Section 1: 10-Q (10-Q)

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

FORM 10-Q

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

For the Quarterly Period Ended: March 31, 2019

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 1-13759

REDWOOD TRUST, INC.

(Exact Name of Registrant as Specified in Its Charter)

Maryland	**68-0329422**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
One Belvedere Place, Suite 300 **Mill Valley, California**	**94941**
(Address of Principal Executive Offices)	(Zip Code)

(415) 389-7373
(Registrant’s Telephone Number, Including Area Code)

Not Applicable
(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files). Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	☒	Accelerated filer	☐
Non-accelerated filer	☐	Smaller reporting company	☐
		Emerging growth company	☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

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

Title of each class	Trading symbol(s)	Name of each exchange on which registered

Common stock, par value $0.01 per share	RWT	New York Stock Exchange

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock, $0.01 par value per share	96,876,974 shares outstanding as of May 6, 2019

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2019 FORM 10-Q REPORT
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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

REDWOOD TRUST, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

(In Thousands, except Share Data) (Unaudited)	March 31, 2019	December 31, 2018
ASSETS [1]		
Residential loans, held-for-sale, at fair value	$ 819,221	$ 1,048,801
Residential loans, held-for-investment, at fair value	6,455,080	6,205,941
Business purpose residential loans, at fair value	160,612	141,258
Multifamily loans, held-for-investment, at fair value	2,175,899	2,144,598
Real estate securities, at fair value	1,543,152	1,452,494
Other investments	414,198	438,518
Cash and cash equivalents	200,837	175,764
Restricted cash	14,614	29,313
Goodwill and intangible assets	52,895	—
Accrued interest receivable	48,972	47,105
Derivative assets	22,283	35,789
Other assets	285,596	217,825
Total Assets	$ 12,193,359	$ 11,937,406
LIABILITIES AND EQUITY [1]		
Liabilities		
Short-term debt, net [2]	$ 2,163,231	$ 2,400,279
Accrued interest payable	39,526	42,528
Derivative liabilities	110,942	84,855
Accrued expenses and other liabilities	119,428	78,719
Asset-backed securities issued, at fair value	5,637,644	5,410,073
Long-term debt, net	2,572,661	2,572,158
Total liabilities	10,643,432	10,588,612
Commitments and Contingencies (see *Note 16)*		
Equity		
Common stock, par value $0.01 per share, 180,000,000 shares authorized; 96,866,464 and 84,884,344 issued and outstanding	969	849
Additional paid-in capital	1,996,358	1,811,422
Accumulated other comprehensive income	52,684	61,297
Cumulative earnings	1,464,405	1,409,941
Cumulative distributions to stockholders	(1,964,489)	(1,934,715)
Total equity	1,549,927	1,348,794
Total Liabilities and Equity	$ 12,193,359	$ 11,937,406

(1) Our consolidated balance sheets include assets of consolidated variable interest entities ("VIEs") that can only be used to settle obligations of these VIEs and liabilities of consolidated VIEs for which creditors do not have recourse to Redwood Trust, Inc. or its affiliates. At March 31, 2019 and December 31, 2018, assets of consolidated VIEs totaled $6,585,881 and $6,331,191, respectively. At March 31, 2019 and December 31, 2018, liabilities of consolidated VIEs totaled $5,925,677 and $5,709,807, respectively. See *Note 4* for further discussion.

(2) Includes $201 million of convertible notes, which were reclassified from Long-term debt, net to Short-term debt as the maturity of the notes was less than one year as of November 15, 2018. See *Note 13* for further discussion.

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

REDWOOD TRUST, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME

(In Thousands, except Share Data) (Unaudited)	Three Months Ended March 31, 2019	Three Months Ended March 31, 2018
Interest Income		
Residential loans	$ 75,950	$ 50,231
Business purpose residential loans	2,789	—
Multifamily loans	21,388	—
Real estate securities	24,450	25,695
Other interest income	6,464	693
Total interest income	131,041	76,619
Interest Expense		
Short-term debt	(22,218)	(13,435)
Asset-backed securities issued	(55,295)	(11,401)
Long-term debt	(21,763)	(16,678)
Total interest expense	(99,276)	(41,514)
Net Interest Income	31,765	35,105
Non-interest Income		
Mortgage banking activities, net	12,309	26,576
Investment fair value changes, net	20,159	1,609
Other income, net	3,587	2,118
Realized gains, net	10,686	9,363
Total non-interest income, net	46,741	39,666
Operating expenses	(23,159)	(23,030)
Net Income before Provision for Income Taxes	55,347	51,741
Provision for income taxes	(883)	(4,896)
Net Income	$ 54,464	$ 46,845
Basic earnings per common share	$ 0.57	$ 0.60
Diluted earnings per common share	$ 0.49	$ 0.50
Regular dividends declared per common share	$ 0.30	$ 0.28
Basic weighted average shares outstanding	92,685,350	75,396,649
Diluted weighted average shares outstanding	126,278,160	108,194,597

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

REDWOOD TRUST, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In Thousands)	Three Months Ended March 31,	
(Unaudited)	2019	2018
Net Income	$ 54,464	$ 46,845
Other comprehensive loss:		
Net unrealized gain (loss) on available-for-sale securities	6,718	(4,237)
Reclassification of unrealized gain on available-for-sale securities to net income	(9,493)	(9,387)
Net unrealized (loss) gain on interest rate agreements	(5,838)	8,431
Total other comprehensive loss	(8,613)	(5,193)
Total Comprehensive Income	$ 45,851	$ 41,652

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

REDWOOD TRUST, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

For the Three Months Ended March 31, 2019

(In Thousands, except Share Data) (Unaudited)	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Accumulated Other Comprehensive Income	Cumulative Earnings	Cumulative Distributions to Stockholders	Total
December 31, 2018	84,884,344	$ 849	$ 1,811,422	$ 61,297	$ 1,409,941	$ (1,934,715)	$ 1,348,794
Net income	—	—	—	—	54,464	—	54,464
Other comprehensive loss	—	—	—	(8,613)	—	—	(8,613)
Issuance of common stock	11,500,000	115	177,482	—	—	—	177,597
Direct stock purchase and dividend reinvestment plan	399,838	4	6,303	—	—	—	6,307
Employee stock purchase and incentive plans	82,282	1	(1,939)	—	—	—	(1,938)
Non-cash equity award compensation	—	—	3,090	—	—	—	3,090
Common dividends declared	—	—	—	—	—	(29,774)	(29,774)
March 31, 2019	96,866,464	$ 969	$ 1,996,358	$ 52,684	$ 1,464,405	$ (1,964,489)	$ 1,549,927

For the Three Months Ended March 31, 2018

(In Thousands, except Share Data) (Unaudited)	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Accumulated Other Comprehensive Income	Cumulative Earnings	Cumulative Distributions to Stockholders	Total
December 31, 2017	76,599,972	$ 766	$ 1,673,845	$ 85,248	$ 1,290,341	$ (1,837,913)	$ 1,212,287
Net income	—	—	—	—	46,845	—	46,845
Other comprehensive loss	—	—	—	(5,193)	—	—	(5,193)
Employee stock purchase and incentive plans	143,964	1	(284)	—	—	—	(283)
Non-cash equity award compensation	—	—	3,674	—	—	—	3,674
Share repurchases	(1,040,829)	(10)	(15,534)	—	—	—	(15,544)
Common dividends declared	—	—	—	—	—	(21,803)	(21,803)
March 31, 2018	75,703,107	$ 757	$ 1,661,701	$ 80,055	$ 1,337,186	$ (1,859,716)	$ 1,219,983

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

REDWOOD TRUST, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

(In Thousands) (Unaudited)	Three Months Ended March 31, 2019	2018
Cash Flows From Operating Activities:		
Net income	$ 54,464	$ 46,845
Adjustments to reconcile net income to net cash used in operating activities:		
Amortization of premiums, discounts, and securities issuance costs, net	(689)	(3,939)
Depreciation and amortization of non-financial assets	343	299
Originations of held-for-sale loans	(28,968)	—
Purchases of held-for-sale loans	(989,977)	(1,820,002)
Proceeds from sales of held-for-sale loans	851,331	1,581,806
Principal payments on held-for-sale loans	17,450	16,332
Net settlements of derivatives	(9,305)	19,296
Non-cash equity award compensation expense	3,090	3,674
Market valuation adjustments	(31,439)	(25,600)
Realized gains, net	(10,686)	(9,363)
Net change in:		
Accrued interest receivable and other assets	(50,006)	35,824
Accrued interest payable and accrued expenses and other liabilities	(12,119)	11,581
Net cash used in operating activities	(206,511)	(143,247)
Cash Flows From Investing Activities:		
Originations of loans held-for-investment	(7,000)	—
Purchases of loans held-for-investment	(49,489)	—
Principal payments on loans held-for-investment	246,964	159,889
Purchases of real estate securities	(154,871)	(128,069)
Proceeds from sales of real estate securities	74,018	241,570
Principal payments on real estate securities	24,498	16,246
Purchases of servicer advance investments	(68,976)	—
Principal repayments from servicer advance investments	66,532	—
Purchases of excess MSRs	(2,116)	—
Acquisition of 5 Arches, net of cash acquired	(3,714)	—
Net investment in participation in loan warehouse facility	38,209	—
Net investment in multifamily loan fund	(22,316)	—
Other investing activities, net	(1,179)	3,827
Net cash provided by investing activities	140,560	293,463
Cash Flows From Financing Activities:		
Proceeds from borrowings on short-term debt	1,217,915	1,318,754
Repayments on short-term debt	(1,459,648)	(1,753,090)
Proceeds from issuance of asset-backed securities	330,534	441,741
Repayments on asset-backed securities issued	(163,146)	(84,974)
Net settlements of derivatives	(35)	(85)
Net proceeds from issuance of common stock	182,512	88
Net payments on repurchase of common stock	—	(16,315)
Taxes paid on equity award distributions	(2,033)	(371)
Dividends paid	(29,774)	(21,803)
Net cash provided by (used in) financing activities	76,325	(116,055)
Net increase in cash, cash equivalents and restricted cash	10,374	34,161
Cash, cash equivalents and restricted cash at beginning of period (1)	205,077	146,807
Cash, cash equivalents and restricted cash at end of period (1)	$ 215,451	$ 180,968

REDWOOD TRUST, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)

(In Thousands) **(Unaudited)**	**Three Months Ended March 31,**	
	2019	**2018**
Supplemental Cash Flow Information:		
Cash paid during the period for:		
Interest	$ 99,686	$ 38,285
Taxes	77	42
Supplemental Noncash Information:		
Real estate securities retained from loan securitizations	$ 2,601	$ 16,396
Transfers from loans held-for-sale to loans held-for-investment	389,486	507,616
Transfers from loans held-for-investment to loans held-for-sale	22,758	—
Transfers from residential loans to real estate owned	5,035	1,268
Right-of-use asset obtained in exchange for operating lease liability	12,661	—

(1) Cash, cash equivalents, and restricted cash at March 31, 2019 includes cash and cash equivalents of $201 million and restricted cash of $15 million, and at December 31, 2018 includes cash and cash equivalents of $176 million and restricted cash of $29 million.

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

Note 1. Organization

Redwood Trust, Inc., together with its subsidiaries, is a specialty finance company focused on making credit-sensitive investments in single-family residential and multifamily mortgages and related assets and engaging in mortgage banking activities. Our goal is to provide attractive returns to shareholders through a stable and growing stream of earnings and dividends, as well as through capital appreciation. We operate our business in two segments: Investment Portfolio and Mortgage Banking.

Our primary sources of income are net interest income from our investment portfolios and non-interest income from our mortgage banking activities. Net interest income consists of the interest income we earn on investments less the interest expense we incur on borrowed funds and other liabilities. Income from mortgage banking activities is generated through the acquisition of residential loans and their subsequent sale or securitization, as well as through the origination of business purpose residential loans.

Redwood Trust, Inc. has elected to be taxed as a real estate investment trust (“REIT”) under the Internal Revenue Code of 1986, as amended (the “Internal Revenue Code”), beginning with its taxable year ended December 31, 1994. We generally refer, collectively, to Redwood Trust, Inc. and those of its subsidiaries that are not subject to subsidiary-level corporate income tax as “the REIT” or “our REIT.” We generally refer to subsidiaries of Redwood Trust, Inc. that are subject to subsidiary-level corporate income tax as “our operating subsidiaries” or “our taxable REIT subsidiaries” or “TRS.”

Redwood was incorporated in the State of Maryland on April 11, 1994, and commenced operations on August 19, 1994. References herein to “Redwood,” the “company,” “we,” “us,” and “our” include Redwood Trust, Inc. and its consolidated subsidiaries, unless the context otherwise requires.

Note 2. Basis of Presentation

The consolidated financial statements presented herein are at March 31, 2019 and December 31, 2018, and for the three months ended March 31, 2019 and 2018. These interim unaudited consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission ("SEC"). Certain information and note disclosures normally included in our annual financial statements prepared in accordance with U.S. generally accepted accounting principles ("GAAP") — as prescribed by the Financial Accounting Standards Board’s (“FASB”) Accounting Standards Codification (“ASC”) — have been condensed or omitted in these interim financial statements according to these SEC rules and regulations. Management believes that the disclosures included in these interim financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the company's Annual Report on Form 10-K for the year ended December 31, 2018. In the opinion of management, all normal and recurring adjustments to present fairly the financial condition of the company at March 31, 2019 and results of operations for all periods presented have been made. The results of operations for the three months ended March 31, 2019 should not be construed as indicative of the results to be expected for the full year.

Principles of Consolidation

In accordance with GAAP, we determine whether we must consolidate transferred financial assets and variable interest entities (“VIEs”) for financial reporting purposes. We currently consolidate the assets and liabilities of certain Sequoia securitization entities issued prior to 2012 where we maintain an ongoing involvement ("Legacy Sequoia"), as well as entities formed in connection with the securitization of Redwood Choice expanded-prime loans beginning in the third quarter of 2017 ("Sequoia Choice"). In addition, we consolidated the assets and liabilities of certain third-party Freddie Mac K-Series securitizations beginning in the third quarter of 2018, and the assets and liabilities of one third-party Freddie Mac SLST securitization beginning in the fourth quarter of 2018. Each securitization entity is independent of Redwood and of each other and the assets and liabilities are not owned by and are not legal obligations of Redwood Trust, Inc. Our exposure to these entities is primarily through the financial interests we have purchased or retained, although for the consolidated Sequoia entities we are exposed to certain financial risks associated with our role as a sponsor, servicing administrator, or depositor of these entities or as a result of our having sold assets directly or indirectly to these entities.

Note 2. Basis of Presentation - (continued)

For financial reporting purposes, the underlying loans owned at the consolidated Sequoia and Freddie Mac SLST entities are shown under Residential loans, held-for-investment, at fair value, and the underlying loans at the consolidated Freddie Mac K-Series are shown under Multifamily loans held-for-investment, at fair value, on our consolidated balance sheets. The asset-backed securities ("ABS") issued to third parties by these entities are shown under ABS issued. In our consolidated statements of income, we recorded interest income on the loans owned at these entities and interest expense on the ABS issued by these entities as well as other income and expenses associated with these entities' activities. See *Note 14* for further discussion on ABS issued.

Beginning in the fourth quarter of 2018, we consolidated two partnerships ("Servicing Investment" entities) through which we have invested in servicing-related assets. We maintain an 80% ownership interest in each entity and have determined that we are the primary beneficiary of these partnerships.

Beginning in the first quarter of 2019, we consolidated 5 Arches, LLC ("5 Arches"), an originator of business purpose residential loans, pursuant to the exercise of our purchase option and the acquisition of the remaining equity in the company.

See *Note 4* for further discussion on principles of consolidation.

Use of Estimates

The preparation of financial statements requires us to make a number of significant estimates. These include estimates of fair value of certain assets and liabilities, amounts and timing of credit losses, prepayment rates, and other estimates that affect the reported amounts of certain assets and liabilities as of the date of the consolidated financial statements and the reported amounts of certain revenues and expenses during the reported periods. It is likely that changes in these estimates (e.g., valuation changes due to supply and demand, credit performance, prepayments, interest rates, or other reasons) will occur in the near term. Our estimates are inherently subjective in nature and actual results could differ from our estimates and the differences could be material.

Acquisition of 5 Arches, LLC

On March 1, 2019, we completed the previously announced acquisition of the remaining 80% interest in 5 Arches, an originator of business purpose residential loans. In May 2018, Redwood acquired a 20% minority interest in 5 Arches for $10 million in cash, with a one-year option to purchase all remaining equity in the company. At closing, we paid approximately $13 million of cash and the remainder of the consideration, which could total up to an additional $27 million, will be paid in a mix of cash and Redwood common stock and is contingent on the achievement of certain specified loan origination thresholds over the next two years.

Note 2. Basis of Presentation - (continued)

We accounted for the acquisition of 5 Arches under the acquisition method of accounting pursuant to ASC 805. We performed the preliminary purchase price allocation and recorded underlying assets acquired and liabilities assumed based on their estimated fair values using the information available as of the acquisition date, with the excess of the purchase price allocated to goodwill. This preliminary purchase price allocation is summarized in the following table.

Table 2.1 – 5 Arches Purchase Price Allocation

(In Thousands)		March 1, 2019
Purchase price:		
Cash	$	12,575
Contingent consideration, at fair value		24,621
Purchase option, at fair value		5,082
Equity method investment, at fair value		8,052
Total consideration	$	50,330
Allocated to:		
Tangible net assets acquired (1)	$	1,004
Goodwill		28,728
Intangible assets		24,800
Deferred tax liability		(4,202)
Total net assets acquired	$	50,330

(1) 5 Arches net assets acquired consisted of assets of $19 million and liabilities of $18 million as of March 1, 2019.

Because we owned a 20% noncontrolling interest in 5 Arches immediately before obtaining full control, we remeasured our initial minority investment and purchase option at their acquisition-date fair values using the income approach, which resulted in a gain of $2 million that was recorded in Other income, net on our consolidated statements of income.

As part of this acquisition, we identified and recorded finite-lived intangible assets totaling $25 million. The amortization period for each of these assets and the activity for the three months ended March 31, 2019 is summarized in the table below.

Table 2.2 – Intangible Assets – Activity

(Dollars in Thousands)		Carrying Value at December 31, 2018		Additions		Amortization Expense		Carrying Value at March 31, 2019	Weighted Average Amortization Period (in years)
Finite-lived intangible assets:									
Broker network	$	—	$	18,100	$	(301)	$	17,799	5
Non-compete agreements		—		2,900		(81)		2,819	3
Management fee on existing assets under management		—		2,600		(217)		2,383	1
Tradename		—		1,200		(34)		1,166	3
Total	$	—	$	24,800	$	(633)	$	24,167	4

Note 2. Basis of Presentation - (continued)

All of our intangible assets are amortized on a straight-line basis. Estimated amortization expense for the remainder of 2019 and the following years is summarized in the table below.

Table 2.3 – Intangible Asset Amortization Expense by Year

(In Thousands)	March 31, 2019
2019 (9 months)	$ 5,690
2020	5,420
2021	4,987
2022	3,848
2023 and thereafter	4,222
Total Future Intangible Asset Amortization	$ 24,167

We recorded goodwill of $29 million as a result of the total consideration exceeding the fair value of the net assets acquired. The goodwill was attributed to the expected business synergies and expansion into business purpose loan markets, as well as access to the knowledgeable and experienced workforce continuing to provide services to the business. We expect $3 million of our goodwill balance to be deductible for tax purposes. The following table presents the goodwill activity for the three months ended March 31, 2019.

Table 2.4 – Goodwill – Activity

(In Thousands)	Three Months Ended March 31, 2019
Beginning balance	$ —
Goodwill recognized from 5 Arches acquisition	28,728
Impairment	—
Ending Balance	$ 28,728

The liability resulting from the contingent consideration arrangement was recorded at its acquisition-date fair value of $25 million as part of total consideration for the acquisition of 5 Arches.

The following unaudited pro forma financial information presents Net interest income, Non-interest income, and Net income of Redwood and 5 Arches combined, as if the acquisition occurred as of January 1, 2018. These pro forma amounts have been adjusted to include the amortization of intangible assets for both periods, and to exclude the income statement impacts related to our equity method investment in 5 Arches. The unaudited pro forma financial information is not intended to represent or be indicative of the consolidated financial results of operations that would have been reported if the acquisition had been completed as of January 1, 2018 and should not be taken as indicative of our future consolidated results of operations.

Table 2.5 – Unaudited Pro Forma Financial Information

	Three Months Ended March 31,	
(In Thousands)	2019	2018
Supplementary pro forma information:		
Net interest income	$ 32,266	$ 35,331
Non-interest income	43,849	40,968
Net income	50,311	46,035

Note 3. Summary of Significant Accounting Policies

Significant Accounting Policies

Included in *Note 3* to the Consolidated Financial Statements of our Annual Report on Form 10-K for the year ended December 31, 2018 is a summary of our significant accounting policies. Provided below is a summary of additional accounting policies that are significant to the company's consolidated financial position and results of operations for the three months ended March 31, 2019.

Business Combinations

We use the acquisition method of accounting for business combinations, under which the purchase price is allocated to the fair values of the assets acquired and liabilities assumed at the acquisition date. The excess of the purchase price over the amount allocated to the assets acquired and liabilities assumed is recorded as goodwill. Adjustments to the values of the assets acquired and liabilities assumed that could be made during the measurement period, which could be up to one year after the acquisition date, are recorded in the period in which the adjustment is identified, with a corresponding offset to goodwill. Any adjustments made after the measurement period are recorded in the consolidated statements of income. Acquisition related costs are expensed as incurred.

Goodwill and Intangible Assets

Significant judgment is required to estimate the fair value of intangible assets and in assigning their estimated useful lives. Accordingly, we typically seek the assistance of independent third-party valuation specialists for significant intangible assets. The fair value estimates are based on available historical information and on future expectations and assumptions we deem reasonable. We generally use an income-based valuation method to estimate the fair value of intangible assets, which discounts expected future cash flows to present value using estimates and assumptions we deem reasonable.

Determining the estimated useful lives of intangible assets also requires judgment. Our assessment as to which intangible assets are deemed to have finite or indefinite lives is based on several factors including economic barriers of entry for the acquired business, retention trends, and our operating plans, among other factors.

Finite-lived intangible assets are amortized over their estimated useful lives on a straight-line basis and reviewed for impairment if indicators are present. Additionally, useful lives are evaluated each reporting period to determine if revisions to the remaining periods of amortization are warranted. Goodwill is tested for impairment annually or more frequently if indicators of impairment exist. We have elected to make the first day of our fiscal fourth quarter the annual impairment assessment date for goodwill. We first assess qualitative factors to determine whether it is more likely than not that the fair value is less than the carrying value. If, based on that assessment, we believe it is more likely than not that the fair value is less than the carrying value, then a two-step goodwill impairment test is performed.

Loan Originations

Our wholly-owned subsidiary, 5 Arches, originates business purpose residential loans, including single-family rental and residential bridge loans. Single-family rental loans are classified as held-for-sale at fair value, as we have originated these loans with the intent to sell to third parties or transfer to securitization entities. Residential bridge loans are classified as held-for-investment at fair value, if we intend to hold these loans to maturity, or held-for-sale at fair value, if we intend to sell the loans to a third party.

Contingent Consideration

In relation to our acquisition of 5 Arches, we recorded contingent consideration liabilities that represent the estimated fair value (at the date of acquisition) of our obligation to make certain earn-out payments that are contingent on 5 Arches loan origination volumes exceeding certain specified thresholds. These liabilities are carried at fair value and periodic changes in their estimated fair value are recorded through our income statement in Other income, net. The estimate of the fair value of contingent consideration requires significant judgment regarding assumptions about future operating results, discount rates, and probabilities of projected operating result scenarios.

Note 3. Summary of Significant Accounting Policies - (continued)

Leases

Upon adoption of ASU 2016-02, "Leases," in the first quarter of 2019, we recorded a lease liability and right-of-use asset on our consolidated balance sheets. The lease liability is equal to the present value of our remaining lease payments discounted at our incremental borrowing rate and the right-of-use asset is equal to the lease liability adjusted for our deferred rent liability at the adoption of this accounting standard. As lease payments are made, the lease liability is reduced to the present value of the remaining lease payments and the right-of-use asset is reduced by the difference between the lease expense (straight-lined over the lease term) and the theoretical interest expense amount (calculated using the incremental borrowing rate). See *Note 16* for further discussion on leases.

Recent Accounting Pronouncements

Newly Adopted Accounting Standards Updates ("ASUs")

In February 2018, the FASB issued ASU 2018-02, "Income Statement - Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income." This new guidance allows a reclassification from accumulated other comprehensive income ("AOCI") to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act of 2017 (the "Tax Act"). This new guidance is effective for fiscal years beginning after December 15, 2018. However, we did not elect to reclassify any income tax effects of the Tax Act from AOCI to retained earnings as we did not have any tax effects related to the Tax Act remaining in AOCI at December 31, 2018. Our policy is to release any stranded income tax effects from AOCI to income tax expense on an investment-by-investment basis.

In August 2017, the FASB issued ASU 2017-12, "Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities." This new guidance amends previous guidance to better align an entity's risk management activities and financial reporting for hedging relationships through changes to both the designation and measurement guidance for qualifying hedging relationships and the presentation of hedge results. This new guidance is effective for fiscal years beginning after December 15, 2018. Additionally, in October 2018, the FASB issued ASU 2018-16, "Derivatives and Hedging (Topic 815): Inclusion of the Secured Overnight Financing Rate (SOFR) Overnight Index Swap (OIS) Rate as a Benchmark Interest Rate for Hedge Accounting Purposes," which permits the use of the OIS rate based on SOFR as a U.S. benchmark interest rate for hedge accounting purposes under Topic 815. The amendments in this update are required to be adopted concurrently with the amendments in ASU 2017-12. We adopted this guidance, as required, in the first quarter of 2019, which did not have a material impact on our consolidated financial statements.

In July 2017, the FASB issued ASU 2017-11, "Earnings Per Share (Topic 260); Distinguishing Liabilities from Equity (Topic 480); Derivatives and Hedging (Topic 815): (Part I) Accounting for Certain Financial Instruments with Down Round Features, (Part II) Replacement of the Indefinite Deferral for Mandatorily Redeemable Financial Instruments of Certain Nonpublic Entities and Certain Mandatorily Redeemable Noncontrolling Interests with a Scope Exception." This new guidance changes the classification analysis of certain equity-linked financial instruments (or embedded conversion options) with down round features. This new guidance is effective for fiscal years beginning after December 15, 2018. We adopted this guidance, as required, in the first quarter of 2019, which did not have a material impact on our consolidated financial statements.

In March 2017, the FASB issued ASU 2017-08, "Receivables - Nonrefundable Fees and Other Costs (Subtopic 310-20)." This new guidance shortens the amortization period for certain callable debt securities purchased at a premium by requiring the premium to be amortized to the earliest call date. This new guidance is effective for fiscal years beginning after December 15, 2018. We adopted this guidance, as required, in the first quarter of 2019, which did not have a material impact on our consolidated financial statements.

Note 3. Summary of Significant Accounting Policies - (continued)

In February 2016, the FASB issued ASU 2016-02, "Leases." This new guidance requires lessees to recognize most leases on their balance sheet as a right-of-use asset and a lease liability. This new guidance retains a dual lease accounting model, which requires leases to be classified as either operating or capital leases for lessees, for purposes of income statement recognition. This new guidance is effective for fiscal years beginning after December 15, 2018. In July 2018, the FASB issued ASU 2018-10, "Codification Improvements to Topic 842, Leases," which provides more specific guidance on certain aspects of Topic 842. Additionally, in July 2018, the FASB issued ASU 2018-11, "Leases (Topic 842): Targeted Improvements." This new ASU introduces an additional transition method which allows entities to apply the new standard at the adoption date and recognize a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. In March 2019, the FASB issued ASU 2019-01, "Leases (Topic 842): Codification Improvements," which is intended to clarify Codification guidance. We adopted this guidance, as required, in the first quarter of 2019, which did not have a material impact on our consolidated financial statements. We elected the package of practical expedients under the transition guidance within this standard, which allowed us to carry forward the classifications of each of our existing leases as operating leases. In connection with the adoption of this guidance, at March 31, 2019, our lease liability was $13 million, which represented the present value of our remaining lease payments discounted at our incremental borrowing rate and was recorded in Accrued expenses and other liabilities on our consolidated balance sheets. At March 31, 2019, our right-of-use asset was $12 million, which was equal to the lease liability adjusted for our deferred rent liability at adoption and was recorded in Other assets on our consolidated balance sheets. We will continue to record lease expense on a straight-line basis and have included required lease disclosures within *Note 16*.

Other Recent Accounting Pronouncements

In August 2018, the FASB issued ASU 2018-13, "Fair Value Measurement (Topic 820): Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement." This new guidance amends previous guidance by removing and modifying certain existing fair value disclosure requirements, while adding other new disclosure requirements. This new guidance is effective for fiscal years beginning after December 15, 2019. Early adoption is permitted and entities may elect to early adopt the removal or modification of disclosures immediately and delay adoption of the new disclosure requirements until their effective date. We plan to adopt this new guidance by the required date and do not anticipate that this update will have a material impact on our consolidated financial statements.

In July 2018, the FASB issued ASU 2018-09, "Codification Improvements." This new guidance is intended to clarify, correct, and make minor improvements to the FASB Accounting Standards Codification. The transition and effective dates are based on the facts and circumstances of each amendment, with some amendments becoming effective upon issuance of this ASU and others becoming effective for annual periods beginning after December 15, 2018. We plan to adopt this new guidance by the required date and do not anticipate that this update will have a material impact on our consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, "Financial Instruments - Credit Losses." This new guidance provides a new impairment model that is based on expected losses rather than incurred losses to determine the allowance for credit losses. This new guidance is effective for fiscal years beginning after December 15, 2019. Early adoption is permitted for fiscal years beginning after December 15, 2018. In November 2018, the FASB issued ASU 2018-19, "Codification Improvements to Topic 326, Financial Instruments - Credit Losses," which clarifies the scope of the amendments in ASU 2016-13. We currently have only a small balance of loans receivable that are not carried at fair value and would be subject to this new guidance for allowance for credit losses. Separately, we account for our available-for-sale securities under the other-than-temporary impairment ("OTTI") model for debt securities. This new guidance requires that credit impairments on our available-for-sale securities be recorded in earnings using an allowance for credit losses, with the allowance limited to the amount by which the security's fair value is less than its amortized cost basis. Subsequent reversals in credit loss estimates are recognized in income. We plan to adopt this new guidance by the required date and do not anticipate that these updates will have a material impact on our consolidated financial statements as nearly all of our financial instruments are carried at fair value and changes in fair values of these instruments are recorded on our consolidated statements of income in the period in which the valuation change occurs. We will continue evaluating these new standards and caution that any changes in our business or additional amendments to these standards could change our initial assessment.

Note 3. Summary of Significant Accounting Policies - (continued)

Balance Sheet Netting

Certain of our derivatives and short-term debt are subject to master netting arrangements or similar agreements. Under GAAP, in certain circumstances we may elect to present certain financial assets, liabilities and related collateral subject to master netting arrangements in a net position on our consolidated balance sheets. However, we do not report any of these financial assets or liabilities on a net basis, and instead present them on a gross basis on our consolidated balance sheets.

The table below presents financial assets and liabilities that are subject to master netting arrangements or similar agreements categorized by financial instrument, together with corresponding financial instruments and corresponding collateral received or pledged at March 31, 2019 and December 31, 2018.

Table 3.1 – Offsetting of Financial Assets, Liabilities, and Collateral

				Gross Amounts Not Offset in Consolidated Balance Sheet [(1)]		
March 31, 2019 (In Thousands)	**Gross Amounts of Recognized Assets (Liabilities)**	**Gross Amounts Offset in Consolidated Balance Sheet**	**Net Amounts of Assets (Liabilities) Presented in Consolidated Balance Sheet**	**Financial Instruments**	**Cash Collateral (Received) Pledged**	**Net Amount**
Assets [(2)]						
Interest rate agreements	$ 11,490	$ —	$ 11,490	$ (11,490)	$ —	$ —
TBAs	5,826	—	5,826	(5,755)	—	71
Total Assets	$ 17,316	$ —	$ 17,316	$ (17,245)	$ —	$ 71
Liabilities [(2)]						
Interest rate agreements	$ (100,561)	$ —	$ (100,561)	$ 11,490	$ 89,071	$ —
TBAs	(9,609)	—	(9,609)	5,755	2,166	(1,688)
Loan warehouse debt	(526,341)	—	(526,341)	526,341	—	—
Security repurchase agreements	(1,081,079)	—	(1,081,079)	1,081,079	—	—
Total Liabilities	$ (1,717,590)	$ —	$ (1,717,590)	$ 1,624,665	$ 91,237	$ (1,688)

Note 3. Summary of Significant Accounting Policies - (continued)

December 31, 2018 (In Thousands)	Gross Amounts of Recognized Assets (Liabilities)	Gross Amounts Offset in Consolidated Balance Sheet	Net Amounts of Assets (Liabilities) Presented in Consolidated Balance Sheet	Gross Amounts Not Offset in Consolidated Balance Sheet [(1)] Financial Instruments	Gross Amounts Not Offset in Consolidated Balance Sheet [(1)] Cash Collateral (Received) Pledged	Net Amount
Assets [(2)]						
Interest rate agreements	$ 28,211	$ —	$ 28,211	$ (28,211)	$ —	$ —
TBAs	4,665	—	4,665	(3,391)	(835)	439
Total Assets	$ 32,876	$ —	$ 32,876	$ (31,602)	$ (835)	$ 439
Liabilities [(2)]						
Interest rate agreements	$ (70,908)	$ —	$ (70,908)	$ 28,211	$ 42,697	$ —
TBAs	(13,215)	—	(13,215)	3,391	5,620	(4,204)
Loan warehouse debt	(860,650)	—	(860,650)	860,650	—	—
Security repurchase agreements	(988,890)	—	(988,890)	988,890	—	—
Total Liabilities	$ (1,933,663)	$ —	$ (1,933,663)	$ 1,881,142	$ 48,317	$ (4,204)

(1) Amounts presented in these columns are limited in total to the net amount of assets or liabilities presented in the prior column by instrument. In certain cases, there is excess cash collateral or financial assets we have pledged to a counterparty (which may, in certain circumstances, be a clearinghouse) that exceed the financial liabilities subject to a master netting arrangement or similar agreement. Additionally, in certain cases, counterparties may have pledged excess cash collateral to us that exceeds our corresponding financial assets. In each case, any of these excess amounts are excluded from the table although they are separately reported in our consolidated balance sheets as assets or liabilities, respectively.

(2) Interest rate agreements and TBAs are components of derivatives instruments on our consolidated balance sheets. Loan warehouse debt, which is secured by residential mortgage loans, and security repurchase agreements are components of Short-term debt on our consolidated balance sheets.

For each category of financial instrument set forth in the table above, the assets and liabilities resulting from individual transactions within that category between us and a counterparty are subject to a master netting arrangement or similar agreement with that counterparty that provides for individual transactions to be aggregated and treated as a single transaction. For certain categories of these instruments, some of our transactions are cleared and settled through one or more clearinghouses that are substituted as our counterparty. References herein to master netting arrangements or similar agreements include the arrangements and agreements governing the clearing and settlement of these transactions through the clearinghouses. In the event of the termination and close-out of any of those transactions, the corresponding master netting agreement or similar agreement provides for settlement on a net basis. Any such settlement would include the proceeds of the liquidation of any corresponding collateral, subject to certain limitations on termination, settlement, and liquidation of collateral that may apply in the event of the bankruptcy or insolvency of a party. Such limitations should not inhibit the eventual practical realization of the principal benefits of those transactions or the corresponding master netting arrangement or similar agreement and any corresponding collateral.

Note 4. Principles of Consolidation

GAAP requires us to consider whether securitizations we sponsor and other transfers of financial assets should be treated as sales or financings, as well as whether any VIEs that we hold variable interests in – for example, certain legal entities often used in securitization and other structured finance transactions – should be included in our consolidated financial statements. The GAAP principles we apply require us to reassess our requirement to consolidate VIEs each quarter and therefore our determination may change based upon new facts and circumstances pertaining to each VIE. This could result in a material impact to our consolidated financial statements during subsequent reporting periods.

Note 4. Principles of Consolidation - (continued)

Analysis of Consolidated VIEs

At March 31, 2019, we consolidated our Legacy Sequoia and Sequoia Choice securitization entities that we determined were VIEs and for which we determined we were the primary beneficiary. Additionally, beginning in the second half of 2018, we consolidated certain third-party Freddie Mac K-Series securitization entities and the Freddie Mac SLST securitization entity that we determined were VIEs and for which we determined we were the primary beneficiary. Each of these entities is independent of Redwood and of each other and the assets and liabilities of these entities are not owned by and are not legal obligations of ours. Our exposure to these entities is primarily through the financial interests we have retained, although for the consolidated Sequoia entities we are exposed to certain financial risks associated with our role as a sponsor, servicing administrator, or depositor of these entities or as a result of our having sold assets directly or indirectly to these entities. At March 31, 2019, the estimated fair value of our investments in the consolidated Legacy Sequoia, Sequoia Choice, Freddie Mac SLST and Freddie Mac K-Series entities was $11 million, $218 million, $236 million, and $129 million, respectively.

Beginning in the fourth quarter of 2018, we consolidated two Servicing Investment entities formed to invest in servicing-related assets that we determined were VIEs and for which we determined we were the primary beneficiary. At March 31, 2019, we held an 80% ownership interest in, and were responsible for the management of, each entity. See *Note 10* for a further description of these entities and the investments they hold and *Note 12* for additional information on the minority partner's interest. Additionally, beginning in the fourth quarter of 2018, we consolidated an entity that was formed to finance servicing advances that we determined was a VIE and for which we, through our control of one of the aforementioned partnerships, were the primary beneficiary. The servicer advance financing consists of non-recourse short-term securitization debt, secured by servicing advances. We consolidate the securitization entity, but the securitization entity is independent of Redwood and the assets and liabilities are not owned by and are not legal obligations of Redwood. See *Note 13* for additional information on the servicer advance financing. At March 31, 2019, the estimated fair value of our investment in the Servicing Investment entities was $66 million.

The following table presents a summary of the assets and liabilities of these VIEs.

Table 4.1 – Assets and Liabilities of Consolidated VIEs

March 31, 2019 (Dollars in Thousands)	Legacy Sequoia	Sequoia Choice	Freddie Mac SLST	Freddie Mac K-Series	Servicing Investment	Total Consolidated VIEs
Residential loans, held-for-investment	$ 488,645	$ 2,333,248	$ 1,228,317	$ —	$ —	$ 4,050,210
Multifamily loans, held-for-investment	—	—	—	2,175,899	—	2,175,899
Other investments	—	—	—	—	318,677	318,677
Cash and cash equivalents	—	—	—	—	11,375	11,375
Restricted cash	146	14	—	—	3,189	3,349
Accrued interest receivable	776	9,616	3,861	6,587	3,251	24,091
REO	2,280	—	—	—	—	2,280
Total Assets	$ 491,847	$ 2,342,878	$ 1,232,178	$ 2,182,486	$ 336,492	$ 6,585,881
Short-term debt	$ —	$ —	$ —	$ —	$ 249,557	$ 249,557
Accrued interest payable	531	7,854	2,846	6,230	403	17,864
Accrued expenses and other liabilities	—	14	—	—	20,598	20,612
Asset-backed securities issued	479,999	2,117,356	993,032	2,047,257	—	5,637,644
Total Liabilities	$ 480,530	$ 2,125,224	$ 995,878	$ 2,053,487	$ 270,558	$ 5,925,677
Number of VIEs	20	7	1	3	3	34

Note 4. Principles of Consolidation - (continued)

December 31, 2018 (Dollars in Thousands)	Legacy Sequoia	Sequoia Choice	Freddie Mac SLST	Freddie Mac K-Series	Servicing Investment	Total Consolidated VIEs
Residential loans, held-for-investment	$ 519,958	$ 2,079,382	$ 1,222,669	$ —	$ —	$ 3,822,009
Multifamily loans, held-for-investment	—	—	—	2,144,598	—	2,144,598
Other investments	—	—	—	—	312,688	312,688
Restricted cash	146	1,022	—	—	25,363	26,531
Accrued interest receivable	822	8,988	3,926	6,595	1,091	21,422
REO	3,943	—	—	—	—	3,943
Total Assets	$ 524,869	$ 2,089,392	$ 1,226,595	$ 2,151,193	$ 339,142	$ 6,331,191
Short-term debt	$ —	$ —	$ —	$ —	$ 262,740	$ 262,740
Accrued interest payable	571	7,180	2,907	6,239	483	17,380
Accrued expenses and other liabilities	—	1,022	—	—	18,592	19,614
Asset-backed securities issued	512,240	1,885,010	993,748	2,019,075	—	5,410,073
Total Liabilities	$ 512,811	$ 1,893,212	$ 996,655	$ 2,025,314	$ 281,815	$ 5,709,807
Number of VIEs	20	6	1	3	3	33

We consolidate the assets and liabilities of certain Sequoia securitization entities, as we did not meet the GAAP sale criteria at the time we transferred financial assets to these entities. Our involvement in consolidated Sequoia entities continues in the following ways: (i) we continue to hold subordinate investments in each entity, and for certain entities, more senior investments; (ii) we maintain certain discretionary rights associated with our sponsorship of, or our subordinate investments in, each entity; and (iii) we continue to hold a right to call the assets of certain entities (once they have been paid down below a specified threshold) at a price equal to, or in excess of, the current outstanding principal amount of the entity's asset-backed securities issued. These factors have resulted in our continuing to consolidate the assets and liabilities of these Sequoia entities in accordance with GAAP.

We consolidate the assets and liabilities of certain Freddie Mac K-Series securitization trusts and a Freddie Mac SLST securitization trust resulting from our investment in subordinate securities issued by these trusts. Additionally, we consolidate the assets and liabilities of Servicing Investment entities from our investment in servicer advance investments and excess MSRs. In each case, we maintain certain discretionary rights associated with the ownership of these investments that we determined reflected a controlling financial interest, as we have both the power to direct the activities that most significantly impact the economic performance of the VIEs and the right to receive benefits of and the obligation to absorb losses from the VIEs that could potentially be significant to the VIEs.

