously disclosed as Level 2 to Level 3. Additional information regarding the effect of the adjustments in our financial statements are contained in Item 15, Notes 4, Securitized Loans Held for Investment, 5, Fair Value Measurements, and 16, Restatement.

Impact of Restatement

Notes 16 and 17 of the accompanying consolidated financial statements present the impact of the Restatement to our Consolidated Statements of Financial Condition, Consolidated Statements of Operations and Comprehensive Income (Loss), Consolidated Statements of Changes in Stockholders' Equity, and Consolidated Statements of Cash Flows for the annual and quarterly periods affected, each as compared with the amounts presented in the original Annual Reports on Form 10-Q previously filed with the Securities and Exchange Commission ("SEC").

Internal Control over Financial Reporting and Disclosure Controls and Procedures

In connection with matters related to the Restatement, we have determined that a material weakness existed in our internal control over financial reporting for all periods from inception to December 31, 2011. As of December 31, 2011, the design and operating effectiveness of controls over the selection, application and review of the implementation of accounting policies were not sufficient to ensure amounts recorded and disclosed were fairly stated in accordance with GAAP. This material weakness resulted in the Restatement. In addition, solely as a result of this material weakness, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were not effective for the year ended December 31, 2011. Notwithstanding this material weakness, our management, based upon the substantial work performed during the Restatement process, has concluded that the Company's consolidated financial statements for the periods covered by and included in this Annual Report on Form 10-K are prepared in accordance with GAAP and fairly present, in all material respects, our financial position, results of operation and cash flows for each of the periods presented herein. For more information see "Part II – Item 9A – Controls and Procedures."

Special Note Regarding this 2011 Form 10-K

Unless otherwise indicated herein or as may be required by law (including, without limitation, to reflect the effects of the Restatement), the disclosure included in this 2011 Form 10-K is presented as of December 31, 2011. Accordingly, this 2011 Form 10-K does not reflect all events occurring after December 31, 2011, and we have not undertaken to update each and every item included in this 2011 Form 10-K to reflect such events (except as required by ASC 855, Subsequent Events). Therefore, this 2011 Form 10-K should be read in conjunction with our filings we have previously made with the Securities and Exchange Commission subsequent to December 31, 2011, and the filings we expect to make following the date of this 2011 Form 10-K (including, without limitation, our Forms 10-Q for the quarterly periods ended March 31, June 30 and September 30, 2012, and our Annual Report on Form 10-K for the year ended December 31, 2012, each of which is currently delinquent).

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

We make forward-looking statements in this report that are subject to risks and uncertainties. These forward-looking statements include information about possible or assumed future results of our business, financial condition, liquidity, results of operations, plans and objectives. When we use the words ''believe,'' ''expect,'' ''anticipate,'' ''estimate,'' ''plan,'' ''continue,'' ''intend,'' ''should,'' ''may,'' ''would,'' ''will'' or similar expressions, we intend to identify forward-looking statements. Statements regarding the following subjects, among others, are forward-looking by their nature:

our business and investment strategy;

our ability to maintain existing financing arrangements, obtain future financing arrangements and the terms of such arrangements, particularly in light of the Restatement and other matters discussed above under "Explanatory Note";

our ability to timely file our periodic reports with the SEC

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general volatility of the securities markets in which we invest;

the impact of and changes to various government programs;

our expected investments;

changes in the value of our investments;

interest rate mismatches between our investments and our borrowings used to fund such purchases;

changes in interest rates and mortgage prepayment rates;

effects of interest rate caps on our adjustable-rate investments;

rates of default or decreased recovery rates on our investments;

prepayments of the mortgage and other loans underlying our mortgage-backed or other asset-backed securities;

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;

availability of investment opportunities in real estate-related and other securities;

availability of qualified personnel;

estimates relating to our ability to make distributions to our stockholders in the future;

our understanding of our competition;

market trends in our industry, interest rates, the debt securities markets or the general economy;

our ability to maintain our classification as a REIT for federal income tax purposes; and

our ability to maintain our exemption from registration under the Investment Company Act of 1940.