Analysis of Unconsolidated VIEs with Continuing Involvement

Since 2012, we have transferred residential loans to 44 Sequoia securitization entities sponsored by us that are still outstanding as of March 31, 2019, and accounted for these transfers as sales for financial reporting purposes, in accordance with ASC 860. We also determined we were not the primary beneficiary of these VIEs as we lacked the power to direct the activities that will have the most significant economic impact on the entities. For certain of these transfers to securitization entities, for the transferred loans where we held the servicing rights prior to the transfer and continued to hold the servicing rights following the transfer, we recorded mortgage servicing rights ("MSRs") on our consolidated balance sheets, and classified those MSRs as Level 3 assets. We also retained senior and subordinate securities in these securitizations that we classified as Level 3 assets. Our continuing involvement in these securitizations is limited to customary servicing obligations associated with retaining servicing rights (which we retain a third-party sub-servicer to perform) and the receipt of interest income associated with the securities we retained.

During the three months ended March 31, 2019, the master servicer for one of our unconsolidated Sequoia entities exercised their right to call the securitization and paid off the underlying securities. We realized a $4 million gain related to the called securities, which was recognized through Realized gains, net on our consolidated statements of income. In connection with this called securitization, Redwood acquired $39 million of residential real estate loans that are held in both our held-for-sale and held-for-investment portfolios at Redwood at March 31, 2019.

Note 4. Principles of Consolidation - (continued)

The following table presents information related to securitization transactions that occurred during the three months ended March 31, 2019 and 2018.

Table 4.2 – Securitization Activity Related to Unconsolidated VIEs Sponsored by Redwood

	Three Months Ended March 31,	
(In Thousands)	**2019**	**2018**
Principal balance of loans transferred	$ 348,257	$ 1,280,468
Trading securities retained, at fair value	1,716	12,491
AFS securities retained, at fair value	885	3,905

The following table summarizes the cash flows during the three months ended March 31, 2019 and 2018 between us and the unconsolidated VIEs sponsored by us and accounted for as sales since 2012.

Table 4.3 – Cash Flows Related to Unconsolidated VIEs Sponsored by Redwood

	Three Months Ended March 31,	
(In Thousands)	**2019**	**2018**
Proceeds from new transfers	$ 352,371	$ 1,289,687
MSR fees received	3,060	3,414
Funding of compensating interest, net	(90)	(25)
Cash flows received on retained securities	7,546	7,043

The following table presents the key weighted-average assumptions used to measure MSRs and securities retained at the date of securitization for securitizations completed during the three months ended March 31, 2019 and 2018.

Table 4.4 – Assumptions Related to Assets Retained from Unconsolidated VIEs Sponsored by Redwood

	Three Months Ended March 31, 2019		Three Months Ended March 31, 2018	
At Date of Securitization	**Senior IO Securities**	**Subordinate Securities**	**Senior IO Securities**	**Subordinate Securities**
Prepayment rates	16%	14%	8%	10%
Discount rates	14%	8%	14%	7%
Credit loss assumptions	0.20%	0.20%	0.20%	0.20%

Note 4. Principles of Consolidation - (continued)

The following table presents additional information at March 31, 2019 and December 31, 2018, related to unconsolidated VIEs sponsored by Redwood and accounted for as sales since 2012.

Table 4.5 – Unconsolidated VIEs Sponsored by Redwood

(In Thousands)	March 31, 2019	December 31, 2018
On-balance sheet assets, at fair value:		
Interest-only, senior and subordinate securities, classified as trading	$ 128,273	$ 129,111
Subordinate securities, classified as AFS	150,630	162,314
Mortgage servicing rights	53,657	58,572
Maximum loss exposure (1)	$ 332,560	$ 349,997
Assets transferred:		
Principal balance of loans outstanding	$ 10,632,174	$ 10,580,216
Principal balance of loans 30+ days delinquent	27,229	21,805

(1) Maximum loss exposure from our involvement with unconsolidated VIEs pertains to the carrying value of our securities and MSRs retained from these VIEs and represents estimated losses that would be incurred under severe, hypothetical circumstances, such as if the value of our interests and any associated collateral declines to zero. This does not include, for example, any potential exposure to representation and warranty claims associated with our initial transfer of loans into a securitization.

The following table presents key economic assumptions for assets retained from unconsolidated VIEs and the sensitivity of their fair values to immediate adverse changes in those assumptions at March 31, 2019 and December 31, 2018.

Table 4.6 – Key Assumptions and Sensitivity Analysis for Assets Retained from Unconsolidated VIEs Sponsored by Redwood

March 31, 2019 (Dollars in Thousands)	MSRs	Senior Securities (1)	Subordinate Securities
Fair value at March 31, 2019	$ 53,657	$ 57,536	$ 221,367
Expected life (in years) (2)	8	7	15
Prepayment speed assumption (annual CPR) (2)	8%	10%	8%
Decrease in fair value from:			
10% adverse change	$ 1,749	$ 1,951	$ 92
25% adverse change	4,199	4,924	927
Discount rate assumption (2)	11%	12%	5%
Decrease in fair value from:			
100 basis point increase	$ 2,092	$ 1,783	$ 22,094
200 basis point increase	4,036	3,629	40,797
Credit loss assumption (2)	N/A	0.20%	0.20%
Decrease in fair value from:			
10% higher losses	N/A	$ —	$ 1,504
25% higher losses	N/A	—	3,754

Note 4. Principles of Consolidation - (continued)

December 31, 2018 **(Dollars in Thousands)**	**MSRs**	**Senior Securities** (1)	**Subordinate Securities**
Fair value at December 31, 2018	$ 58,572	$ 61,178	$ 230,247
Expected life (in years) (2)	8	7	15
Prepayment speed assumption (annual CPR) (2)	7%	10%	9%
Decrease in fair value from:			
10% adverse change	$ 1,668	$ 2,151	$ 201
25% adverse change	4,027	5,127	1,372
Discount rate assumption (2)	11%	12%	6%
Decrease in fair value from:			
100 basis point increase	$ 2,323	$ 2,190	$ 21,982
200 basis point increase	4,493	4,226	40,641
Credit loss assumption (2)	N/A	0.20%	0.20%
Decrease in fair value from:			
10% higher losses	N/A	$ —	$ 1,387
25% higher losses	N/A	—	3,471

(1) Senior securities included $58 million and $61 million of interest-only securities at March 31, 2019 and December 31, 2018, respectively.

(2) Expected life, prepayment speed assumption, discount rate assumption, and credit loss assumption presented in the tables above represent weighted averages.

Analysis of Unconsolidated Third-Party VIEs

Third-party VIEs are securitization entities in which we maintain an economic interest, but do not sponsor. Our economic interest may include several securities and other investments from the same third-party VIE, and in those cases, the analysis is performed in consideration of all of our interests. The following table presents a summary of our interests in third-party VIEs at March 31, 2019 and December 31, 2018, grouped by asset type.

Table 4.7 – Third-Party Sponsored VIE Summary

(In Thousands)	**March 31, 2019**	**December 31, 2018**
Mortgage-Backed Securities		
Senior	$ 173,102	$ 185,107
Mezzanine	664,496	547,249
Subordinate	426,651	428,713
Total Mortgage-Backed Securities	1,264,249	1,161,069
Excess MSR	14,234	15,092
Total Investments in Third-Party Sponsored VIEs	$ 1,278,483	$ 1,176,161

We determined that we are not the primary beneficiary of these third-party VIEs, as we do not have the required power to direct the activities that most significantly impact the economic performance of these entities. Specifically, we do not service or manage these entities or otherwise solely hold decision making powers that are significant. As a result of this assessment, we do not consolidate any of the underlying assets and liabilities of these third-party VIEs – we only account for our specific interests in them.

Our assessments of whether we are required to consolidate a VIE may change in subsequent reporting periods based upon changing facts and circumstances pertaining to each VIE. Any related accounting changes could result in a material impact to our financial statements.

Note 5. Fair Value of Financial Instruments

For financial reporting purposes, we follow a fair value hierarchy established under GAAP that is used to determine the fair value of financial instruments. This hierarchy prioritizes relevant market inputs in order to determine an “exit price” at the measurement date, or the price at which an asset could be sold or a liability could be transferred in an orderly process that is not a forced liquidation or distressed sale. Level 1 inputs are observable inputs that reflect quoted prices for identical assets or liabilities in active markets. Level 2 inputs are observable inputs other than quoted prices for an asset or liability that are obtained through corroboration with observable market data. Level 3 inputs are unobservable inputs (e.g., our own data or assumptions) that are used when there is little, if any, relevant market activity for the asset or liability required to be measured at fair value.

In certain cases, inputs used to measure fair value fall into different levels of the fair value hierarchy. In such cases, the level at which the fair value measurement falls is determined based on the lowest level input that is significant to the fair value measurement. Our assessment of the significance of a particular input requires judgment and considers factors specific to the asset or liability being measured.

Note 5. Fair Value of Financial Instruments - (continued)

The following table presents the carrying values and estimated fair values of assets and liabilities that are required to be recorded or disclosed at fair value at March 31, 2019 and December 31, 2018.

Table 5.1 – Carrying Values and Fair Values of Assets and Liabilities

	March 31, 2019		December 31, 2018	
(In Thousands)	Carrying Value	Fair Value	Carrying Value	Fair Value
Assets				
Residential loans, held-for-sale				
At fair value	$ 819,111	$ 819,111	$ 1,048,690	$ 1,048,690
At lower of cost or fair value	110	130	111	131
Residential loans, held-for-investment	6,455,080	6,455,080	6,205,941	6,205,941
Business purpose residential loans	160,612	160,612	141,258	141,258
Multifamily loans	2,175,899	2,175,899	2,144,598	2,144,598
Trading securities	1,255,224	1,255,224	1,118,612	1,118,612
Available-for-sale securities	287,928	287,928	333,882	333,882
Servicer advance investments (1)	303,920	303,920	300,468	300,468
MSRs (1)	55,284	55,284	60,281	60,281
Participation in loan warehouse facility (1)	—	—	39,703	39,703
Excess MSRs (1)	28,992	28,992	27,312	27,312
Cash and cash equivalents	200,837	200,837	175,764	175,764
Restricted cash	14,614	14,614	29,313	29,313
Accrued interest receivable	48,972	48,972	47,105	47,105
Derivative assets	22,283	22,283	35,789	35,789
REO (2)	7,275	7,531	3,943	4,396
Margin receivable (2)	154,549	154,549	100,773	100,773
FHLBC stock (2)	43,393	43,393	43,393	43,393
Guarantee asset (2)	2,342	2,342	2,618	2,618
Pledged collateral (2)	42,631	42,631	42,433	42,433
Liabilities				
Short-term debt facilities	$ 1,713,749	$ 1,713,749	$ 1,937,920	$ 1,937,920
Short-term debt - servicer advance financing	249,557	249,557	262,740	262,740
Accrued interest payable	39,526	39,526	42,528	42,528
Margin payable (3)	19	19	835	835
Guarantee obligation (3)	16,359	16,210	16,711	16,774
Contingent consideration (3)	24,621	24,621	—	—
Derivative liabilities	110,942	110,942	84,855	84,855
ABS issued at fair value	5,637,644	5,637,644	5,410,073	5,410,073
FHLBC long-term borrowings	1,999,999	1,999,999	1,999,999	1,999,999
Convertible notes, net	633,994	632,470	633,196	618,271
Trust preferred securities and subordinated notes, net	138,593	100,440	138,582	102,533

(1) These investments are included in Other investments on our consolidated balance sheets.

(2) These assets are included in Other assets on our consolidated balance sheets.

(3) These liabilities are included in Accrued expenses and other liabilities on our consolidated balance sheets.

Note 5. Fair Value of Financial Instruments - (continued)

During the three months ended March 31, 2019, we elected the fair value option for $32 million of residential senior securities, $120 million of subordinate securities, $1.00 billion of residential loans (principal balance), $65 million of business purpose residential loans (principal balance), $69 million of servicer advance investments, and $2 million of excess MSRs. We anticipate electing the fair value option for all future purchases of residential loans that we intend to sell to third parties or transfer to securitizations, as well as for business purpose residential loans and for certain securities we purchase, including IO securities and fixed-rate securities rated investment grade or higher.

The following table presents the assets and liabilities that are reported at fair value on our consolidated balance sheets on a recurring basis at March 31, 2019 and December 31, 2018, as well as the fair value hierarchy of the valuation inputs used to measure fair value.

Table 5.2 – Assets and Liabilities Measured at Fair Value on a Recurring Basis

March 31, 2019	Carrying	Fair Value Measurements Using		
(In Thousands)	Value	Level 1	Level 2	Level 3
Assets				
Residential loans	$ 7,274,191	$ —	$ —	$ 7,274,191
Business purpose residential loans	160,612	—	—	160,612
Multifamily loans	2,175,899	—	—	2,175,899
Trading securities	1,255,224	—	—	1,255,224
Available-for-sale securities	287,928	—	—	287,928
Servicer advance investments	303,920	—	—	303,920
MSRs	55,284	—	—	55,284
Excess MSRs	28,992	—	—	28,992
Derivative assets	22,283	5,826	11,490	4,967
Pledged collateral	42,631	42,631	—	—
FHLBC stock	43,393	—	43,393	—
Guarantee asset	2,342	—	—	2,342
Liabilities				
Contingent consideration	$ 24,621	$ —	$ —	$ 24,621
Derivative liabilities	110,942	9,609	100,561	772
ABS issued	5,637,644	—	—	5,637,644

Note 5. Fair Value of Financial Instruments - (continued)

December 31, 2018 (In Thousands)	Carrying Value	Fair Value Measurements Using		
		Level 1	Level 2	Level 3
Assets				
Residential loans	$ 7,254,631	$ —	$ —	$ 7,254,631
Business purpose residential loans	141,258	—	—	141,258
Multifamily loans	2,144,598	—	—	2,144,598
Trading securities	1,118,612	—	—	1,118,612
Available-for-sale securities	333,882	—	—	333,882
Servicer advance investments	300,468	—	—	300,468
MSRs	60,281	—	—	60,281
Excess MSRs	27,312	—	—	27,312
Derivative assets	35,789	4,665	28,211	2,913
Pledged collateral	42,433	42,433	—	—
FHLBC stock	43,393	—	43,393	—
Guarantee asset	2,618	—	—	2,618
Liabilities				
Derivative liabilities	$ 84,855	$ 13,215	$ 70,908	$ 732
ABS issued	5,410,073	—	—	5,410,073

The following table presents additional information about Level 3 assets and liabilities measured at fair value on a recurring basis for the three months ended March 31, 2019.

Table 5.3 – Changes in Level 3 Assets and Liabilities Measured at Fair Value on a Recurring Basis

	Assets								
(In Thousands)	Residential Loans	Business Purpose Residential Loans	Multifamily Loans	Trading Securities	AFS Securities	Servicer Advance Investments	MSRs	Excess MSRs	Guarantee Asset
Beginning balance - December 31, 2018	$ 7,254,631	$ 141,258	$ 2,144,598	$ 1,118,612	$ 333,882	$ 300,468	$ 60,281	$ 27,312	$ 2,618
Acquisitions	1,022,198	29,093	—	152,587	4,885	68,976	104	2,117	—
Originations	—	35,968	—	—	—	—	—	—	—
Sales	(833,078)	(20,590)	—	(32,002)	(42,016)	—	—	—	—
Principal paydowns	(240,406)	(20,992)	(3,071)	(5,832)	(18,666)	(66,532)	—	—	—
Gains (losses) in net income, net	70,833	871	34,372	21,859	12,616	1,008	(5,101)	(437)	(276)
Unrealized losses in OCI, net	—	—	—	—	(2,773)	—	—	—	—
Other settlements, net (2)	13	(4,996)	—	—	—	—	—	—	—
Ending Balance - March 31, 2019	$ 7,274,191	$ 160,612	$ 2,175,899	$ 1,255,224	$ 287,928	$ 303,920	$ 55,284	$ 28,992	$ 2,342

Note 5. Fair Value of Financial Instruments - (continued)

Table 5.3 – Changes in Level 3 Assets and Liabilities Measured at Fair Value on a Recurring Basis (continued)

		Liabilities	
(In Thousands)	**Derivatives(1)**	**Contingent Consideration**	**ABS Issued**
Beginning balance - December 31, 2018	$ 2,181	$ —	$ 5,410,073
Acquisitions	—	24,621	330,535
Principal paydowns	—	—	(163,146)
Gains (losses) in net income, net	11,452	—	60,182
Other settlements, net (2)	(9,438)	—	—
Ending Balance - March 31, 2019	$ 4,195	$ 24,621	$ 5,637,644

(1) For the purpose of this presentation, derivative assets and liabilities, which consist of loan purchase and forward sale commitments, are presented on a net basis.

(2) Other settlements, net for residential and business purpose residential loans represents the transfer of loans to REO, and for derivatives, the settlement of forward sale commitments and the transfer of the fair value of loan purchase commitments at the time loans are acquired to the basis of residential loans.

Note 5. Fair Value of Financial Instruments - (continued)

The following table presents the portion of gains or losses included in our consolidated statements of income that were attributable to Level 3 assets and liabilities recorded at fair value on a recurring basis and held at March 31, 2019 and 2018. Gains or losses incurred on assets or liabilities sold, matured, called, or fully written down during the three months ended March 31, 2019 and 2018 are not included in this presentation.

Table 5.4 – Portion of Net Gains (Losses) Attributable to Level 3 Assets and Liabilities Still Held at March 31, 2019 and 2018 Included in Net Income

	Included in Net Income	
	Three Months Ended March 31,	
(In Thousands)	2019	2018
Assets		
Residential loans at Redwood	$ 35,801	$ (42,195)
Residential loans at consolidated Sequoia entities	14,472	20,548
Residential loans at consolidated Freddie Mac SLST entity	23,527	—
Business purpose residential loans	1,050	—
Multifamily loans at consolidated Freddie Mac K-Series entities	34,372	—
Trading securities	21,543	(3,951)
Servicer advance investments	1,008	—
MSRs	(4,295)	3,933
Excess MSRs	(437)	—
Loan purchase commitments	4,962	3,919
Other assets - Guarantee asset	(277)	186
Liabilities		
Loan purchase commitments	$ (753)	$ (2,554)
Loan forward sale commitments	—	(1,269)
ABS issued	(60,182)	(20,735)

The following table presents information on assets recorded at fair value on a non-recurring basis at March 31, 2019. This table does not include the carrying value and gains or losses associated with the asset types below that were not recorded at fair value on our consolidated balance sheets at March 31, 2019.

Table 5.5 – Assets and Liabilities Measured at Fair Value on a Non-Recurring Basis at March 31, 2019

March 31, 2019	Carrying	Fair Value Measurements Using			Gain (Loss) for Three Months Ended
(In Thousands)	Value	Level 1	Level 2	Level 3	March 31, 2019
Assets					
REO	$ 5,821	$ —	$ —	$ 5,821	$ (272)

Note 5. Fair Value of Financial Instruments - (continued)

The following table presents the net market valuation gains and losses recorded in each line item of our consolidated statements of income for the three months ended March 31, 2019 and 2018.

Table 5.6 – Market Valuation Gains and Losses, Net

	Three Months Ended March 31,	
(In Thousands)	**2019**	**2018**
Mortgage Banking Activities, Net		
Residential loans held-for-sale, at fair value	$ 3,533	$ 4,774
Residential loan purchase and forward sale commitments	11,311	(6,968)
Single-family rental loans held-for-sale, at fair value	1,603	—
Single-family rental loan purchase commitments	141	—
Residential bridge loans	86	—
Risk management derivatives, net	(4,984)	28,432
Total mortgage banking activities, net (1)	$ 11,690	$ 26,238
Investment Fair Value Changes, Net		
Residential loans held-for-investment, at Redwood	$ 28,108	$ (38,985)
Residential bridge loans held-for-investment	(303)	—
Trading securities	21,860	(2,955)
Servicer advance investments	1,008	—
Excess MSRs	(437)	—
Net investments in Legacy Sequoia entities (2)	(374)	(8)
Net investments in Sequoia Choice entities (2)	3,265	(86)
Net investment in Freddie Mac SLST entity (2)	6,365	—
Net investments in Freddie Mac K-Series entities (2)	3,119	—
Risk-sharing investments	(77)	(139)
Risk management derivatives, net	(42,375)	43,782
Total investment fair value changes, net	$ 20,159	$ 1,609
Other Income (Expense), Net		
MSRs	$ (5,102)	$ 2,892
Risk management derivatives, net	2,251	(5,139)
Gain on re-measurement of 5 Arches investment	2,441	—
Total other expense, net (3)	$ (410)	$ (2,247)
Total Market Valuation Gains, Net	$ 31,439	$ 25,600

(1) Mortgage banking activities, net presented above does not include fee income or provisions for repurchases that are components of Mortgage banking activities, net presented on our consolidated statements of income, as these amounts do not represent market valuation changes.

(2) Includes changes in fair value of the residential loans held-for-investment, REO and the ABS issued at the entities, which netted together represent the change in value of our retained investments at the consolidated VIEs.

(3) Other income, net presented above does not include net MSR fee income or provisions for repurchases for MSRs, as these amounts do not represent market valuation adjustments.

At March 31, 2019, our valuation policy and processes had not changed from those described in our Annual Report on Form 10-K for the year ended December 31, 2018. The following table provides quantitative information about the significant unobservable inputs used in the valuation of our Level 3 assets and liabilities measured at fair value.

Note 5. Fair Value of Financial Instruments - (continued)

Table 5.7 – Fair Value Methodology for Level 3 Financial Instruments

March 31, 2019 (Dollars in Thousands, except Input Values)	Fair Value	Unobservable Input	Input Values Range		Weighted Average
Assets					
Residential loans, at fair value:					
Jumbo fixed-rate loans	$ 2,436,401	Whole loan spread to TBA price	$ 2.25 - $ 2.25		$ 2.25
		Whole loan spread to swap rate	80 - 215	bps	158 bps
Jumbo hybrid loans	400,412	Prepayment rate (annual CPR)	15 - 15	%	15 %
		Whole loan spread to swap rate	40 - 155	bps	107 bps
Jumbo loans committed to sell	387,168	Whole loan committed sales price	$ 101.30 - $ 103.13		$ 101.83
Loans held by Legacy Sequoia (1)	488,645	Liability price	N/A		N/A
Loans held by Sequoia Choice (1)	2,333,248	Liability price	N/A		N/A
Loans held by Freddie Mac SLST	1,228,317	Liability price	N/A		N/A
Business purpose residential loans:					
Single-family rental loans	56,696	IO discount rate	12 - 12	%	12 %
		Prepayment rate (annual CPR)	2 - 10	%	5 %
		Senior credit spread	95 - 95	bps	95 bps
		Subordinate credit spread	140 - 1,200	bps	296 bps
		Senior credit support	35 - 35	%	35 %
Residential bridge loans	103,915	Discount rate	7 - 7	%	7 %
Multifamily loans held by Freddie Mac K-Series (1)	2,175,899	Liability price	N/A		N/A
Trading and AFS securities	1,543,152	Discount rate	2 - 14	%	5 %
		Prepayment rate (annual CPR)	— - 60	%	9 %
		Default rate	— - 20	%	2 %
		Loss severity	— - 40	%	21 %
Servicer advance investments	303,920	Discount rate	5 - 5	%	5 %
		Prepayment rate (annual CPR)	8 - 16	%	14 %
		Expected remaining life (2)	2 - 2	years	2 years
		Mortgage servicing income	6 - 14	bps	10 bps
MSRs	55,284	Discount rate	11 - 30	%	11 %
		Prepayment rate (annual CPR)	5 - 64	%	9 %
		Per loan annual cost to service	$ 82 - $ 82		$ 82
Excess MSRs	28,992	Discount rate	12 - 18	%	15 %
		Prepayment rate (annual CPR)	8 - 14	%	11 %
		Excess mortgage servicing income	7 - 18	bps	12 bps
Guarantee asset	2,342	Discount rate	11 - 11	%	11 %
		Prepayment rate (annual CPR)	11 - 11	%	11 %
REO	5,821	Loss severity	7 - 51	%	10 %

Loan purchase commitments, net	4,195	MSR multiple		0.9	-		4.9	x		2.6	x
		Pull-through rate		8	-		100	%		69	%
		Whole loan spread to TBA price	$	2.25	-	$	2.25		$	2.25	
		Whole loan spread to swap rate - fixed rate		95	-		215	bps		187	bps
		Prepayment rate (annual CPR)		15	-		15	%		15	%
		Whole loan spread to swap rate - hybrid		85	-		155	bps		109	bps

Note 5. Fair Value of Financial Instruments - (continued)

Table 5.7 – Fair Value Methodology for Level 3 Financial Instruments (continued)

March 31, 2019			Input Values		
(Dollars in Thousands, except Input Values)	Fair Value	Unobservable Input	Range		Weighted Average
Liabilities					
ABS issued (1):					
At consolidated Sequoia entities	2,597,355	Discount rate	4	- 15 %	4 %
		Prepayment rate (annual CPR)	8	- 65 %	18 %
		Default rate	—	- 9 %	2 %
		Loss severity	20	- 22 %	22 %
At consolidated Freddie Mac SLST entity	993,032	Discount rate	3	- 3 %	3 %
		Prepayment rate (annual CPR)	6	- 6 %	6 %
		Default rate	2	- 2 %	2 %
		Loss severity	30	- 30 %	30 %
At consolidated Freddie Mac K-Series entities	2,047,257	Discount rate	3	- 9 %	3 %
		Prepayment rate (annual CPR)	—	- — %	— %
		Default rate	1	- 1 %	1 %
		Loss severity	20	- 20 %	20 %
Contingent consideration	24,621	Discount rate	23	- 23 %	23 %
		Probability of outcomes (3)	—	- 100 %	90 %

(1) The fair value of the loans held by consolidated entities was based on the fair value of the ABS issued by these entities, which we determined were more readily observable, in accordance with accounting guidance for collateralized financing entities.

(2) Represents the estimated average duration of outstanding servicer advances at a given point in time (not taking into account new advances made with respect to the pool).

(3) Represents the probability of a full payout of contingent purchase consideration.

Determination of Fair Value

A description of the instruments measured at fair value as well as the general classification of such instruments pursuant to the Level 1, Level 2, and Level 3 valuation hierarchy is listed herein. We generally use both market comparable information and discounted cash flow modeling techniques to determine the fair value of our Level 3 assets and liabilities. Use of these techniques requires determination of relevant inputs and assumptions, some of which represent significant unobservable inputs as indicated in the preceding table. Accordingly, a significant increase or decrease in any of these inputs – such as anticipated credit losses, prepayment rates, interest rates, or other valuation assumptions – in isolation would likely result in a significantly lower or higher fair value measurement.

Residential loans at Redwood

Estimated fair values for residential loans are determined using models that incorporate various observable inputs, including pricing information from whole loan sales and securitizations. Certain significant inputs in these models are considered unobservable and are therefore Level 3 in nature. Pricing inputs obtained from market whole loan transaction activity include indicative spreads to indexed to be announced ("TBA") prices and indexed swap rates for fixed-rate loans and indexed swap rates for hybrid loans (Level 3). Pricing inputs obtained from market securitization activity include indicative spreads to indexed TBA prices for senior residential mortgage-backed securities ("RMBS") and indexed swap rates for subordinate RMBS, and credit support levels (Level 3). Other unobservable inputs also include assumed future prepayment rates. Observable inputs include benchmark interest rates, swap rates, and TBA prices. These assets would generally decrease in value based upon an increase in the credit spread, prepayment speed, or credit support assumptions.

Note 5. Fair Value of Financial Instruments - (continued)

Residential and multifamily loans at consolidated entities

We have elected to account for our consolidated securitization entities as CFEs in accordance with GAAP. A CFE is a variable interest entity that holds financial assets and issues beneficial interests in those assets, and these beneficial interests have contractual recourse only to the related assets of the CFE. Accounting guidance for CFEs allow companies to elect to measure both the financial assets and financial liabilities of a CFE using the more observable of the fair value of the financial assets or fair value of the financial liabilities. Pursuant to this guidance, we use the fair value of the ABS issued by the CFEs (which we determined to be more observable) to determine the fair value of the loans held at these entities, whereby the net assets we consolidate in our financial statements related to these entities represent the estimated fair value of our retained interests in the CFEs.

Business purpose residential loans

Business purpose residential loans include single-family rental loans and residential bridge loans that are generally illiquid in nature and trade infrequently. Significant inputs in the valuation analysis are predominantly Level 3 in nature, due to the lack of readily available market quotes and related inputs.

Prices for our single-family rental loans are determined using market comparable information. Significant inputs obtained from market activity include indicative spreads to indexed swap rates for senior and subordinate mortgage-backed securities ("MBS"), IO MBS discount rates, senior credit support levels, and assumed future prepayment rates (Level 3). These assets would generally decrease in value based upon an increase in the credit spread or prepayment speed assumptions.

Prices for our residential bridge loans are determined using discounted cash flow modeling, which incorporates a primary significant unobservable input of discount rate. These assets would generally decrease in value based upon an increase in the discount rate.

Real estate securities

Real estate securities include residential, multifamily, and other mortgage-backed securities that are generally illiquid in nature and trade infrequently. Significant inputs in the valuation analysis are predominantly Level 3 in nature, due to the lack of readily available market quotes and related inputs. For real estate securities, we utilize both market comparable pricing and discounted cash flow analysis valuation techniques. Relevant market indicators that are factored into the analysis include bid/ask spreads, the amount and timing of credit losses, interest rates, and collateral prepayment rates. Estimated fair values are based on applying the market indicators to generate discounted cash flows (Level 3). These cash flow models use significant unobservable inputs such as a discount rate, prepayment rate, default rate and loss severity. The estimated fair value of our securities would generally decrease based upon an increase in discount rate, default rates, loss severities, or a decrease in prepayment rates.

As part of our securities valuation process, we request and consider indications of value from third-party securities dealers. For purposes of pricing our securities at March 31, 2019, we received dealer price indications on 87% of our securities, representing 95% of our carrying value. In the aggregate, our internal valuations of the securities for which we received dealer price indications were within 2% of the aggregate average dealer valuations. Once we receive the price indications from dealers, they are compared to other relevant market inputs, such as actual or comparable trades, and the results of our discounted cash flow analysis. In circumstances where relevant market inputs cannot be obtained, increased reliance on discounted cash flow analysis and management judgment are required to estimate fair value.

Derivative assets and liabilities

Our derivative instruments include swaps, TBAs, loan purchase commitments ("LPCs"), and forward sale commitments ("FSCs"). Fair values of derivative instruments are determined using quoted prices from active markets, when available, or from valuation models and are supported by valuations provided by dealers active in derivative markets. Fair values of TBAs and financial futures are generally obtained using quoted prices from active markets (Level 1). Our derivative valuation models for swaps require a variety of inputs, including contractual terms, market prices, yield curves, credit curves, measures of volatility, prepayment rates, and correlations of certain inputs. Model inputs can generally be verified and model selection does not involve significant management judgment (Level 2).

LPC and FSC fair values for residential jumbo and single-family rental loans are estimated based on the estimated fair values of the underlying loans (as described in "*Residential loans at Redwood*" and "*Business purpose residential loans*" above). In addition, fair values for LPCs are estimated based on the probability that the mortgage loan will be purchased (the "Pull-through rate") (Level 3).

Note 5. Fair Value of Financial Instruments - (continued)

For other derivatives, valuations are based on various factors such as liquidity, bid/ask spreads, and credit considerations for which we rely on available market inputs. In the absence of such inputs, management’s best estimate is used (Level 3).

Servicer advance investments

Estimated fair values for servicer advance investments are determined through internal pricing models that estimate future cash flows and utilize certain significant inputs that are considered unobservable and are therefore Level 3 in nature. Our estimations of cash flows include the combined cash flows of all of the components that comprise the servicer advance investments: existing advances, the requirement to purchase future advances, the recovery of advances, and the right to a portion of the associated mortgage servicing fee ("mortgage servicing income"). The valuation technique is based on discounted cash flows. Significant inputs used in the valuations included prepayment rate (of the loans underlying the investments), mortgage servicing income, servicer advance WAL (the weighted-average expected remaining life of servicer advances), and discount rate. These assets would generally decrease in value based upon an increase in prepayment rates, an increase in servicer advance WAL, or an increase in discount rate, or a decrease in mortgage servicing income.

MSRs

MSRs include the rights to service jumbo and conforming residential mortgage loans. Significant inputs in the valuation analysis are predominantly Level 3, due to the nature of these instruments and the lack of readily available market quotes. Changes in the fair value of MSRs occur primarily due to the collection/realization of expected cash flows, as well as changes in valuation inputs and assumptions. Estimated fair values are based on applying the inputs to generate the net present value of estimated future MSR income (Level 3). These discounted cash flow models utilize certain significant unobservable inputs including market discount rates, assumed future prepayment rates of serviced loans, and the market cost of servicing. An increase in these unobservable inputs would generally reduce the estimated fair value of the MSRs.

As part of our MSR valuation process, we received a valuation estimate from a third-party valuations firm. In the aggregate, our internal valuation of the MSRs were within 2% of the third-party valuation.

Excess MSRs

Estimated fair values for excess MSRs are determined through internal pricing models that estimate future cash flows and utilize certain significant inputs that are considered unobservable and are therefore Level 3 in nature. The valuation technique is based on discounted cash flows. Significant inputs used in the valuations included prepayment rate (of the loans underlying the investments), the amount of excess servicing income expected to be received ("excess mortgage servicing income"), and discount rate. These assets would generally decrease in value based upon an increase in prepayment rates or discount rate, or a decrease in excess mortgage servicing income.

FHLBC stock

Our Federal Home Loan Bank ("FHLB") member subsidiary is required to purchase Federal Home Loan Bank of Chicago ("FHLBC") stock under a borrowing agreement between our FHLB-member subsidiary and the FHLBC. Under this agreement, the stock is redeemable at face value, which represents the carrying value and fair value of the stock (Level 2).

Guarantee asset

The guarantee asset represents the estimated fair value of cash flows we are contractually entitled to receive related to a risk-sharing arrangement with Fannie Mae. Significant inputs in the valuation analysis are Level 3, due to the nature of this asset and the lack of market quotes. The fair value of the guarantee asset is determined using a discounted cash flow model, for which significant unobservable inputs include assumed future prepayment rates and market discount rate (Level 3). An increase in prepayment rates or discount rate would generally reduce the estimated fair value of the guarantee asset.

Pledged collateral

Pledged collateral consists of cash and U.S. Treasury securities held by a custodian in association with certain agreements we have entered into. Treasury securities are carried at their fair value, which is determined using quoted prices in active markets (Level 1).

Note 5. Fair Value of Financial Instruments - (continued)

Cash and cash equivalents

Cash and cash equivalents include cash on hand and highly liquid investments with original maturities of three months or less. Fair values equal carrying values (Level 1).

Restricted cash

Restricted cash primarily includes interest-earning cash balances related to risk-sharing transactions with the Agencies, cash held in association with borrowings from the FHLBC, cash held at Servicing Investment entities, and cash held at consolidated Sequoia entities for the purpose of distribution to investors and reinvestment. Due to the short-term nature of the restrictions, fair values approximate carrying values (Level 1).

Accrued interest receivable and payable

Accrued interest receivable and payable includes interest due on our assets and payable on our liabilities. Due to the short-term nature of when these interest payments will be received or paid, fair values approximate carrying values (Level 1).

Real estate owned

Real estate owned ("REO") includes properties owned in satisfaction of foreclosed loans. Fair values are determined using available market quotes, appraisals, broker price opinions, comparable properties, or other indications of value (Level 3).

Margin receivable

Margin receivable reflects cash collateral we have posted with our various derivative and debt counterparties as required to satisfy margin requirements. Fair values approximate carrying values (Level 2).

Contingent consideration

Contingent consideration is related to our acquisition of 5 Arches and is estimated and recorded at fair value as part of purchase consideration. Each reporting period we estimate the change in fair value of the contingent consideration, and such change is recognized in our consolidated statements of income, unless it is determined to be a measurement period adjustment. The estimate of the fair value of contingent consideration requires significant judgment and assumptions to be made about future operating results, discount rates, and probabilities of projected operating result scenarios (Level 3).

Short-term debt

Short-term debt includes our credit facilities for residential and business purpose residential loans and real estate securities as well as non-recourse short-term borrowings used to finance servicer advance investments. As these borrowings are secured and subject to margin calls and as the rates on these borrowings reset frequently to market rates, we believe that carrying values approximate fair values (Level 2).

ABS issued

ABS issued includes asset-backed securities issued through the Legacy Sequoia and Sequoia Choice securitization entities, as well as securities issued by certain third-party Freddie Mac SLST and K-series securitization entities which we consolidate. These instruments are generally illiquid in nature and trade infrequently. Significant inputs in the valuation analysis are predominantly Level 3, due to the nature of these instruments and the lack of readily available market quotes. For ABS issued, we utilize both market comparable pricing and discounted cash flow analysis valuation techniques. Relevant market indicators factored into the analysis include bid/ask spreads, the amount and timing of collateral credit losses, interest rates, and collateral prepayment rates. Estimated fair values are based on applying the market indicators to generate discounted cash flows (Level 3). These cash flow models use significant unobservable inputs such as a discount rates, prepayment rate, default rate, loss severity and credit support. A decrease in credit losses or discount rate, or an increase in prepayment rates, would generally cause the fair value of the ABS issued to decrease (i.e., become a larger liability).

Note 5. Fair Value of Financial Instruments - (continued)

FHLBC borrowings

FHLBC borrowings include amounts borrowed from the FHLBC that are secured, generally by residential mortgage loans. As these borrowings are secured and subject to margin calls and as the rates on these borrowings reset frequently to market rates, we believe that carrying values approximate fair values (Level 2).

Financial Instruments Carried at Amortized Cost

Participation in loan warehouse facility

Our participation in a loan warehouse facility is carried at amortized cost (Level 2).

Guarantee obligations

In association with our risk-sharing transactions with the Agencies, we have made certain guarantees which are carried on our balance sheet at amortized cost (Level 3).

Convertible notes

Convertible notes include unsecured convertible and exchangeable senior notes that are carried at their unpaid principal balance net of any unamortized deferred issuance costs. The fair value of the convertible notes is determined using quoted prices in generally active markets (Level 2).

Trust preferred securities and subordinated notes

Trust preferred securities and subordinated notes are carried at their unpaid principal balance net of any unamortized deferred issuance costs (Level 3).

Note 6. Residential Loans

We acquire residential loans from third-party originators and may sell or securitize these loans or hold them for investment. The following table summarizes the classifications and carrying values of the residential loans owned at Redwood and at consolidated Sequoia entities at March 31, 2019 and December 31, 2018.

Table 6.1 – Classifications and Carrying Values of Residential Loans

March 31, 2019 (In Thousands)	**Redwood**	**Legacy Sequoia**	**Sequoia Choice**	**Freddie Mac SLST**	**Total**
Held-for-sale					
At fair value	$ 819,111	$ —	$ —	$ —	$ 819,111
At lower of cost or fair value	110	—	—	—	110
Total held-for-sale	819,221	—	—	—	819,221
Held-for-investment at fair value	2,404,870	488,645	2,333,248	1,228,317	6,455,080
Total Residential Loans	$ 3,224,091	$ 488,645	$ 2,333,248	$ 1,228,317	$ 7,274,301

Note 6. Residential Loans - (continued)

December 31, 2018 **(In Thousands)**	**Redwood**	**Legacy Sequoia**	**Sequoia Choice**	**Freddie Mac SLST**	**Total**
Held-for-sale					
At fair value	$ 1,048,690	$ —	$ —	$ —	$ 1,048,690
At lower of cost or fair value	111	—	—	—	111
Total held-for-sale	1,048,801	—	—	—	1,048,801
Held-for-investment at fair value	2,383,932	519,958	2,079,382	1,222,669	6,205,941
Total Residential Loans	$ 3,432,733	$ 519,958	$ 2,079,382	$ 1,222,669	$ 7,254,742

At March 31, 2019, we owned mortgage servicing rights associated with $2.46 billion (principal balance) of consolidated residential loans purchased from third-party originators. The value of these MSRs is included in the carrying value of the associated loans on our consolidated balance sheets. We contract with licensed sub-servicers that perform servicing functions for these loans.

Residential Loans Held-for-Sale

At Fair Value

At March 31, 2019, we owned 1,109 loans held-for-sale at fair value with an aggregate unpaid principal balance of $802 million and a fair value of $819 million, compared to 1,484 loans with an aggregate unpaid principal balance of $1.03 billion and a fair value of $1.05 billion at December 31, 2018. At both March 31, 2019 and December 31, 2018, one of these loans with a fair value of $0.6 million was greater than 90 days delinquent and none of these loans were in foreclosure.

During the three months ended March 31, 2019 and 2018, we purchased $0.96 billion and $1.80 billion (principal balance) of loans, respectively, for which we elected the fair value option, and we sold $1.16 billion and $2.01 billion (principal balance) of loans, respectively, for which we recorded net market valuation gains of $4 million and $5 million, respectively, through Mortgage banking activities, net on our consolidated statements of income. At March 31, 2019, loans held-for-sale with a market value of $579 million were pledged as collateral under short-term borrowing agreements.

At Lower of Cost or Fair Value

At both March 31, 2019 and December 31, 2018, we held two residential loans at the lower of cost or fair value with $0.1 million in outstanding principal balance and carrying values of $0.1 million. At both March 31, 2019 and December 31, 2018, none of these loans were greater than 90 days delinquent or in foreclosure.

Residential Loans Held-for-Investment at Fair Value

At Redwood

At March 31, 2019, we owned 3,314 held-for-investment loans at Redwood with an aggregate unpaid principal balance of $2.38 billion and a fair value of $2.40 billion, compared to 3,296 loans with an aggregate unpaid principal balance of $2.39 billion and a fair value of $2.38 billion at December 31, 2018. At March 31, 2019, two of these loans with an aggregate fair value of $1 million were greater than 90 days delinquent and one of these loans with a fair value of $0.4 million was in foreclosure. At December 31, 2018, two of these loans with an aggregate fair value of $1 million were greater than 90 days delinquent and none of these loans were in foreclosure.

During the three months ended March 31, 2019, we purchased $39 million (principal balance) of loans, for which we elected the fair value option, and did not sell any loans. During the three months ended March 31, 2019 and 2018, we transferred loans with a fair value of $39 million and $56 million, respectively, from held-for-sale to held-for-investment. During the three months ended March 31, 2019, we transferred loans with a fair value of $23 million from held-for-investment to held-for-sale. During the three months ended March 31, 2018, we did not transfer any loans from held-for-investment to held-for-sale. During the three months ended March 31, 2019 and 2018, we recorded a net market valuation gain of $28 million and a net market valuation loss of $39 million, respectively, on residential loans held-for-investment at fair value through Investment fair value changes, net on our consolidated statements of income. At March 31, 2019, loans with a fair value of $2.41 billion were pledged as collateral under a borrowing agreement with the FHLBC.

Note 6. Residential Loans - (continued)

The outstanding loans held-for-investment at Redwood at March 31, 2019 were prime-quality, first lien loans, of which 96% were originated between 2013 and 2019, and 4% were originated in 2012 and prior years. The weighted average Fair Isaac Corporation ("FICO") score of borrowers backing these loans was 768 (at origination) and the weighted average loan-to-value ("LTV") ratio of these loans was 66% (at origination). At March 31, 2019, these loans were comprised of 88% fixed-rate loans with a weighted average coupon of 4.15%, and the remainder were hybrid or ARM loans with a weighted average coupon of 4.21%.

At Consolidated Legacy Sequoia Entities

At March 31, 2019, we consolidated 2,504 held-for-investment loans at consolidated Legacy Sequoia entities, with an aggregate unpaid principal balance of $508 million and a fair value of $489 million, as compared to 2,641 loans at December 31, 2018, with an aggregate unpaid principal balance of $545 million and a fair value of $520 million. At origination, the weighted average FICO score of borrowers backing these loans was 727, the weighted average LTV ratio of these loans was 66%, and the loans were nearly all first lien and prime-quality.

At March 31, 2019 and December 31, 2018, the aggregate unpaid principal balance of loans at consolidated Legacy Sequoia entities delinquent greater than 90 days was $13 million and $14 million, respectively, of which the aggregate unpaid principal balance of loans in foreclosure was $6 million and $5 million, respectively. During the three months ended March 31, 2019 and 2018, we recorded net market valuation gains of $5 million and $29 million, respectively, on these loans through Investment fair value changes, net on our consolidated statements of income. Pursuant to the collateralized financing entity guidelines, the market valuation changes of these loans are based on the estimated fair value of the associated ABS issued. The net impact to our income statement associated with our retained economic investment in the Legacy Sequoia securitization entities is presented in *Note 5*.

At Consolidated Sequoia Choice Entities

At March 31, 2019, we consolidated 3,143 held-for-investment loans at the consolidated Sequoia Choice entities, with an aggregate unpaid balance of $2.28 billion and a fair value of $2.33 billion, as compared to 2,800 loans at December 31, 2018 with an aggregate unpaid principal balance of $2.04 billion and a fair value of $2.08 billion. At origination, the weighted average FICO score of borrowers backing these loans was 745, the weighted average LTV ratio of these loans was 75%, and the loans were all first lien and prime-quality. At March 31, 2019, two of these loans with an aggregate unpaid principal balance of $1 million were greater than 90 days delinquent and none of these loans were in foreclosure. At December 31, 2018, three of these loans with an aggregate unpaid principal balance of $2 million were greater than 90 days delinquent and none of these loans were in foreclosure.

During the three months ended March 31, 2019 and 2018, we transferred loans with a fair value of $350 million and $452 million, respectively, from held-for-sale to held-for-investment associated with Choice securitizations. During the three months ended March 31, 2019 and 2018, we recorded a net market valuation gain of $10 million and a net market valuation loss of $8 million, respectively, on these loans through Investment fair value changes, net on our consolidated statements of income. Pursuant to the collateralized financing entity guidelines, the market valuation changes of these loans are based on the estimated fair value of the ABS issued associated with Choice securitizations. The net impact to our income statement associated with our retained economic investment in the Sequoia Choice securitization entities is presented in *Note 5*.

At Consolidated Freddie Mac SLST Entity

During the fourth quarter of 2018, we invested in subordinate securities issued by a Freddie Mac SLST securitization trust and were required to consolidate the underlying seasoned re-performing and non-performing residential loans owned at this entity for financial reporting purposes in accordance with GAAP. At securitization, which occurred during the fourth quarter of 2018, each of these mortgage loans was a fully amortizing, fixed- or step-rate, first-lien loan that had been modified. At March 31, 2019, we consolidated 7,844 held-for-investment loans at the consolidated Freddie Mac SLST entity, with an aggregate unpaid balance of $1.29 billion and a fair value of $1.23 billion, compared to 7,900 loans at December 31, 2018 with an aggregate unpaid principal balance of $1.31 billion and a fair value of $1.22 billion. At securitization, the weighted average FICO score of borrowers backing these loans was 597 and the weighted average LTV ratio of these loans was 69%. At March 31, 2019, 520 of these loans with an unpaid principal balance of $84 million were greater than 90 days delinquent and none of these loans were in foreclosure. At December 31, 2018, 306 of these loans with an aggregate unpaid principal balance of $51 million were greater than 90 days delinquent and none of these loans were in foreclosure.

Note 6. Residential Loans - (continued)

During the three months ended March 31, 2019, we recorded a net market valuation gain of $24 million on these loans through Investment fair value changes, net on our consolidated statements of income. Pursuant to the collateralized financing entity guidelines, the market valuation changes of these loans are based on the estimated fair value of the ABS issued associated with the Freddie Mac SLST securitization. The net impact to our income statement associated with our economic investment in the Freddie Mac SLST securitization entity is presented in *Note 5*.

Note 7. Business Purpose Residential Loans

As a result of our acquisition of 5 Arches on March 1, 2019, we now originate business purpose residential loans, including single-family rental loans and residential bridge loans.

Business Purpose Residential Loan Originations

During the period from March 1, 2019 to March 31, 2019, we originated $36 million of business purpose residential loans, of which $21 million were sold to a third party. The remaining business purpose residential loans were transferred to our investment portfolio (residential bridge loans), or retained in our mortgage banking business (single-family rental loans). Prior to the transfer of residential bridge loans to our investment portfolio, we recorded net market valuation gains of $0.1 million on these loans through Mortgage banking activities, net on our consolidated statements of income. Market valuation adjustments on our single-family rental loans are also recorded in Mortgage banking activities, net on our consolidated statements of income. Additionally, during the three months ended March 31, 2019, we recorded loan origination fee income of $0.5 million through Mortgage banking activities, net on our consolidated statements of income.

The following table summarizes the classifications and carrying values of the business purpose residential loans owned at Redwood at March 31, 2019 and December 31, 2018.

Table 7.1 – Classifications and Carrying Values of Business Purpose Residential Loans

(In Thousands)	March 31, 2019	December 31, 2018
Single-family rental loans, held-for-sale at fair value	$ 56,696	$ 28,460
Residential bridge loans, held-for-investment at fair value	103,916	112,798
Total Business Purpose Residential Loans	$ 160,612	$ 141,258

Single-Family Rental Loans Held-for-Sale at Fair Value

At March 31, 2019, we owned 26 single-family rental loans with an aggregate unpaid principal balance of $54 million and a fair value of $57 million, compared to 11 loans at December 31, 2018 with an aggregate unpaid principal balance of $28 million and a fair value of $28 million. At both March 31, 2019 and December 31, 2018, none of these loans were greater than 90 days delinquent or in foreclosure.

Prior to our acquisition of 5 Arches, for the period from January 1, 2019 to February 28, 2019, we purchased $19 million (principal balance) of loans from 5 Arches, for which we elected the fair value option, and we did not sell any loans. During the three months ended March 31, 2019, we recorded a net market valuation gain of $1 million on single-family rental loans held-for-sale at fair value through Mortgage banking activities, net on our consolidated statements of income. At March 31, 2019, loans held-for-sale with a market value of $49 million were pledged as collateral under short-term borrowing agreements. Additionally, single-family rental loans with a fair value of $5 million and other assets of $7 million at 5 Arches served as collateral under the business purpose loan working capital line at March 31, 2019.

The outstanding single-family rental loans held-for-sale at March 31, 2019 were first lien, fixed-rate loans with maturities of five, seven, or ten years. At March 31, 2019, the weighted average coupon of our single-family rental loans was 5.72% and the weighted average loan term was seven years. At origination, the weighted average LTV ratio of these loans was 65% and the weighted average debt service coverage ratio ("DSCR") was 1.28 times.

Residential Bridge Loans Held-for-Investment at Fair Value

At March 31, 2019, we owned 158 residential bridge loans held-for-investment with an aggregate unpaid principal balance of $103 million and a fair value of $104 million, compared to 157 loans at December 31, 2018 with an aggregate unpaid principal balance of $112 million and a fair value of $113 million.

As part of our credit risk management practices, our residential bridge loans are subject to individual risk assessment using an internal borrower and collateral quality evaluation framework. At March 31, 2019, seven loans with an aggregate fair value of $9 million were greater than 90 days delinquent, and four of these loans with an aggregate fair value of $8 million were in foreclosure. At December 31, 2018, seven loans with an aggregate fair value of $12 million were greater than 90 days delinquent and four of these loans with an aggregate fair value of $11 million were in foreclosure. During the three months ended March 31, 2019, we transferred one loan with a fair value of $5 million to REO, which is included in Other assets on our consolidated balance sheets. We recognized a loss of $0.3 million related to this loan for the three months ended March 31, 2019, which was included in Investment fair value changes, net on our consolidated statements of income.

Prior to our acquisition of 5 Arches, for the period from January 1, 2019 to February 28, 2019, we purchased $10 million (principal balance) of residential bridge loans from 5 Arches, and we did not sell any loans. During the three months ended March 31, 2019, we recorded a net market valuation loss of $0.3 million on residential bridge loans held-for-investment at fair value through Investment fair value changes, net on our consolidated statements of income. At March 31, 2019, loans with a market value of $93 million were pledged as collateral under short-term borrowing agreements.

The outstanding residential bridge loans held-for-investment at March 31, 2019 were first lien, fixed-rate, interest-only loans with a weighted average coupon of 9.13% and original maturities of 6 to 24 months. At origination, the weighted average FICO score of borrowers backing these loans was 677, the weighted average LTV ratio of these loans was 75%, and the estimated rehabilitated LTV ratio was 60%.

As of March 31, 2019, we had a $4 million commitment to fund residential bridge loans. See *Note 16* for additional information on this commitment.

Note 8. Multifamily Loans

During the second half of 2018, we invested in multifamily subordinate securities issued by three Freddie Mac K-Series securitization trusts and were required to consolidate the underlying multifamily loans owned at these entities for financial reporting purposes in accordance with GAAP. At March 31, 2019, we consolidated 162 held-for-investment multifamily loans, with an aggregate unpaid principal balance of $2.12 billion and a fair value of $2.18 billion, compared to 162 loans at December 31, 2018 with an aggregate unpaid principal balance of $2.13 billion and a fair value of $2.14 billion. The outstanding multifamily loans held-for-investment at the Freddie Mac K-Series entities at March 31, 2019 were first lien, fixed-rate loans that were originated in 2015 and 2016 and had original loan terms of seven to ten years and an original weighted average LTV ratio of 69%. At March 31, 2019, the weighted average coupon of these multifamily loans was 4.16% and the weighted average remaining loan term was seven years. At both March 31, 2019 and December 31, 2018, none of these loans were greater than 90 days delinquent or in foreclosure.

During the three months ended March 31, 2019, we recorded a net market valuation gain of $34 million on these loans through Investment fair value changes, net on our consolidated statements of income. Pursuant to the collateralized financing entity guidelines, the market valuation changes of these loans are based on the estimated fair value of the ABS issued associated with the securitizations. The net impact to our income statement associated with our economic investment in the securities of the Freddie Mac K-Series securitization entities is presented in *Note 5*.

Note 9. Real Estate Securities

We invest in real estate securities that we acquire from third parties or create and retain from our Sequoia securitizations. The following table presents the fair values of our real estate securities by type at March 31, 2019 and December 31, 2018.

Table 9.1 – Fair Values of Real Estate Securities by Type

(In Thousands)	March 31, 2019	December 31, 2018
Trading	$ 1,255,224	$ 1,118,612
Available-for-sale	287,928	333,882
Total Real Estate Securities	$ 1,543,152	$ 1,452,494

Our real estate securities include mortgage-backed securities, which are presented in accordance with their general position within a securitization structure based on their rights to cash flows. Senior securities are those interests in a securitization that generally have the first right to cash flows and are last in line to absorb losses. Mezzanine securities are interests that are generally subordinate to senior securities in their rights to receive cash flows, and have subordinate securities below them that are first to absorb losses. Most of our mezzanine classified securities were initially rated AA through BBB- and issued in 2012 or later. Subordinate securities are all interests below mezzanine. Nearly all of our residential securities are supported by collateral that was designated as prime at the time of issuance.

Trading Securities

The following table presents the fair value of trading securities by position and collateral type at March 31, 2019 and December 31, 2018.

Table 9.2 – Trading Securities by Position

(In Thousands)	March 31, 2019	December 31, 2018
Senior	$ 182,883	$ 158,670
Mezzanine	730,855	610,819
Subordinate	341,486	349,123
Total Trading Securities	$ 1,255,224	$ 1,118,612

We elected the fair value option for certain securities and classify them as trading securities. Our trading securities include both residential and multifamily mortgage-backed securities. At March 31, 2019, trading securities with a carrying value of $881 million as well as $146 million, $196 million, and $18 million of securities we owned that were issued by consolidated Sequoia Choice, Freddie Mac SLST, and Freddie Mac K-Series securitizations, respectively, were pledged as collateral under short-term borrowing agreements. See *Note 13* for additional information on short-term debt.

At March 31, 2019 and December 31, 2018, our senior trading securities included $76 million and $82 million of interest-only securities, respectively, for which there is no principal balance, and the remaining unpaid principal balance of our senior trading securities was $107 million and $78 million, respectively. Our interest-only securities included $41 million and $43 million of A-IO-S securities at March 31, 2019 and December 31, 2018, respectively, which are securities we retained from certain of our Sequoia securitizations that represent certificated servicing strips.

At March 31, 2019 and December 31, 2018, our mezzanine and subordinate trading securities had an unpaid principal balance of $1.21 billion and $1.12 billion, respectively. At March 31, 2019 and December 31, 2018, the fair value of our mezzanine and subordinate securities was $1.07 billion and $960 million, respectively, and included $230 million and $238 million, respectively, of Agency residential mortgage credit risk transfer (or "CRT") securities, $71 million and $68 million, respectively, of Sequoia securities, $259 million and $225 million, respectively, of other third-party residential securities, and $512 million and $429 million, respectively, of third-party commercial/multifamily securities.

Note 9. Real Estate Securities - (continued)

During the three months ended March 31, 2019 and 2018, we acquired $154 million and $145 million (principal balance), respectively, of securities for which we elected the fair value option and classified as trading, and sold $29 million and $182 million, respectively, of such securities. During the three months ended March 31, 2019 and 2018, we recorded net market valuation gains of $22 million and losses of $3 million, respectively, on trading securities, included in Investment fair value changes, net on our consolidated statements of income.

AFS Securities

The following table presents the fair value of our available-for-sale securities by position and collateral type at March 31, 2019 and December 31, 2018.

Table 9.3 – Available-for-Sale Securities by Position

(In Thousands)	March 31, 2019	December 31, 2018
Senior	$ 47,755	$ 87,615
Mezzanine	31,133	36,407
Subordinate	209,040	209,860
Total AFS Securities	$ 287,928	$ 333,882

At March 31, 2019 and December 31, 2018, all of our available-for-sale securities were comprised of residential mortgage-backed securities. At March 31, 2019, AFS securities with a carrying value of $85 million were pledged as collateral under short-term borrowing agreements. See *Note 13* for additional information on short-term debt.

During the three months ended March 31, 2019 and 2018, we purchased $5 million and $4 million of AFS securities, respectively, and sold $42 million and $51 million of AFS securities, respectively, which resulted in net realized gains of $7 million and $9 million, respectively.

We often purchase AFS securities at a discount to their outstanding principal balances. To the extent we purchase an AFS security that has a likelihood of incurring a loss, we do not amortize into income the portion of the purchase discount that we do not expect to collect due to the inherent credit risk of the security. We may also expense a portion of our investment in the security to the extent we believe that principal losses will exceed the purchase discount. We designate any amount of unpaid principal balance that we do not expect to receive and thus do not expect to earn or recover as a credit reserve on the security. Any remaining net unamortized discounts or premiums on the security are amortized into income over time using the effective yield method.

At March 31, 2019, there were no AFS securities with contractual maturities less than five years, $2 million with contractual maturities greater than five years but less than 10 years, and the remainder of our AFS securities had contractual maturities greater than 10 years.

The following table presents the components of carrying value (which equals fair value) of AFS securities at March 31, 2019 and December 31, 2018.

Table 9.4 – Carrying Value of AFS Securities

March 31, 2019

(In Thousands)	Senior	Mezzanine	Subordinate	Total
Principal balance	$ 48,527	$ 31,002	$ 292,680	$ 372,209
Credit reserve	(1,382)	—	(33,452)	(34,834)
Unamortized discount, net	(15,853)	(3,280)	(122,880)	(142,013)
Amortized cost	31,292	27,722	136,348	195,362
Gross unrealized gains	16,495	3,411	72,734	92,640
Gross unrealized losses	(32)	—	(42)	(74)
Carrying Value	$ 47,755	$ 31,133	$ 209,040	$ 287,928

Note 9. Real Estate Securities - (continued)

December 31, 2018 **(In Thousands)**	**Senior**	**Mezzanine**	**Subordinate**	**Total**
Principal balance	$ 91,736	$ 36,852	$ 302,524	$ 431,112
Credit reserve	(7,790)	—	(33,580)	(41,370)
Unamortized discount, net	(18,460)	(3,697)	(129,043)	(151,200)
Amortized cost	65,486	33,155	139,901	238,542
Gross unrealized gains	22,178	3,252	70,458	95,888
Gross unrealized losses	(49)	—	(499)	(548)
Carrying Value	$ 87,615	$ 36,407	$ 209,860	$ 333,882

The following table presents the changes for the three months ended March 31, 2019, in unamortized discount and designated credit reserves on residential AFS securities.

Table 9.5 – Changes in Unamortized Discount and Designated Credit Reserves on AFS Securities

	Three Months Ended March 31, 2019	
(In Thousands)	**Credit Reserve**	**Unamortized Discount, Net**
Beginning balance	$ 41,370	$ 151,200
Amortization of net discount	—	(1,930)
Realized credit losses	(166)	—
Acquisitions	677	354
Sales, calls, other	(6,392)	(8,266)
(Release of) transfers to credit reserves, net	(655)	655
Ending Balance	$ 34,834	$ 142,013

AFS Securities with Unrealized Losses

The following table presents the components comprising the total carrying value of residential AFS securities that were in a gross unrealized loss position at March 31, 2019 and December 31, 2018.

Table 9.6 – Components of Fair Value of Residential AFS Securities by Holding Periods

	Less Than 12 Consecutive Months			**12 Consecutive Months or Longer**		
(In Thousands)	**Amortized Cost**	**Unrealized Losses**	**Fair Value**	**Amortized Cost**	**Unrealized Losses**	**Fair Value**
March 31, 2019	$ 2	$ (2)	$ —	$ 11,360	$ (72)	$ 11,288
December 31, 2018	12,923	(499)	12,424	7,464	(49)	7,415

At March 31, 2019, after giving effect to purchases, sales, and extinguishment due to credit losses, our consolidated balance sheet included 120 AFS securities, of which four were in an unrealized loss position and three were in a continuous unrealized loss position for 12 consecutive months or longer. At December 31, 2018, our consolidated balance sheet included 128 AFS securities, of which seven were in an unrealized loss position and three were in a continuous unrealized loss position for 12 consecutive months or longer.

Note 9. Real Estate Securities - (continued)

Evaluating AFS Securities for Other-than-Temporary Impairments

Gross unrealized losses on our AFS securities were $0.1 million at March 31, 2019. We evaluate all securities in an unrealized loss position to determine if the impairment is temporary or other-than-temporary (resulting in an OTTI). At March 31, 2019, we did not intend to sell any of our AFS securities that were in an unrealized loss position, and it is more likely than not that we will not be required to sell these securities before recovery of their amortized cost basis, which may be at their maturity. We review our AFS securities that are in an unrealized loss position to identify those securities with losses that are other-than-temporary based on an assessment of changes in expected cash flows for such securities, which considers recent security performance and expected future performance of the underlying collateral.

For both the three months ended March 31, 2019 and 2018, there were no other-than-temporary impairments related to our AFS securities. AFS securities for which OTTI is recognized have experienced, or are expected to experience, credit-related adverse cash flow changes. In determining our estimate of cash flows for AFS securities we may consider factors such as structural credit enhancement, past and expected future performance of underlying mortgage loans, including timing of expected future cash flows, which are informed by prepayment rates, default rates, loss severities, delinquency rates, percentage of non-performing loans, FICO scores at loan origination, year of origination, loan-to-value ratios, and geographic concentrations, as well as general market assessments. Changes in our evaluation of these factors impacted the cash flows expected to be collected at the OTTI assessment date and were used to determine if there were credit-related adverse cash flows and if so, the amount of credit related losses. Significant judgment is used in both our analysis of the expected cash flows for our AFS securities and any determination of the credit loss component of OTTI.

The table below summarizes the significant valuation assumptions we used for our AFS securities in unrealized loss positions at March 31, 2019.

Table 9.7 – Significant Valuation Assumptions

March 31, 2019	**Range for Securities**		
Prepayment rates	6%	-	12%
Projected losses	0.20%	-	7%

The following table details the activity related to the credit loss component of OTTI (i.e., OTTI recognized through earnings) for AFS securities held at March 31, 2019 and 2018, for which a portion of an OTTI was recognized in other comprehensive income.

Table 9.8 – Activity of the Credit Component of Other-than-Temporary Impairments

	Three Months Ended March 31,	
(In Thousands)	**2019**	**2018**
Balance at beginning of period	$ 18,652	$ 21,037
Reductions		
Securities sold, or expected to sell	—	(99)
Securities with no outstanding principal at period end	—	(14)
Balance at End of Period	$ 18,652	$ 20,924

Note 9. Real Estate Securities - (continued)

Gains and losses from the sale of AFS securities are recorded as Realized gains, net, in our consolidated statements of income. The following table presents the gross realized gains and losses on sales and calls of AFS securities for the three months ended March 31, 2019 and 2018.

Table 9.9 – Gross Realized Gains and Losses on AFS Securities

	Three Months Ended March 31,	
(In Thousands)	**2019**	**2018**
Gross realized gains - sales	$ 6,660	$ 9,363
Gross realized gains - calls	4,026	—
Total Realized Gains on Sales and Calls of AFS Securities, net	$ 10,686	$ 9,363

Note 10. Other Investments

Other investments at March 31, 2019 and December 31, 2018 are summarized in the following table.

Table 10.1 – Components of Other Investments

(In Thousands)	**March 31, 2019**	**December 31, 2018**
Servicer advance investments	$ 303,920	$ 300,468
Mortgage servicing rights	55,284	60,281
Excess MSRs	28,992	27,312
Investment in multifamily loan fund	22,416	—
Other notes receivable	3,586	—
Participation in loan warehouse facility	—	39,703
Investment in 5 Arches	—	10,754
Total Other Investments	$ 414,198	$ 438,518

Servicer advance investments

In 2018, we and a third-party co-investor, through two partnerships (“SA Buyers”) consolidated by us, purchased the outstanding servicer advances and excess MSRs related to a portfolio of legacy residential mortgage-backed securitizations serviced by the co-investor (See *Note 4* for additional information regarding the transaction). At March 31, 2019, we had funded $66 million of capital to the SA Buyers and expected to fund an additional $19 million of capital under an outstanding commitment (see *Note 16* for additional detail).

Our servicer advance investments (owned by the consolidated SA Buyers) are comprised of outstanding servicer advance receivables, the requirement to purchase all future servicer advances made with respect to a specified pool of residential mortgage loans, and a portion of the mortgage servicing fees from the underlying loan pool. A portion of the remaining mortgage servicing fees from the underlying loan pool are paid directly to the third-party servicer for the performance of servicing duties and a portion is paid to excess MSRs that we own as a separate investment. We hold our servicer advance investments at our taxable REIT subsidiary.

Servicer advances are non-interest bearing and a customary feature of residential mortgage securitization transactions. Servicer advances are generally reimbursable cash payments made by a servicer when the borrower fails to make scheduled payments due on a residential mortgage loan or to support the value of the collateral property. Servicer advances typically fall into three categories:

- Principal and Interest Advances: cash payments made by the servicer to cover scheduled principal and interest payments on a residential mortgage loan that have not been paid on a timely basis by the borrower.

- Escrow Advances (Taxes and Insurance Advances): Cash payments made by the servicer to third parties on behalf of the borrower for real estate taxes and insurance premiums on the property that have not been paid on a timely basis by the borrower.

Note 10. Other Investments - (continued)

- Corporate Advances: Cash payments made by the servicer to third parties for the reimbursable costs and expenses incurred in connection with the foreclosure, preservation and sale of the mortgaged property, including attorneys' and other professional fees.

Servicer advances are generally permitted to be repaid from amounts received with respect to the related residential mortgage loan, including payments from the borrower or amounts received from the liquidation of the property securing the loan. Residential mortgage servicing agreements generally require a servicer to make advances in respect of serviced residential mortgage loans unless the servicer determines in good faith that the advance would not be ultimately recoverable from the proceeds of the related residential mortgage loan or the mortgaged property.

At March 31, 2019, our servicer advance investments had a carrying value of $304 million and were associated with a portfolio of residential mortgage loans with an unpaid principal balance of $8.79 billion. The outstanding servicer advance receivables associated with this investment were $282 million at March 31, 2019, which were financed with short-term non-recourse securitization debt (see *Note 13* for additional detail on this debt). The $282 million of servicer advance receivables were comprised of the following types of advances:

Table 10.2 – Components of Servicer Advance Receivables

(In Thousands)	**March 31, 2019**	**December 31, 2018**
Principal and interest advances	$ 122,339	$ 144,336
Escrow advances (taxes and insurance advances)	105,776	94,828
Corporate advances	53,647	47,614
Total Servicer Advance Receivables	$ 281,762	$ 286,778

We account for our servicer advance investments at fair value and during the three months ended March 31, 2019, we recorded $3 million of interest income associated with these investments and recorded a net market valuation gain of $1 million through Investment fair value changes, net in our consolidated statements of income.

Mortgage Servicing Rights

We invest in mortgage servicing rights associated with residential mortgage loans and contract with licensed sub-servicers to perform all servicing functions for these loans. The majority of our investments in MSRs were made through the retention of servicing rights associated with the residential jumbo mortgage loans that we acquired and subsequently transferred to third parties. We hold our MSR investments at our taxable REIT subsidiary.

At March 31, 2019 and December 31, 2018, our MSRs had a fair value of $55 million and $60 million, respectively, and were associated with loans with an aggregate principal balance of $4.86 billion and $4.93 billion, respectively.

Note 10. Other Investments - (continued)

The following table presents activity for MSRs for the three months ended March 31, 2019 and 2018.

Table 10.3 – Activity for MSRs

	Three Months Ended March 31,	
(In Thousands)	**2019**	**2018**
Balance at beginning of period	$ 60,281	$ 63,598
Additions	104	—
Changes in fair value due to:		
Changes in assumptions (1)	(3,586)	4,346
Other changes (2)	(1,515)	(1,448)
Balance at End of Period	$ 55,284	$ 66,496

(1) Primarily reflects changes in prepayment assumptions due to changes in market interest rates.

(2) Represents changes due to the realization of expected cash flows.

The following table presents the components of our MSR income for the three months ended March 31, 2019 and 2018.

Table 10.4 – Components of MSR Income, net

	Three Months Ended March 31,	
(In Thousands)	**2019**	**2018**
Servicing income	$ 3,610	$ 3,796
Cost of sub-servicer	(503)	(592)
Net servicing fee income	3,107	3,204
Market valuation changes of MSRs	(5,101)	2,892
Market valuation changes of associated derivatives	2,251	(5,139)
MSR Income, Net (1)	$ 257	$ 957

(1) MSR income, net is included in Other income, net on our consolidated statements of income.

Excess MSRs

In association with our servicer advance investments described above, in the fourth quarter of 2018, we (through our consolidated SA Buyers) also invested in excess MSRs associated with the same portfolio of legacy residential mortgage-backed securitizations. Additionally, in the fourth quarter of 2018, we invested in excess MSRs associated with a specified pool of multifamily loans. We account for our excess MSRs at fair value and during the three months ended March 31, 2019, we recognized $2 million of interest income and recorded a net market valuation loss of $0.4 million through Investment fair value changes, net on our consolidated statements of income.

Investment in Multifamily Loan Fund

In January 2019, we invested in a limited partnership created to acquire floating rate, light-renovation multifamily loans from Freddie Mac. We committed to fund an aggregate of $78 million to the partnership, and have funded approximately $22 million at March 31, 2019. Freddie Mac is providing a debt facility to finance loans purchased by the partnership. After the partnership's acquisitions have reached a specific threshold, the partnership and Freddie Mac may agree to include the related loans in a Freddie Mac-sponsored securitization and the limited partners may acquire the subordinate securities issued in any such securitization.

Note 10. Other Investments - (continued)

We account for our ownership interest in this partnership using the equity method of accounting as we are able to exert significant influence over but do not control the activities of the investee. At March 31, 2019, the carrying amount of our investment in the partnership was $22 million. We have elected to record our share of earnings or losses from this investment on a one-quarter lag, and as such, we did not record any equity method investment earnings or losses associated with this investment during the three months ended March 31, 2019.

Participation in Loan Warehouse Facility

In the second quarter of 2018, we invested in a subordinated participation in a revolving mortgage loan warehouse credit facility of one of our loan sellers. We accounted for this subordinated participation interest as a loan receivable at amortized cost, and all associated interest income was recorded as a component of Other interest income in our consolidated statements of income. During the first quarter of 2019, our agreement associated with this investment was terminated and the balance outstanding under this agreement was repaid.

Investment in 5 Arches

In May 2018, we acquired a 20% minority interest in 5 Arches for $10 million, which included a one-year option to purchase all remaining equity in the company for a combination of cash and stock totaling $40 million. In March 2019, we closed on our option to acquire the remaining 80% interest in 5 Arches. See *Note 2* for discussion of this acquisition.

During 2018 and through February 28, 2019, we accounted for our minority ownership interest in 5 Arches using the equity method of accounting as we were able to exert significant influence over but did not control the activities of the investee. During the period from January 1, 2019 to February 28, 2019, we recorded $0.3 million of gross income associated with this investment and, including amortization of certain intangible assets, recorded $0.1 million of net earnings in Other income, net on our consolidated statements of income.

Note 11. Derivative Financial Instruments

The following table presents the fair value and notional amount of our derivative financial instruments at March 31, 2019 and December 31, 2018.

Table 11.1 – Fair Value and Notional Amount of Derivative Financial Instruments

	March 31, 2019		December 31, 2018	
(In Thousands)	**Fair Value**	**Notional Amount**	**Fair Value**	**Notional Amount**
Assets - Risk Management Derivatives				
Interest rate swaps	$ 11,490	$ 1,674,000	$ 28,211	$ 2,106,500
TBAs	5,826	910,000	4,665	520,000
Assets - Other Derivatives				
Loan purchase commitments	4,967	586,736	2,913	331,161
Total Assets	$ 22,283	$ 3,170,736	$ 35,789	$ 2,957,661
Liabilities - Cash Flow Hedges				
Interest rate swaps	$ (40,296)	$ 139,500	$ (34,492)	$ 139,500
Liabilities - Risk Management Derivatives				
Interest rate swaps	(60,265)	2,296,000	(36,416)	1,742,000
TBAs	(9,609)	1,265,000	(13,215)	935,000
Liabilities - Other Derivatives				
Loan purchase commitments	(772)	181,123	(732)	137,224
Total Liabilities	$ (110,942)	$ 3,881,623	$ (84,855)	$ 2,953,724
Total Derivative Financial Instruments, Net	$ (88,659)	$ 7,052,359	$ (49,066)	$ 5,911,385

Note 11. Derivative Financial Instruments - (continued)

Risk Management Derivatives

To manage, to varying degrees, risks associated with certain assets and liabilities on our consolidated balance sheets, we may enter into derivative contracts. At March 31, 2019, we were party to swaps with an aggregate notional amount of $3.97 billion and TBA agreements sold with an aggregate notional amount of $2.18 billion. At December 31, 2018, we were party to swaps with an aggregate notional amount of $3.85 billion and TBA agreements sold with an aggregate notional amount of $1.46 billion.

During the three months ended March 31, 2019 and 2018, risk management derivatives had a net market valuation loss of $45 million and a net valuation gain of $67 million, respectively. These market valuation gains and losses are recorded in Mortgage banking activities, net, Investment fair value changes, net, and Other income, net on our consolidated statements of income.

Loan Purchase and Forward Sale Commitments

LPCs and FSCs that qualify as derivatives are recorded at their estimated fair values. For the three months ended March 31, 2019 and 2018, LPCs and FSCs had a net market valuation gain of $11 million and a net market valuation loss of $7 million, respectively, that were recorded in Mortgage banking activities, net on our consolidated statements of income.

Derivatives Designated as Cash Flow Hedges

To manage the variability in interest expense related to portions of our long-term debt and certain adjustable-rate securitization entity liabilities that are included in our consolidated balance sheets for financial reporting purposes, we designated certain interest rate swaps as cash flow hedges with an aggregate notional balance of $140 million.

For the three months ended March 31, 2019 and 2018, changes in the values of designated cash flow hedges were negative $6 million and positive $8 million, respectively, and were recorded in Accumulated other comprehensive income, a component of equity. For interest rate agreements currently or previously designated as cash flow hedges, our total unrealized loss reported in Accumulated other comprehensive income was $40 million and $34 million at March 31, 2019 and December 31, 2018, respectively.

The following table illustrates the impact on interest expense of our interest rate agreements accounted for as cash flow hedges for the three months ended March 31, 2019 and 2018.

Table 11.2 – Impact on Interest Expense of Interest Rate Agreements Accounted for as Cash Flow Hedges

	Three Months Ended March 31,	
(In Thousands)	**2019**	**2018**
Net interest expense on cash flows hedges	$ (637)	$ (998)
Total Interest Expense	$ (637)	$ (998)

Derivative Counterparty Credit Risk

As discussed in our Annual Report on Form 10-K for the year ended December 31, 2018, we consider counterparty risk as part of our fair value assessments of all derivative financial instruments at each quarter-end. At March 31, 2019, we assessed this risk as remote and did not record a specific valuation adjustment.

At March 31, 2019, we had outstanding derivative agreements with two counterparties (other than clearinghouses) and were in compliance with ISDA agreements governing our open derivative positions.

Note 12. Other Assets and Liabilities

Other assets at March 31, 2019 and December 31, 2018, are summarized in the following table.

Table 12.1 – Components of Other Assets

(In Thousands)	March 31, 2019	December 31, 2018
Margin receivable	$ 154,549	$ 100,773
FHLBC stock	43,393	43,393
Pledged collateral	42,631	42,433
Right-of-use asset	11,681	—
REO	7,275	3,943
Investment receivable	6,494	6,959
Fixed assets and leasehold improvements (1)	5,159	5,106
Other	14,414	15,218
Total Other Assets	$ 285,596	$ 217,825

(1) Fixed assets and leasehold improvements had a basis of $11 million and accumulated depreciation of $5 million at March 31, 2019.

Accrued expenses and other liabilities at March 31, 2019 and December 31, 2018 are summarized in the following table.

Table 12.2 – Components of Accrued Expenses and Other Liabilities

(In Thousands)	March 31, 2019	December 31, 2018
Contingent consideration	$ 24,621	$ —
Payable to minority partner	16,696	14,331
Guarantee obligations	16,359	16,711
Lease liability	13,188	—
Deferred tax liabilities	11,986	9,022
Accrued compensation	10,506	19,769
Residential bridge loan holdbacks	8,187	—
Residential loan and MSR repurchase reserve	4,328	4,189
Accrued operating expenses	4,046	3,122
Accrued income taxes payable	2,446	423
Legal reserve	2,000	2,000
Margin payable	19	835
Other	5,046	8,317
Total Accrued Expenses and Other Liabilities	$ 119,428	$ 78,719

Margin Receivable and Payable

Margin receivable and payable resulted from margin calls between us and our counterparties under derivatives, master repurchase agreements, and warehouse facilities, whereby we or the counterparty posted collateral.

FHLBC Stock

In accordance with our FHLB-member subsidiary's borrowing agreement with the FHLBC, our subsidiary is required to purchase and hold stock in the FHLBC. See *Note 3* and *Note 15* for additional information on this borrowing agreement.

Note 12. Other Assets and Liabilities - (continued)

Pledged Collateral and Guarantee Obligations

The pledged collateral and guarantee obligations presented in the tables above are related to our risk-sharing arrangements with Fannie Mae and Freddie Mac. In accordance with these arrangements, we are required to pledge collateral to secure our guarantee obligations. See *Note 3* and *Note 16* for additional information on our risk-sharing arrangements.

Contingent Consideration

The contingent consideration presented in the table above is related to our acquisition of 5 Arches in the first quarter of 2019. See *Note 16* for additional information on our contingent consideration liabilities.

Lease Liability and Right-of-Use Asset

The lease liability and right-of-use asset presented in the tables above resulted from our adoption of ASU 2016-02, "Leases," in the first quarter of 2019. The lease liability is equal to the present value of our remaining lease payments discounted at our incremental borrowing rate and the right-of-use asset is equal to the lease liability adjusted for our deferred rent liability. These balances are reduced as lease payments are made. See *Note 16* for additional information on leases.

Residential Bridge Loan Holdbacks

Residential bridge loan holdbacks represent loan amounts payable to residential bridge loan borrowers subject to the completion of various phases of property rehabilitation.

Investment Receivable

At March 31, 2019, investment receivable primarily consisted of unsettled trade receivables related to real estate securities sales. In accordance with our policy to record purchases and sales of securities on the trade date, if the trade and settlement of a purchase or sale crosses over a quarterly reporting period, we will record an investment receivable for sales and an unsettled trades liability for purchases.

REO

The carrying value of REO at March 31, 2019 was $7 million, which included $2 million of REO from our Legacy Sequoia entities and $5 million from our residential bridge loan portfolio. During the three months ended March 31, 2019, transfers into REO included less than $0.1 million from Legacy Sequoia entities and a $5 million residential bridge loan. During the three months ended March 31, 2019, there were Legacy Sequoia REO liquidations of $2 million, resulting in $0.2 million of unrealized gains which were recorded in Investment fair value changes, net, on our consolidated statements of income. At March 31, 2019, there were nine REO properties at our Legacy Sequoia entities and one residential bridge loan REO property recorded on our consolidated balance sheets. At December 31, 2018, there were 13 REO properties recorded, all of which were owned at consolidated Legacy Sequoia entities.

Legal and Repurchase Reserves

See *Note 16* for additional information on the legal and residential repurchase reserves.

Payable to Minority Partner

In 2018, Redwood and a third-party co-investor, through two partnership entities consolidated by Redwood, purchased servicer advances and excess MSRs related to a portfolio of residential mortgage loans serviced by the co-investor (see *Note 4* and *Note 10* for additional information on the partnership entities and associated investments). We account for the co-investor’s interests in the entities as liabilities and at March 31, 2019, the carrying value of their interests was $17 million, representing their current economic interest in the entities. Earnings from the partnership entities are allocated to the co-investors on a proportional basis and during the three months ended March 31, 2019, we allocated $0.2 million of losses to the co-investors, which was recorded in Other income, net on our consolidated statements of income.

Note 13. Short-Term Debt

We enter into repurchase agreements, bank warehouse agreements, and other forms of collateralized (and generally uncommitted) short-term borrowings with several banks and major investment banking firms. At March 31, 2019, we had outstanding agreements with several counterparties and we were in compliance with all of the related covenants. For additional information about these financial covenants and our short-term debt, see Part I, Item 2 – *Management's Discussion and Analysis of Financial Condition and Results of Operations* of this Quarterly Report on Form 10-Q and Part II, Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2018.

The table below summarizes our short-term debt, including the facilities that are available to us, the outstanding balances, the weighted average interest rate, and the maturity information at March 31, 2019 and December 31, 2018.

Table 13.1 – Short-Term Debt

	March 31, 2019					
(Dollars in Thousands)	**Number of Facilities**	**Outstanding Balance**	**Limit**	**Weighted Average Interest Rate**	**Maturity**	**Weighted Average Days Until Maturity**
Facilities						
Residential loan warehouse (1)	4	$ 526,341	$ 1,425,000	3.96%	8/2019-03/2020	253
Real estate securities repo (1)	9	1,081,079	—	3.53%	04/2019-06/2019	23
Single-family rental loan warehouse (2)	2	37,436	400,000	4.75%	6/2020-6/2021	505
Residential bridge loan warehouse (2)	2	61,593	80,000	5.21%	11/2019-04/2021	529
Business purpose loan working capital (2)	1	7,300	15,000	5.00%	12/2020	611
Total Short-Term Debt Facilities	18	1,713,749				
Servicer advance financing	1	249,557	350,000	4.34%	11/2019	243
Convertible notes, net	N/A	199,925	—	5.63%	11/2019	229
Total Short-Term Debt		$ 2,163,231				

Note 13. Short-Term Debt - (continued)

	December 31, 2018					
(Dollars in Thousands)	Number of Facilities	Outstanding Balance	Limit	Weighted Average Interest Rate	Maturity	Weighted Average Days Until Maturity
Facilities						
Residential loan warehouse (1)	4	$ 860,650	$ 1,425,000	4.10%	2/2019-12/2019	178
Real estate securities repo (1)	9	988,890	—	3.47%	01/2019-03/2019	26
Single-family rental loan warehouse (2)	2	22,053	400,000	4.77%	6/2020-6/2021	560
Residential bridge loan warehouse (2)	2	66,327	80,000	5.20%	11/2019-04/2021	629
Total Short-Term Debt Facilities	17	1,937,920				
Servicer advance financing	1	262,740	350,000	4.32%	11/2019	333
Convertible notes, net	N/A	199,619		5.63%	11/2019	319
Total Short-Term Debt		$ 2,400,279				

(1) Borrowings under our facilities are generally charged interest based on a specified margin over the one-month LIBOR interest rate. At March 31, 2019, all of these borrowings were under uncommitted facilities and were due within 364 days (or less) of the borrowing date.