The forward-looking statements are based on our beliefs, assumptions and expectations of our future performance, taking into account all information currently available to us. You should not place undue reliance on these forward-looking statements. These beliefs, assumptions and expectations can change as a result of many possible events or factors, not all of which are known to us. Some of these factors are described under the caption ''Risk Factors'' in this 2011 Form 10-K. If a change occurs, our business, financial condition, liquidity and results of operations may vary materially from those expressed in our forward-looking statements. Any forward-looking statement speaks only as of the date on which it is made. New risks and uncertainties arise from time to time, and it is impossible for us to predict those events or how they may affect us. Except as required by law, we are not obligated to, and do not intend to, update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

PART I

Item 1. Business

The Company

We are a specialty finance company that invests, either directly or indirectly through our subsidiaries, in residential mortgage-backed securities, or RMBS, residential mortgage loans, commercial mortgage loans, real estate-related securities and various other asset classes. We elected to be taxed as a real estate investment trust, or REIT, for federal income tax purposes commencing with our taxable year ended December 31, 2007. Therefore, we generally will not be subject to federal income tax on our taxable income that is distributed to our stockholders. We were incorporated in Maryland in June 2007 and commenced operations in November 2007. We listed our common stock on the New York Stock Exchange, or NYSE, in November 2007 and trade under the symbol “CIM”.

We are externally managed by Fixed Income Discount Advisory Company, which we refer to as our Manager or FIDAC. Our Manager is an investment advisor registered with the SEC. Additionally, our Manager is a wholly-owned subsidiary of Annaly Capital Management, Inc., or Annaly, a NYSE-listed REIT, which has a long track record of managing investments in U.S. government agency mortgage-backed securities.

Our objective is to provide attractive risk-adjusted returns to our investors over the long-term, primarily through dividends and secondarily through capital appreciation. We intend to achieve this objective by investing in a broad class of financial assets to construct an investment portfolio that is designed to achieve attractive risk-adjusted returns and that is structured to comply with the various federal income tax requirements for REIT status and to maintain our exemption from registration under the Investment Company Act of 1940, or 1940 Act.

Our Manager

We are externally managed and advised by FIDAC, a fixed-income management company, pursuant to a management agreement. All of our officers are employees of our Manager or one of its affiliates. We believe our relationship with our Manager enables us to leverage our Manager’s well-respected and established portfolio management resources for each of our targeted asset classes and we utilize our Manager’s infrastructure, including its investment professionals that focus on residential mortgage loans, U.S. government agency residential mortgage-backed securities, or Agency RMBS, that are guaranteed by the Federal National Mortgage Association, or Fannie Mae, the Federal Home Loan Mortgage Corporation, or Freddie Mac, and the Government National Mortgage Association, or Ginnie Mae, Non-Agency RMBS, commercial mortgage loans, commercial mortgage-backed securities, or CMBS, and other asset-backed securities, or ABS. Additionally, we utilize our Manager’s finance and administration functions, which address accounting, legal, compliance, investor relations and operational matters, including portfolio management, trade allocation and execution, securities valuation, risk management and information technologies in connection with the performance of its duties. Our Manager commenced active investment management operations in 1994.

Our Manager is responsible for administering our business activities and day-to-day operations. Pursuant to the terms of the management agreement, our Manager provides us with our management team, including our officers, along with appropriate support personnel. Our Manager is at all times subject to the supervision and oversight of our board of directors and has only such functions and authority as we delegate to it.

Our Investment Strategy

Our objective is to provide attractive risk-adjusted returns to our investors over the long-term, primarily through dividends and secondarily through capital appreciation. We intend to achieve this objective by investing in a diversified investment portfolio of RMBS, residential mortgage loans, real estate-related securities and various other asset classes, subject to maintaining our REIT status and exemption from registration under the 1940 Act. The RMBS, ABS, CMBS, and collateralized debt obligations, or CDOs, we purchase may include investment-grade and non-investment grade classes, including the BB-rated, B-rated and non-rated classes.

We rely on our Manager's expertise in identifying assets within our target asset classes. Our Manager makes investment decisions based on various factors, including expected cash yield, relative value, risk-adjusted returns, current and projected credit fundamentals, current and projected macroeconomic considerations, current and projected supply and demand, credit and market risk concentration limits, liquidity, cost of financing and financing availability, as well as maintaining our REIT qualification and our exemption from registration under the 1940 Act.

Over time, we will modify our investment allocation strategy as market conditions change to seek to maximize the returns from our investment portfolio. We believe this strategy, combined with our Manager's experience, will enable us to pay dividends and achieve capital appreciation throughout changing interest rate and credit cycles and provide attractive long-term returns to investors.