(2) Due to the revolving nature of the borrowings under these facilities, we have classified these facilities as short-term debt at March 31, 2019. Borrowings under these facilities will be repaid as the underlying loans mature or are sold to third parties or transferred to securitizations.

At March 31, 2019 and December 31, 2018, the fair value of held-for-sale residential loans pledged as collateral under our short-term debt facilities was $579 million and $935 million, respectively. At March 31, 2019, the fair value of real estate securities pledged as collateral under our short-term debt facilities was $966 million, and also included $146 million of securities retained from our consolidated Sequoia Choice securitizations as well as $196 million and $18 million of securities we owned that were issued by consolidated Freddie Mac SLST and Freddie Mac K-series securitizations, respectively. At December 31, 2018, the fair value of real estate securities pledged as collateral under our short-term debt facilities was $844 million, and also included $130 million of securities retained from our consolidated Sequoia Choice securitizations as well as $229 million and $18 million of securities we owned that were issued by consolidated Freddie Mac SLST and Freddie Mac K-series securitizations, respectively. The fair value of single-family rental and residential bridge loans pledged as collateral under our warehouse facilities was $49 million and $93 million, respectively, at March 31, 2019 and $28 million and $98 million, respectively, at December 31, 2018. Additionally, single-family rental loans with a fair value of $5 million, as well as $7 million of other assets at 5 Arches, served as collateral under the business purpose loan working capital line at March 31, 2019.

For the three months ended March 31, 2019 and 2018, the average balances of our short-term debt facilities were $1.61 billion and $1.37 billion, respectively. At both March 31, 2019 and December 31, 2018, accrued interest payable on our short-term debt facilities was $4 million.

Servicer advance financing consists of non-recourse short-term securitization debt used to finance servicer advance investments. We consolidate the securitization entity that issued the debt, but the entity is independent of Redwood and the assets and liabilities are not owned by and are not legal obligations of Redwood. At March 31, 2019, the fair value of servicer advances collateralizing the securitization financing was $282 million. At March 31, 2019, the accrued interest payable balance on this financing was $0.4 million and the unamortized capitalized commitment costs were $2 million.

During the fourth quarter of 2018, $201 million principal amount of 5.625% exchangeable senior notes and $1 million of unamortized deferred issuance costs were reclassified from long-term debt to short-term debt as the maturity of the notes was less than one year as of November 2018. At March 31, 2019, the accrued interest payable balance on this debt was $4 million. See *Note 15* for additional information on our convertible notes.

We also maintain a $10 million committed line of credit with a financial institution that is secured by certain mortgage-backed securities with a fair market value of $4 million at March 31, 2019. At both March 31, 2019 and December 31, 2018, we had no outstanding borrowings on this facility.

Note 13. Short-Term Debt - (continued)

Remaining Maturities of Short-Term Debt

The following table presents the remaining maturities of our secured short-term debt by the type of collateral securing the debt as well as our convertible notes at March 31, 2019.

Table 13.2 – Short-Term Debt by Collateral Type and Remaining Maturities

	March 31, 2019			
(In Thousands)	**Within 30 days**	**31 to 90 days**	**Over 90 days**	**Total**
Collateral Type				
Held-for-sale residential loans	$ —	$ —	$ 526,341	$ 526,341
Real estate securities	857,877	223,202	—	1,081,079
Single-family rental loans	—	—	37,436	37,436
Residential bridge loans	—	—	61,593	61,593
Business purpose loan working capital	7,300	—	—	7,300
Total Secured Short-Term Debt	865,177	223,202	625,370	1,713,749
Servicer advance financing	—	—	249,557	249,557
Convertible notes, net	—	—	199,925	199,925
Total Short-Term Debt	$ 865,177	$ 223,202	$ 1,074,852	$ 2,163,231

Note 14. Asset-Backed Securities Issued

Through our Sequoia securitization program, we sponsor securitization transactions in which securities backed by residential mortgage loans (ABS) are issued by Sequoia entities. We consolidated the Legacy Sequoia and Sequoia Choice securitization entities, and beginning in 2018, certain third-party Freddie Mac K-Series and SLST securitization entities, that we determined were VIEs and for which we determined we were the primary beneficiary. Each consolidated securitization entity is independent of Redwood and of each other and the assets and liabilities are not owned by and are not legal obligations of Redwood. Our exposure to these entities is primarily through the financial interests we have retained, although we are exposed to certain financial risks associated with our role as a sponsor, servicing administrator, or depositor of these entities or as a result of our having sold assets directly or indirectly to these entities.

We account for the ABS issued under our consolidated entities at fair value, with periodic changes in fair value recorded in Investment fair value changes, net on our consolidated statements of income. Pursuant to the CFE guidelines, the market valuation changes on our loans are based on the estimated fair value of the associated ABS issued. The net impact to our income statement associated with our retained economic investment in each of these securitization entities is presented in *Note 5*.

The ABS issued by these entities consist of various classes of securities that pay interest on a monthly basis. All ABS issued by the Sequoia Choice and Freddie Mac K-Series, and Freddie Mac SLST entities pay fixed rates of interest and substantially all ABS issued by the Legacy Sequoia entities pay variable rates of interest, which are indexed to one-, three-, or six-month LIBOR. ABS issued also includes some interest-only classes with coupons set at a fixed spread to a benchmark rate, or set at a spread to the interest rates earned on the assets less the interest rates paid on the liabilities of a securitization entity.

Note 14. Asset-Backed Securities Issued - (continued)

The carrying values of ABS issued by Sequoia securitization entities we sponsored at March 31, 2019 and December 31, 2018, along with other selected information, are summarized in the following table.

Table 14.1 – Asset-Backed Securities Issued

March 31, 2019 **(Dollars in Thousands)**	**Legacy Sequoia**	**Sequoia Choice**	**Freddie Mac SLST**	**Freddie Mac K-Series**	**Total**
Certificates with principal balance	$ 501,300	$ 2,053,345	$ 975,780	$ 1,933,620	$ 5,464,045
Interest-only certificates	1,527	23,744	—	125,296	150,567
Market valuation adjustments	(22,828)	40,267	17,252	(11,659)	23,032
ABS Issued, Net	$ 479,999	$ 2,117,356	$ 993,032	$ 2,047,257	$ 5,637,644
Range of weighted average interest rates, by series	2.48% to 3.60%	4.12% to 4.96%	3.50%	3.39% to 4.08%	
Stated maturities	2024 - 2036	2047 - 2049	2028	2025 - 2049	
Number of series	20	7	1	3	

December 31, 2018 **(Dollars in Thousands)**	**Legacy Sequoia**	**Sequoia Choice**	**Freddie Mac SLST**	**Freddie Mac K-Series**	**Total**
Certificates with principal balance	$ 540,456	$ 1,838,758	$ 993,659	$ 1,936,691	$ 5,309,564
Interest-only certificates	1,537	25,662	—	131,600	158,799
Market valuation adjustments	(29,753)	20,590	89	(49,216)	(58,290)
ABS Issued, Net	$ 512,240	$ 1,885,010	$ 993,748	$ 2,019,075	$ 5,410,073
Range of weighted average interest rates, by series	1.36% to 3.60%	4.46% to 4.97%	3.51%	3.39% to 4.08%	
Stated maturities	2024 - 2036	2047 - 2048	2028	2025 - 2049	
Number of series	20	6	1	3	

The actual maturity of each class of ABS issued is primarily determined by the rate of principal prepayments on the assets of the issuing entity. Each series is also subject to redemption prior to the stated maturity according to the terms of the respective governing documents of each ABS issuing entity. As a result, the actual maturity of ABS issued may occur earlier than its stated maturity. At March 31, 2019, all of the ABS issued and outstanding had contractual maturities beyond five years. The following table summarizes the accrued interest payable on ABS issued at March 31, 2019 and December 31, 2018. Interest due on consolidated ABS issued is payable monthly.

Table 14.2 – Accrued Interest Payable on Asset-Backed Securities Issued

(In Thousands)	**March 31, 2019**	**December 31, 2018**
Legacy Sequoia	$ 531	$ 571
Sequoia Choice	7,854	7,180
Freddie Mac SLST	2,846	2,907
Freddie Mac K-Series	6,230	6,239
Total Accrued Interest Payable on ABS Issued	$ 17,461	$ 16,897

Note 14. Asset-Backed Securities Issued - (continued)

The following table summarizes the carrying value components of the collateral for ABS issued and outstanding at March 31, 2019 and December 31, 2018.

Table 14.3 – Collateral for Asset-Backed Securities Issued

March 31, 2019 (In Thousands)	**Legacy Sequoia**	**Sequoia Choice**	**Freddie Mac SLST**	**Freddie Mac K-Series**	**Total**
Residential loans	$ 488,645	$ 2,333,248	$ 1,228,317	$ —	$ 4,050,210
Multifamily loans	—	—	—	2,175,899	2,175,899
Restricted cash	146	14	—	—	160
Accrued interest receivable	776	9,616	3,861	6,587	20,840
REO	2,280	—	—	—	2,280
Total Collateral for ABS Issued	$ 491,847	$ 2,342,878	$ 1,232,178	$ 2,182,486	$ 6,249,389

December 31, 2018 (In Thousands)	**Legacy Sequoia**	**Sequoia Choice**	**Freddie Mac SLST**	**Freddie Mac K-Series**	**Total**
Residential loans	$ 519,958	$ 2,079,382	$ 1,222,669	$ —	$ 3,822,009
Multifamily loans	—	—	—	2,144,598	2,144,598
Restricted cash	146	1,022	—	—	1,168
Accrued interest receivable	822	8,988	3,926	6,595	20,331
REO	3,943	—	—	—	3,943
Total Collateral for ABS Issued	$ 524,869	$ 2,089,392	$ 1,226,595	$ 2,151,193	$ 5,992,049

Note 15. Long-Term Debt

FHLBC Borrowings

In July 2014, our FHLB-member subsidiary entered into a borrowing agreement with the Federal Home Loan Bank of Chicago. At March 31, 2019, under this agreement, our subsidiary could incur borrowings up to $2.00 billion, also referred to as “advances,” from the FHLBC secured by eligible collateral, including residential mortgage loans. During the three months ended March 31, 2019, our FHLB-member subsidiary made no additional borrowings under this agreement. Under a final rule published by the Federal Housing Finance Agency in January 2016, our FHLB-member subsidiary will remain an FHLB member through the five-year transition period for captive insurance companies. Our FHLB-member subsidiary's existing $2.00 billion of FHLB debt, which matures beyond this transition period, is permitted to remain outstanding until its stated maturity. As residential loans pledged as collateral for this debt pay down, we are permitted to pledge additional loans or other eligible assets to collateralize this debt; however, we do not expect to be able to increase our subsidiary's FHLB debt above the existing $2.00 billion maximum.

At March 31, 2019, $2.00 billion of advances were outstanding under this agreement, which were classified as long-term debt, with a weighted average interest rate of 2.65% and a weighted average maturity of approximately six years. At December 31, 2018, $2.00 billion of advances were outstanding under this agreement, which were classified as long-term debt, with a weighted average interest rate of 2.52% and a weighted average maturity of seven years. Advances under this agreement incur interest charges based on a specified margin over the FHLBC’s 13-week discount note rate, which resets every 13 weeks. At March 31, 2019, total advances under this agreement were secured by residential mortgage loans with a fair value of $2.41 billion. This agreement also requires our subsidiary to purchase and hold stock in the FHLBC in an amount equal to a specified percentage of outstanding advances. At March 31, 2019, our subsidiary held $43 million of FHLBC stock that is included in Other assets in our consolidated balance sheets.

Note 15. Long-Term Debt - (continued)

The following table presents maturities of our FHLBC borrowings by year at March 31, 2019.

Table 15.1 – Maturities of FHLBC Borrowings by Year

(In Thousands)	March 31, 2019
2024	$ 470,171
2025	887,639
2026	642,189
Total FHLBC Borrowings	$ 1,999,999

For additional information about our FHLBC borrowings, see Part I, Item 2 of Quarterly Report on Form 10-Q under the heading "*Risks Relating to Debt Incurred under Short- and Long-Term Borrowing Facilities.*"

Convertible Notes

In June 2018, we issued $200 million principal amount of 5.625% convertible senior notes due 2024 at an issuance price of 99.5%. These convertible notes require semi-annual interest payments at a fixed coupon rate of 5.625% until maturity or conversion, which will be no later than July 15, 2024. After deducting the issuance discount, the underwriting discount and offering costs, we received $194 million of net proceeds. Including amortization of deferred debt issuance costs and the debt discount, the weighted average interest expense yield on these convertible notes is approximately 6.2% per annum. These notes are convertible at the option of the holder at a conversion rate of 54.7645 common shares per $1,000 principal amount of convertible senior notes (equivalent to a conversion price of $18.26 per common share). Upon conversion of these notes by a holder, the holder will receive shares of our common stock. At March 31, 2019, the outstanding principal amount of these notes was $200 million and the accrued interest payable on this debt was $2 million. At March 31, 2019, the unamortized deferred issuance costs and debt discount were $4 million and $1 million, respectively.

In August 2017, we issued $245 million principal amount of 4.75% convertible senior notes due 2023. These convertible notes require semi-annual interest payments at a fixed coupon rate of 4.75% until maturity or conversion, which will be no later than August 15, 2023. After deducting the underwriting discount and offering costs, we received $238 million of net proceeds. Including amortization of deferred debt issuance costs, the weighted average interest expense yield on these convertible notes is approximately 5.3% per annum. At March 31, 2019, these notes were convertible at the option of the holder at a conversion rate of 53.9060 common shares per $1,000 principal amount of convertible senior notes (equivalent to a conversion price of $18.55 per common share). Upon conversion of these notes by a holder, the holder will receive shares of our common stock. At March 31, 2019, the outstanding principal amount of these notes was $245 million. At March 31, 2019, the accrued interest payable balance on this debt was $1 million and the unamortized deferred issuance costs were $6 million.

In November 2014, RWT Holdings, Inc., a wholly-owned subsidiary of Redwood Trust, Inc., issued $205 million principal amount of 5.625% exchangeable senior notes due 2019. These exchangeable notes require semi-annual interest payments at a fixed coupon rate of 5.625% until maturity or exchange, which will be no later than November 15, 2019. After deducting the underwriting discount and offering costs, we received $198 million of net proceeds. Including amortization of deferred debt issuance costs, the weighted average interest expense yield on these exchangeable notes is approximately 6.3% per annum. At March 31, 2019, these notes were exchangeable at the option of the holder at an exchange rate of 46.2370 common shares per $1,000 principal amount of exchangeable senior notes (equivalent to an exchange price of $21.63 per common share). Upon exchange of these notes by a holder, the holder will receive shares of our common stock. During 2016, we repurchased $4 million par value of these notes at a discount and recorded a gain on extinguishment of debt of $0.3 million in Realized gains, net on our consolidated statements of income. Additionally, during the fourth quarter of 2018, $201 million principal amount of these notes and $1 million of unamortized deferred issuance costs were reclassified from long-term debt to short-term debt as the maturity of the notes was less than one year as of November 2018. At March 31, 2019, the outstanding principal amount of these notes was $201 million. At March 31, 2019, the accrued interest payable balance on this debt was $4 million and the unamortized deferred issuance costs were $1 million.

Note 15. Long-Term Debt - (continued)

Trust Preferred Securities and Subordinated Notes

At March 31, 2019, we had trust preferred securities and subordinated notes outstanding of $100 million and $40 million, respectively. This debt requires quarterly interest payments at a floating rate equal to three-month LIBOR plus 2.25% until the notes are redeemed. The $100 million trust preferred securities will be redeemed no later than January 30, 2037, and the $40 million subordinated notes will be redeemed no later than July 30, 2037. Prior to 2014, we entered into interest rate swaps with aggregate notional values totaling $140 million to hedge the variability in this long-term debt interest expense. Including hedging costs and amortization of deferred debt issuance costs, the weighted average interest expense yield on our trust preferred securities and subordinated notes is approximately 6.8% per annum. At both March 31, 2019 and December 31, 2018, the accrued interest payable balance on our trust preferred securities and subordinated notes was $1 million.

Under the terms of this debt, we covenant, among other things, to use our best efforts to continue to qualify as a REIT. If an event of default were to occur in respect of this debt, we would generally be restricted under its terms (subject to certain exceptions) from making dividend distributions to stockholders, from repurchasing common stock or repurchasing or redeeming any other then-outstanding equity securities, and from making any other payments in respect of any equity interests in us or in respect of any then-outstanding debt that is pari passu or subordinate to this debt.

Note 16. Commitments and Contingencies

Lease Commitments

At March 31, 2019, we were obligated under five non-cancelable operating leases with expiration dates through 2028 for $16 million of cumulative lease payments. Our principal executive and administrative office is located in Mill Valley, California and we have several additional offices, as disclosed in *Part I, Item 2* of our Annual Report on Form 10-K for the year ended December 31, 2018. Additionally, with our acquisition of 5 Arches in the first quarter of 2019, we added an executive and administrative office located in Irvine, California. Our operating lease expense was $1 million for both three-month periods ended March 31, 2019 and 2018.

The following table presents our future lease commitments and a reconciliation to our lease liability at March 31, 2019.

Table 16.1 – Future Lease Commitments by Year

(In Thousands)	March 31, 2019
2019 (9 months)	$ 1,921
2020	2,538
2021	1,770
2022	1,468
2023 and thereafter	8,749
Total Lease Commitments	16,446
Less: Imputed interest	(3,258)
Lease Liability	$ 13,188

During the three months ended March 31, 2019, we adopted ASU 2016-02, "Leases," which required us to recognize a lease liability that was equal to the present value of our remaining lease payments of $16 million discounted at various incremental borrowing rates, and a right-of-use asset, which was equal to our lease liability adjusted for our deferred rent liability. We elected to apply the new guidance using the optional transition method, which permits lessees to measure the lease liability and right-of-use asset at January 1, 2019, without adjusting the comparative periods presented. We elected the package of practical expedients under the transition guidance within this standard, which allowed us to carry forward the classifications of each of our four existing leases as operating leases and to continue to expense lease payments on a straight-line basis. As one of our operating leases qualifies for the short-term lease exception under this guidance, we will continue to account for this lease under legacy GAAP and did not include this lease in our calculation of the lease liability and right-of-use asset. At March 31, 2019, our lease liability was $13 million, which was a component of Accrued expenses and other liabilities, and our right-of-use asset was $12 million, which was a component of Other assets.

Note 16. Commitments and Contingencies - (continued)

We determined that the four remaining leases did not contain an implicit interest rate and used a discount rate equal to our incremental borrowing rate on a collateralized basis to determine the present value of our total lease payments. As such, we determined the applicable discount rate for each of our leases using a swap rate plus an applicable spread for borrowing arrangements secured by our real estate loans and securities for a length of time equal to the remaining lease term on the date of adoption. At March 31, 2019, the weighted-average remaining lease term and weighted-average discount rate for our leases was 8 years and 5.3%, respectively.

Commitment to Fund Residential Bridge Loans

As of March 31, 2019, we had commitments to fund $4 million of residential bridge loans. These commitments are generally subject to loan agreements with covenants regarding the financial performance of the customer and other terms regarding advances that must be met before we fund the commitment. We may also advance funds related to loans sold under a separate loan sale agreement that are generally repaid immediately by the loan purchaser and do not generally expose us to loss (outstanding commitments related to these loans that we may temporarily fund totaled approximately $82 million at March 31, 2019).

Commitment to Fund Partnerships

In the fourth quarter of 2018, we invested in two partnerships created to acquire and manage certain mortgage servicing related assets (see *Note 10* for additional detail). At March 31, 2019, we had an outstanding commitment to fund an additional $19 million to these partnerships to acquire additional outstanding servicer advances and excess MSRs. We expect to fund the remainder before the end of July 2019. In connection with this investment, we are also required to fund future net servicer advances related to the underlying mortgage loans. The actual amount of net servicer advances we may fund in the future is subject to significant uncertainty and will be based on the credit and prepayment performance of the underlying loans.

In the first quarter of 2019, we invested in a partnership created to acquire floating rate, light-renovation multifamily loans from Freddie Mac (see *Note 10* for additional detail). At March 31, 2019, we had an outstanding commitment to fund an additional $56 million to the partnership. Additionally, in connection with this transaction, we have made a guarantee to Freddie Mac in the event of losses incurred on the loans that exceed the equity available in the partnership to absorb such losses. At March 31, 2019, the carrying value of this guarantee was $0.1 million. We believe the likelihood of performance under the guarantee is remote. Our maximum loss exposure from this guarantee arrangement is $135 million.

5 Arches Contingent Consideration

As part of the consideration for our acquisition of 5 Arches, we are committed to make earn-out payments up to $27 million, payable in a mix of cash and Redwood common stock, which will be calculated following each of the first two anniversaries of the option closing date based on loan origination volumes exceeding certain specified thresholds. These contingent earn-out payments are classified as contingent consideration liabilities and carried at fair value. At March 31, 2019, our estimated fair value of these contingent liabilities were $25 million.

Commitment to Participate in Loan Warehouse Facility

In the second quarter of 2018, we invested in a participation in the mortgage loan warehouse credit facility of one of our loan sellers. This investment included a commitment to participate in (and an obligation to fund) a designated amount of the loan seller's borrowings under this warehouse credit facility. Our commitment to participate in this facility was terminated in the first quarter of 2019. See *Note 12* for additional detail on our participation in a loan warehouse facility.

Note 16. Commitments and Contingencies - (continued)

Loss Contingencies — Risk-Sharing

During 2015 and 2016, we sold conforming loans to the Agencies with an original unpaid principal balance of $3.19 billion, subject to our risk-sharing arrangements with the Agencies. At March 31, 2019, the maximum potential amount of future payments we could be required to make under these arrangements was $44 million and this amount was fully collateralized by assets we transferred to pledged accounts and is presented as pledged collateral in Other assets on our consolidated balance sheets. We have no recourse to any third parties that would allow us to recover any amounts related to our obligations under the arrangements. At March 31, 2019, we had not incurred any losses under these arrangements. For the three months ended March 31, 2019 and 2018, other income related to these arrangements was $1 million for both periods, and net market valuation losses related to these investments were $0.1 million for both periods.

All of the loans in the reference pools subject to these risk-sharing arrangements were originated in 2014 and 2015, and at March 31, 2019, the loans had an unpaid principal balance of $1.80 billion and a weighted average FICO score of 759 (at origination) and LTV ratio of 76% (at origination). At March 31, 2019, $6 million of the loans were 90 days or more delinquent, of which $1 million were in foreclosure. At March 31, 2019, the carrying value of our guarantee obligation was $16 million and included $5 million designated as a non-amortizing credit reserve, which we believe is sufficient to cover current expected losses under these obligations.

Our consolidated balance sheets include assets of special purpose entities ("SPEs") associated with these risk-sharing arrangements (i.e., the "pledged collateral" referred to above) that can only be used to settle obligations of these SPEs for which the creditors of these SPEs (the Agencies) do not have recourse to Redwood Trust, Inc. or its affiliates. At March 31, 2019 and December 31, 2018, assets of such SPEs totaled $48 million and $47 million, respectively, and liabilities of such SPEs totaled $16 million and $17 million, respectively.

Loss Contingencies — Residential Repurchase Reserve

We maintain a repurchase reserve for potential obligations arising from representation and warranty violations related to residential loans we have sold to securitization trusts or third parties and for conforming residential loans associated with MSRs that we have purchased from third parties. We do not originate residential loans and we believe the initial risk of loss due to loan repurchases (i.e., due to a breach of representations and warranties) would generally be a contingency to the companies from whom we acquired the loans. However, in some cases, for example, where loans were acquired from companies that have since become insolvent, repurchase claims may result in our being liable for a repurchase obligation.

At both March 31, 2019 and December 31, 2018, our repurchase reserve associated with our residential loans and MSRs was $4 million and was recorded in Accrued expenses and other liabilities on our consolidated balance sheets. We received four and two repurchase requests during the three months ended March 31, 2019 and 2018, respectively, and did not repurchase any loans during either of these periods. During the three months ended March 31, 2019 and 2018, we recorded repurchase provisions of $0.1 million and $0.3 million, respectively, that were recorded in Mortgage banking activities, net and Other income, net on our consolidated statements of income.

Loss Contingencies — Litigation

On or about December 23, 2009, the Federal Home Loan Bank of Seattle (the “FHLB-Seattle”) filed a complaint in the Superior Court for the State of Washington (case number 09-2-46348-4 SEA) against Redwood Trust, Inc., our subsidiary, Sequoia Residential Funding, Inc. (“SRF”), Morgan Stanley & Co., and Morgan Stanley Capital I, Inc. (collectively, the “FHLB-Seattle Defendants”), which alleged that the FHLB-Seattle Defendants made false or misleading statements in offering materials for a mortgage pass-through certificate (the “Seattle Certificate”) issued in the Sequoia Mortgage Trust 2005-4 securitization transaction (the “2005-4 RMBS”) and purchased by the FHLB-Seattle. The Seattle Certificate was issued with an original principal amount of approximately $133 million, and, at March 31, 2019, approximately $126 million of principal and $12 million of interest payments had been made in respect of the Seattle Certificate. The matter was subsequently resolved and the claims were dismissed by the FHLB Seattle as to all the FHLB Seattle Defendants. At the time the Seattle Certificate was issued, Redwood agreed to indemnify the underwriters of the 2005-4 RMBS, which underwriters were named as defendants in the action, for certain losses and expenses they might incur as a result of claims made against them relating to this RMBS, including, without limitation, certain legal expenses. Regardless of the resolution of this litigation, we could incur a loss as a result of these indemnities.

Note 16. Commitments and Contingencies - (continued)

On or about July 15, 2010, The Charles Schwab Corporation ("Schwab") filed a complaint in the Superior Court for the State of California in San Francisco (case number CGC-10-501610) against SRF and 26 other defendants (collectively, the "Schwab Defendants"), which alleged that the Schwab Defendants made false or misleading statements in offering materials for various residential mortgage-backed securities sold or issued by the Schwab Defendants. Schwab alleged only a claim for negligent misrepresentation under California state law against SRF and sought unspecified damages and attorneys' fees and costs from SRF. Schwab claimed that SRF made false or misleading statements in offering materials for a mortgage pass-through certificate (the "Schwab Certificate") issued in the 2005-4 RMBS and purchased by Schwab. The Schwab Certificate was issued with an original principal amount of approximately $15 million, and, at March 31, 2019, approximately $14 million of principal and $1 million of interest payments had been made in respect of the Schwab Certificate. On November 14, 2014, Schwab voluntarily dismissed with prejudice its negligent misrepresentation claim, which resulted in the dismissal with prejudice of SRF from the action. Subsequently, the matter was resolved and Schwab dismissed its claims against the lead underwriter of the 2005-4 RMBS. At the time the Schwab Certificate was issued, Redwood agreed to indemnify the underwriters of the 2005-4 RMBS, which underwriters were also named as defendants in the action, for certain losses and expenses they might incur as a result of claims made against them relating to this RMBS, including, without limitation, certain legal expenses. Regardless of the resolution of this litigation, Redwood could incur a loss as a result of these indemnities.

Through certain of our wholly-owned subsidiaries, we have in the past engaged in, and expect to continue to engage in, activities relating to the acquisition and securitization of residential mortgage loans. In addition, certain of our wholly-owned subsidiaries have in the past engaged in activities relating to the acquisition and securitization of debt obligations and other assets through the issuance of collateralized debt obligations (commonly referred to as CDO transactions). Because of this involvement in the securitization and CDO businesses, we could become the subject of litigation relating to these businesses, including additional litigation of the type described above, and we could also become the subject of governmental investigations, enforcement actions, or lawsuits, and governmental authorities could allege that we violated applicable law or regulation in the conduct of our business. As an example, in July 2016 we became aware of a complaint filed by the State of California on April 1, 2016 against Morgan Stanley & Co. and certain of its affiliates alleging, among other things, that there were misleading statements contained in offering materials for 28 different mortgage pass-through certificates purchased by various California investors, including various California public pension systems, from Morgan Stanley and alleging that Morgan Stanley made false or fraudulent claims in connection with the sale of those certificates. Of the 28 mortgage pass-through certificates that were the subject of the complaint, two were Sequoia mortgage pass-through certificates issued in 2004 and two were Sequoia mortgage pass-through certificates issued in 2007. With respect to each of those certificates, our wholly-owned subsidiary, RWT Holdings, Inc., was the sponsor and our wholly-owned subsidiary, Sequoia Residential Funding, Inc., was the depositor. The plaintiffs subsequently withdrew from the litigation their claims based on eight of the 28 mortgage pass-through certificates, including one of the Sequoia mortgage pass-through certificates issued in 2004. We believe this matter was subsequently resolved and the plaintiffs withdrew their remaining claims. At the time these Sequoia mortgage pass-through certificates were issued, Sequoia Residential Funding, Inc. and Redwood Trust agreed to indemnify the underwriters of these certificates for certain losses and expenses they might incur as a result of claims made against them relating to these certificates, including, without limitation, certain legal expenses. Regardless of the resolution of this litigation, we could incur a loss as a result of these indemnities.

In accordance with GAAP, we review the need for any loss contingency reserves and establish reserves when, in the opinion of management, it is probable that a matter would result in a liability and the amount of loss, if any, can be reasonably estimated. Additionally, we record receivables for insurance recoveries relating to litigation-related losses and expenses if and when such amounts are covered by insurance and recovery of such losses or expenses are due. At March 31, 2019, the aggregate amount of loss contingency reserves established in respect of the FHLB-Seattle and Schwab litigation matters described above was $2 million. We review our litigation matters each quarter to assess these loss contingency reserves and make adjustments in these reserves, upwards or downwards, as appropriate, in accordance with GAAP based on our review.

In the ordinary course of any litigation matter, including certain of the above-referenced matters, we have engaged and may continue to engage in formal or informal settlement communications with the plaintiffs or co-defendants. Settlement communications we have engaged in relating to certain of the above-referenced litigation matters are one of the factors that have resulted in our determination to establish the loss contingency reserves described above. We cannot be certain that any of these matters will be resolved through a settlement prior to trial and we cannot be certain that the resolution of these matters, whether through trial or settlement, will not have a material adverse effect on our financial condition or results of operations in any future period.

Note 16. Commitments and Contingencies - (continued)

Future developments (including resolution of substantive pre-trial motions relating to these matters, receipt of additional information and documents relating to these matters (such as through pre-trial discovery), new or additional settlement communications with plaintiffs relating to these matters, or resolutions of similar claims against other defendants in these matters) could result in our concluding in the future to establish additional loss contingency reserves or to disclose an estimate of reasonably possible losses in excess of our established reserves with respect to these matters. Our actual losses with respect to the above-referenced litigation matters may be materially higher than the aggregate amount of loss contingency reserves we have established in respect of these litigation matters, including in the event that any of these matters proceeds to trial and the plaintiff prevails. Other factors that could result in our concluding to establish additional loss contingency reserves or estimate additional reasonably possible losses, or could result in our actual losses with respect to the above-referenced litigation matters being materially higher than the aggregate amount of loss contingency reserves we have established in respect of these litigation matters include that: there are significant factual and legal issues to be resolved; information obtained or rulings made during the lawsuits could affect the methodology for calculation of the available remedies; and we may have additional obligations pursuant to indemnity agreements, representations and warranties, and other contractual provisions with other parties relating to these litigation matters that could increase our potential losses.

Note 17. Equity

The following table provides a summary of changes to accumulated other comprehensive income by component for the three months ended March 31, 2019 and 2018.

Table 17.1 – Changes in Accumulated Other Comprehensive Income by Component

	Three Months Ended March 31, 2019		Three Months Ended March 31, 2018	
(In Thousands)	**Net Unrealized Gains on Available-for-Sale Securities**	**Net Unrealized Losses on Interest Rate Agreements Accounted for as Cash Flow Hedges**	**Net Unrealized Gains on Available-for-Sale Securities**	**Net Unrealized Losses on Interest Rate Agreements Accounted for as Cash Flow Hedges**
Balance at beginning of period	$ 95,342	$ (34,045)	$ 128,201	$ (42,953)
Other comprehensive income (loss) before reclassifications	6,718	(5,838)	(4,237)	8,431
Amounts reclassified from other accumulated comprehensive income	(9,493)	—	(9,387)	—
Net current-period other comprehensive (loss) income	(2,775)	(5,838)	(13,624)	8,431
Balance at End of Period	$ 92,567	$ (39,883)	$ 114,577	$ (34,522)

The following table provides a summary of reclassifications out of accumulated other comprehensive income for the three months ended March 31, 2019 and 2018.

Table 17.2 – Reclassifications Out of Accumulated Other Comprehensive Income

		Amount Reclassified From Accumulated Other Comprehensive Income	
		Three Months Ended March 31,	
(In Thousands)	**Affected Line Item in the Income Statement**	**2019**	**2018**
Net Realized (Gain) Loss on AFS Securities			
Gain on sale of AFS securities	Realized gains, net	$ (9,493)	$ (9,387)
		$ (9,493)	$ (9,387)

Note 17. Equity - (continued)

Issuance of Common Stock

In the fourth quarter of 2018, we established a program to sell up to an aggregate of $150 million of common stock from time to time in at-the-market ("ATM") offerings. During the fourth quarter of 2018, we issued 1,550,819 common shares for net proceeds of approximately $25 million through ATM offerings. At March 31, 2019, approximately $125 million remained outstanding for future offerings under this program.

On January 29, 2019, we sold 11,500,000 shares of common stock in an underwritten public offering, resulting in net proceeds of approximately $177 million.

Direct Stock Purchase and Dividend Reinvestment Plan

During the three months ended March 31, 2019, we issued 399,838 shares of common stock through our Direct Stock Purchase and Dividend Reinvestment Plan, resulting in net proceeds of approximately $6 million.

Earnings per Common Share

The following table provides the basic and diluted earnings per common share computations for the three months ended March 31, 2019 and 2018.

Table 17.3 – Basic and Diluted Earnings per Common Share

	Three Months Ended March 31,	
(In Thousands, except Share Data)	**2019**	**2018**
Basic Earnings per Common Share:		
Net income attributable to Redwood	$ 54,464	$ 46,845
Less: Dividends and undistributed earnings allocated to participating securities	(1,539)	(1,433)
Net income allocated to common shareholders	$ 52,925	$ 45,412
Basic weighted average common shares outstanding	92,685,350	75,396,649
Basic Earnings per Common Share	$ 0.57	$ 0.60
Diluted Earnings per Common Share:		
Net income attributable to Redwood	$ 54,464	$ 46,845
Less: Dividends and undistributed earnings allocated to participating securities	(1,539)	(1,394)
Add back: Interest expense on convertible notes for the period, net of tax	8,687	8,641
Net income allocated to common shareholders	$ 61,612	$ 54,092
Weighted average common shares outstanding	92,685,350	75,396,649
Net effect of dilutive equity awards	150,170	34,827
Net effect of assumed convertible notes conversion to common shares	33,442,640	32,763,121
Diluted weighted average common shares outstanding	126,278,160	108,194,597
Diluted Earnings per Common Share	$ 0.49	$ 0.50

We included participating securities, which are certain equity awards that have non-forfeitable dividend participation rights, in the calculations of basic and diluted earnings per common share as we determined that the two-class method was more dilutive than the alternative treasury stock method for these shares. Dividends and undistributed earnings allocated to participating securities under the basic and diluted earnings per share calculations require specific shares to be included that may differ in certain circumstances.

Note 17. Equity - (continued)

During the three months ended March 31, 2019 and 2018, certain of our convertible notes were determined to be dilutive and were included in the calculation of diluted EPS under the "if-converted" method. Under this method, the periodic interest expense (net of applicable taxes) for dilutive notes is added back to the numerator and the weighted average number of shares that the notes are entitled to (if converted, regardless of whether they are in or out of the money) are included in the denominator.

For the three months ended March 31, 2019 and 2018, the number of outstanding equity awards that were antidilutive totaled 7,376 and 6,838, respectively.

Stock Repurchases

In February 2018, our Board of Directors approved an authorization for the repurchase of our common stock, increasing the total amount authorized for repurchases of common stock to $100 million, and also authorized the repurchase of outstanding debt securities, including convertible and exchangeable debt. This authorization increased the previous share repurchase authorization approved in February 2016 and has no expiration date. This repurchase authorization does not obligate us to acquire any specific number of shares or securities. Under this authorization, shares or securities may be repurchased in privately negotiated and/or open market transactions, including under plans complying with Rule 10b5-1 under the Securities Exchange Act of 1934, as amended. At March 31, 2019, $100 million of the current authorization remained available for the repurchase of shares of our common stock.

Note 18. Equity Compensation Plans

At March 31, 2019 and December 31, 2018, 4,298,376 and 4,616,776 shares of common stock, respectively, were available for grant under our Incentive Plan. The unamortized compensation cost of awards issued under the Incentive Plan and purchases under the Employee Stock Purchase Plan totaled $29 million at March 31, 2019, as shown in the following table.

Table 18.1 – Activities of Equity Compensation Costs by Award Type

	Three Months Ended March 31, 2019					
(In Thousands)	**Restricted Stock Awards**	**Restricted Stock Units**	**Deferred Stock Units**	**Performance Stock Units**	**Employee Stock Purchase Plan**	**Total**
Unrecognized compensation cost at beginning of period	$ 3,498	$ 74	$ 14,489	$ 7,061	$ —	$ 25,122
Equity grants	—	2,953	3,951	—	160	7,064
Equity grant forfeitures	—	—	—	—	—	—
Equity compensation expense	(395)	(66)	(1,617)	(835)	(40)	(2,953)
Unrecognized Compensation Cost at End of Period	$ 3,103	$ 2,961	$ 16,823	$ 6,226	$ 120	$ 29,233

At March 31, 2019, the weighted average amortization period remaining for all of our equity awards was two years.

Restricted Stock Awards ("RSAs")

At March 31, 2019 and December 31, 2018, there were 218,022 and 339,482 shares, respectively, of RSAs outstanding. Restrictions on these shares lapse through 2022. During the three months ended March 31, 2019, there were no RSAs granted, restrictions on 116,584 RSAs lapsed and those shares were distributed, and no RSAs forfeited.

Restricted Stock Units ("RSUs")

At March 31, 2019 and December 31, 2018, there were 197,480 and 4,876 shares, respectively, of RSUs outstanding. Restrictions on these shares lapse through 2023. During the three months ended March 31, 2019, there were 192,604 RSUs granted, no RSUs distributed, and no RSUs forfeited.

Note 18. Equity Compensation Plans - (continued)

Deferred Stock Units ("DSUs")

At March 31, 2019 and December 31, 2018, there were 2,396,886 and 2,336,720 DSUs, respectively, outstanding of which 1,119,692 and 1,181,622, respectively, had vested. During the three months ended March 31, 2019, there were 266,173 DSUs granted, 206,007 DSUs distributed, and no DSUs forfeited. Unvested DSUs at March 31, 2019 vest through 2023.

Performance Stock Units ("PSUs")

At both March 31, 2019 and December 31, 2018, the target number of PSUs that were unvested was 725,616. Vesting for all PSUs will generally occur at the end of three years from their grant date based on various TSR performance calculations, as discussed in our Annual Report on Form 10-K for the year ended December 31, 2018.

Employee Stock Purchase Plan ("ESPP")

The ESPP allows a maximum of 450,000 shares of common stock to be purchased in aggregate for all employees. As of March 31, 2019 and December 31, 2018, 397,945 and 390,569 shares had been purchased, respectively, and there remained a negligible amount of uninvested employee contributions in the ESPP at March 31, 2019.

Note 19. Mortgage Banking Activities, Net

The following table presents the components of Mortgage banking activities, net, recorded in our consolidated statements of income for the three months ended March 31, 2019 and 2018.

Table 19.1 – Mortgage Banking Activities

	Three Months Ended March 31,	
(In Thousands)	**2019**	**2018**
Residential Mortgage Banking Activities, Net		
Changes in fair value of:		
Residential loans, at fair value (1)	$ 14,844	$ (2,194)
Risk management derivatives (2)	(4,138)	28,432
Other income, net (3)	121	338
Total residential mortgage banking activities, net	10,827	26,576
Business Purpose Mortgage Banking Activities, Net:		
Changes in fair value of:		
Single-family rental loans, at fair value (1)	1,744	—
Risk management derivatives (2)	(846)	—
Residential bridge loans, at fair value	86	—
Other income, net (4)	498	—
Total business purpose mortgage banking activities, net	1,482	—
Mortgage Banking Activities, Net	$ 12,309	$ 26,576

(1) Includes changes in fair value for associated loan purchase and forward sale commitments.

(2) Represents market valuation changes of derivatives that were used to manage risks associated with our accumulation of loans.

(3) Amounts in this line item include other fee income from loan acquisitions and the provision for repurchases expense, presented net.

(4) Amounts in this line item include other fee income from loan originations.

Note 20. Investment Fair Value Changes, Net

The following table presents the components of Investment fair value changes, net, recorded in our consolidated statements of income for the three months ended March 31, 2019 and 2018.

Table 20.1 – Investment Fair Value Changes

(In Thousands)	Three Months Ended March 31, 2019	Three Months Ended March 31, 2018
Investment Fair Value Changes, Net		
Changes in fair value of:		
Residential loans held-for-investment, at Redwood	$ 28,108	$ (38,985)
Residential bridge loans held-for-investment	(303)	—
Trading securities	21,860	(2,955)
Servicer advance investments	1,008	—
Excess MSRs	(437)	—
Net investments in Legacy Sequoia entities (1)	(374)	(8)
Net investments in Sequoia Choice entities (1)	3,265	(86)
Net investment in Freddie Mac SLST entity (1)	6,365	—
Net investments in Freddie Mac K-Series entities (1)	3,119	—
Risk-sharing investments	(77)	(139)
Risk management derivatives, net	(42,375)	43,782
Investment Fair Value Changes, Net	$ 20,159	$ 1,609

(1) Includes changes in fair value of the loans held-for-investment, REO and the ABS issued at the entities, which netted together represent the change in value of our investments at the consolidated VIEs.

Note 21. Operating Expenses

Components of our operating expenses for the three months ended March 31, 2019 and 2018 are presented in the following table.

Table 21.1 – Components of Operating Expenses

	Three Months Ended March 31,	
(In Thousands)	**2019**	**2018**
Fixed compensation expense	$ 8,205	$ 6,439
Variable compensation expense	4,402	6,907
Equity compensation expense	2,953	2,697
Total compensation expense	15,560	16,043
Systems and consulting	1,828	1,866
Loan acquisition costs (1)	1,477	1,818
Office costs	1,304	1,140
Accounting and legal	1,125	834
Corporate costs	674	504
Other operating expenses	1,191	825
Total Operating Expenses	$ 23,159	$ 23,030

(1) Loan acquisition costs primarily includes underwriting and due diligence costs related to the acquisition of residential loans held-for-sale at fair value.

Note 22. Taxes

For the three months ended March 31, 2019 and 2018, we recognized a provision for income taxes of $1 million and $5 million, respectively. The following is a reconciliation of the statutory federal and state tax rates to our effective tax rate at March 31, 2019 and 2018.

Table 22.1 – Reconciliation of Statutory Tax Rate to Effective Tax Rate

	March 31, 2019	**March 31, 2018**
Federal statutory rate	21.0 %	21.0 %
State statutory rate, net of Federal tax effect	8.6 %	8.6 %
Differences in taxable (loss) income from GAAP income	(8.5)%	(4.1)%
Change in valuation allowance	(4.1)%	(3.9)%
Dividends paid deduction	(15.4)%	(12.1)%
Effective Tax Rate	1.6 %	9.5 %

We assessed our tax positions for all open tax years (i.e., Federal, 2015 to 2019, and State, 2014 to 2019) at March 31, 2019 and December 31, 2018, and concluded that we had no uncertain tax positions that resulted in material unrecognized tax benefits.

Note 23. Segment Information

Redwood operates in two segments: Investment Portfolio and Mortgage Banking. Our segments are based on our organizational and management structure, which aligns with how our results are monitored and performance is assessed. For a full description of our segments, see *Part I, Item 1—Business* in our Annual Report on Form 10-K for the year ended December 31, 2018.

Our Mortgage Banking segment includes activity from both our residential and business purpose mortgage banking operations. Our business purpose mortgage banking operations includes activity from our wholly-owned subsidiary 5 Arches and our single-family rental loans that we are aggregating for subsequent sale or securitization. In connection with our acquisition of 5 Arches on March 1, 2019, the goodwill, intangible assets, and contingent consideration we recorded on our consolidated balance sheets were included in our Mortgage Banking segment. The gain on re-measurement of our initial minority investment and purchase option in 5 Arches during the three months ended March 31, 2019 was included in Corporate/Other.

Segment contribution represents the measure of profit that management uses to assess the performance of our business segments and make resource allocation and operating decisions. Certain corporate expenses not directly assigned or allocated to one of our two segments, as well as activity from certain consolidated Sequoia entities, are included in the Corporate/Other column as reconciling items to our consolidated financial statements. These unallocated corporate expenses primarily include interest expense associated with certain long-term debt, indirect operating expenses, and other expense.

The following tables present financial information by segment for the three months ended March 31, 2019 and 2018.

Table 23.1 – Business Segment Financial Information

	Three Months Ended March 31, 2019			
(In Thousands)	**Investment Portfolio**	**Mortgage Banking**	**Corporate/ Other**	**Total**
Interest income	$ 115,452	$ 10,377	$ 5,212	$ 131,041
Interest expense	(77,887)	(5,564)	(15,825)	(99,276)
Net interest income (loss)	37,565	4,813	(10,613)	31,765
Non-interest income				
Mortgage banking activities, net	—	12,309	—	12,309
Investment fair value changes, net	20,556	—	(397)	20,159
Other income (expense), net	1,221	(167)	2,533	3,587
Realized gains, net	10,686	—	—	10,686
Total non-interest income, net	32,463	12,142	2,136	46,741
Direct operating expenses	(2,661)	(8,104)	(12,394)	(23,159)
Provision for income taxes	(342)	(541)	—	(883)
Segment Contribution	$ 67,025	$ 8,310	$ (20,871)	
Net Income				$ 54,464
Non-cash amortization income (expense), net	$ 2,368	$ (723)	$ (1,300)	$ 345

Note 23. Segment Information - (continued)

(In Thousands)	Three Months Ended March 31, 2018 Investment Portfolio	Mortgage Banking	Corporate/ Other	Total
Interest income	$ 58,757	$ 12,897	$ 4,965	$ 76,619
Interest expense	(19,863)	(6,137)	(15,514)	(41,514)
Net interest income (loss)	38,894	6,760	(10,549)	35,105
Non-interest income				
Mortgage banking activities, net	—	26,576	—	26,576
Investment fair value changes, net	1,590	—	19	1,609
Other income, net	2,118	—	—	2,118
Realized gains, net	9,363	—	—	9,363
Total non-interest income, net	13,071	26,576	19	39,666
Direct operating expenses	(2,007)	(8,632)	(12,391)	(23,030)
Provision for income taxes	(888)	(4,008)	—	(4,896)
Segment Contribution	$ 49,070	$ 20,696	$ (22,921)	
Net Income				$ 46,845
Non-cash amortization income (expense), net	$ 4,617	$ (22)	$ (954)	$ 3,641

The following table presents the components of Corporate/Other for the three months ended March 31, 2019 and 2018.

Table 23.2 – Components of Corporate/Other

	Three Months Ended March 31,					
	2019			2018		
(In Thousands)	Legacy Consolidated VIEs (1)	Other	Total	Legacy Consolidated VIEs (1)	Other	Total
Interest income	$ 4,853	$ 359	$ 5,212	$ 4,812	$ 153	$ 4,965
Interest expense	(4,115)	(11,710)	(15,825)	(3,852)	(11,662)	(15,514)
Net interest income (loss)	738	(11,351)	(10,613)	960	(11,509)	(10,549)
Non-interest income						
Investment fair value changes, net	(374)	(23)	(397)	(8)	27	19
Other income	—	2,533	2,533	—	—	—
Total non-interest income, net	(374)	2,510	2,136	(8)	27	19
Direct operating expenses	—	(12,394)	(12,394)	—	(12,391)	(12,391)
Total	$ 364	$ (21,235)	$ (20,871)	$ 952	$ (23,873)	$ (22,921)

(1) Legacy consolidated VIEs represent Legacy Sequoia entities that are consolidated for GAAP financial reporting purposes. See *Note 4* for further discussion on VIEs.

Note 23. Segment Information - (continued)

The following table presents supplemental information by segment at March 31, 2019 and December 31, 2018.

Table 23.3 – Supplemental Segment Information

(In Thousands)	Investment Portfolio	Mortgage Banking	Corporate/ Other	Total
March 31, 2019				
Residential loans	$ 5,988,583	$ 797,073	$ 488,645	$ 7,274,301
Business purpose residential loans	103,916	56,696	—	160,612
Multifamily loans	2,175,899	—	—	2,175,899
Real estate securities	1,543,152	—	—	1,543,152
Other investments	411,853	2,345	—	414,198
Goodwill and intangible assets	—	52,895	—	52,895
Total assets	10,444,279	942,596	806,484	12,193,359
December 31, 2018				
Residential loans	$ 5,685,983	$ 1,048,801	$ 519,958	$ 7,254,742
Business purpose residential loans	112,798	28,460	—	141,258
Multifamily loans	2,144,598	—	—	2,144,598
Real estate securities	1,452,494	—	—	1,452,494
Other investments	427,764	—	10,754	438,518
Total assets	10,093,993	1,103,090	740,323	11,937,406

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

INTRODUCTION

Management’s Discussion and Analysis of Financial Condition and Results of Operations (“MD&A”) is intended to provide a reader of our financial statements with a narrative from the perspective of our management on our financial condition, results of operations, liquidity and certain other factors that may affect our future results. Our MD&A is presented in six main sections:

- Overview
- Results of Operations
- Liquidity and Capital Resources
- Off-Balance Sheet Arrangements and Contractual Obligations
- Critical Accounting Policies and Estimates
- New Accounting Standards

Our MD&A should be read in conjunction with the Consolidated Financial Statements and related Notes included in Part I, Item 1 of this Quarterly Report on Form 10-Q and in Part II, Item 8, Financial Statements and Supplementary Data in our most recent Annual Report on Form 10-K, as well as the sections entitled “Risk Factors” in Part I, Item 1A of our most recent Annual Report on Form 10-K and Part II, Item 1A of this Quarterly Report on Form 10-Q, as well as other cautionary statements and risks described elsewhere in this report and our most recent Annual Report on Form 10-K. The discussion in this MD&A contains forward-looking statements that involve substantial risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors, such as those discussed in the Cautionary Statement below.

References herein to “Redwood,” the “company,” “we,” “us,” and “our” include Redwood Trust, Inc. and its consolidated subsidiaries, unless the context otherwise requires. Financial information concerning our business is set forth in this “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” and our consolidated financial statements and notes thereto, which are included in Part I, Item 1 of this Quarterly Report on Form 10-Q.

Our website can be found at www.redwoodtrust.com. We make available, free of charge through the investor information section of our website, access to our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the U.S. Securities Exchange Act of 1934, as well as proxy statements, as soon as reasonably practicable after we electronically file such material with, or furnish it to, the U.S. Securities and Exchange Commission (“SEC”). We also make available, free of charge, access to our charters for our Audit Committee, Compensation Committee, and Governance and Nominating Committee, our Corporate Governance Standards, and our Code of Ethics governing our directors, officers, and employees. Within the time period required by the SEC and the New York Stock Exchange, we will post on our website any amendment to the Code of Ethics and any waiver applicable to any executive officer or director of Redwood. In addition, our website includes information concerning purchases and sales of our equity securities by our executive officers and directors, and may include disclosure relating to certain non-GAAP financial measures (as defined in the SEC’s Regulation G) that we may make public orally, telephonically, by webcast, by broadcast, or by similar means from time to time. The information on our website is not part of this Quarterly Report on Form 10-Q.

Our Investor Relations Department can be contacted at One Belvedere Place, Suite 300, Mill Valley, CA 94941, Attn: Investor Relations, telephone (866) 269-4976.

Our Business

Redwood Trust, Inc., together with its subsidiaries, is a specialty finance company focused on making credit-sensitive investments in single-family residential and multifamily mortgages and related assets and engaging in mortgage banking activities. Our goal is to provide attractive returns to shareholders through a stable and growing stream of earnings and dividends, as well as through capital appreciation. We operate our business in two segments: Investment Portfolio and Mortgage Banking. Our segments are based on our organizational and management structure, which aligns with how our results are monitored and performance is assessed. For a full description of our segments, see Item 1—Business in our Annual Report on Form 10-K for the year ended December 31, 2018.

Our primary sources of income are net interest income from our investment portfolio and non-interest income from our mortgage banking activities. Net interest income consists of the interest income we earn on investments less the interest expense we incur on borrowed funds and other liabilities. Income from mortgage banking activities is generated through the acquisition of loans and their subsequent sale or securitization.

Redwood Trust, Inc. has elected to be taxed as a real estate investment trust ("REIT") under the Internal Revenue Code of 1986, as amended (the "Internal Revenue Code"), beginning with its taxable year ended December 31, 1994. We generally refer, collectively, to Redwood Trust, Inc. and those of its subsidiaries that are not subject to subsidiary-level corporate income tax as "the REIT" or "our REIT." We generally refer to subsidiaries of Redwood Trust, Inc. that are subject to subsidiary-level corporate income tax as "our operating subsidiaries" or "our taxable REIT subsidiaries" or "TRS." Our mortgage banking activities and investments in MSRs are generally carried out through our taxable REIT subsidiaries, while our portfolio of mortgage- and other real estate-related investments is primarily held at our REIT. We generally intend to retain profits generated and taxed at our taxable REIT subsidiaries, and to distribute as dividends at least 90% of the taxable income we generate at our REIT.

Redwood Trust, Inc. was incorporated in the State of Maryland on April 11, 1994, and commenced operations on August 19, 1994. Our executive offices are located at One Belvedere Place, Suite 300, Mill Valley, California 94941.

Cautionary Statement

This Quarterly Report on Form 10-Q and the documents incorporated by reference herein contain forward-looking statements within the meaning of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements involve numerous risks and uncertainties. Our actual results may differ from our beliefs, expectations, estimates, and projections and, consequently, you should not rely on these forward-looking statements as predictions of future events. Forward-looking statements are not historical in nature and can be identified by words such as "anticipate," "estimate," "will," "should," "expect," "believe," "intend," "seek," "plan" and similar expressions or their negative forms, or by references to strategy, plans, or intentions. These forward-looking statements are subject to risks and uncertainties, including, among other things, those described in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017 and this Quarterly Report on Form 10-Q, in each case under the caption "Risk Factors." Other risks, uncertainties, and factors that could cause actual results to differ materially from those projected may be described from time to time in reports we file with the SEC, including reports on Forms 10-Q and 8-K. We undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise.

Statements regarding the following subjects, among others, are forward-looking by their nature: (i) statements we make regarding Redwood's business strategy and strategic focus, including statements relating to our overall market position, strategy and long-term prospects (including trends driving the flow of capital in the housing finance market, our strategic initiatives designed to capitalize on those trends, our ability to attract capital to finance those initiatives, our approach to raising capital, our ability to pay higher sustainable dividends in the future, and the prospects for federal housing finance reform); (ii) statements related to our financial outlook and expectations for 2019, including with respect to our investment portfolio and mortgage banking activities; (iii) statements related to our mortgage banking activities, including our ability to continue to improve workflow efficiencies and capital turnover and expectations for second quarter loan purchase activity; (iv) statements related to our investment portfolio and investment opportunities, including the potential for earnings upside on deeper-discount securities, expectations regarding the increased pace of capital deployment during 2019, driven in part by access to 5 Arches' origination pipeline, and utilization of new financing structures that we expect will positively impact net margins; (v) statements relating to the potential for regulatory reform and positioning Redwood to capitalize on resulting opportunities, including the likelihood of administrative actions to emphasize a greater role for the private sector, such as building on the success of GSE risk-sharing transactions; (vi) statements relating to acquiring residential mortgage loans in the future that we have identified for purchase or plan to purchase, including the amount of such loans that we identified for purchase during the first quarter of 2019 and at March 31, 2019, and expected fallout and the corresponding volume of residential mortgage loans expected to be available for purchase; (vii) statements relating to our estimate of our available capital (including that we estimate our available capital at March 31, 2019 was approximately $100 million); (viii) statements we make regarding future dividends, including with respect to our regular quarterly dividends in 2019; and (ix) statements regarding our expectations and estimates relating to the characterization for income tax purposes of our dividend distributions, our expectations and estimates relating to tax accounting, tax liabilities and tax savings, and GAAP tax provisions, and our estimates of REIT taxable income and TRS taxable income.

Important factors, among others, that may affect our actual results include:

- the pace at which we redeploy our available capital into new investments and initiatives;
- our ability to scale our platform and systems, particularly with respect to our new initiatives;
- interest rate volatility, changes in credit spreads, and changes in liquidity in the market for real estate securities and loans;
- changes in the demand from investors for residential mortgages and investments, and our ability to distribute residential mortgages through our whole-loan distribution channel;
- our ability to finance our investments in securities and our acquisition of residential mortgages with short-term debt;
- changes in the values of assets we own;
- general economic trends, the performance of the housing, real estate, mortgage, credit, and broader financial markets, and their effects on the prices of earning assets and the credit status of borrowers;
- federal and state legislative and regulatory developments, and the actions of governmental authorities, including the new U.S. presidential administration, and in particular those affecting the mortgage industry or our business (including, but not limited to, the Federal Housing Finance Agency's rules relating to FHLB membership requirements and the implications for our captive insurance subsidiary's membership in the FHLB);
- strategic business and capital deployment decisions we make;
- developments related to the fixed income and mortgage finance markets and the Federal Reserve's statements regarding its future open market activity and monetary policy;
- our exposure to credit risk and the timing of credit losses within our portfolio;
- the concentration of the credit risks we are exposed to, including due to the structure of assets we hold and the geographical concentration of real estate underlying assets we own;
- our exposure to adjustable-rate mortgage loans;
- the efficacy and expense of our efforts to manage or hedge credit risk, interest rate risk, and other financial and operational risks;
- changes in credit ratings on assets we own and changes in the rating agencies' credit rating methodologies;
- changes in interest rates; changes in mortgage prepayment rates;
- changes in liquidity in the market for real estate securities and loans;
- our ability to finance the acquisition of real estate-related assets with short-term debt;
- the ability of counterparties to satisfy their obligations to us;
- our involvement in securitization transactions, the profitability of those transactions, and the risks we are exposed to in engaging in securitization transactions;
- exposure to claims and litigation, including litigation arising from our involvement in securitization transactions;
- ongoing litigation against various trustees of RMBS transactions;
- whether we have sufficient liquid assets to meet short-term needs;
- our ability to successfully compete and retain or attract key personnel;
- our ability to adapt our business model and strategies to changing circumstances;
- changes in our investment, financing, and hedging strategies and new risks we may be exposed to if we expand our business activities;
- our exposure to a disruption or breach of the security of our technology infrastructure and systems;
- exposure to environmental liabilities;
- our failure to comply with applicable laws and regulations;
- our failure to maintain appropriate internal controls over financial reporting and disclosure controls and procedures;
- the impact on our reputation that could result from our actions or omissions or from those of others; changes in accounting principles and tax rules;
- our ability to maintain our status as a REIT for tax purposes;
- limitations imposed on our business due to our REIT status and our status as exempt from registration under the Investment Company Act of 1940;
- decisions about raising, managing, and distributing capital; and
- other factors not presently identified.

This Quarterly Report on Form 10-Q may contain statistics and other data that in some cases have been obtained from or compiled from information made available by servicers and other third-party service providers.

OVERVIEW

Business Update

Our first quarter 2019 results reflected both strong operational progress and improved market conditions, collectively driving a resurgence in our GAAP financial results. GAAP earnings were $0.49 per share for the first quarter, as compared with a loss of $0.02 per share in the fourth quarter of 2018. Our GAAP book value increased to $16.00 per share at March 31, 2019, as compared to $15.89 per share at December 31, 2018.

We raised $184 million of equity capital in the first quarter and deployed $163 million, ending the quarter with approximately $100 million of capital available for investment at March 31, 2019. Investment activity in the first quarter was down slightly from our recent pace, but up over 50% from the first quarter of 2018. While we are still in the early stages of execution, this increase in capital deployment has begun to drive returns higher and scale our platform - both key strategic initiatives.

As we evaluate the return profiles on our investments, our focus remains on creating durable, long-term cash flows and optimizing our balance sheet, with the goal of being able to support a sustainable higher dividend. The biggest driver of returns in our portfolio is credit performance, which remained strong in the first quarter. Our recent investments are, by design, highly structured and differentiated; and thanks to the recent increased pace of deployment, many are relatively unseasoned with long projected lifespans. Collectively, our portfolio construction is driving towards a mix of strong near-term returns, complemented by deeper-discount securities with earnings upside if credit performance meets or exceeds modeled expectations.

During the first quarter of 2019, we completed the acquisition of 5 Arches, and work is underway to fully integrate the new platform. We continue to build our pipeline of single-family rental loans, and are beginning to reap the benefits of a consistent market presence in the form of repeat borrowers and more bespoke investment opportunities. Additionally, we expect to begin deploying incremental capital into the short-term bridge products that the platform produces, while continuing to monitor overall market demand for these loans. The financing market for bridge loans remains favorable, and we are utilizing structures that we expect will positively impact net margins. First quarter origination volume for the platform was lower than in the fourth quarter of 2018, driven in part by a portion of the pipeline pulling forward into the second quarter of 2019.

Turning to our residential mortgage banking operations, volumes remained under pressure in the first quarter - partly as a result of seasonality - but gross margins were quite strong as a result of strong securitization execution and robust demand from whole-loan buyers. We completed one Select and one Choice transaction during the quarter, along with significant whole loan sale activity, which represented 41% of our total distribution. Redwood Choice remains an important contributor to earnings and accounted for 44% of locked loans during the first quarter. Gross margins for Choice loans were significantly higher than those of our traditional Select loans as we achieved particularly strong execution on our Choice securitization.

We continued making progress towards managing our residential mortgage banking operations more efficiently by increasing asset turnover, which allows us to free up capital for reinvestment. Our goal remains to continue managing our capital down from an average of approximately $200 million last year, and we remain on track to do so.

As we work to optimize our platforms and plan for the future, we are closely monitoring the potential for regulatory reform and how we should position Redwood to capitalize on any resulting opportunities. Recently, Mark Calabria was confirmed as the new Director of the Federal Housing Finance Agency, and the Trump Administration directed both Treasury and HUD to develop and submit housing finance reform plans as soon as practicable. We expect the plans will likely identify reform measures that can be implemented through both administrative and legislative means but note that there continues to be little bi-partisan support for finding a permanent solution for the conservatorship of Fannie Mae and Freddie Mac.

In the near term, it is more likely that change will come from administrative actions that have emphasized a greater role for the private sector, such as building on the success of GSE risk-sharing transactions. We believe we are well positioned to take advantage of any reforms that promote a leveling of the playing field between the public and private sectors. From our vantage point as a seasoned private-label RMBS issuer, private market participants are willing and able to step up with capital. That said, affirmative signals must be sent by Washington that investment in the infrastructure and staff necessary to participate in private-label transactions will not be undermined by policies aimed at crowding out private capital. We note that for the first time in many years, the private markets are speaking for an increasing share of loans that are eligible for sale to the GSEs, and we believe they can speak for more without a negative impact on interest rates to available borrowers.

Overall, we exited the first quarter more optimistic about 2019 than we began it. Our second quarter of 2019 loan purchase activity is on pace to exceed the first quarter’s, and we expect the pace of capital deployment to increase over the course of 2019, driven in part by access to 5 Arches’ origination pipeline. In funding the growth of our asset base, our focus is on utilizing our available capital, while continuing to generate capital through security sales and financing structures that optimize our balance sheet.

Financial and Operational Overview - First Quarter of 2019

Highlights

The following table presents key earnings metrics for the three months ended March 31, 2019.

Table 1 – Key Earnings and Return Metrics

(In Thousands, except per Share Data)	Three Months Ended March 31, 2019	
Net income	$	54,464
Net income per diluted common share	$	0.49
Annualized GAAP return on equity		15%
Book value per share	$	16.00
Economic return on book value [(1)]		2.6%
REIT taxable income per share	$	0.30
Dividends per share	$	0.30

(1) Economic return on book value is based on the periodic change in GAAP book value per common share plus dividends declared per common share during the period.

- GAAP earnings per share increased in the first quarter, as spreads tightened and asset prices improved, recovering a significant portion of the market valuation losses we incurred in the fourth quarter from spread widening. Mortgage banking produced solid results in the first quarter, as consistent lock volume was supported by strong gross margins.
- In January, we raised $177 million of equity capital in a follow-on offering.
- We deployed $163 million of capital into new investments in the first quarter of 2019, a majority of which were proprietary.
- Residential jumbo loan purchase commitments were $1.20 billion, and we purchased $1.02 billion of jumbo loans during the first quarter of 2019.
- During the first quarter of 2019, we completed $1.18 billion of jumbo residential loan sales, including one Select securitization of $353 million and one Choice securitization of $350 million. Additionally, we sold $0.5 billion of whole loans to third parties.
- On March 1, 2019, we completed our purchase of the remaining 80% interest in 5 Arches. The impact to GAAP net income in the first quarter from the acquisition and one month of operations was approximately $0.02 per share. Our balance sheet at March 31, 2019 reflected the impact of this acquisition and included $29 million of goodwill, $24 million of intangible assets, $25 million of contingent consideration liabilities, and $4 million of deferred tax liabilities.

Book Value per Share

At March 31, 2019, our book value was $1.55 billion, or $16.00 per share, an increase from $15.89 per share at December 31, 2018. The following table sets forth the changes in our book value per share for the three months ended March 31, 2019.

Table 2 – Changes in Book Value per Share

(In Dollars, per share basis)	**Three Months Ended March 31, 2019**
Beginning book value per share	$ 15.89
Net income	0.49
Changes in unrealized gains on securities, net, from:	
Realized gains recognized in net income	(0.08)
Amortization income recognized in net income	(0.02)
Mark-to-market adjustments, net	0.10
Total change in unrealized gains on securities, net	—
Dividends	(0.30)
Issuance of common stock	(0.05)
Equity compensation, net	(0.02)
Changes in unrealized losses on derivatives hedging long-term debt	(0.06)
Other, net	0.05
Ending Book Value per Share	$ 16.00

Our GAAP book value per share increased $0.11 per share to $16.00 per share during the first quarter of 2019. This increase was primarily driven by earnings exceeding the dividend due to positive market valuation adjustments on our portfolio investments, partially offset by a decrease in the value of derivatives hedging our long-term debt, the effect of distributions of stock-based compensation, and dilution from our January common stock issuance.

Unrealized gains on our available-for-sale securities resulted in a $0.10 per share increase in mark-to-market adjustments, offset by $0.08 per share of previously unrealized net gains that were realized as income from the sale of securities, as well as $0.02 per share of discount accretion income recognized in earnings from the appreciation in the amortized cost basis of our available-for-sale securities.

Lower benchmark interest rates during the first quarter of 2019 resulted in a $0.06 per share decrease to book value due to an increase in unrealized losses on the derivatives hedging a portion of our long-term debt. At March 31, 2019, the cumulative unrealized loss on these derivatives, which is included in our GAAP book value per share, was $0.41 per share.

Capital Allocation Summary

This section provides an overview of our capital position and how it was allocated at March 31, 2019. A detailed discussion of our liquidity and capital resources is provided in the *Liquidity and Capital Resources* section of this MD&A that follows.

We use a combination of equity and corporate debt (which we collectively refer to as “capital”) to fund our business. Our total capital was $2.32 billion at March 31, 2019, and included $1.55 billion of equity capital and $0.77 billion of unsecured corporate debt, including $201 million of exchangeable debt due in 2019, $245 million of convertible debt due in 2023, $200 million of convertible debt due in 2024, and $140 million of trust-preferred securities due in 2037.

We also utilize various forms of collateralized short-term and long-term debt to finance certain investments and to warehouse some of our inventory of residential loans held-for-sale. We do not consider this collateralized debt as "capital" and, therefore, it is presented separately from allocated capital in the table below. The following table presents how our capital was allocated between business segments and investment types at March 31, 2019.

Table 3 – Capital Allocation Summary

At March 31, 2019 **(Dollars in Thousands)**	**Fair Value**	**Collateralized Debt**	**Allocated Capital**	**% of Total Capital**
Investment portfolio				
Residential loans [1]	$ 2,447,507	$ (1,999,999)	$ 447,508	19%
Securities portfolio				
Sequoia residential securities [2]	494,795	(205,643)	289,152	12%
Agency CRT securities	258,709	(34,905)	223,804	10%
Multifamily securities [3]	640,888	(417,599)	223,289	10%
Re-performing residential loan securities [4]	355,701	(171,758)	183,943	8%
Third-party residential securities	372,878	(251,174)	121,704	5%
Total securities portfolio	2,122,971	(1,081,079)	1,041,892	45%
Business purpose residential loans	103,916	(61,719)	42,197	2%
Other investments	442,476	(270,557)	171,919	7%
Other assets/(other liabilities)	169,765	(106,095)	63,670	3%
Cash and liquidity capital			359,971	N/A
Total investment portfolio	$ 5,286,635	$ (3,519,449)	2,127,157	92%
Residential			130,000	6%
Business purpose			65,358	3%
Total mortgage banking			195,358	8%
Total			$ 2,322,515	100%

(1) Includes $43 million of FHLB stock.

(2) Sequoia residential securities presented above includes $216 million of securities retained from our consolidated Sequoia Choice securitizations. For GAAP purposes we consolidated $2.33 billion of residential loans and $2.12 billion of non-recourse ABS debt associated with these retained securities.

(3) Multifamily securities presented above includes $129 million of subordinate investments in the Freddie Mac K-Series securitizations. For GAAP purposes we consolidated $2.18 billion of multifamily loans and $2.05 billion of non-recourse ABS debt associated with these securities.

(4) Re-performing residential loan securities presented above represent third-party securities collateralized by seasoned re-performing, and to a lesser extent, non-performing residential loans and includes $235 million of subordinate and mezzanine investments in the Freddie Mac SLST securitization. For GAAP purposes we consolidated $1.23 billion of residential loans and $993 million of non-recourse ABS debt associated with these securities.

Over the last several quarters, we have increased our allocation of capital to multifamily and re-performing securities, and expect to continue allocating capital into these investment types going forward. During the first quarter of 2019, we reallocated capital from our residential mortgage banking business to our investment portfolio, leveraging operational changes that allow us to manage our mortgage banking business with less capital.

As of March 31, 2019, our cash and liquidity capital included $100 million of capital available for investment. To fund new investments going forward, we will consider the most efficient sources of capital both from optimization within our portfolio and from the capital markets.

RESULTS OF OPERATIONS

Within this *Results of Operations* section, we provide commentary that compares results year-over-year for 2019 and 2018. Most tables include a "change" column that shows the amount by which the results from 2019 are greater or less than the results from the respective period in 2018. Unless otherwise specified, references in this section to increases or decreases during the "three-month periods" refer to the change in results for the first quarter of 2019, compared to the first quarter of 2018.

The following table presents the components of our net income for the three months ended March 31, 2019 and 2018.

Table 4 – Net Income

	Three Months Ended March 31,		
(In Thousands, except per Share Data)	**2019**	**2018**	**Change**
Net Interest Income	$ 31,765	$ 35,105	$ (3,340)
Non-interest Income			
Mortgage banking activities, net	12,309	26,576	(14,267)
Investment fair value changes, net	20,159	1,609	18,550
Other income, net	3,587	2,118	1,469
Realized gains, net	10,686	9,363	1,323
Total non-interest income, net	46,741	39,666	7,075
Operating expenses	(23,159)	(23,030)	(129)
Net income before income taxes	55,347	51,741	3,606
Provision for income taxes	(883)	(4,896)	4,013
Net Income	$ 54,464	$ 46,845	$ 7,619
Diluted earnings per common share	$ 0.49	$ 0.50	$ (0.01)

Net Interest Income

The decrease in net interest income during the three-month periods was driven primarily by lower average balances of residential loans held-for-sale and higher interest rates on our variable rate financing during the first quarter of 2019. This decrease was partially offset by increased interest income from additional portfolio investments that we made during the past year that in part utilized capital we raised in July of 2018 and January of 2019.

We utilize hedges to manage interest rate risk in our investment portfolio and the net interest paid or received from these instruments is a component of our Investment fair value changes line item, which is discussed below. Net hedge interest expense associated with portfolio hedges decreased in 2019 and on a combined basis, net interest income plus net interest income (expense) on hedges increased by $4 million for the three-month periods.

Additional detail on changes in net interest income is provided in the *"Net Interest Income"* section that follows.

Mortgage Banking Activities, Net

The decrease in income from mortgage banking activities during the three-month periods was predominantly due to a decrease in loan purchase volume in 2019, relative to 2018, on lower margins from our residential mortgage banking operations. This decrease was partially offset by an increase in income from our business purpose mortgage banking operations, including from the acquisition of 5 Arches. A more detailed analysis of the changes in this line item is included in the "*Results of Operations by Segment*" section that follows.

Investment Fair Value Changes, Net

Investment fair value changes, net, is primarily comprised of the change in fair values of our portfolio investments accounted for under the fair value option and interest rate hedges associated with these investments. During the three months ended March 31, 2019, the positive investment fair value changes were primarily driven by tightening credit spreads during the first quarter of 2019 in several parts of our portfolio, helping us to recover a significant amount of the fair value decline these investments experienced in the fourth quarter of 2018 from spread widening. Credit spreads on our residential loan portfolio remained largely unchanged from the fourth quarter. Additional detail on our investment fair value changes is included in the Investment Portfolio portion of the "*Results of Operations by Segment*" section that follows.

Other Income, Net

Other income is primarily comprised of MSR income and income from our residential loan risk-sharing arrangements with Fannie Mae and Freddie Mac. The increase in other income for the three-month periods was primarily due to a $2 million gain associated with the re-measurement of our initial minority investment and purchase option in 5 Arches and asset management fee income earned by 5 Arches. This increase was partially offset by a decrease in income from our MSR investments, as well as amortization expense from intangible assets we recorded in connection with the acquisition of 5 Arches.

Realized Gains, Net

During the three months ended March 31, 2019, we realized gains of $11 million, primarily from the sale of $42 million of AFS securities and the call of a seasoned Sequoia securitization. During the three months ended March 31, 2018, we realized gains of $9 million, primarily from the sale of $51 million of AFS securities.

Operating Expenses

Operating expenses remained consistent during the three-month periods, as a decrease in variable compensation expense in the first quarter of 2019 was mostly offset by additional expenses consolidated from 5 Arches.

Provision for Income Taxes

Our provision for income taxes is almost entirely related to activity at our taxable REIT subsidiaries, which primarily includes our mortgage banking activities and MSR investments, as well as certain other investment and hedging activities. For the three-month periods, the decrease in provision for income taxes was driven primarily by lower GAAP income earned at our TRS as well as the recognition of certain tax benefits related to the 5 Arches acquisition. For additional detail on income taxes, see the "*Taxable Income and Tax Provision*" section that follows.

Net Interest Income

The following table presents the components of net interest income for the three months ended March 31, 2019 and 2018.

Table 5 – Net Interest Income

	Three Months Ended March 31,					
	2019			2018		
(Dollars in Thousands)	**Interest Income/ (Expense)**	**Average Balance (1)**	**Yield**	**Interest Income/ (Expense)**	**Average Balance (1)**	**Yield**
Interest Income						
Residential loans, held-for-sale	$ 9,458	$ 786,678	4.8 %	$ 12,686	$ 1,201,028	4.2 %
Residential loans - HFI at Redwood (2)	24,191	2,380,655	4.1 %	23,799	2,395,596	4.0 %
Residential loans - HFI at Legacy Sequoia (2)	4,850	495,355	3.9 %	4,811	616,499	3.1 %
Residential loans - HFI at Sequoia Choice (2)	25,657	2,141,331	4.8 %	8,935	747,875	4.8 %
Residential loans - HFI at Freddie Mac SLST (2)	11,794	1,214,925	3.9 %	—	—	— %
Business purpose residential loans	2,789	152,501	7.3 %	—	—	— %
Multifamily loans - HFI at Freddie Mac K-Series	21,388	2,142,892	4.0 %	—	—	— %
Trading securities	18,713	1,160,680	6.4 %	16,166	918,197	7.0 %
Available-for-sale securities	5,737	214,298	10.7 %	9,529	363,266	10.5 %
Other interest income	6,464	579,958	4.5 %	693	239,439	1.2 %
Total interest income	131,041	11,269,273	4.7 %	76,619	6,481,900	4.7 %
Interest Expense						
Short-term debt facilities	(15,477)	1,607,598	(3.9)%	(10,424)	1,369,437	(3.0)%
Short-term debt - servicer advance financing	(3,613)	266,585	(5.4)%	—	—	— %
Short-term debt - convertible notes, net	(3,128)	199,823	(6.3)%	(3,011)	250,346	(4.8)%
ABS issued - Legacy Sequoia (2)	(4,115)	487,768	(3.4)%	(3,852)	606,551	(2.5)%
ABS issued - Sequoia Choice (2)	(22,113)	1,965,726	(4.5)%	(7,549)	671,881	(4.5)%
ABS issued - Freddie Mac SLST (2)	(8,747)	984,763	(3.6)%	—	—	— %
ABS issued - Freddie Mac K-Series	(20,320)	2,016,711	(4.0)%	—	—	— %
Long-term debt - FHLBC	(13,182)	1,999,999	(2.6)%	(8,027)	1,999,999	(1.6)%
Long-term debt - other	(8,581)	572,494	(6.0)%	(8,651)	575,400	(6.0)%
Total interest expense	(99,276)	10,101,467	(3.9)%	(41,514)	5,473,614	(3.0)%
Net Interest Income	$ 31,765			$ 35,105		

(1) Average balances for residential loans held-for-sale, residential loans held-for-investment, business purpose residential loans, multifamily loans held-for-investment, and trading securities are calculated based upon carrying values, which represent estimated fair values. Average balances for available-for-sale securities and debt are calculated based upon amortized historical cost, except for ABS issued, which is based upon fair value.

(2) Interest income from residential loans held-for-investment ("HFI") at Redwood exclude loans HFI at consolidated Sequoia or Freddie Mac SLST entities. Interest income from residential loans - HFI at Legacy Sequoia and the interest expense from ABS issued - Legacy Sequoia represent activity from our consolidated Legacy Sequoia entities. Interest income from residential loans - HFI at Sequoia Choice and the interest expense from ABS issued - Sequoia Choice represent activity from our consolidated Sequoia Choice entities. Interest income from residential loans - HFI at Freddie Mac SLST and the interest expense from ABS issued - Freddie Mac SLST represent activity from our consolidated Freddie Mac SLST entity.

The following table presents net interest income by segment for the three months ended March 31, 2019 and 2018.

Table 6 – Net Interest Income by Segment

	Three Months Ended March 31,		
(In Thousands)	**2019**	**2018**	**Change**
Net Interest Income by Segment			
Investment Portfolio	$ 37,565	$ 38,894	$ (1,329)
Mortgage Banking	4,813	6,760	(1,947)
Corporate/Other	(10,613)	(10,549)	(64)
Net Interest Income	$ 31,765	$ 35,105	$ (3,340)

Additional details regarding the activities impacting net interest income at each segment are included in the "*Results of Operations by Segment*" section that follows.

The Corporate/Other line item in the table above primarily includes interest expense related to long-term debt not directly allocated to our segments and net interest income from consolidated Legacy Sequoia entities. Details regarding consolidated Legacy Sequoia entities are included in the "*Results of Consolidated Legacy Sequoia Entities*" section that follows.

The following table presents the net interest rate spread between the yield on unsecuritized loans and securities and the debt yield of the short-term debt used in part to finance each investment type at March 31, 2019.

Table 7 – Interest Expense — Specific Borrowing Costs

March 31, 2019	**Residential Loans Held-for-Sale**	**Single-Family Rental Loans**	**Residential Bridge Loans**	**Residential Securities**
Asset yield	4.75%	5.72%	9.12%	4.71%
Short-term debt yield	3.96%	4.75%	5.21%	3.53%
Net Spread	0.79%	0.97%	3.91%	1.18%

For additional discussion on short-term debt, including information regarding margin requirements and financial covenants, see "*Risks Relating to Debt Incurred under Short-Term and Long-Term Borrowing Facilities*" in the *Liquidity and Capital Resources* section of this MD&A.

Results of Operations by Segment

We report on our business using two distinct segments: Investment Portfolio and Mortgage Banking. Our segments are based on our organizational and management structure, which aligns with how our results are monitored and performance is assessed. For additional information on our segments, refer to *Note 23* of our *Notes to Consolidated Financial Statements* in Part I, Item I of this Quarterly Report on Form 10-Q. The following table presents the segment contribution from our two segments, reconciled to our consolidated net income, for the three months ended March 31, 2019 and 2018.

Table 8 – Segment Results Summary

	Three Months Ended March 31,		
(In Thousands)	**2019**	**2018**	**Change**
Segment Contribution from:			
Investment Portfolio	$ 67,025	$ 49,070	$ 17,955
Mortgage Banking	8,310	20,696	(12,386)
Corporate/Other	(20,871)	(22,921)	2,050
Net Income	$ 54,464	$ 46,845	$ 7,619

The following sections provide a detailed discussion of the results of operations at each of our two business segments for the three months ended March 31, 2019 and 2018.

The decrease in net expense from Corporate/Other for the three-month periods was primarily due to a $2 million gain associated with the re-measurement of our initial minority investment and purchase option in 5 Arches.

<u>Investment Portfolio Segment</u>

Our Investment Portfolio segment is where we hold our housing-focused credit-sensitive investments in residential mortgage loans, mortgage-backed securities, and related assets. Our portfolio is primarily comprised of prime jumbo residential mortgage loans financed through the FHLBC, mortgage-backed securities collateralized by both residential and multifamily mortgages, and business purpose residential loans, which are mortgage loans to investors in residential properties.

The following table presents the components of segment contribution for the Investment Portfolio segment for the three months ended March 31, 2019 and 2018.

Table 9 – Investment Portfolio Segment Contribution

	Three Months Ended March 31,		
(In Thousands)	**2019**	**2018**	**Change**
Interest income	$ 115,452	$ 58,757	$ 56,695
Interest expense	(77,887)	(19,863)	(58,024)
Net interest income	37,565	38,894	(1,329)
Non-interest income			
Investment fair value changes, net	20,556	1,590	18,966
Other income, net	1,221	2,118	(897)
Realized gains, net	10,686	9,363	1,323
Total non-interest income, net	32,463	13,071	19,392
Direct operating expenses	(2,661)	(2,007)	(654)
Segment contribution before income taxes	67,367	49,958	17,409
Provision for income taxes	(342)	(888)	546
Total Segment Contribution	$ 67,025	$ 49,070	$ 17,955

The following table presents our primary portfolios of investment assets in our Investment Portfolio segment at March 31, 2019 and December 31, 2018.

Table 10 – Investment Portfolio

(In Thousands)	March 31, 2019	December 31, 2018	Change
Residential loans held-for-investment at Redwood	$ 2,404,870	$ 2,383,932	$ 20,938
Residential loans held-for-investment at Sequoia Choice (1)	2,333,248	2,079,382	253,866
Residential loans held-for-investment at Freddie Mac SLST (1)	1,228,317	1,222,669	5,648
Residential bridge loans held-for-investment	103,916	112,798	(8,882)
Multifamily loans held-for-investment at Freddie Mac K-Series (1)	2,175,899	2,144,598	31,301
Residential securities	1,030,906	1,023,415	7,491
Multifamily securities	512,246	429,079	83,167
Other investments	411,853	427,764	(15,911)
Other assets	243,024	270,356	(27,332)
Total Assets at Investment Portfolio	$ 10,444,279	$ 10,093,993	$ 350,286

(1) Our economic investment in the consolidated Sequoia Choice entities at March 31, 2019 and December 31, 2018 was $218 million and $196 million, respectively. Our economic investment in the consolidated Freddie Mac SLST entity at March 31, 2019 and December 31, 2018 was $236 million and $230 million, respectively. Our economic investment in the consolidated Freddie Mac K-Series entities at March 31, 2019 and December 31, 2018 was $129 million and $126 million, respectively. For additional details on our Choice, Freddie Mac SLST and multifamily loans, see the subsections titled "*Residential Loans Held-for-Investment at Sequoia Choice Portfolio,*" "*Residential Loans Held-for-Investment at Freddie Mac SLST Portfolio,*" and "*Multifamily Loans Held-for-Investment at Freddie Mac K-Series Portfolio*" that follow.