Our targeted asset classes and the principal investments we have made and may in the future invest follows:

Asset Class	Principal Investments
RMBS	Non-Agency RMBS, including investment-grade and non-investment grade classes, including the BB-rated, B-rated and non-rated classes.
	Agency RMBS.
Residential Mortgage Loans	Prime mortgage loans, which are mortgage loans that conform to the underwriting guidelines of Fannie Mae and Freddie Mac, which we refer to as Agency Guidelines; and jumbo prime mortgage loans, which are mortgage loans that conform to the Agency Guidelines except as to loan size.
	Alt-A mortgage loans, which are mortgage loans that may have been originated using documentation standards that are less stringent than the documentation standards applied by certain other first lien mortgage loan purchase programs, such as the Agency Guidelines, but have one or more compensating factors such as a borrower with a strong credit or mortgage history or significant assets.
	FHA/VA insured loans, which are mortgage loans that comply to the underwriting guidelines of the Federal Housing Administration (FHA) or Department of Veteran Affairs (VA) and which are guaranteed by the FHA or VA, respectively.
	Mortgage servicing rights associated with residential mortgage loans, which reflect the value of the future stream of expected cash flows from the contractual rights to service a given pool of residential mortgage loans.

Commercial Mortgage Loans	First or second lien loans secured by multifamily properties, which are residential rental properties consisting of five or more dwelling units; and mixed residential or other commercial properties; retail properties; office properties; or industrial properties, which may or may not conform to the Agency Guidelines.
Other Asset-Backed Securities	CMBS.
	Debt and equity tranches of CDOs.
	Consumer and non-consumer ABS, including investment-grade and non-investment grade classes, including the BB-rated, B-rated and non-rated classes.

Since we commenced operations in November 2007, we have focused our investment activities on acquiring Non-Agency and Agency RMBS and on purchasing residential mortgage loans that have been originated by select originators, including the retail lending operations of leading commercial banks. Our investment portfolio at December 31, 2011 was weighted toward Non-Agency RMBS. At December 31, 2011, based on the principal value of our interest earning assets, approximately 75.4% of our investment portfolio was Non-Agency RMBS, 21.1% of our investment portfolio was Agency RMBS, and 3.5% of our investment portfolio was securitized residential mortgage loans. At December 31, 2010, based on the principal value of our interest earning assets, approximately 79.5% of our investment portfolio was Non-Agency RMBS, 15.5% of our investment portfolio was Agency RMBS, and 5.0% of our investment portfolio was securitized residential mortgage loans. We expect that over the near term, our investment portfolio will continue to be weighted toward RMBS, subject to maintaining our REIT qualification and our 1940 Act exemption.

Following our initial public offering we initially engaged in transactions with residential mortgage lending operations of leading commercial banks and other originators in which we identified and re-underwrote residential mortgage loans owned by such entities, and purchased and securitized such residential mortgage loans ourselves. In the past we have also acquired formerly AAA-rated Non-Agency RMBS and immediately re-securitize those securities. We sold the resulting AAA-rated super senior RMBS and retained the rated or unrated mezzanine RMBS. More recently we have engaged in transactions with residential mortgage lending operations of leading commercial banks and other originators in which we identified and re-underwrote residential mortgage loans owned by such entities, and rather than purchasing and securitizing such residential mortgage loans ourselves, we and the originator or another entity, such as an investment bank, would structure the securitization and we would purchase the resulting mezzanine and subordinate Non-Agency RMBS. Structuring the securitizations in this manner enabled us to only acquire the resulting mezzanine and subordinate Non-Agency RMBS without having to actually acquire the loans underlying the securitizations. Our investment decisions, however, will depend on prevailing market conditions and our business opportunities at such time and we expect that these will change over time. As a result, we cannot predict the percentage of our assets that will be invested in each asset class or whether we will invest in other classes of investments. We may change our investment strategy and policies without a vote of our stockholders.

Our investment strategy is intended to take advantage of opportunities in the current interest rate and credit environment. We will adjust our strategy to changing market conditions by shifting our asset allocations across these various asset classes as interest rate and credit cycles change over time. We believe that our strategy, combined with FIDAC's experience, will enable us to pay dividends and achieve capital appreciation throughout changing market cycles. We expect to take a long-term view of assets and liabilities, and our reported earnings and estimates of the fair value of our investments at the end of a financial reporting period will not significantly impact our objective of providing attractive risk-adjusted returns to our stockholders over the long-term.

We use leverage to seek to increase our potential returns and to fund the acquisition of our assets. Our income is generated primarily by the difference, or net spread, between the income we earn on our assets and the cost of our borrowings. We expect to finance our investments using a variety of financing sources including, when available, repurchase agreements, warehouse facilities, securitizations, commercial paper and term financing CDOs. We may manage our debt by utilizing interest rate hedges, such as interest rate swaps, to reduce the effect of interest rate fluctuations related to our debt.

We have elected to be taxed as a REIT and operate our business to be exempt from registration under the 1940 Act, and therefore we are required to invest a substantial majority of our assets in loans secured by mortgages on real estate and real estate-related assets (as defined). Subject to maintaining our REIT qualification and our 1940 Act exemption, we do not have any limitations on the amounts we may invest in any of our targeted asset classes.

Investment Portfolio