Overview

During the first quarter of 2019, we deployed $163 million of capital towards new residential and multifamily investments, including $40 million to purchase the remaining equity in 5 Arches. We also continued our focus on optimizing our investment portfolio by selling assets that had appreciated in value with lower current yields, and redeployed capital into higher-yielding opportunities. Net interest income decreased year-over-year mostly due to increased interest expense from rising benchmark interest rates. Inclusive of the interest on our hedges, net interest income increased during the three-month periods. Meanwhile, spread tightening benefited valuations in our securities portfolio in the first quarter of 2019. Credit fundamentals in our investment portfolio remain strong, reflecting continued strength in the general economy and in housing.

Net Interest Income

Net interest income from our Investment Portfolio primarily includes interest income from our securities and residential loans held-for-investment, as well as the associated interest expense from short-term debt, FHLBC borrowings, and ABS issued. The following table presents the components of net interest income for our Investment Portfolio segment by investment type for the three months ended March 31, 2019 and 2018.

Table 11 - Net Interest Income ("NII") from Investment Portfolio

	Three Months Ended March 31,		
(In Thousands)	**2019**	**2018**	**Change**
Net interest income from:			
Residential securities	$ 13,660	$ 19,520	$ (5,860)
Multifamily securities	1,703	1,888	(185)
HFI residential loans at Redwood	11,008	15,772	(4,764)
HFI residential loans at Sequoia Choice	3,544	1,386	2,158
HFI residential bridge loans	1,374	—	1,374
HFI residential loans at Freddie Mac SLST	3,047	—	3,047
HFI multifamily loans at Freddie Mac K-Series	1,068	—	1,068
Other interest income	2,161	328	1,833
NII from Investment Portfolio	$ 37,565	$ 38,894	$ (1,329)
Supplemental information:			
Hedge interest income (expense), net	$ 2,718	$ (2,884)	$ 5,602

The decrease in net interest income from our Investment Portfolio segment for the three-month periods was primarily due to higher interest expense on our variable-rate borrowings during the first quarter of 2019 resulting from rising benchmark interest rates over the past year. This decrease was partially offset by increased interest income from additional portfolio investments that we made during the past year that in part utilized capital we raised in July of 2018 and January of 2019.

The table above also presents supplemental information about interest income (expense) from hedges that we use to manage interest rate risk in our investment portfolio, which are a component of Investment fair value changes, net on our consolidated statements of income. On a combined basis, net interest income in our investment portfolio segment plus interest income (expense) from hedges used to manage interest rate risk in our investment portfolio increased by $4 million in the three-month periods.

Investment fair value changes, net

Market valuation changes included in Investment fair value changes, net, result from changes in the fair value of investments and their associated hedges, generally due to changes in market interest rates, changes in credit spreads, and reductions in the basis of investments due to changes in principal balances. See *Note 20* of our *Notes to Consolidated Financial Statements* in Part I, Item I of this Quarterly Report on Form 10-Q for additional detail regarding the components of Investment fair value changes, net presented on our consolidated statements of income.

The following table presents the components of investment fair value changes for our Investment Portfolio segment, which is comprised of market valuation gains and losses by investment type, inclusive of fair value changes of associated risk management derivatives, for the three months ended March 31, 2019 and 2018.

Table 12 - Investment Portfolio Fair Value Changes, Net by Investment Type

	Three Months Ended March 31,		
(In Thousands)	**2019**	**2018**	**Change**
Market valuation changes:			
Residential loans held-for-investment at Redwood	$ (1,816)	$ (451)	$ (1,365)
Residential bridge loans held-for-investment	(303)	—	(303)
Net investments in Sequoia Choice entities (1)	3,265	(86)	3,351
Net investment in Freddie Mac SLST entity (1)	6,365	—	6,365
Net investments in Freddie Mac K-Series entities (1)	3,119	—	3,119
Residential trading securities	508	1,202	(694)
Multifamily trading securities	6,206	3,948	2,258
Servicer advance investments	1,008	—	1,008
Excess MSRs	(437)	—	(437)
Hedge interest expense, net	2,718	(2,884)	5,602
Other valuation changes	(77)	(139)	62
Investment Fair Value Changes, Net	$ 20,556	$ 1,590	$ 18,966

(1) Includes changes in fair value of the loans held-for-investment and the ABS issued at the entities, which netted together represent the change in value of our investments (senior and subordinate securities) at the consolidated VIEs.

During the three months ended March 31, 2019, the positive investment fair value changes were primarily driven by tightening credit spreads during the first quarter of 2019 in several parts of our portfolio, helping us to recover a significant amount of the fair value decline these investments experienced in the fourth quarter of 2018 from spread widening. Credit spreads on our residential loan portfolio remained largely unchanged from the fourth quarter.

Other Income, net

The following table presents the components of Other income, net for our investment portfolio for the three months ended March 31, 2019 and 2018.

Table 13 – Other Income, net

	Three Months Ended March 31,	
(In Thousands)	**2019**	**2018**
MSR income, net	$ 257	$ 957
Risk share income	646	778
FHLBC capital stock dividend	547	383
Other	(229)	—
Other Income, Net from Investment Portfolio	$ 1,221	$ 2,118

Realized Gains, net

During the three months ended March 31, 2019, we realized gains of $11 million, primarily from the sale of $42 million of AFS securities and the call of a seasoned Sequoia securitization. During the three months ended March 31, 2018, we realized gains of $9 million, primarily from the sale of $51 million of AFS securities.

Direct Operating Expenses and Provision for Income Taxes

The increase in operating expenses at our Investment Portfolio segment for the three-month periods was primarily related to additional personnel added in 2018 to support our new business initiatives.

The provision for income taxes at our Investment Portfolio segment primarily results from GAAP income earned at our TRS from MSRs and certain securities. For the three-month periods, the decrease in the tax provision primarily resulted from decreased GAAP income at our TRS in this segment.

Residential Loans Held-for-Investment at Redwood Portfolio

The following table provides the activity of residential loans held-for-investment at Redwood during the three months ended March 31, 2019.

Table 14 – Residential Loans Held-for-Investment at Redwood - Activity

(In Thousands)	Three Months Ended March 31, 2019
Fair value at beginning of period	$ 2,383,932
Acquisitions	39,269
Transfers between portfolios [(1)]	17,144
Principal repayments	(63,583)
Changes in fair value, net	28,108
Fair Value at End of Period	$ 2,404,870

(1) Represents the net transfers of loans into our Investment Portfolio segment from our Mortgage Banking segment and their reclassification from held-for-sale to held-for-investment.

The increase in the balance of loans held-for-investment during the three months ended March 31, 2019 was primarily due to an increase in fair value of the loans during this period, resulting from a decrease in benchmark interest rates. As our loans held-for-investment are generally fixed-rate and sensitive to changes in interest rates, we utilize various interest rate derivatives to hedge our interest rate risk for these investments. As a result of declining interest rates during the three months ended March 31, 2019, interest rate derivatives associated with these investments decreased in value by $27 million.

At March 31, 2019, $2.41 billion of loans were held by our FHLB-member subsidiary and financed with $2.00 billion of borrowings from the FHLBC. In connection with these borrowings, our FHLB-member subsidiary is required to hold $43 million of FHLB stock.

At March 31, 2019, the weighted average maturity of these FHLB borrowings was approximately six years and they had a weighted average cost of 2.65% per annum. While the interest costs on these borrowings is variable and resets every 13 weeks, we utilize various interest rate derivative instruments to hedge our interest rate risk in this portfolio.

Under a final rule published by the Federal Housing Finance Agency in January 2016, our FHLB-member subsidiary will remain an FHLB member through the five-year transition period for captive insurance companies. Our FHLB-member subsidiary's existing $2.00 billion of FHLB debt, which matures beyond this transition period, is permitted to remain outstanding until its stated maturity. As residential loans pledged as collateral for this debt pay down, we are permitted to pledge additional loans or other eligible assets to collateralize this debt; however, we do not expect to be able to increase our subsidiary's FHLB debt above the existing $2.00 billion.

The following table presents the unpaid principal balances for residential real estate loans held-for-investment at fair value by product type at March 31, 2019.

Table 15 – Characteristics of Residential Real Estate Loans Held-for-Investment at Redwood

March 31, 2019		
(Dollars in Thousands)	**Principal Balance**	**Weighted Average Coupon**
Fixed - 30 year	$ 2,033,428	4.16%
Fixed - 15, 20, & 25 year	59,352	3.65%
Hybrid	284,561	4.21%
Total Outstanding Principal	$ 2,377,341	

The outstanding loans held-for-investment at Redwood at March 31, 2019 were prime-quality, first lien loans, of which 96% were originated between 2013 and 2019 and 4% were originated in 2012 and prior years. The weighted average FICO score of borrowers backing these loans was 768 (at origination) and the weighted average loan-to-value ("LTV") ratio was 66% (at origination). At March 31, 2019, two of these loans with an aggregate fair value of $1 million were greater than 90 days delinquent and one of these loans with a fair value of $0.4 million was in foreclosure.

Residential Bridge Loans Held-for-Investment at Redwood Portfolio

Our $104 million of residential bridge loans held-for-investment at March 31, 2019 were primarily acquired in 2018 and comprised of first-lien, fixed-rate, interest-only loans with a weighted average coupon of 9.13% and original maturities of six to 24 months. At origination, the weighted average FICO score of borrowers backing these loans was 677, the weighted average LTV ratio of these loans was 75%, and the estimated rehabilitated LTV ratio was 60%. At March 31, 2019, of the 158 loans in this portfolio, seven loans with an aggregate fair value of $9 million were greater than 90 days delinquent and four of these loans with an aggregate fair value of $8 million were in foreclosure.

Real Estate Securities Portfolio

The following table sets forth our real estate securities activity by collateral type in our Investment Portfolio segment for the three months ended March 31, 2019.

Table 16 – Real Estate Securities Activity by Collateral Type

Three Months Ended March 31, 2019	**Residential**			**Multifamily**	
(In Thousands)	**Senior**	**Mezzanine**	**Subordinate**	**Mezzanine**	**Total**
Beginning fair value	$ 246,285	$ 218,147	$ 558,983	$ 429,079	$ 1,452,494
Acquisitions					
Sequoia securities	1,716	—	885	—	2,601
Third-party securities	30,691	31,794	13,000	79,386	154,871
Sales					
Sequoia securities	—	—	(4,727)	—	(4,727)
Third-party securities	(38,780)	—	(22,579)	(7,932)	(69,291)
Gains on sales and calls, net	5,749	268	4,669	—	10,686
Effect of principal payments (1)	(4,746)	(6,978)	(9,103)	(2,555)	(23,382)
Change in fair value, net	(10,277)	6,511	9,398	14,268	19,900
Ending Fair Value (2)	$ 230,638	$ 249,742	$ 550,526	$ 512,246	$ 1,543,152

(1) The effect of principal payments reflects the change in fair value due to principal payments, which is calculated as the cash principal received on a given security during the period multiplied by the prior quarter ending price or acquisition price for that security.

(2) At March 31, 2019, excludes $216 million of securities retained from our consolidated Sequoia Choice securitizations as well as $235 million and $129 million of securities we owned that were issued by consolidated Freddie Mac SLST and Freddie Mac K-Series securitizations, respectively. For additional details on our Choice, Freddie Mac SLST, and multifamily loans, see the subsections titled "*Residential Loans Held-for-Investment at Sequoia Choice Portfolio,*" *"Residential Loans Held-for-Investment at Freddie Mac SLST Portfolio,"* and "*Multifamily Loans Held-for-Investment at Freddie Mac K-Series Portfolio"* that follow.

During the three months ended March 31, 2019, we sold $74 million of mostly lower-yielding securities as part of our ongoing portfolio optimization activities.

At March 31, 2019, our securities consisted of fixed-rate assets (78%), adjustable-rate assets (17%), hybrid assets that reset within the next year (4%), and hybrid assets that reset between 12 and 36 months (1%). For the portions of our securities portfolio that are sensitive to changes in interest rates, we seek to minimize this interest rate risk by using various derivative instruments.

We directly finance our holdings of real estate securities with a combination of capital and collateralized debt in the form of repurchase (or "repo") financing. The following table presents the fair value of our residential securities that were financed with repurchase debt at March 31, 2019.

Table 17 – Real Estate Securities Financed with Repurchase Debt

March 31, 2019 (Dollars in Thousands, except Weighted Average Price)	**Real Estate Securities** (1)	**Repurchase Debt**	**Allocated Capital**	**Weighted Average Price**(2)	**Financing Haircut**(3)
Residential Securities					
Senior	$ 149,528	$ (133,826)	$ 15,702	$ 100	11%
Mezzanine (4)	580,814	(472,178)	108,636	95	19%
Subordinate	70,339	(57,476)	12,863	97	18%
Total Residential Securities	800,681	(663,480)	137,201	96	17%
Multifamily Securities (5)	525,717	(417,599)	108,118	97	21%
Total	$ 1,326,398	$ (1,081,079)	$ 245,319		

(1) Amounts represent carrying value of securities, which are held at GAAP fair value.

(2) GAAP fair value per $100 of principal.

(3) Allocated capital divided by GAAP fair value.

(4) Includes $146 million and $196 million of securities retained from our consolidated Sequoia Choice and Freddie Mac SLST securitizations, respectively.

(5) Includes $18 million of securities we owned that were issued by consolidated Freddie Mac K-Series securitizations.

At March 31, 2019, we had short-term debt incurred through repurchase facilities of $1.08 billion, which was secured by $1.33 billion of real estate securities. The remaining $797 million of our securities, including certain securities we own that were issued by consolidated Sequoia Choice and Freddie Mac K-Series securitization entities, were financed with capital. Our repo borrowings were made under facilities with nine different counterparties, and the weighted average cost of funds for these facilities during the first quarter of 2019 was approximately 3.62% per annum.

At March 31, 2019, the credit performance on the securities we financed through repurchase facilities generally continued to perform in line with, or better than our expectations. In addition to the allocated capital listed in the table above that directly supports our repurchase facilities (the "financing haircut"), we continue to hold a designated amount of supplemental risk capital available for potential margin calls or future obligations relating to these facilities.

The majority of the $150 million of senior securities noted in the table above are supported by seasoned residential loans originated prior to 2008. The $581 million of mezzanine securities financed through repurchase facilities at March 31, 2019 primarily carry investment grade credit ratings and are supported by residential loans originated between 2012 and 2018. The majority of the loans underlying these securities have experienced minimal delinquencies to date. The $526 million of multifamily securities financed through repurchase facilities at March 31, 2019 primarily carry investment grade credit ratings with 7%-8% of structural credit enhancement.

The following table presents our real estate securities at March 31, 2019 and December 31, 2018, categorized by portfolio vintage (the years the securities were issued), and by priority of cash flows (senior, mezzanine, and subordinate). We have additionally separated securities issued through our Sequoia platform or by third parties, including the Agencies.

Table 18 – Real Estate Securities by Vintage and Type

March 31, 2019 (In Thousands)	**Sequoia 2012-2019**	**Third Party 2013-2019**	**Agency CRT 2013-2019**	**Third Party <=2008**	**Total Residential Securities**	**Multifamily 2016-2019**	**Total Real Estate Securities**
Senior (1)	$ 57,536	$ 125,342	$ —	$ 47,760	$ 230,638	$ —	$ 230,638
Mezzanine (2)	97,491	152,251	—	—	249,742	512,246	761,988
Subordinate (1)	123,875	177,387	234,101	15,163	550,526	—	550,526
Total Securities (3)	$ 278,902	$ 454,980	$ 234,101	$ 62,923	$ 1,030,906	$ 512,246	$ 1,543,152

December 31, 2018 (In Thousands)	Sequoia 2012-2018	Third Party 2013-2018	Agency CRT 2013-2018	Third Party <=2008	Total Residential Securities	Multifamily 2015-2018	Total Real Estate Securities
Senior [1]	$ 61,179	$ 96,069	$ —	$ 89,037	$ 246,285	$ —	$ 246,285
Mezzanine [2]	99,977	118,170	—	—	218,147	429,079	647,226
Subordinate [1]	130,271	174,879	237,841	15,992	558,983	—	558,983
Total Securities [3]	$ 291,427	$ 389,118	$ 237,841	$ 105,029	$ 1,023,415	$ 429,079	$ 1,452,494

(1) At March 31, 2019 and December 31, 2018, senior Sequoia and third-party securities included $76 million and $82 million of IO securities, respectively. At both March 31, 2019 and December 31, 2018, subordinate third-party securities included $12 million of IO securities. Our interest-only securities included $41 million and $43 million of A-IO-S securities at March 31, 2019 and December 31, 2018, respectively, that we retained from certain of our Sequoia securitizations. These securities represent certificated servicing strips and therefore may be negatively impacted by the operating and funding costs related to servicing the associated securitized mortgage loans.

(2) Mezzanine includes securities initially rated AA through BBB- and issued in 2012 or later.

(3) At March 31, 2019, excluded $216 million, $235 million, and $129 million of securities we owned that were issued by consolidated Sequoia Choice, Freddie Mac SLST, and Freddie Mac K-Series securitizations, respectively. At December 31, 2018, excluded $194 million, $229 million, and $126 million of securities we owned that were issued by consolidated Sequoia Choice, Freddie Mac SLST, and Freddie Mac K-Series securitizations, respectively. For GAAP purposes we consolidated $5.74 billion of residential loans and $5.16 billion of non-recourse ABS debt associated with these retained securities.

The following tables present the components of the interest income we earned on AFS securities for the three months ended March 31, 2019 and 2018.

Table 19 – Interest Income — AFS Securities

Three Months Ended March 31, 2019					Yield as a Result of		
(Dollars in Thousands)	Interest Income	Discount (Premium) Amortization	Total Interest Income	Average Amortized Cost	Interest Income	Discount (Premium) Amortization	Total Interest Income
Residential							
Senior	$ 822	$ 990	$ 1,812	$ 46,158	7.12%	8.58%	15.70%
Mezzanine	304	150	454	30,992	3.92%	1.94%	5.86%
Subordinate	2,681	790	3,471	137,148	7.82%	2.30%	10.12%
Total AFS Securities	$ 3,807	$ 1,930	$ 5,737	$ 214,298	7.11%	3.60%	10.71%

Three Months Ended March 31, 2018					Yield as a Result of		
(Dollars in Thousands)	Interest Income	Discount (Premium) Amortization	Total Interest Income	Average Amortized Cost	Interest Income	Discount (Premium) Amortization	Total Interest Income
Residential							
Senior	$ 1,826	$ 2,486	$ 4,312	$ 131,064	5.57%	7.59%	13.16%
Mezzanine	766	316	1,082	73,112	4.19%	1.73%	5.92%
Subordinate	2,877	1,258	4,135	159,090	7.23%	3.16%	10.39%
Total AFS Securities	$ 5,469	$ 4,060	$ 9,529	$ 363,266	6.02%	4.47%	10.49%

Residential Loans Held-for-Investment at Sequoia Choice Portfolio

As of March 31, 2019, we had issued seven securitizations primarily comprised of expanded-prime Choice loans that we consolidate for financial reporting purposes in accordance with GAAP. These entities are independent of Redwood and the assets and liabilities of these entities are not, respectively, owned by us or legal obligations of ours. We record the assets and liabilities of the consolidated Sequoia Choice entities at fair value, based on the estimated fair value of the debt securities (ABS) issued from the securitizations, in accordance with GAAP provisions for collateralized financing entities. At March 31, 2019, our economic investment in the consolidated Sequoia Choice entities had an estimated fair value of $218 million, and was comprised of retained senior and subordinate securities.

The following tables present the statements of income for the three months ended March 31, 2019 and 2018 and the balance sheets of the consolidated Sequoia Choice entities at March 31, 2019 and December 31, 2018. All amounts in the statements of income and balance sheets presented below are included in our consolidated financial statements and are included in our Investment Portfolio segment.

Table 20 – Consolidated Sequoia Choice Entities Statements of Income

	Three Months Ended March 31,		
(In Thousands)	**2019**	**2018**	**Change**
Interest income	$ 25,662	$ 8,935	$ 16,727
Interest expense	(22,113)	(7,549)	(14,564)
Net interest income	3,549	1,386	2,163
Investment fair value changes, net	3,265	(86)	3,351
Net Income from Consolidated Sequoia Choice Entities	$ 6,814	$ 1,300	$ 5,514

Table 21 – Consolidated Sequoia Choice Entities Balance Sheets

(In Thousands)	**March 31, 2019**	**December 31, 2018**
Residential loans, held-for-investment, at fair value	$ 2,333,248	$ 2,079,382
Other assets	9,630	10,010
Total Assets	$ 2,342,878	$ 2,089,392
Other liabilities	$ 7,868	$ 8,202
Asset-backed securities issued, at fair value	2,117,356	1,885,010
Total liabilities	2,125,224	1,893,212
Equity (fair value of Redwood's retained investments in entities)	217,654	196,180
Total Liabilities and Equity	$ 2,342,878	$ 2,089,392

The following table presents residential loan activity at the consolidated Sequoia Choice entities for the three months ended March 31, 2019.

Table 22 – Residential Loans Held-for-Investment at Sequoia Choice - Activity

(In Thousands)	**Three Months Ended March 31, 2019**
Balance at beginning of period	$ 2,079,382
New securitization issuance	349,583
Principal repayments	(105,682)
Changes in fair value, net	9,965
Balance at End of Period	$ 2,333,248

During the three months ended March 31, 2019, we had transfers of $350 million of consolidated Sequoia Choice loans from our Mortgage Banking segment to our Investment Portfolio segment associated with one securitization issuance. The outstanding loans held-for-investment at our Sequoia Choice entities at March 31, 2019 were primarily comprised of prime-quality, first-lien, 30-year, fixed-rate loans originated in 2017 or 2018. The gross weighted average coupon of these loans was 4.77%, the weighted average FICO score of borrowers backing these loans was 745 (at origination) and the weighted average original LTV ratio was 75% (at origination). At March 31, 2019, two of these loans with an aggregate unpaid principal balance of $1 million were greater than 90 days delinquent and none of these loans were in foreclosure. At December 31, 2018, three of these loans with an aggregate unpaid principal balance of $2 million were greater than 90 days delinquent and none of these loans were in foreclosure.

Residential Loans Held-for-Investment at Freddie Mac SLST Portfolio

During the fourth quarter of 2018, we invested in certain subordinate securities backed by a pool of seasoned re-performing residential mortgage loans that were issued by a Freddie Mac SLST securitization entity and we were required to consolidate this entity for financial reporting purposes in accordance with GAAP. This entity is independent of Redwood and the assets and liabilities of this entity are not, respectively, owned by us or legal obligations of ours. We record the assets and liabilities of the consolidated Freddie Mac SLST entity at fair value, based on the estimated fair value of the debt securities (ABS) issued from the securitization, in accordance with GAAP provisions for collateralized financing entities. At March 31, 2019, our economic investment in the consolidated Freddie Mac SLST entity had an estimated fair value of $236 million, and was comprised of subordinate securities.

The following tables present the statements of income for the three months ended March 31, 2019 and 2018 and the balance sheets of the consolidated Freddie Mac SLST entity at March 31, 2019 and December 31, 2018. All amounts in the statements of income and balance sheets presented below are included in our consolidated financial statements and are included in our Investment Portfolio segment.

Table 23 – Consolidated Freddie Mac SLST Entity Statements of Income

	Three Months Ended March 31,		
(In Thousands)	**2019**	**2018**	**Change**
Interest income	$ 11,794	$ —	$ 11,794
Interest expense	(8,747)	—	(8,747)
Net interest income	3,047	—	3,047
Investment fair value changes, net	6,365	—	6,365
Net Income from Consolidated Freddie Mac SLST Entity	$ 9,412	$ —	$ 9,412

Table 24 – Consolidated Freddie Mac SLST Entity Balance Sheets

(In Thousands)	**March 31, 2019**	**December 31, 2018**
Residential loans, held-for-investment, at fair value	$ 1,228,317	$ 1,222,669
Other assets	3,861	3,926
Total Assets	$ 1,232,178	$ 1,226,595
Other liabilities	$ 2,846	$ 2,907
Asset-backed securities issued, at fair value	993,032	993,748
Total liabilities	995,878	996,655
Equity (fair value of Redwood's investments in entity)	236,300	229,940
Total Liabilities and Equity	$ 1,232,178	$ 1,226,595

The following table presents residential loan activity at the consolidated Freddie Mac SLST entity for the three months ended March 31, 2019.

Table 25 – Residential Loans Held-for-Investment at Freddie Mac SLST - Activity

	Three Months Ended
(In Thousands)	**March 31, 2019**
Balance at beginning of period	$ 1,222,669
Principal repayments	(17,879)
Changes in fair value, net	23,527
Balance at End of Period	$ 1,228,317

The outstanding re-performing and non-performing residential loans held-for-investment at the Freddie Mac SLST entity at March 31, 2019 were first-lien, fixed- or step-rate loans that have been modified. At securitization, in December 2018, the weighted average FICO score of borrowers backing these loans was 597 and the weighted average LTV ratio of these loans was 69%. At March 31, 2019, 520 of these loans with an aggregate unpaid principal balance of $84 million were greater than 90 days delinquent and none of these loans were in foreclosure. At December 31, 2018, 306 of these loans with an aggregate unpaid principal balance of $51 million were greater than 90 days delinquent and none of these loans were in foreclosure. Due to the credit profile of re-performing and non-performing loans, our investment in the subordinate securities issued by the Freddie Mac SLST entity was made based on an expectation of defaults and credit losses that will occur on the underlying pool of residential mortgage loans, which was reflected in our purchase price yield. At March 31, 2019, delinquencies and credit losses in the portfolio were in line with our expectations.

Multifamily Loans Held-for-Investment at Freddie Mac K-Series Portfolio

During the third and fourth quarters of 2018, we invested in certain subordinate securities issued by Freddie Mac K-Series securitization entities and were required to consolidate these entities for financial reporting purposes in accordance with GAAP. Each of these entities is independent of Redwood and of each other and the assets and liabilities of these entities are not, respectively, owned by us or legal obligations of ours. We record the assets and liabilities of the consolidated Freddie Mac K-Series entities at fair value, based on the estimated fair value of the debt securities (ABS) issued from the securitizations, in accordance with GAAP provisions for collateralized financing entities. At March 31, 2019, our economic investment in the consolidated Freddie Mac K-Series entities had an estimated fair value of $129 million, and was comprised of subordinate securities.

The following tables present the statements of income for the three months ended March 31, 2019 and 2018 and the balance sheets of the consolidated Freddie Mac K-Series entities at March 31, 2019 and December 31, 2018. All amounts in the statements of income and balance sheets presented below are included in our consolidated financial statements and are included in our Investment Portfolio segment.

Table 26 – Consolidated Freddie Mac K-Series Entities Statements of Income

	Three Months Ended March 31,		
(In Thousands)	**2019**	**2018**	**Change**
Interest income	$ 21,388	$ —	$ 21,388
Interest expense	(20,320)	—	(20,320)
Net interest income	1,068	—	1,068
Investment fair value changes, net	3,119	—	3,119
Net Income from Consolidated Freddie Mac K-Series Entities	$ 4,187	$ —	$ 4,187

Table 27 – Consolidated Freddie Mac K-Series Entities Balance Sheets

(In Thousands)	**March 31, 2019**	**December 31, 2018**
Multifamily loans, held-for-investment, at fair value	$ 2,175,899	$ 2,144,598
Other assets	6,587	6,595
Total Assets	$ 2,182,486	$ 2,151,193
Other liabilities	$ 6,230	$ 6,239
Asset-backed securities issued, at fair value	2,047,257	2,019,075
Total liabilities	2,053,487	2,025,314
Equity (fair value of Redwood's retained investments in entities)	128,999	125,879
Total Liabilities and Equity	$ 2,182,486	$ 2,151,193

The following table presents multifamily loan activity at the consolidated Freddie Mac K-Series entities for the three months ended March 31, 2019.

Table 28 – Multifamily Loans Held-for-Investment at Freddie Mac K-Series - Activity

(In Thousands)		Three Months Ended March 31, 2019
Balance at beginning of period	$	2,144,598
Principal repayments		(3,071)
Changes in fair value, net		34,372
Balance at End of Period	$	2,175,899

The outstanding multifamily loans held-for-investment at the Freddie Mac K-Series entities at March 31, 2019 were first lien, fixed-rate loans that were originated in 2015 and 2016 and had original loan terms of seven to ten years and an original weighted average LTV ratio of 69%. At March 31, 2019, the weighted average coupon of these loans was 4.16% and the weighted average loan term was seven years. At both March 31, 2019 and December 31, 2018, none of these loans were greater than 90 days delinquent or in foreclosure.

Mortgage Servicing Rights Portfolio

Our MSRs are held and managed at our taxable REIT subsidiary and typically are acquired together with loans from originators and then separately recognized under GAAP when the MSR is retained and the associated loan is sold to a third party or transferred to a Sequoia residential securitization sponsored by us that meets the GAAP criteria for sale. In addition, in the past we have also purchased MSRs on a flow basis from third parties that sold the associated loans directly to the Agencies. Although we own the rights to service loans, we contract with sub-servicers to perform these activities. Our receipt of MSR income is not subject to any covenants other than customary performance obligations associated with servicing residential loans. If a sub-servicer we contract with was to fail to perform these obligations, our servicing rights could be terminated and we would evaluate our MSR asset for impairment at that time.

The following table provides the activity for MSRs for the three months ended March 31, 2019.

Table 29 – MSR Activity

(In Thousands)		Three Months Ended March 31, 2019
Balance at beginning of period	$	60,281
Additions		
MSRs retained from third-party loan sales		104
Market valuation adjustments		(5,101)
Balance at End of Period	$	55,284

The following table presents characteristics of our MSR investments and their associated loans at March 31, 2019.

Table 30 – Characteristics of MSR Investments Portfolio

(Dollars in Thousands)	**March 31, 2019**
Unpaid principal balance	$ 4,856,491
Fair value of MSRs	$ 55,284
MSR values as percent of unpaid principal balance	1.14%
Gross cash yield (1)	0.26%
Number of loans	7,476
Average loan size	$ 650
Average coupon	3.97%
Average loan age (months)	55
Average original loan-to-value	67%
Average original FICO score	771
60+ day delinquencies	0.10%

(1) Gross cash yield is calculated by dividing the annualized quarterly gross servicing fees we received for the three months ended March 31, 2019, by the weighted average notional balance of loans associated with MSRs we owned during that period.

At March 31, 2019, nearly all of our MSRs were comprised of base MSRs and within this portfolio we did not own any portion of a servicing right related to any loan where we did not own the entire servicing right. At both March 31, 2019 and December 31, 2018, we had $1 million of servicer advances outstanding related to our MSRs, which are presented in Other assets on our consolidated balance sheets.

Servicing Investments

In December 2018, we invested in servicer advances and excess MSRs associated with legacy RMBS (See *Note 10* of our *Notes to Consolidated Financial Statements* in Part I, Item I of this Quarterly Report on Form 10-Q for additional detail). At March 31, 2019, our servicer advance investments and excess MSRs associated with this investment had a carrying value of $304 million and $15 million, respectively. The following table presents characteristics of the residential mortgage loans underlying these investments at March 31, 2019.

Table 31 – Characteristics of Servicing Investments

(Dollars in Thousands)	**March 31, 2019**
Unpaid principal balance	$ 8,793,928
Number of loans	43,516
Average loan size	$ 202
Average coupon	5.06%
Average loan age (months)	163
Average original loan-to-value	76%
Average original FICO score	699
60+ day delinquencies (1)	10.69%

(1) Includes unpaid principal balance of $555 million, or 6% of total portfolio, of loans in foreclosure or transferred to REO.

Mortgage Banking Segment

Our Mortgage Banking segment includes activity from both our residential and business purpose mortgage banking operations. Our business purpose mortgage banking operations includes activity from our wholly-owned subsidiary 5 Arches and our single-family rental loans that we are aggregating for subsequent sale or securitization. The following table presents the components of segment contribution for the Mortgage Banking segment for the three months ended March 31, 2019 and 2018.

Table 32 – Mortgage Banking Segment Contribution

	Three Months Ended March 31,		
(In Thousands)	**2019**	**2018**	**Change**
Interest income	$ 10,377	$ 12,897	$ (2,520)
Interest expense	(5,564)	(6,137)	573
Net interest income	4,813	6,760	(1,947)
Mortgage banking activities, net	12,309	26,576	(14,267)
Other income (expense), net	(167)	—	(167)
Direct operating expenses	(8,104)	(8,632)	528
Segment contribution before income taxes	8,851	24,704	(15,853)
Provision for income taxes	(541)	(4,008)	3,467
Segment Contribution	$ 8,310	$ 20,696	$ (12,386)

The following tables provide the activity of unsecuritized residential loans during the three months ended March 31, 2019 and 2018.

Table 33 – Residential Loans Held-for-Sale — Activity

	Three Months Ended March 31,					
	2019			2018		
(In Thousands)	**Select**	**Choice**	**Total**	**Select**	**Choice**	**Total**
Balance at beginning of period	$ 716,193	$ 332,608	$ 1,048,801	$ 1,101,356	$ 326,589	$ 1,427,945
Acquisitions	549,548	433,381	982,929	1,267,930	547,364	1,815,294
Sales	(797,230)	(35,848)	(833,078)	(1,590,741)	(3,790)	(1,594,531)
Transfers between portfolios (1)	22,083	(388,755)	(366,672)	—	(507,616)	(507,616)
Principal repayments	(8,133)	(9,292)	(17,425)	(13,234)	(3,783)	(17,017)
Changes in fair value, net	1,728	2,938	4,666	794	5,316	6,110
Balance at End of Period	$ 484,189	$ 335,032	$ 819,221	$ 766,105	$ 364,080	$ 1,130,185

(1) Represents the net transfers of loans out of our Mortgage Banking segment into our Investment Portfolio segment and their reclassification from held-for-sale to held-for-investment. Includes $350 million of Choice loans securitized during the three months ended March 31, 2019, respectively, which were not treated as sales for GAAP purposes and continue to be reported on our consolidated balance sheets within our Investment Portfolio segment.

Overview

Segment contribution from our mortgage banking business decreased during the three-month periods, driven by lower loan purchase volumes and lower margins as compared to the prior year. Our jumbo residential loan purchase volume decreased 37% from the prior quarter, consistent with industry-wide declines. During the first quarter of 2019, we purchased $983 million of predominately prime residential jumbo loans, securitized $353 million of jumbo Select loans that were accounted for as sales, and sold $480 million of jumbo loans to third parties. Additionally, we transferred $350 million of jumbo Choice loans that did not qualify for sales accounting treatment under GAAP to Sequoia securitization entities and we had net transfers of $17 million of loans to our Investment Portfolio segment that were financed with borrowings from the FHLBC. Our pipeline of residential loans identified for purchase at March 31, 2019 included $768 million of jumbo loans. During the first quarter of 2019, we reduced the capital allocated to our residential mortgage banking business, leveraging operational changes that allow us to manage this part of the mortgage banking business with less capital.

We utilize a combination of capital and our residential loan warehouse facilities to manage our inventory of residential loans held-for-sale. At March 31, 2019, we had $526 million of warehouse debt outstanding to fund our residential loans held-for-sale. The weighted average cost of the borrowings outstanding under these facilities during the first quarter of 2019 was 4.03% per annum. Jumbo loan warehouse capacity at March 31, 2019 totaled $1.43 billion across four separate counterparties, and our business purpose residential loan warehouse capacity totaled $400 million across two separate counterparties, which should continue to provide sufficient liquidity to fund our mortgage banking operations in the near-term.

At March 31, 2019, residential mortgage banking had 478 loan sellers, down from 501 at the end of 2018. This included 188 jumbo sellers and 290 sellers from various FHLB districts participating in the FHLB's MPF Direct program.

Net Interest Income

Net interest income from mortgage banking is primarily comprised of interest income earned on loans from the time we purchase the loans to when we sell or securitize them, offset by interest expense incurred on short-term warehouse debt used in part to finance the loans while we hold them on our balance sheet.

The decrease in net interest income during the three-month periods was primarily due to a decrease in interest income driven by a lower average balance of residential loans.

The amount of net interest income we earn on loans held-for-sale is dependent on many variables, including the amount of loans and the time they are outstanding on our consolidated balance sheet and their interest rates, as well as the amount of leverage we employ through the use of short-term debt to finance the loans and the interest rates on that debt. These factors will impact net interest income in future periods.

Mortgage Banking Activities, Net

Mortgage banking activities, net, includes the changes in market value of both the loans we hold for sale and commitments for loans we intend to purchase (collectively, our loan pipeline), as well as the effect of derivative instruments we utilize to manage risks associated with our loan pipeline. Our loan sale profit margins are measured over the period from when we commit to purchase a loan and subsequently sell or securitize the loan or transfer it into our investment portfolio. Accordingly, these profit margins may encompass positive or negative market valuation adjustments on loans, hedging gains or losses associated with our loan pipeline, and any other related transaction expenses, and may be realized over the course of one or more quarters for financial reporting purposes. In addition, beginning in the first quarter of 2019, mortgage banking activities includes fees from the origination of loans from our business purpose mortgage banking operations.

The following table presents the components of mortgage banking activities, net. Amounts presented include both the changes in market values for loans that were sold and associated derivative positions that were settled during the periods presented, as well as changes in market values of loans, derivatives and hedges outstanding at the end of each period.

Table 34 – Components of Mortgage Banking Activities, Net

	Three Months Ended March 31,		
(In Thousands)	**2019**	**2018**	**Change**
Residential Mortgage Banking Activities, Net			
Changes in fair value of:			
Residential loans, at fair value (1)	$ 14,844	$ (2,194)	$ 17,038
Risk management derivatives (2)	(4,138)	28,432	(32,570)
Other income, net (3)	121	338	(217)
Total residential mortgage banking activities, net	10,827	26,576	(15,749)
Business Purpose Mortgage Banking Activities, Net			
Changes in fair value of:			
Single-family rental loans, at fair value (1)	1,744	—	1,744
Risk management derivatives (2)	(846)	—	(846)
Residential bridge loans, at fair value	86	—	86
Other income, net (3)	498	—	498
Total business purpose mortgage banking activities, net	1,482	—	1,482
Mortgage Banking Activities, Net	$ 12,309	$ 26,576	$ (14,267)

(1) Includes changes in fair value for loan purchase commitments.

(2) Represents market valuation changes of derivatives that are used to manage risks associated with our accumulation of loans.

(3) Includes other fee income from loan originations and acquisitions as well as the provision for repurchase expense, presented net.

The decrease in mortgage banking activities, net for the three-month periods was mostly the result of a decrease in residential loan purchase volume on lower gross margins as compared to the prior year period. This was partially offset by income from business purpose mortgage banking activities, including activity from 5 Arches, which was acquired in the first quarter of 2019.

Residential loan purchase commitments ("LPCs"), adjusted for fallout expectations, were $1.20 billion for the three months ended March 31, 2019. Our gross margins for our residential loans in the first quarter of 2019, which we define as net interest income plus income from mortgage banking activities, divided by LPCs, were above our long-term expectations, driven primarily by improved securitization execution in the first quarter of 2019.

At both March 31, 2019 and December 31, 2018, we had repurchase reserves of $4 million outstanding related to residential loans sold through this segment. For the three months ended March 31, 2019 and 2018, we recorded repurchase provisions of $0.1 million and $0.3 million, respectively, that were included in income from mortgage banking activities, net, in this segment. We review our loan repurchase reserves each quarter and adjust them as necessary based on current information available at each reporting date.

The following table details outstanding principal balances for residential loans held-for-sale by product type at March 31, 2019.

Table 35 – Characteristics of Residential Loans Held-for-Sale

March 31, 2019 **(Dollars in Thousands)**	**Principal Value**	**Weighted Average Coupon**
First Lien Prime		
Fixed - 30 year	$ 563,871	4.86%
Fixed - 10, 15, & 20 year	49,338	4.04%
Hybrid	189,010	4.36%
ARM	147	4.45%
Total Outstanding Principal	$ 802,366	

Operating Expenses and Taxes

Operating expenses for this segment primarily include costs associated with the origination, purchase and sale of residential and business purpose loans, including $2 million of expenses from the 5 Arches platform we acquired in March 2019. For the three-month periods, a decrease in operating expenses in the first quarter of 2019 from lower variable compensation expense tied to lower segment earnings in the period was partially offset by additional expenses from the consolidated 5 Arches operations.

All mortgage banking activities are performed at our taxable REIT subsidiary and the provision for income taxes is generally correlated to the amount of this segment's contribution before income taxes in relation to the TRS's overall GAAP income and associated tax provision. The decrease in provision for income taxes resulted primarily from the reduction in GAAP income earned in this segment.

Single-Family Rental Loans Held-for-Sale

The $57 million of outstanding single-family rental loans held-for-sale at March 31, 2019 were first-lien, fixed-rate loans with maturities of five, seven, or ten years. At March 31, 2019, the weighted average coupon of our single-family rental loans was 5.72% and the weighted average loan term was seven years. At origination, the weighted average LTV ratio of these loans was 65% and the weighted average debt service coverage ratio ("DSCR") was 1.28 times.

Results of Consolidated Legacy Sequoia Entities

We sponsored Sequoia securitization entities prior to 2012 that are reported on our consolidated balance sheets for financial reporting purposes in accordance with GAAP. Each of these entities is independent of Redwood and of each other and the assets and liabilities of these entities are not, respectively, owned by us or legal obligations of ours. We record the assets and liabilities of the consolidated Legacy Sequoia entities at fair value, based on the estimated fair value of the debt securities (ABS) issued from the securitizations, in accordance with GAAP provisions for collateralized financing entities. At March 31, 2019, the estimated fair value of our investments in the consolidated Legacy Sequoia entities was $11 million.

The following tables present the statements of income for the three months ended March 31, 2019 and 2018 and the balance sheets of the consolidated Legacy Sequoia entities at March 31, 2019 and December 31, 2018. All amounts in the statements of income and balance sheets presented below are included in our consolidated financial statements.

Table 36 – Consolidated Legacy Sequoia Entities Statements of Income

	Three Months Ended March 31,		
(In Thousands)	**2019**	**2018**	**Change**
Interest income	$ 4,853	$ 4,812	$ 41
Interest expense	(4,115)	(3,852)	(263)
Net interest income	738	960	(222)
Investment fair value changes, net	(374)	(8)	(366)
Net Income from Consolidated Legacy Sequoia Entities	$ 364	$ 952	$ (588)

Table 37 – Consolidated Legacy Sequoia Entities Balance Sheets

(In Thousands)	March 31, 2019	December 31, 2018
Residential loans, held-for-investment, at fair value	$ 488,645	$ 519,958
Other assets	3,202	4,911
Total Assets	$ 491,847	$ 524,869
Other liabilities	$ 531	$ 571
Asset-backed securities issued, at fair value	479,999	512,240
Total liabilities	480,530	512,811
Equity (fair value of Redwood's retained investments in entities)	11,317	12,058
Total Liabilities and Equity	$ 491,847	$ 524,869

Net Interest Income at Consolidated Legacy Sequoia Entities

The decrease in net interest income for the three-month periods was primarily attributable to the continued paydown of loans at the consolidated entities.

Investment Fair Value Changes, net at Consolidated Legacy Sequoia Entities

Investment fair value changes, net at consolidated Legacy Sequoia entities includes the change in fair value of the residential loans held-for-investment, REO, and the ABS issued at the entities, which netted together represent the change in value of our retained investments in the consolidated Legacy Sequoia entities. The negative investment fair value changes in each of the periods presented was primarily related to the decline in fair value changes on retained IO securities, as the basis of these assets continue to diminish.

Residential Loans at Consolidated Legacy Sequoia Entities

The following table provides details of residential loan activity at consolidated Legacy Sequoia entities for the three months ended March 31, 2019 and 2018.

Table 38 – Residential Loans at Consolidated Legacy Sequoia Entities — Activity

	Three Months Ended March 31,	
(In Thousands)	2019	2018
Balance at beginning of period	$ 519,958	$ 632,817
Principal repayments	(35,780)	(34,222)
Transfers to REO	(39)	(1,268)
Changes in fair value, net	4,506	28,824
Balance at End of Period	$ 488,645	$ 626,151

First lien adjustable rate mortgage ("ARM") and hybrid loans comprise all of the loans in the consolidated Legacy Sequoia entities and were primarily originated in 2006 or prior. For outstanding loans at consolidated Legacy Sequoia entities at March 31, 2019, the weighted average FICO score of borrowers backing these loans was 727 (at origination) and the weighted average original LTV ratio was 66% (at origination). At March 31, 2019 and December 31, 2018, the aggregate unpaid principal balance of loans at consolidated Legacy Sequoia entities delinquent greater than 90 days was $13 million and $14 million, respectively, of which the aggregate unpaid principal balance of loans in foreclosure was $6 million and $5 million, respectively.

Taxable Income and Tax Provision

Taxable Income

The following table summarizes our taxable income and distributions to shareholders for the three months ended March 31, 2019 and 2018.

Table 39 – Taxable Income

	Three Months Ended March 31,	
(In Thousands, except per Share Data)	**2019 est. (1)**	**2018 est. (1)**
REIT taxable income	$ 28,761	$ 33,474
Taxable REIT subsidiary income	6,697	24,081
Total Taxable Income	$ 35,458	$ 57,555
REIT taxable income per share	$ 0.30	$ 0.44
Total taxable income per share	$ 0.37	$ 0.76
Distributions to shareholders	$ 28,998	$ 21,195
Distributions to shareholders per share	$ 0.30	$ 0.28

(1) Our tax results for the three months ended March 31, 2019 and 2018 are estimates until we file tax returns for these years.

Under normal circumstances, our minimum REIT dividend requirement would be 90% of our annual REIT taxable income. However, we currently maintain a $39 million federal net operating loss carry forward (NOL) at the REIT that affords us the option of retaining REIT taxable income up to the NOL amount, tax free, rather than distributing it as dividends. Federal income tax rules require the dividends paid deduction to be applied to reduce REIT taxable income before the applicability of NOLs is considered. It is possible our estimated REIT taxable income will exceed our dividend distributions in 2019; therefore, we may utilize a portion of our NOL in 2019 and any remaining amount will carry forward into 2020.

We also currently expect all or nearly all of the distributions to shareholders in 2019 will be taxable as dividend income and a smaller portion, if any, will be a return of capital, which is generally non-taxable. Additionally, a portion of our 2019 dividend distributions are expected to be characterized as long-term capital gains for federal income tax purposes.

Tax Provision under GAAP

For the three months ended March 31, 2019 and 2018, we recorded tax provisions of $1 million and $5 million, respectively. Our tax provision is primarily derived from the activities at our TRS as we do not book a material tax provision associated with income generated at our REIT. The reduction in tax provision year-over-year was primarily the result of the lower GAAP income earned at our TRS as well as the recognition of discrete tax benefits in the quarter ancillary to the 5 Arches acquisition, which impacted our tax provision by less than $2 million. Our TRS effective tax rate in 2019 is expected to be approximately equal to the federal corporate tax rate, excluding the one-time discrete tax benefits. The income or loss generated at our TRS will not directly affect the tax characterization of our 2019 dividends.

Realization of our deferred tax assets ("DTAs") is dependent on many factors, including generating sufficient taxable income prior to the expiration of NOL carryforwards and generating sufficient capital gains in future periods prior to the expiration of capital loss carryforwards. We determine the extent to which realization of our DTAs is not assured and establish a valuation allowance accordingly. At December 31, 2018, we reported net federal ordinary and capital deferred tax liabilities ("DTLs"), and, as such, had no associated valuation allowance. As a result of GAAP income at our TRS, we forecast that we will report net federal ordinary and capital DTLs at December 31, 2019 and consequently no valuation allowance is expected to be recorded against any federal DTA. Consistent with prior periods, we continued to maintain a valuation allowance against our net state DTAs. Our estimate of net deferred tax assets could change in future periods to the extent that actual or revised estimates of future taxable income during the carryforward periods change from current expectations.

Differences between Estimated Total Taxable Income and GAAP Income

Differences between estimated taxable income and GAAP income are largely due to the following: (i) we cannot establish loss reserves for future anticipated events for tax but we can for GAAP, as realized credit losses are expensed when incurred for tax and these losses are anticipated through lower yields on assets or through loss provisions for GAAP; (ii) the timing, and possibly the amount, of some expenses (e.g., certain compensation expenses) are different for tax than for GAAP; (iii) since amortization and impairments differ for tax and GAAP, the tax and GAAP gains and losses on sales may differ, resulting in differences in realized gains on sale; (iv) at the REIT and certain TRS entities, unrealized gains and losses on market valuation adjustments of securities and derivatives are not recognized for tax until the instrument is sold or extinguished; (v) for tax, basis may not be assigned to mortgage servicing rights retained when whole loans are sold resulting in lower tax gain on sale; (vi) for tax, we do not consolidate securitization entities as we do under GAAP; and, (vii) dividend distributions to our REIT from our TRS are included in REIT taxable income, but not GAAP income. As a result of these differences in accounting, our estimated taxable income can vary significantly from our GAAP income during certain reporting periods.

The table below reconciles our estimated total taxable income to our GAAP income for the three months ended March 31, 2019.

Table 40 – Differences between Estimated Total Taxable Income and GAAP Net Income

	Three Months Ended March 31, 2019				
(In Thousands, except per Share Data)	**REIT (Est.)**	**TRS (Est.)**	**Total Tax (Est.)**	**GAAP**	**Differences**
Interest income	$ 61,361	$ 13,245	$ 74,606	$ 131,041	$ (56,435)
Interest expense	(30,987)	(13,042)	(44,029)	(99,276)	55,247
Net interest income	30,374	203	30,577	31,765	(1,188)
Realized credit losses	(9)	—	(9)	—	(9)
Mortgage banking activities, net	—	12,025	12,025	12,309	(284)
Investment fair value changes, net	149	125	274	20,159	(19,885)
Operating expenses	(12,667)	(9,550)	(22,217)	(23,159)	942
Other income, net	311	3,603	3,914	3,587	327
Realized gains, net	10,678	350	11,028	10,686	342
Provision for income taxes	(75)	(59)	(134)	(883)	749
Net Income	$ 28,761	$ 6,697	$ 35,458	$ 54,464	$ (19,006)
Income per basic common share	$ 0.30	$ 0.07	$ 0.37	$ 0.57	$ (0.20)

Potential Taxable Income Volatility

We expect period-to-period volatility in our estimated taxable income. A description of the factors that can cause this volatility is described in the Taxable Income portion of the *Results of Operations* section in the MD&A included in Part II, Item 7, of our Annual Report on Form 10-K.

LIQUIDITY AND CAPITAL RESOURCES

Summary

In addition to the proceeds from equity and debt capital-raising transactions, our principal sources of cash consist of borrowings under mortgage loan warehouse facilities, securities repurchase agreements, payments of principal and interest we receive from our investment portfolios, and cash generated from our operating activities. Our most significant uses of cash are to purchase mortgage loans for our mortgage banking operations, to fund investments in residential loans, to purchase investment securities and make other investments, to repay principal and interest on our warehouse facilities, repurchase agreements, and long-term debt, to make dividend payments on our capital stock, and to fund our operations.

At March 31, 2019, our total capital was $2.32 billion and included $1.55 billion of equity capital and $0.77 billion of convertible notes and long-term debt on our consolidated balance sheet, including $201 million of exchangeable debt due in 2019, $245 million of convertible debt due in 2023, $200 million of convertible debt due in 2024, and $140 million of trust-preferred securities due in 2037.

As of March 31, 2019, our cash and liquidity capital included $100 million of available capital. While we believe our available capital is sufficient to fund our currently contemplated investment activities and repay existing debt, we may raise capital from time to time to make long-term investments or for other purposes. To the extent we seek additional capital to fund our operations and investment activities, our approach to raising capital will continue to be based on what we believe to be in the best interest of our shareholders.

We are subject to risks relating to our liquidity and capital resources, including risks relating to incurring debt under residential loan warehouse facilities, securities repurchase facilities, and other short- and long-term debt facilities and other risks relating to our use of derivatives. A further discussion of these risks is set forth below under the heading "*Risks Relating to Debt Incurred under Short-and Long-Term Borrowing Facilities*."

Cash Flows and Liquidity for the Three Months Ended March 31, 2019

Cash flows from our mortgage banking activities and our investments can be volatile from quarter to quarter depending on many factors, including the timing and amount of loan and securities acquisitions and sales and repayments, the profitability of mortgage banking activities, as well as changes in interest rates, prepayments, and credit losses. Therefore, cash flows generated in the current period are not necessarily reflective of the long-term cash flows we will receive from these investments or activities.

Cash Flows from Operating Activities

Cash flows from operating activities were negative $207 million during the three months ended March 31, 2019. This amount includes the net cash utilized during the period from the purchase and sale of residential mortgage loans associated with our mortgage banking activities. Purchases of loans are financed to a large extent with short-term debt, for which changes in cash are included as a component of financing activities. Excluding cash flows from the purchase, sale, and principal payments of loans classified as held-for-sale, cash flows from operating activities were negative $56 million and positive $79 million during the first three months of 2019 and 2018, respectively.

Cash Flows from Investing Activities

During the three months ended March 31, 2019, our net cash provided by investing activities was $141 million and primarily resulted from proceeds from principal payments on loans held-for-investment and sales of real estate securities. Although we generally intend to hold our investment securities as long-term investments, we may sell certain of these securities in order to manage our interest rate risk and liquidity needs, to meet other operating objectives, and to adapt to market conditions. We cannot predict the timing and impact of future sales of investment securities, if any.

Because many of our investment securities are financed through repurchase agreements, a significant portion of the proceeds from any sales or principal payments of our investment securities could be used to repay balances under these financing sources. Similarly, all or a significant portion of cash flows from principal payments of loans at consolidated Sequoia and Freddie Mac K-Series entities would generally be used to repay ABS issued by those entities.

During the three months ended March 31, 2019, we deployed capital into several new investments, including residential and multifamily securities, a limited partnership to acquire light-renovation multifamily loans, as well as to complete our purchase of the remaining 80% ownership interest in 5 Arches. In association with this acquisition, we paid $13 million of cash and assumed $11 million of cash and restricted cash.

As presented in the "*Supplemental Noncash Information*" subsection of our consolidated statements of cash flows, during the three months ended March 31, 2019, we transferred residential loans between held-for-sale and held-for-investment classification, retained securities from Sequoia securitizations we sponsored, and consolidated certain multifamily and re-performing residential securitization trusts which represent significant non-cash transactions that were not included in cash flows from investing activities.

Cash Flows from Financing Activities

During the three months ended March 31, 2019, our net cash provided by financing activities was $76 million. This primarily resulted from proceeds of $331 million from the issuance of asset-backed securities from our Sequoia Choice securitizations and proceeds of $183 million from the issuance of common stock in January 2019. These cash inflows were partially offset by $242 million of net repayments of short-term debt and $163 million of repayments of ABS issued.

In February 2019, the Board of Directors declared a regular dividend of $0.30 per share for the first quarter of 2019, which was payable on March 29, 2019 to shareholders of record on March 15, 2019. During the three months ended March 31, 2019, we paid $30 million of cash dividends on our common stock, representing cumulative dividends of $0.30 per share.

In accordance with the terms of our outstanding deferred stock units, which are stock-based compensation awards, each time we declare and pay a dividend on our common stock, we are required to make a dividend equivalent payment in that same per share amount on each outstanding deferred stock unit.

Repurchase Authorization

In February 2018, our Board of Directors approved an authorization for the repurchase of our common stock, increasing the total amount authorized for repurchases of common stock to $100 million, and also authorized the repurchase of outstanding debt securities, including convertible and exchangeable debt. This authorization increased the previous share repurchase authorization approved in February 2016 and has no expiration date. This repurchase authorization does not obligate us to acquire any specific number of shares or securities. Under this authorization, shares or securities may be repurchased in privately negotiated and/or open market transactions, including under plans complying with Rule 10b5-1 under the Securities Exchange Act of 1934, as amended. At March 31, 2019, $100 million of the current authorization remained available for the repurchase of shares of our common stock. Like other investments we may make, any repurchases of our common stock or debt securities under this authorization would reduce our available capital described above.

Short-Term Debt

In the ordinary course of our business, we use recourse debt through several different types of borrowing facilities and use cash borrowings under these facilities to, among other things, fund the acquisition of residential loans (including those we acquire and originate in anticipation of securitization), finance investments in securities and other investments, and otherwise fund our business and operations.

At March 31, 2019, we had four short-term residential loan warehouse facilities with a total outstanding debt balance of $526 million (secured by residential loans with an aggregate fair value of $579 million) and a total uncommitted borrowing limit of $1.43 billion. In addition, at March 31, 2019, we had an aggregate outstanding short-term debt balance of $1.08 billion under nine securities repurchase facilities, which were secured by securities with a fair market value of $966 million. In addition, at March 31, 2019, the fair value of our real estate securities pledged as collateral included $146 million of securities retained from our consolidated Sequoia Choice securitizations, as well as $196 million and $18 million of securities we owned that were issued by consolidated Freddie Mac SLST and Freddie Mac K-series securitizations, respectively. We also had a secured line of credit with no outstanding debt balance and a total borrowing limit of $10 million (secured by securities with a fair market value of $4 million) at March 31, 2019.

To finance our business purpose residential loan investments, at March 31, 2019, we had two single-family rental loan warehouse facilities with a total outstanding debt balance of $37 million (secured by single-family rental loans with an aggregate fair value of $49 million) and a total uncommitted borrowing limit of $400 million. In addition, at March 31, 2019, we had two residential bridge loan warehouse facilities with a total outstanding debt balance of $62 million (secured by residential bridge loans with an aggregate fair value of $93 million) and a total uncommitted borrowing limit of $80 million. We also had a business purpose loan working capital line with an outstanding debt balance of $7 million (secured by single-family rental loans with an aggregate fair value of $5 million and other assets of $7 million) and a total uncommitted borrowing limit of $15 million.

Servicer advance financing consists of non-recourse short-term securitization debt used to finance servicer advance investments we made in the fourth quarter of 2018. At March 31, 2019, the fair value of servicer advances pledged as collateral was $282 million. At March 31, 2019, the accrued interest payable balance on this debt was $0.4 million and the unamortized capitalized commitment costs were $2 million.

During the fourth quarter of 2018, $201 million principal amount of 5.625% exchangeable senior notes and $1 million of unamortized deferred issuance costs were reclassified from long-term debt to short-term debt as the maturity of the notes was less than one year as of November 2018. At March 31, 2019, the accrued interest payable balance on this debt was $4 million. See *Note 15* for additional information on our convertible notes.

At March 31, 2019, we had $2.16 billion of short-term debt outstanding. During the first three months of 2019, the highest balance of our short-term debt outstanding was $2.48 billion.

Long-Term Debt

FHLBC Borrowings

In July 2014, our FHLB-member subsidiary entered into a borrowing agreement with the Federal Home Loan Bank of Chicago. At March 31, 2019, under this agreement, our subsidiary could incur borrowings up to $2.00 billion, also referred to as “advances,” from the FHLBC secured by eligible collateral, including, but not limited to residential mortgage loans. During the three months ended March 31, 2019, our FHLB-member subsidiary made no additional borrowings under this agreement. Under a final rule published by the Federal Housing Finance Agency in January 2016, our FHLB-member subsidiary will remain an FHLB member through a five-year transition period for captive insurance companies. Our FHLB-member subsidiary's existing $2.00 billion of FHLB debt, which matures beyond this transition period, is permitted to remain outstanding until stated maturity. As residential loans pledged as collateral for this debt pay down, we are permitted to pledge additional loans or other eligible assets to collateralize this debt; however, we do not expect to be able to increase our subsidiary's FHLB debt above the existing $2.00 billion maximum.

At March 31, 2019, $2.00 billion of advances were outstanding under this agreement, which were classified as long-term debt, with a weighted average interest rate of 2.65% per annum and a weighted average maturity of six years. At March 31, 2019, accrued interest payable on these borrowings was $9 million. Advances under this agreement are charged interest based on a specified margin over the FHLBC’s 13-week discount note rate, which resets every 13 weeks. Our total advances under this agreement were secured by residential mortgage loans with a fair value of $2.41 billion at March 31, 2019. This agreement also requires our subsidiary to purchase and hold stock in the FHLBC in an amount equal to a specified percentage of outstanding advances. At March 31, 2019, our subsidiary held $43 million of FHLBC stock that is included in Other assets on our consolidated balance sheets.

Convertible Notes

In June 2018, we issued $200 million principal amount of 5.625% convertible senior notes due 2024 at an issuance price of 99.5%. After deducting the issuance discount, the underwriting discount and offering costs, we received approximately $194 million of net proceeds. Including amortization of deferred debt issuance costs and the debt discount, the weighted average interest expense yield on these convertible notes is approximately 6.2% per annum. At March 31, 2019, the outstanding principal amount of these notes was $200 million and the accrued interest payable balance on this debt was $2 million.

In August 2017, we issued $245 million principal amount of 4.75% convertible senior notes due 2023. After deducting the underwriting discount and offering costs, we received approximately $238 million of net proceeds. Including amortization of deferred debt issuance costs, the weighted average interest expense yield on these convertible notes is approximately 5.3% per annum. At March 31, 2019, the outstanding principal amount of these notes was $245 million and the accrued interest payable balance on this debt was $1 million.

In November 2014, one of our taxable subsidiaries issued $205 million principal amount of 5.625% exchangeable senior notes due 2019. After deducting the underwriting discount and offering costs, we received approximately $198 million of net proceeds. Including amortization of deferred debt issuance costs, the weighted average interest expense yield on these exchangeable notes is approximately 6.3% per annum. During the first quarter of 2016, we repurchased $4 million par value of these notes at a discount and recorded a gain on extinguishment of debt of $0.3 million in Realized gains, net on our consolidated statements of income. During the fourth quarter of 2018, $201 million principal amount of 5.625% exchangeable senior notes and $1 million of unamortized deferred issuance costs were reclassified from long-term debt to short-term debt as the maturity of the notes was less than one year as of November 2018. At March 31, 2019, the outstanding principal amount of these notes was $201 million and the accrued interest payable balance on this debt was $4 million.

Trust Preferred Securities and Subordinated Notes

At March 31, 2019, we had trust preferred securities and subordinated notes outstanding of $100 million and $40 million, respectively, issued by us in 2006 and 2007. This debt requires quarterly interest payments at a floating rate equal to three-month LIBOR plus 2.25% and must be redeemed no later than 2037. Prior to 2014, we entered into interest rate swaps with aggregate notional values totaling $140 million to hedge the variability in this long-term debt interest expense. Including hedging costs and amortization of deferred debt issuance costs, the weighted average interest expense yield on our trust preferred securities and subordinated notes is approximately 6.8% per annum. These swaps are accounted for as cash flow hedges with all interest recorded as a component of net interest income and other valuation changes recorded as a component of equity.

Asset-Backed Securities

At March 31, 2019, there were $508 million (principal balance) of loans owned at consolidated Legacy Sequoia securitization entities, which were funded with $501 million (principal balance) of ABS issued at these entities. At March 31, 2019, there were $2.28 billion (principal balance) of loans owned at consolidated Sequoia Choice securitization entities, which were funded with $2.05 billion (principal balance) of ABS issued at these entities. At March 31, 2019, there were $1.29 billion (principal balance) of loans owned at the consolidated Freddie Mac SLST securitization entity, which were funded with $976 million (principal balance) of ABS issued at this entity. At March 31, 2019, there were $2.12 billion (principal balance) of loans owned at the consolidated Freddie Mac K-Series securitization entities, which were funded with $1.93 billion (principal balance) of ABS issued at these entities. The loans and ABS issued from these entities are reported at estimated fair value. See the subsections titled "*Results of Consolidated Legacy Sequoia Entities,*" "*Residential Loans Held-for-Investment at Sequoia Choice Portfolio," "Residential Loans Held-for-Investment at Freddie Mac SLST Portfolio,"* and *"Multifamily Loans Held-for-Investment at Freddie Mac K-Series Portfolio"* in the *Results of Operations* section of this MD&A for additional details on these entities.

Risks Relating to Debt Incurred under Short- and Long-Term Borrowing Facilities

As described above under the heading "*Results of Operations,*" in the ordinary course of our business, we use debt financing obtained through several different types of borrowing facilities to, among other things, finance the acquisition of mortgage loans (including those we acquire in anticipation of sale or securitization), and finance investments in securities and other investments. We may also use short- and long-term borrowings to fund other aspects of our business and operations, including the repurchase of shares of our common stock. Debt incurred under these facilities is generally either the direct obligation of Redwood Trust, Inc., or the direct obligation of subsidiaries of Redwood Trust, Inc. and guaranteed by Redwood Trust, Inc. Risks relating to debt incurred under these facilities are described in Part I, Item 2 of our Annual Report on Form 10-K for the year ended December 31, 2018, under the caption "*Risks Relating to Debt Incurred under Short- and Long-Term Borrowing Facilities.*"

Our sources of debt financing include short-term secured borrowings under mortgage loan warehouse facilities, short-term securities repurchase facilities, a $10 million committed line of short-term secured credit from a bank, and secured borrowings by our wholly-owned subsidiary, RWT Financial, LLC, under its borrowing facility with the FHLBC.

Aggregate borrowing limits are stated under certain of these facilities, and certain other facilities have no stated borrowing limit, but each of the facilities (with the exception of the $10 million committed line of short-term secured credit and the two business purpose residential loan warehouse facilities secured by residential bridge loans) is uncommitted, which means that any request we make to borrow funds under these uncommitted facilities may be declined for any reason, even if at the time of the borrowing request we have then-outstanding borrowings that are less than the borrowing limits under these facilities. In general, financing under these facilities is obtained by transferring or pledging mortgage loans or securities to the counterparty in exchange for cash proceeds (in an amount less than 100% of the principal amount of the transferred or pledged assets). While transferred or pledged assets are financed under a facility, to the extent the market value of the assets declines, we are generally required to either immediately reacquire the assets or meet a margin requirement to transfer or pledge additional assets or cash in an amount at least equal to the decline in value. Margin call provisions under these facilities are further described in Part I, Item 2 of our Annual Report on Form 10-K for the year ended December 31, 2018 under the caption "*Risks Relating to Debt Incurred under Short- and Long-Term Borrowing Facilities - Margin Call Provisions Associated with Short-Term Debt and Other Debt Financing.*" Financial covenants included in these facilities are further described Part I, Item 2 of our Annual Report on Form 10-K for the year ended December 31, 2018 under the caption "*Risks Relating to Debt Incurred under Short- and Long-Term Borrowing Facilities - Financial Covenants Associated with Short-Term Debt and Other Debt Financing.*"

Because these borrowing facilities are uncommitted (except the two business purpose residential loan warehouse facilities secured by residential bridge loans), at any given time we may not be able to obtain additional financing under them when we need it, exposing us to, among other things, liquidity risks of the types described in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2018 under the heading "*Risk Factors,*" and in Part II, Item 7A of our Annual Report on Form 10-K for the year ended December 31, 2018 under the heading "*Market Risks.*" In addition, with respect to mortgage loans that at any given time are already being financed through these warehouse facilities, we are exposed to market, credit, liquidity, and other risks of the types described in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2018 under the heading "*Risk Factors,*" and in Part II, Item 7A of our Annual Report on Form 10-K for the year ended December 31, 2018 under the heading "*Market Risks,*" if and when those loans or securities become ineligible to be financed, decline in value, or have been financed for the maximum term permitted under the applicable facility. Additionally, our access to financing under the borrowing facility with the FHLBC is subject to the risks described under the heading *"Risk Factors - Federal regulations may limit, eliminate, or reduce the attractiveness of our subsidiary's ability to use borrowings from the Federal Home Loan Bank of Chicago to finance the mortgage loans and securities it holds and acquires, which could negatively impact our business and operating results"* in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2018.

At March 31, 2019, and through the date of this Quarterly Report on Form 10-Q, we were in compliance with the financial covenants associated with our short-term debt and other debt financing facilities. In particular, with respect to: (i) financial covenants that require us to maintain a minimum dollar amount of stockholders' equity or tangible net worth, at March 31, 2019 our level of stockholders' equity and tangible net worth resulted in our being in compliance with these covenants by more than $200 million; and (ii) financial covenants that require us to maintain recourse indebtedness below a specified ratio, at March 31, 2019 our level of recourse indebtedness resulted in our being in compliance with these covenants at a level such that we could incur at least $600 million in additional recourse indebtedness.

OFF-BALANCE SHEET ARRANGEMENTS AND CONTRACTUAL OBLIGATIONS

In the normal course of business, we enter into transactions that may require future cash payments. As required by GAAP, some of these obligations are recorded on the balance sheet, while others are off-balance sheet or recorded on the balance sheet in amounts different from the full contract or notional amount of the transaction.

For additional information on our contractual obligations, see the *Off-Balance Sheet Arrangements and Contractual Obligations* section in the MD&A included in Part II, Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2018.

For additional information on our commitments and contingencies as of March 31, 2019, see *Note 16* of our *Notes to Consolidated Financial Statements* in Part I, Item I of this Quarterly Report on Form 10-Q.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reported periods. Actual results could differ from those estimates. A discussion of critical accounting policies and the possible effects of changes in estimates on our consolidated financial statements is included in *Note 3 — Summary of Significant Accounting Policies* included in Part I, Item 1 of this Quarterly Report on Form 10-Q and in Part I, Item 8 of our Annual Report on Form 10-K for the year ended December 31, 2018. Management discusses the ongoing development and selection of these critical accounting policies with the audit committee of the board of directors.

We expect quarter-to-quarter GAAP earnings volatility from our business activities. This volatility can occur for a variety of reasons, including the timing and amount of purchases, sales, calls, and repayment of consolidated assets, changes in the fair values of consolidated assets and liabilities, increases or decreases in earnings from mortgage banking activities, and certain non-recurring events. In addition, the amount or timing of our reported earnings may be impacted by technical accounting issues and estimates. Our critical accounting policies and the possible effects of changes in estimates on our consolidated financial statements are included in the "*Critical Accounting Policies and Estimates*" section of Part II, Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2018.

Market Risks

We seek to manage risks inherent in our business — including but not limited to credit risk, interest rate risk, prepayment risk, liquidity risk, and fair value risk — in a prudent manner designed to enhance our earnings and dividends and preserve our capital. In general, we seek to assume risks that can be quantified from historical experience, to actively manage such risks, and to maintain capital levels consistent with these risks. Information concerning the risks we are managing, how these risks are changing over time, and potential GAAP earnings and taxable income volatility we may experience as a result of these risks is discussed in Part II, Item 7A of our Annual Report on Form 10-K for the fiscal year ended December 31, 2018.

Other Risks

In addition to the market and other risks described above, our business and results of operations are subject to a variety of types of risks and uncertainties, including, among other things, those described under the caption "*Risk Factors*" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2018 and in this Quarterly Report on Form 10-Q.

NEW ACCOUNTING STANDARDS

A discussion of new accounting standards and the possible effects of these standards on our consolidated financial statements is included in *Note 3 — Summary of Significant Accounting Policies* included in Part I, Item 1 of this Quarterly Report on Form 10-Q.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Information concerning market risk is incorporated herein by reference to Part II, Item 7A of our Annual Report on Form 10-K for the fiscal year ended December 31, 2018, as supplemented by the information under "*Management's Discussion and Analysis of Financial Condition and Results of Operations*" and "*Market Risks*" within Item 2 above. Other than the developments described thereunder, including changes in the fair values of our assets, there have been no other material changes in our quantitative or qualitative exposure to market risk since December 31, 2018.

Item 4. Controls and Procedures

We have adopted and maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed on our reports under the Securities Exchange Act of 1934, as amended (the Exchange Act), is recorded, processed, summarized, and reported within the time periods specified in the U.S. Securities and Exchange Commission’s rules and forms and that the 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 required disclosure. In designing and evaluating the disclosure controls 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.

As required by Rule 13a-15(b) of the Exchange Act, we have carried out an evaluation, under the supervision and with the participation of management, including our chief executive officer and chief financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the quarter covered by this report. Based on the foregoing, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures were effective at a reasonable assurance level.

There have been no changes in our internal control over financial reporting during the first quarter of 2019 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

On or about December 23, 2009, the Federal Home Loan Bank of Seattle (the "FHLB-Seattle") filed a complaint in the Superior Court for the State of Washington (case number 09-2-46348-4 SEA) against Redwood Trust, Inc., our subsidiary, Sequoia Residential Funding, Inc. ("SRF"), Morgan Stanley & Co., and Morgan Stanley Capital I, Inc. (collectively, the "FHLB-Seattle Defendants"), which alleged that the FHLB-Seattle Defendants made false or misleading statements in offering materials for a mortgage pass-through certificate (the "Seattle Certificate") issued in the Sequoia Mortgage Trust 2005-4 securitization transaction (the "2005-4 RMBS") and purchased by the FHLB-Seattle. The Seattle Certificate was issued with an original principal amount of approximately $133 million, and, at March 31, 2019, approximately $126 million of principal and $12 million of interest payments had been made in respect of the Seattle Certificate. As of March 31, 2019, the Seattle Certificate had a remaining outstanding principal amount of approximately $8 million. The matter was subsequently resolved and the claims were dismissed by the FHLB Seattle as to all the FHLB Seattle Defendants. At the time the Seattle Certificate was issued, Redwood agreed to indemnify the underwriters of the 2005-4 RMBS, which underwriters were named as defendants in the action, for certain losses and expenses they might incur as a result of claims made against them relating to this RMBS, including, without limitation, certain legal expenses. Regardless of the resolution of this litigation, we could incur a loss as a result of these indemnities.

On or about July 15, 2010, The Charles Schwab Corporation ("Schwab") filed a complaint in the Superior Court for the State of California in San Francisco (case number CGC-10-501610) against SRF and 26 other defendants (collectively, the "Schwab Defendants"), which alleged that the Schwab Defendants made false or misleading statements in offering materials for various residential mortgage-backed securities sold or issued by the Schwab Defendants. Schwab alleged only a claim for negligent misrepresentation under California state law against SRF and sought unspecified damages and attorneys' fees and costs from SRF. Schwab claimed that SRF made false or misleading statements in offering materials for a mortgage pass-through certificate (the "Schwab Certificate") issued in the 2005-4 RMBS and purchased by Schwab. The Schwab Certificate was issued with an original principal amount of approximately $15 million, and, at March 31, 2019, approximately $14 million of principal and $1 million of interest payments had been made in respect of the Schwab Certificate. As of March 31, 2019, the Schwab Certificate had a remaining outstanding principal amount of approximately $1 million. On November 14, 2014, Schwab voluntarily dismissed with prejudice its negligent misrepresentation claim, which resulted in the dismissal with prejudice of SRF from the action. Subsequently, the matter was resolved and Schwab dismissed its claims against the lead underwriter of the 2005-4 RMBS. At the time the Schwab Certificate was issued, Redwood agreed to indemnify the underwriters of the 2005-4 RMBS, which underwriters were also named as defendants in the action, for certain losses and expenses they might incur as a result of claims made against them relating to this RMBS, including, without limitation, certain legal expenses. Regardless of the resolution of this litigation, Redwood could incur a loss as a result of these indemnities.

Through certain of our wholly-owned subsidiaries, we have in the past engaged in, and expect to continue to engage in, activities relating to the acquisition and securitization of residential mortgage loans. In addition, certain of our wholly-owned subsidiaries have in the past engaged in activities relating to the acquisition and securitization of debt obligations and other assets through the issuance of collateralized debt obligations (commonly referred to as CDO transactions). Because of this involvement in the securitization and CDO businesses, we could become the subject of litigation relating to these businesses, including additional litigation of the type described above, and we could also become the subject of governmental investigations, enforcement actions, or lawsuits, and governmental authorities could allege that we violated applicable law or regulation in the conduct of our business. As an example, in July 2016 we became aware of a complaint filed by the State of California on April 1, 2016 against Morgan Stanley & Co. and certain of its affiliates alleging, among other things, that there were misleading statements contained in offering materials for 28 different mortgage pass-through certificates purchased by various California investors, including various California public pension systems, from Morgan Stanley and alleging that Morgan Stanley made false or fraudulent claims in connection with the sale of those certificates. Of the 28 mortgage pass-through certificates that were the subject of the complaint, two were Sequoia mortgage pass-through certificates issued in 2004 and two were Sequoia mortgage pass-through certificates issued in 2007. With respect to each of those certificates, our wholly-owned subsidiary, RWT Holdings, Inc., was the sponsor and our wholly-owned subsidiary, Sequoia Residential Funding, Inc., was the depositor. The plaintiffs subsequently withdrew from the litigation their claims based on eight of the 28 mortgage pass-through certificates, including one of the Sequoia mortgage pass-through certificates issued in 2004. We believe this matter was subsequently resolved and the plaintiffs withdrew their remaining claims. At the time these Sequoia mortgage pass-through certificates were issued, Sequoia Residential Funding, Inc. and Redwood Trust agreed to indemnify the underwriters of these certificates for certain losses and expenses they might incur as a result of claims made against them relating to these certificates, including, without limitation, certain legal expenses. Regardless of the resolution of this litigation, we could incur a loss as a result of these indemnities.

In accordance with GAAP, we review the need for any loss contingency reserves and establish reserves when, in the opinion of management, it is probable that a matter would result in a liability and the amount of loss, if any, can be reasonably estimated. Additionally, we record receivables for insurance recoveries relating to litigation-related losses and expenses if and when such amounts are covered by insurance and recovery of such losses or expenses are due. At March 31, 2019, the aggregate amount of loss contingency reserves established in respect of the FHLB-Seattle and Schwab litigation matters described above was $2 million. We review our litigation matters each quarter to assess these loss contingency reserves and make adjustments in these reserves, upwards or downwards, as appropriate, in accordance with GAAP based on our review.

In the ordinary course of any litigation matter, including certain of the above-referenced matters, we have engaged and may continue to engage in formal or informal settlement communications with the plaintiffs or co-defendants. Settlement communications we have engaged in relating to certain of the above-referenced litigation matters are one of the factors that have resulted in our determination to establish the loss contingency reserves described above. We cannot be certain that any of these matters will be resolved through a settlement prior to trial and we cannot be certain that the resolution of these matters, whether through trial or settlement, will not have a material adverse effect on our financial condition or results of operations in any future period.

Future developments (including resolution of substantive pre-trial motions relating to these matters, receipt of additional information and documents relating to these matters (such as through pre-trial discovery), new or additional settlement communications with plaintiffs relating to these matters, or resolutions of similar claims against other defendants in these matters) could result in our concluding in the future to establish additional loss contingency reserves or to disclose an estimate of reasonably possible losses in excess of our established reserves with respect to these matters. Our actual losses with respect to the above-referenced litigation matters may be materially higher than the aggregate amount of loss contingency reserves we have established in respect of these litigation matters, including in the event that any of these matters proceeds to trial and the plaintiff prevails. Other factors that could result in our concluding to establish additional loss contingency reserves or estimate additional reasonably possible losses, or could result in our actual losses with respect to the above-referenced litigation matters being materially higher than the aggregate amount of loss contingency reserves we have established in respect of these litigation matters include that: there are significant factual and legal issues to be resolved; information obtained or rulings made during the lawsuits could affect the methodology for calculation of the available remedies; and we may have additional obligations pursuant to indemnity agreements, representations and warranties, and other contractual provisions with other parties relating to these litigation matters that could increase our potential losses.

Item 1A. Risk Factors

Our risk factors are discussed under Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2018. In addition, the following risk factor reflects recent developments.

Our acquisition of 5 Arches could fail to improve our business or result in diminished returns, could expose us to new or increased risks, and could increase our cost of doing business.

On March 1, 2019, we completed the acquisition of the remaining 80% interest in 5 Arches, an originator of business-purpose real estate loans. Prior to the completion of this acquisition, we have not previously acquired an operating company, and we have not been engaged in directly originating mortgage loans since 2016, when we ceased our commercial origination and mortgage banking activities. If we experience challenges with the integration of the 5 Arches platform that we did not anticipate or cannot mitigate, the returns we expected with respect to this investment may not be generated. For example, originating business purpose mortgage loans could fail to improve our business or financial results if we do not have the opportunity to originate quality investments or if our estimates or projections of overall rates of return on such investments are incorrect. If our assumptions are wrong, or if market conditions change, we may, as a result, not have capital available for deployment into more profitable businesses and investments. Integrating the 5 Arches business and directly originating mortgage loans could also expose us to new or increased risks, including increased regulation by federal and state authorities, challenges in effectively integrating operations, failure to maintain effective internal controls, procedures and policies, and other unknown liabilities and unforeseen increased expenses or delays associated with the acquisition or the business of originating mortgage loans.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

During the three months ended March 31, 2019, we did not sell any equity securities that were not registered under the Securities Act of 1933, as amended.

In February 2018, our Board of Directors approved an authorization for the repurchase of our common stock, increasing the total amount authorized for repurchases of common stock to $100 million, and also authorized the repurchase of outstanding debt securities, including convertible and exchangeable debt. This authorization increased the previous share repurchase authorization approved in February 2016 and has no expiration date. This repurchase authorization does not obligate us to acquire any specific number of shares or securities. Under this authorization, shares or securities may be repurchased in privately negotiated and/or open market transactions, including under plans complying with Rule 10b5-1 under the Securities Exchange Act of 1934, as amended. At March 31, 2019, $100 million of this current authorization remained available for the repurchase of shares of our common stock.

The following table contains information on the shares of our common stock that we purchased or otherwise acquired during the three months ended March 31, 2019.

(In Thousands, except per Share Data)	Total Number of Shares Purchased or Acquired	Average Price per Share Paid	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number (or approximate dollar value) of Shares that May Yet be Purchased under the Plans or Programs
January 1, 2019 - January 31, 2019	—	$ —	—	$ —
February 1, 2019 - February 28, 2019	5	$ 15.44	—	$ —
March 1, 2019 - March 31, 2019	32	$ 15.30	—	$ 100,000
Total	37	$ —	—	$ 100,000

Item 3. Defaults Upon Senior Securities

None.

Item 4. Not Applicable

Item 5. Other Information

On May 7, 2019, Redwood amended its employments agreements with Christopher J. Abate (Redwood’s CEO), Dashiell I. Robinson (Redwood’s President), and Andrew P. Stone (Redwood’s Executive Vice President, General Counsel, and Secretary). These agreements were amended to, among other things: (i) update base salary and target bonus amounts set forth in the agreements, which updated amounts were previously approved by the Compensation Committee of the Board of Directors and which updates were previously disclosed within the Company’s Form 8-K filed on December 17, 2018; (ii) amend the provisions of the agreements related to severance payments and severance-related benefits continuation terms; and (iii) update provisions of the agreements relating to confidentiality obligations. The three amended employments employment agreements are filed as Exhibits 10.1, 10.2, and 10.3 to this Quarterly Report on Form 10-Q (collectively, the “Amended Employment Agreements”) and the description of the Amended Employment Agreements set forth in this Part II, Item 5 is qualified in its entirety by reference to the full text of the Amended Employment Agreements.

Item 6. Exhibits

Exhibit Number	Exhibit
3.1	Articles of Amendment and Restatement of the Registrant, effective July 6, 1994 (incorporated by reference to the Registrant's Quarterly Report on Form 10-Q, Exhibit 3.1, filed on August 6, 2008)
3.1.1	Articles Supplementary of the Registrant, effective August 10, 1994 (incorporated by reference to the Registrant's Quarterly Report on Form 10-Q, Exhibit 3.1.1, filed on August 6, 2008)
3.1.2	Articles Supplementary of the Registrant, effective August 11, 1995 (incorporated by reference to the Registrant's Quarterly Report on Form 10-Q, Exhibit 3.1.2, filed on August 6, 2008)
3.1.3	Articles Supplementary of the Registrant, effective August 9, 1996 (incorporated by reference to the Registrant's Quarterly Report on Form 10-Q, Exhibit 3.1.3, filed on August 6, 2008)
3.1.4	Certificate of Amendment of the Registrant, effective June 30, 1998 (incorporated by reference to the Registrant's Quarterly Report on Form 10-Q, Exhibit 3.1.4, filed on August 6, 2008)
3.1.5	Articles Supplementary of the Registrant, effective April 7, 2003 (incorporated by reference to the Registrant's Quarterly Report on Form 10-Q, Exhibit 3.1.5, filed on August 6, 2008)
3.1.6	Articles of Amendment of the Registrant, effective June 12, 2008 (incorporated by reference to the Registrant's Quarterly Report on Form 10-Q, Exhibit 3.1.6, filed on August 6, 2008)
3.1.7	Articles of Amendment of the Registrant, effective May 19, 2009 (incorporated by reference to the Registrant's Current Report on Form 8-K, Exhibit 3.1, filed on May 21, 2009)
3.1.8	Articles of Amendment of the Registrant, effective May 24, 2011 (incorporated by reference to the Registrant's Current Report on Form 8-K, Exhibit 3.1, filed on May 20, 2011)
3.1.9	Articles of Amendment of the Registrant, effective May 18, 2012 (incorporated by reference to the Registrant's Current Report on Form 8-K, Exhibit 3.1, filed on May 21, 2012)
3.1.10	Articles of Amendment of the Registrant, effective May 16, 2013 (incorporated by reference to the Registrant's Current Report on Form 8-K, Exhibit 3.1, filed on May 21, 2013)
3.2.1	Amended and Restated Bylaws of the Registrant, as adopted on March 5, 2008 (incorporated by reference to the Registrant's Quarterly Report on Form 10-Q, Exhibit 3.2.1, filed on August 8, 2018)
3.2.2	First Amendment to Amended and Restated Bylaws of the Registrant, as adopted on May 17, 2012 (incorporated by reference to the Registrant's Quarterly Report on Form 10-Q, Exhibit 3.2.2, filed on August 8, 2018)
3.2.3	Second Amendment to Amended and Restated Bylaws of the Registrant, as adopted on May 22, 2018 (incorporated by reference to the Registrant's Quarterly Report on Form 10-Q, Exhibit 3.2.3, filed on August 8, 2018)
10.1*	Third Amended and Restated Employment Agreement, dated as of May 7, 2019, by and between Christopher J. Abate and the Registrant (filed herewith)
10.2*	Third Amended and Restated Employment Agreement, dated as of May 7, 2019, by and between Andrew P. Stone and the Registrant (filed herewith)
10.3*	First Amended and Restated Employment Agreement, dated as of May 7, 2019, by and between Dashiell I. Robinson and the Registrant (filed herewith)
31.1	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of the Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of the Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101	Pursuant to Rule 405 of Regulation S-T, the following financial information from the Company's Quarterly Report on Form 10-Q for the period ended March 31, 2019, is filed in XBRL-formatted interactive data files: (i) Consolidated Balance Sheets at March 31, 2019 and December 31, 2018; (ii) Consolidated Statements of Income for the three months ended March 31, 2019 and 2018; (iii) Statements of Consolidated Comprehensive Income for the three months ended March 31, 2019 and 2018; (iv) Consolidated Statements of Changes in Stockholders' Equity for the three months ended March 31, 2019 and 2018; (v) Consolidated Statements of Cash Flows for the three months ended March 31, 2019 and 2018; and (vi) Notes to Consolidated Financial Statements.

* Indicates exhibits that include management contracts or compensatory plan or arrangements.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

REDWOOD TRUST, INC.

Date:	May 9, 2019	By:	/s/ Christopher J. Abate
			Christopher J. Abate Chief Executive Officer (Principal Executive Officer)
Date:	May 9, 2019	By:	/s/ Collin L. Cochrane
			Collin L. Cochrane Chief Financial Officer (Principal Financial Officer)
Date:	May 9, 2019	By:	/s/ Lola Bondar
			Lola Bondar Managing Director, Chief Accounting Officer (Principal Accounting Officer)

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Section 2: EX-10.1 (EXHIBIT 10.1)

EXHIBIT 10.1

THIRD AMENDED AND RESTATED EMPLOYMENT AGREEMENT

This Third Amended and Restated Employment Agreement ("Agreement"), effective as of May 7, 2019 (the "Effective Date"), is entered into by and between **Christopher J. Abate** (the "Executive") and **Redwood Trust, Inc.,** a Maryland corporation (the "Company"), and amends and restates in its entirety that certain Second Amended and Restated Employment Agreement by and between the Executive and the Company effective May 22, 2018 (as subsequently amended, the "Prior Agreement").

The Company desires to establish its right to the continued services of the Executive, in the capacity, on the terms and conditions, and subject to the rights of termination hereinafter set forth, and the Executive is willing to accept such continued employment in such capacity, on such terms and conditions, and subject to such rights of termination.

In consideration of the mutual agreements hereinafter set forth, the Executive and the Company have agreed and do hereby agree as follows:

1. Employment and Responsibilities. During the Term, the Executive shall serve as Chief Executive Officer of the Company, reporting to the Board of Directors of the Company (the "Board"). The Executive does hereby accept and agree to such employment. The Executive's duties shall be such executive and managerial duties as the Board shall from time to time prescribe and as provided in the By-Laws of the Company. The Executive does hereby accept and agree to such continued employment. The Board of Directors may, from time to time, in its sole discretion, modify, reassign and/or augment the Executive's responsibilities, and any such modification, reassignment and/or augmentation shall be deemed a waiver by the Executive of his rights under Section 6(e)(i) hereof only with his express written consent. Any such modification, reassignment or augmentation of responsibilities shall be in writing. The Executive shall devote such time, energy and skill to the performance of his duties for the

Company and for the benefit of the Company as may be necessary or required for the effective conduct and operation of the Company's business. Furthermore, the Executive shall act only in good faith and exercise due diligence and care in the performance of his duties to the Company under this Agreement.

2. Term of Agreement. The term of this Agreement (the "Term") shall commence on the Effective Date and shall continue through December 31, 2019; provided, however, that (i) on January 1, 2020 and each succeeding January 1, the Term shall automatically be extended for one additional year unless, not later than three months prior to any such January 1, either party shall have given written notice to the other that it does not wish to extend the Term and (ii) such one year extensions of the Term shall not occur on and after the January 1 of the year in which the Executive will attain age sixty-five (65) but instead the Term shall be extended only until the date of the Executive's sixty-fifth (65th) birthday.

3. Compensation.

(a) Base Salary. The Company shall pay the Executive, and the Executive agrees to accept from the Company, in payment for his services to the Company a base salary (the "Base Salary") at the rate of $750,000 per year, paid in accordance with the customary payroll practices of the Company subject to annual review and increase by the Board in its sole discretion (or by the Board's separately designated Compensation Committee in its sole discretion). For the avoidance of doubt, references to the Board in this Section 3 shall include the Board's separately designated Compensation Committee.

(b) Performance Bonus - Board of Directors' Discretion. The Executive shall be eligible to receive an annual bonus. The Board in its discretion will determine whether such annual bonus will be paid, the amount of such bonus and its form of payment. The Executive's target annual bonus amount is 175% of his Base Salary (the "Target Bonus"). If the Board determines in its discretion that the Executive's performance meets or exceeds the criteria established by the Board for the award of a Target Bonus, the Board may award the Executive the Target Bonus or a higher amount. Likewise, if the Executive's performance does not meet said criteria, the Board may award a lesser amount, or no bonus may be awarded. Unless otherwise provided in this Agreement, the Executive's eligibility to receive any bonus under this Section 3(b) shall be expressly conditioned on, among other things, the Executive remaining employed with the Company up through any designated distribution date set by the Board.

(c) Equity Incentive Awards. Executive shall be eligible to receive grants of equity-based long-term incentive awards, which may include options to purchase Company stock, performance or restricted stock units and Company restricted stock contributions to Company's deferred compensation plan, or other equity-based awards. Such awards shall be determined in the discretion of the Board. In the event of a Change of Control (as defined in the Redwood Trust, Inc. Executive Deferred Compensation Plan) in which the surviving or acquiring corporation does not assume the Executive's outstanding equity-related awards (including options and equity-based awards granted both before and after the Effective Date) or substitute similar equity-related awards, such equity-related awards shall immediately vest and become exercisable if the Executive's service with the Company has not terminated before the effective date of the Change of Control; provided, however, that the foregoing provision shall only apply if the Company is not the surviving corporation or if shares of the Company's common stock are converted into or exchanged for other securities or cash.

(d) Annual Review. The Executive's performance shall be reviewed at least annually. The performance evaluations shall consider and assess the Executive's performance of his duties and responsibilities, the timely accomplishment of existing performance objectives, his level of efficiency and overall effectiveness and/or other factors or criteria that the Company, in its sole discretion, may deem relevant. The frequency of performance evaluations may vary depending upon, among other things, length of service, past performance, changes in job duties or performance levels. The Board shall, at least annually, review the Executive's entire compensation package to determine whether it continues to meet the Company's compensation objectives. Such annual review will include a determination of (i) whether to increase the Base Salary in accordance with Section 3(a); (ii) the incentive performance bonus to be awarded in accordance with Section 3(b); and (iii) the amount and type of any equity awards granted in accordance with Section 3(c). Positive performance evaluations do not guarantee salary increases or incentive bonuses. Salary increases and incentive bonus awards are solely within the discretion of the Board and may depend upon many factors other than the Executive's performance.

4. Fringe Benefits. The Executive shall be entitled to participate in any benefit programs adopted from time to time by the Company for the benefit of its senior executive employees, and the Executive shall be entitled to receive such other fringe benefits as may be granted to him from time to time by the Board.

(a) Benefit Plans. The Executive shall be entitled to participate in any benefit plans relating to equity-based compensation awards, pension, thrift, profit sharing, life insurance, medical coverage, education, deferred compensation, or other retirement or employee benefits available to other senior executive employees of the Company, subject to any restrictions (including waiting periods) specified in such plans and/or related individual agreements. The Company shall make commercially reasonable efforts to obtain medical and disability insurance, and such other forms of insurance as the Board shall from time to time determine, for its senior executive employees.

(b) Paid Time Off. The Executive shall be entitled to twenty-five (25) days of paid time off ("PTO") per calendar year pursuant to the Company's policies applicable to similarly situated employees of the Company, as in effect from time to time and consistent with the Executive's satisfactory performance of the duties set forth in Section 1; provided, however, that the Executive may only accrue up to a maximum of fifty (50) days of PTO. The Executive may use PTO for any reason, including vacation, sick time, personal time and family illness. Any vacation shall be taken at the reasonable and mutual convenience of the Company and the Executive.

5. Business Expenses. The Company shall reimburse the Executive for any and all necessary, customary and usual expenses, properly receipted in accordance with Company policies, incurred by Executive on behalf of the Company.

6. Termination of Executive's Employment.

(a) Death. If the Executive dies while employed by the Company, his employment shall immediately terminate. The Company's obligation to pay the Executive's Base Salary shall cease as of the date of the Executive's death, and any unpaid Base Salary shall be paid to the Executive's estate. In addition, within fifteen (15) days of the Executive's death, the Company shall pay to the Executive's estate an incentive performance bonus based on Executive's Target Bonus then in effect, prorated for the number of days of employment completed by the Executive during the year of his death. Executive's beneficiaries or his estate shall receive benefits in accordance with the Company's retirement, insurance and other applicable programs and plans then in effect. All stock options or other equity-related awards with time-based vesting, including deferred or restricted stock units, shall vest in full and, in the case of stock options, shall be exercisable for such period as set forth in the applicable award agreement by which such awards are evidenced. All stock options or other equity-related awards with performance-based vesting, including performance stock units, shall remain outstanding and shall continue to be eligible to vest and become payable based on the number of target shares and the performance goals set forth in the applicable award agreement by which such awards are evidenced, with any stock options remaining exercisable for such period as set forth in the applicable award agreement.

(b) Disability. If, as a result of the Executive's incapacity due to physical or mental illness ("Disability"), Executive shall have been absent from the full-time performance of his duties with the Company for six (6) consecutive months, and, within thirty (30) days after written notice is provided to him by the Company, he shall not have returned to the full-time performance of his duties, the Executive's employment under this Agreement may be terminated by the Company for Disability. During any period prior to such termination during which the Executive is absent from the full-time performance of his duties with the Company due to Disability, the Company shall continue to pay the Executive his Base Salary at the rate in effect at the commencement of such period of Disability. Subsequent to such termination, the Executive's benefits shall be determined under the Company's retirement, insurance and other compensation programs then in effect in accordance with the terms of such programs. In addition, within fifteen (15) days of such termination, the Company shall pay to the Executive an incentive performance bonus based on Executive's Target Bonus then in effect, prorated for the number of days of employment completed by the Executive during the year in which his employment terminated. The Executive, the Executive's beneficiaries or his estate shall receive benefits in accordance with the Company's retirement, insurance and other applicable programs and plans then in effect. All stock options or other equity-related awards with time-based vesting, including deferred or restricted stock units, shall vest in full and, in the case of stock options, shall be exercisable for such period as set forth in the applicable award agreement by which such awards are evidenced. All stock options or other equity-related awards with performance-based vesting, including performance stock units, shall remain outstanding and shall continue to be eligible to vest and become payable based on the number of target shares and the performance goals set forth in the applicable award agreement by which such awards are evidenced, with any stock options remaining exercisable for such period as set forth in the applicable award agreement.

(c) Termination By The Company For Cause. The Company may terminate the Executive's employment under this Agreement for Cause, at any time prior to expiration of the Term of the Agreement; <u>provided</u>, <u>however</u>, that prior to any termination of employment for Cause pursuant to subsection (i), (ii), or (iii) below, the Company must first provide written notice describing the reason for such termination of employment (and, with respect to subsections (ii) and (iii) below, such notice may be provided on the same date as the termination date). For purposes of this Agreement, "Cause" shall mean (i) the Executive's material failure to substantially perform the reasonable and lawful duties of his position for the Company, which failure shall continue for thirty (30) days after written notice thereof by the Company to the Executive; (ii) acts or omissions constituting gross negligence, recklessness or willful misconduct on the part of the Executive in respect of the performance of his duties hereunder, his fiduciary obligations or otherwise relating to the business of the Company; (iii) the habitual or repeated neglect of his duties by Executive; (iv) the Executive's conviction of a felony; (v) theft or embezzlement, or attempted theft or embezzlement, of money or tangible or intangible assets or property of the Company or its employees, customers, clients, or others having business relations with the Company; (vi) any act of moral turpitude by Executive injurious to the interest, property, operations, business or reputation of the Company; or (vii) unauthorized use or disclosure of trade secrets or confidential or proprietary information pertaining to Company business.

In the event of a termination under this Section 6(c), the Company will pay only the portion of Base Salary or previously awarded bonus unpaid as of the termination date. Fringe benefits which have accrued and/or vested on the termination date will continue in effect according to their terms.

(d) Termination By The Company Without Cause. The Company may terminate Executive's employment hereunder at any time without Cause upon 30 days written notice to Executive or pay in lieu thereof. In the event of a termination under this Section 6(d), the Executive shall be entitled to the benefits set forth in Section 7.

(e) Termination By The Executive For Good Reason. The Executive shall have the right to terminate this Agreement for Good Reason. For purposes of this Agreement, "Good Reason" shall mean the occurrence, without the Executive's express written consent, of any one or more of the following events:

(i) A material reduction in Executive's responsibilities; title, duties or authority;

(ii) A material reduction in the Executive's Base Salary or a material reduction by the Company in the value of the Executive's total compensation package (salary, bonus opportunity, equity incentive award opportunity and benefits) if such a reduction is not made in proportion to an across-the-board reduction for all senior executives of the Company;

(iii) The relocation of the Executive's principal Company office to a location more than twenty-five (25) miles from its location as of the Effective Date (which location is the Company's headquarters in Mill Valley, California) except for required travel on the Company's business to the extent necessary to fulfill the Executive's obligations under Section 1;

(iv) A failure at any time to renew this Agreement for successive one-year periods pursuant to Section 2;

(v) The complete liquidation of the Company; or

(vi) In the event of a merger, consolidation, transfer, or closing of a sale of all or substantially all the assets of the Company with or to any other individual or entity, the failure of the Company's successor to affirmatively adopt this Agreement or to otherwise comply with its obligations pursuant to Section 13 below.

Notwithstanding the foregoing, the Executive will not be deemed to have resigned for Good Reason for purposes of subclause (i) unless (1) the Executive provides the Company with written notice setting forth in reasonable detail the facts and circumstances claimed by the Executive to constitute Good Reason within ninety (90) days after the date of the occurrence of any event that the Executive knows or should reasonably have known to constitute Good Reason, (2) the Company fails to cure such acts or omissions within thirty (30) days following its receipt of such notice, and (3) the effective date of the Executive's termination for Good Reason occurs no later than thirty (30) days after the expiration of the Company's cure period. In the event of a termination under this Section 6(e), the Executive shall be entitled to the benefits set forth in Section 7.

(f) Termination By The Executive Without Good Reason. The Executive may at any time during the Term terminate his employment hereunder for any reason or no reason by giving the Company notice in writing not less than sixty (60) days in advance of such termination. The Executive shall have no further obligations to the Company after the effective date of termination, as set forth in the notice. In the event of a termination by the Executive under this Section 6(f), the Company will pay only the portion of Base Salary or previously awarded bonus unpaid as of the termination date. Fringe benefits which have accrued and/or vested on the termination date will continue in effect according to their terms.

7. Compensation Upon Termination By the Company without Cause or By The Executive for Good Reason.

(a) If the Executive's employment shall be terminated by the Company without Cause or by the Executive for Good Reason, the Executive shall be entitled to the following benefits:

(i) Payment of Unpaid Base Salary. The Company shall immediately pay the Executive any portion of the Executive's Base Salary through the date of termination or previously awarded bonus not paid prior to the termination date.

(ii) Severance Payment.

(A) In the event such termination is not a CIC Termination (as defined below), then the Company shall provide the Executive (x) an amount equal to two (2) times the Executive's Annual Base Salary as in effect immediately prior to his termination and (y) an amount equal to the Executive's Annual Base Salary in effect immediately prior to his termination pro-rated for the number of days of employment completed by the Executive during the year in which his employment is terminated.

(B) In the event such termination of employment occurs within three months prior to, on, or within 24 months following a Change of Control (a "CIC Termination"), then instead of providing the payments in Section 7(a)(ii)(A), the Company shall provide the Executive an amount equal to the sum of (x) the Executive's Target Bonus in effect immediately prior to his termination, prorated for the number of days of employment completed by the Executive during the year in which his employment terminated; (y) two (2) times the Executive's Annual Base Salary as in effect immediately prior to his termination; and (z) two (2) times the Executive's Target Bonus in effect immediately prior to his termination. Notwithstanding the foregoing, the maximum aggregate amount that the Company shall pay to the Executive pursuant to this Section 7(a)(ii)(B) is $6,500,000.

(iii) Equity Awards. All stock options or other equity-related awards with time-based vesting, including deferred or restricted stock units, shall vest in full and, in the case of stock options, shall be exercisable for such period as set forth in the applicable award agreement by which such awards are evidenced. If the Executive's employment shall be terminated by the Company without Cause, all stock options or other equity-related awards with performance-based vesting, including performance stock units, shall remain outstanding and shall continue to be eligible to vest and become payable or exercisable based on (x) the performance goals set forth in the applicable award agreement by which such awards are evidenced and (y) a reduced number of target shares adjusted on a pro-rata basis to reflect the number of days of employment completed during the applicable vesting period in which termination occurs, with any stock options remaining exercisable for such period as set forth in the applicable award agreement. If the Executive's employment shall be terminated by the Executive for Good Reason, all stock options or other equity-related awards with performance-based vesting, including performance stock units, shall remain outstanding and shall continue to be eligible to vest and become payable based on the number of target shares and the performance goals set forth in the applicable award agreement by which such awards are evidenced, with any stock options remaining exercisable for such period as set forth in the applicable award agreement.

(iv) Continuation of Fringe Benefits. For a period of up to twelve (12) months (or, in the event of a CIC Termination, twenty-four (24) months) following the date of Executive's termination of employment with Company, subject to the Executive's valid election to continue healthcare coverage under Section 4980B of the Internal Revenue Code of 1986, as amended (the "Code") and the regulations thereunder, the Company shall continue to provide the Executive and the Executive's eligible dependents with coverage under its group health plans at the same levels and the same cost to the Executive as would have applied if the Executive's employment had not been terminated based on the Employee's elections in effect on the date of termination (the "Continued Coverage"), provided that (1) if any plan pursuant to which such benefits are provided is not, or ceases prior to the expiration of the period of continuation coverage to be, exempt from the application of Section 409A of the Code under Treasury Regulation Section 1.409A-1(a)(5), or (2) the Company is otherwise unable to continue to cover the Executive under its group health plans without penalty under applicable law (including without limitation, Section 2716 of the Public Health Service Act or the Patient Protection and Affordable Care Act), the Company may in its sole discretion provide that (i) the Executive shall pay to the Company, on an after-tax basis, a monthly amount equal to the full premium cost of the Continued Coverage for such month and (ii) within 30 days of such premium payment, the Company shall reimburse the Executive in cash (less required withholding) an amount equal to the sum of (A) the excess of (x) the full premium cost of the Continued Coverage for such month over (y) any premium amount that would have been payable by the Executive if the Executive had been actively employed by the Company for such month and (B) an additional tax "gross up" payment to cover all estimated applicable local, state and federal income and payroll taxes imposed on the Executive with respect to the Continued Coverage. For the twelve (12) month (or, in the event of a CIC Termination, twenty-four (24) month) period following the termination of the Executive's employment, the Company shall also continue to provide the

Executive with all life insurance, disability insurance and other fringe benefits set forth in Section 4 as if the Executive's employment under the Agreement had not been terminated; provided, however, that such life insurance, disability insurance and other fringe benefits shall cease as of the date the Executive receives such coverage from a subsequent employer.

(v) Payment/Benefit Limitation. If any payment or benefit due under this Agreement, together with all other payments and benefits that the Executive receives or is entitled to receive from the Company or any of its subsidiaries, affiliates or related entities, would (if paid or provided) constitute an "excess parachute payment" for purposes of Section 280G of the Code, the amounts otherwise payable and benefits otherwise due under this Agreement will either (i) be delivered in full, or (ii) be limited to the minimum extent necessary to ensure that no portion thereof will fail to be tax-deductible to the Company by reason of Section 280G of the Code (and therefore, no portion thereof will be subject to the excise tax imposed under Section 4999 of the Code), whichever of the foregoing amounts, taking into account applicable federal, state and local income and employment taxes and the excise tax imposed under Section 4999 of the Code, results in the receipt by the Executive, on an after-tax basis, of the greatest amount of payments and benefits, notwithstanding that all or some portion of such payments and/or benefits may be subject to the excise tax imposed under Section 4999 of the Code. Unless otherwise specified in writing by the Executive, in the event that the payments and/or benefits are to be reduced pursuant to this Section 7(a)(v), such payments and benefits shall be reduced such that the reduction of cash compensation to be provided to the Executive as a result of this Section 7 is minimized. In applying this principle, the reduction shall be made in a manner consistent with the requirements of Section 409A of the Code and where two economically equivalent amounts are subject to reduction but payable at different times, such amounts shall be reduced on a pro rata basis but not below zero. All determinations required to be made under this Section 7(a)(v) shall be made by the Company's independent public accounting firm (or such other nationally recognized public accounting firm as may be selected by the Company and to which selection the Executive consents (such consent not to be unreasonably withheld)) which shall provide detailed supporting calculations both to the Company and the Executive within fifteen (15) business days of the receipt of notice from the Executive that there has been a payment or benefit subject to this Section 7(a)(v), or such earlier time as is requested by the Company.

(b) No Mitigation Required; No Other Entitlement To Benefits Under Agreement. The Executive shall not be required in any way to mitigate the amount of any payment provided for in this Section 7, including, without limitation, by seeking other employment, nor shall the amount of any payment provided for in this Section 7 be reduced by any compensation earned by the Executive as the result of employment with another employer after the termination date of employment, or otherwise. Except as set forth in this Section 7, following a termination governed by this Section 7, the Executive shall not be entitled to any other compensation or benefits set forth in this Agreement, except as may be separately negotiated by the parties and approved the Board in writing in conjunction with the termination of Executive's employment under this Section 7.

(c) Release Agreement. As a condition of receiving any of the payments, vesting and benefits set forth in this Section 7 (other than the payment provided for in sub-section 7(a)(i)), the Executive shall be required to execute a mutual release agreement in the form attached hereto as Exhibit A or Exhibit B, as appropriate, and such release agreement must have become effective in accordance with its terms within 60 days following the termination date. The Company, in its sole discretion, may modify the term of the required release agreement to comply with applicable law and may incorporate the required release agreement into a termination agreement or other agreement with the Executive

(d) Timing of Severance Payments. Notwithstanding any other provision of this Agreement, all severance payments provided under this Agreement in connection with the termination of the employment of the Executive shall be payable in an amount equal to 75% of such payments on the date that is six months after the termination date, and the remaining 25% shall be payable in six equal monthly installments beginning on the date that is seven months after the termination date and continuing on the same date of each of the five months thereafter.

(e) Timing of Bonus Payments. Notwithstanding any other provision of this Agreement, all bonus payments provided under this Agreement in connection with the termination of the employment of the Executive shall be payable on the date that is six months after the termination date.

8. Disputes Relating To Executive's Termination of Employment For Good Reason. If the Executive resigns his employment with the Company alleging in good faith as the basis for such resignation "Good Reason" as defined in Section 6(e), and if the Company then disputes the Executive's right to the payment of benefits under Section 7, the Company shall continue to pay the Executive the full compensation (including, without limitation, his Base Salary) in effect at the date the Executive provided written notice of such resignation, and the Company shall continue the Executive as a participant in all compensation, benefit and insurance plans in which the Executive was then a participant, until the earlier of the expiration of the Term or the date the dispute is finally resolved, either by mutual written agreement of the parties or by application of the provisions of Section 11. For the purposes of this Section 8, the Company shall bear the burden of proving that the grounds for the Executive's resignation do not fall within the scope of Section 6(e), and there shall be a rebuttable presumption that the Executive alleged such grounds in good faith.

9. Restrictive Covenant Provisions.

(a) Noncompetition. The Executive agrees that during the Term prior to any termination of his employment hereunder, he will not, directly or indirectly, without the prior written consent of a majority of the non-employee members of the Board, manage, operate, join, control, participate in, or be connected as a stockholder (other than as a holder of shares publicly traded on a stock exchange or the NASDAQ National Market System), partner, or other equity holder with, or as an officer, director or employee of, any real estate or mortgage investment organization whose business strategy is competitive with that of the Company, as determined by a majority of the non-employee members of the Board. It is further expressly agreed that the Company will or would suffer irreparable injury if the Executive were to compete with the Company or any subsidiary or affiliate of the Company in violation of this Agreement and that the Company would by reason of such competition be entitled to injunctive relief in a court of appropriate jurisdiction, and the Executive further consents and stipulates to the entry of such injunctive relief in such a court prohibiting the Executive from competing with the Company or any subsidiary or affiliate of the Company, in the areas of business set forth above, in violation of this Agreement.

(b) Duty To Avoid Conflict Of Interest. During his employment by the Company, Executive agrees not to engage or participate in, directly or indirectly, any activities in conflict with the best interests of the Company. The Company shall be the final decision-maker with regard to any conflict of interest issue.

(c) Right To Company Materials. The Executive agrees that all styles, designs, lists, materials, books, files, reports, correspondence, records, and other documents ("Company Materials") used, prepared, or made available to the Executive shall be and shall remain the property of the Company. Upon the termination of employment or the expiration of this Agreement, the Executive shall immediately return to the Company all Company Materials, and the Executive shall not make or retain any copies thereof.

(d) Nonsolicitation. The Executive promises and agrees that he will not directly or indirectly solicit any of the Company's employees to work for any competing real estate or mortgage investment organization as determined under Section 9 (a) for a period of one (1) year following the occurrence of any event entitling the Executive to payments and benefits, provided the Company makes all such payments when due according to the provisions herein.

(e) Confidential And Proprietary Information.

(1) It is hereby acknowledged that Executive has and shall gain knowledge of trade secrets and confidential information owned by or related to the Company and/or its affiliates including but not limited to the following: (i) the names, lists, buying habits and practices of customers, clients or vendors, (ii) marketing and related information, (iii) relationships with the persons or entities with whom or with which the Company has contracted, (iv) their products, designs, software, developments, improvements and methods of operation, (v) financial condition, profit performance and financial requirements, (vi) the compensation paid to employees, (vii) business plans and the information contained therein, and (viii) all other confidential information of, about or concerning the Company, the manner of operation of the Company and other confidential data of any kind, nature or description relating to the Company (collectively, the "Confidential Information"). Confidential Information does not include information which (A) is or becomes generally available to the public other than as a result of a disclosure by Executive; or (B) becomes available to Executive on a non-confidential basis after the termination or expiration of Executive's obligations under this Agreement from a source other than the Company, provided that such source is not bound by a confidentiality agreement with or other contractual, legal or fiduciary obligation of confidentiality to the Company or any other party with respect to such information; or (C) is independently developed after the termination or expiration of Executive's obligations under this agreement without reference to the Confidential Information, provided such independent development can reasonably be proven by Executive by written records.

(2) The parties hereby acknowledge that the Confidential Information constitutes important, unique, material and confidential trade secrets which affect the successful activities of the Company, and constitute a substantial part of the assets and goodwill of the Company. In view of the foregoing, Executive agrees that he will not at any time whether during or after the term of this Agreement, except as required in the course of Executive's employment by Company and at its direction and for its sole benefit, in any fashion, form or manner, directly or indirectly (i) use or divulge, disclose, communicate or provide or permit access to any person, firm, partnership, corporation or other entity, any Confidential Information of any kind, nature or description, or (ii) remove from Company's premises any notes or records relating thereto, or copies or facsimiles thereof (whether made by electronic, electrical, magnetic, optical, laser, acoustic or other means).

(3) Promptly upon the request of Company, and immediately upon the termination of Executive's employment, Executive shall not transfer to any third person and shall deliver to Company all Confidential Information, and other property belonging to the Company, including all copies thereof, in the possession or under the control of the Executive.

(4) Executive represents that the performance of all the terms of this Agreement will not conflict with, and will not breach, any other invention assignment agreement, confidentiality agreement, employment agreement or non-competition agreement to which Executive is or has been a party. To the extent that Executive has confidential information or materials of any former employer, Executive acknowledges that the Company has directed Executive to not disclose such confidential information or materials to the Company or any of its employees, and that the Company prohibits Executive from using said confidential information or materials in any work that Executive may perform for the Company. Executive agrees that Executive will not bring with Executive to the Company, and will not use or disclose any confidential, proprietary information, or trade secrets acquired by Executive prior to his employment with the Company. Executive will not disclose to the Company or any of its employees, or induce the Company or any of its employees to use, any confidential or proprietary information or material belonging to any previous employers or others, nor will Executive bring to the Company or use in connection with Executive's work for the Company copies of any software, computer files, or any other copyrighted or trademarked materials except those owned by or licensed to the Company. Executive represents that he is not a party to any other agreement that will interfere with his full compliance with this Agreement. Executive further agrees not to enter into any agreement, whether written or oral, in conflict with the provisions of this Agreement.

(5) Notwithstanding the generality of the foregoing, nothing in this Agreement is intended to prohibit the Executive from filing a charge with, reporting possible violations to, or participating or cooperating with the Securities and Exchange Commission or any other federal, state or local regulatory body or law enforcement agency, including in relation to any whistleblower, anti-discrimination, or anti-retaliation provisions of federal, state or local law or regulation. Pursuant to 18 U.S.C. Section 1833(b), the Executive will not be held criminally or civilly liable under any federal or state trade secret law for the disclosure of a trade secret that is made: (x) in confidence to a federal, state or local government official, either directly or indirectly, or to an attorney, and solely for the purpose of reporting or investigating a suspected violation of law; or (y) in a complaint or other document filed in a lawsuit or other proceeding, if such filing is made under seal.

(f) Inventions. Any and all inventions, discoveries or improvements that Executive has conceived or made or may conceive or make during the period of employment relating to or in any way pertaining to or connected with the systems, products, computer programs, software, apparatus or methods employed, manufactured or constructed by the Company or to systems, products, apparatus or methods with respect to which the Company engages in, requests or anticipates research or development, shall be promptly and fully disclosed and described by Executive to the Company and shall be the sole and exclusive property of the Company, and Executive shall assign, and hereby does assign to the Company Executive’s entire right, title and interest in and to all such inventions, discoveries or improvements as well as any modifications or improvements thereto that may be made.

The obligations outlined in this Section 9(f) do not apply to any invention that qualifies fully under California Labor Code Section 2870 (a copy of which is attached hereto as Exhibit C) or to any rights Executive may have acquired in connection with an invention, discovery or improvement that was developed entirely on Executive’s own time for which no equipment, supplies, facilities or trade secret information of the Company was used and (a) that does not relate directly or indirectly to the business of the Company or to the Company’s actual or demonstrable anticipated research or development, or (b) that does not result from any work performed by Executive for the Company.

(g) Maryland Law. The Executive agrees, in accordance with Maryland law, to first offer to the Company corporate opportunities learned of solely as a result of his service as an officer of the Company.

(h) Breach. It is expressly agreed that each breach of this Section 9 is a distinct and material breach of this Agreement and that solely a monetary remedy would be inadequate, impracticable and extremely difficult to prove, and that each such breach would cause the Company irreparable harm. It is further agreed that, in addition to any and all remedies available at law or equity (including money damages), either party shall be entitled to temporary and permanent injunctive relief to enforce the provisions of this Section, without the necessity of proving actual damages. It is further agreed that either party shall be entitled to seek such equitable relief in any forum, including a court of law, notwithstanding the provisions of Section 11. Either party may pursue any of the remedies described herein concurrently or consecutively in any order as to any such breach or violation, and the pursuit of one of such remedies at any time will not be deemed an election of remedies or waiver of the right to pursue any of the other such remedies. Any breach of this Section 9 shall immediately terminate any obligations by the Company to provide Executive with severance and continued benefits pursuant to Section 6 or 7 of this Agreement.

(i) Unenforceability. Should any portion of this Section 9 be deemed unenforceable because of its scope, duration or effect, and only in such event, then the parties expressly consent and agree to such limitation on scope, duration or effect as may be finally adjudicated as enforceable, to give this Section 9 its maximum permissible scope, duration and effect.

10. Notices. All notices and other communications under this Agreement shall be in writing and shall be given by fax or first class mail, certified or registered with return receipt requested, and shall be deemed to have been duly given three (3) days after mailing or twenty-four (24) hours after transmission of a fax to the respective persons named below:

If to the Company: Redwood Trust, Inc.
Attn: General Counsel
One Belvedere Place, Suite 300
Mill Valley, CA 94941
Phone: (415) 389-7373
Fax: (415) 381-1773

If to the Executive: Christopher J. Abate
c/o Redwood Trust, Inc.
One Belvedere Place, Suite 300
Mill Valley, CA 94941
Phone: (415) 389-7373
Fax: (415) 381-1773

Either party may change such party's address for notices by notice duly given pursuant hereto.

11. Resolution of Disputes. To ensure the rapid and economical resolution of disputes that may arise in connection with the Executive's employment with the Company, the Executive and the Company agree that any and all disputes, claims, or causes of action, in law or equity, arising from or relating to the enforcement, breach, performance, or interpretation of this Agreement, the Executive's employment, or the termination of the Executive's employment ("Arbitrable Claims") shall be submitted to confidential mediation in San Francisco, California conducted by a mutually agreeable mediator from Judicial Arbitration and Mediation Services ("JAMS") or its successor under the JAMS Rules of Practice and Procedure then in effect, which can be found at www.jamsadr.com/adr-rules-procedures. The cost of JAMS' mediation fees shall be paid by the Company. In the event that mediation is unsuccessful in resolving the Arbitrable Claims, the Arbitrable Claims shall be resolved, to the fullest extent permitted by law, by final, binding and confidential arbitration in San Francisco, California conducted by JAMS or its successor, under the then applicable rules of JAMS.

The Executive acknowledges that by agreeing to this arbitration procedure, both the Executive and the Company waive the right to resolve any such dispute through a trial by jury or judge or administrative proceeding.

The arbitrator shall: (a) have the authority to compel adequate discovery for the resolution of the dispute and to award such relief as would otherwise be permitted by law; and (b) issue a written arbitration decision including the arbitrator's essential findings and conclusions and a statement of the award. The arbitrator shall be authorized to award any or all remedies that the Executive or the Company would be entitled to seek in a court of law, including, without limitation, the award of attorneys' fees based on a determination of the extent to which each party has prevailed as to the material issues raised in determination of the dispute. The Company shall pay all JAMS' arbitration fees in excess of those which would be required if the dispute were decided in a court of law. Nothing in this Agreement is intended to prevent either the Executive or the Company from obtaining injunctive relief in court to prevent irreparable harm pending the conclusion of any such mediation or arbitration.

12. [Reserved]

13. Assignment; Successors. This Agreement is personal in its nature, and neither of the parties hereto shall, without the consent of the other, assign or transfer this Agreement or any rights or obligations hereunder; provided, however, that, in the event of the merger, consolidation, transfer, or sale of all or substantially all of the assets of the Company with or to any other individual or entity, this Agreement shall, subject to the provisions hereof, be binding upon and inure to the benefit of such successor and such successor shall discharge and perform all the promises, covenants, duties, and obligations of the Company hereunder.

14. Governing Law. This Agreement and the legal relations thus created between the parties hereto shall be governed by and construed under and in accordance with the laws of the State of California.

15. Entire Agreement; Headings. This Agreement embodies the entire agreement of the parties with respect to the subject matter hereof and supersedes in their entirety all other or prior agreements, whether oral or written, with respect thereto, including but not limited to the Prior Agreement, but excluding the plans, programs and equity award agreements under which compensation and benefits are provided pursuant to Sections 3 and 4 hereof to the extent such plans and programs and equity award agreements are not inconsistent with this Agreement. Section headings in this Agreement are included herein for convenience of reference only and shall not constitute a part of this Agreement for any other purpose.

16. Waiver; Modification. Failure to insist upon strict compliance with any of the terms, covenants, or conditions hereof shall not be deemed a waiver of such term, covenant, or condition, nor shall any waiver or relinquishment of, or failure to insist upon strict compliance with, any right or power hereunder at any one or more times be deemed a waiver or relinquishment of such right or power at any other time or times. This Agreement shall not be modified in any respect except by a writing executed by each party hereto.

17. Severability. In the event that a court of competent jurisdiction determines that any portion of this Agreement is in violation of any statute or public policy, only the portions of this Agreement that violate such statute or public policy shall be stricken. All portions of this Agreement that do not violate any statute or public policy shall continue in full force and effect. Further, any court order striking any portion of this Agreement shall modify the stricken terms as narrowly as possible to give as much effect as possible to the intentions of the parties under this Agreement.

18. Indemnification. The Company shall indemnify and hold Executive harmless to the maximum extent permitted by Section 2-418 of the Maryland General Corporations Law or its successor statute, or if greater, by the Company's Bylaws, by any applicable resolution of the Board or by the terms providing the most extensive indemnification contained in any written agreement between the Company and any director or officer of the Company. The Company shall make Executive a named beneficiary under all director and officer liability policies maintained by the Company from time to time for the benefit of its directors and officers, entitled to all benefits provided thereunder to persons serving in a comparable role as an officer of the Company.

19. Section 409A. Any payments under this Agreement subject to Section 409A of the Code that are subject to execution of a waiver and release which may be executed and/or revoked in a calendar year following the calendar year in which the payment event (such as a termination of employment) occurs shall commence payment only in the calendar year in which the consideration period or, if applicable, release revocation period ends, as necessary to comply with Section 409A of the Code. Notwithstanding anything to the contrary in this Agreement, no compensation or benefits shall be paid to the Executive during the six (6)-month period following the Executive's "separation from service" from the Company (within the meaning of Section 409A of the Code, a “Separation from Service”) if the Company determines that paying such amounts at the time or times indicated in this Agreement would be a prohibited distribution under Section 409A(a)(2)(B)(i) of the Code. If the payment of any such amounts is delayed as a result of the previous sentence, then on the first day of the seventh month following the date of Separation from Service (or such earlier date upon which such amount can be paid under Section 409A without resulting in a prohibited distribution, including as a result of the Executive’s death), the Company shall pay the Executive a lump-sum amount equal to the cumulative amount that would have otherwise been payable to the Executive during such period. Any right to a series of installment payments pursuant to this Agreement is to be treated as a right to a series of separate payments. To the extent permitted under Section 409A of the Code, any separate payment or benefit under this Agreement or otherwise shall not be deemed “nonqualified deferred compensation” subject to Section 409A of the Code to the extent provided in the exceptions in Treasury Regulation Section 1.409A-1(b)(4), Section 1.409A-1(b)(9) or any other applicable exception or provision of Section 409A. All payments of nonqualified deferred compensation subject to Section 409A to be made upon a termination of employment under this Agreement may only be made upon the Executive’s “separation from service” from the Company

20. Counterparts. This Agreement may be executed in several counterparts, each of which shall be deemed to be an original but all of which together will constitute one and the same instrument.

21. Successor Sections. References herein to sections or rules of the Code shall be deemed to include any successor sections or rules.

[*Signature Page Follows*]

IN WITNESS WHEREOF, the Company has caused this Agreement to be executed by its duly authorized officer, and the Executive has hereunto signed this Agreement, as of the Effective Date.

REDWOOD TRUST, INC.

By: /s/ Andrew P. Stone
Andrew P. Stone
Executive Vice President & General Counsel

EXECUTIVE

/s/ Christopher J. Abate
Christopher J. Abate

EXHIBIT A

RELEASE AGREEMENT

Except as otherwise set forth in this Release Agreement or in Sections 7 and 18 of the Employment Agreement between Christopher J. Abate and Redwood Trust, Inc., Christopher J. Abate ("Executive") hereby generally and completely releases the Company and its directors, officers, employees, shareholders, partners, agents, attorneys, predecessors, successors, parent and subsidiary entities, insurers, affiliates, and assigns from any and all claims, liabilities and obligations, both known and unknown, that arise out of or are in any way related to events, acts, conduct, or omissions occurring at any time prior to and including the date Executive signs this Release Agreement. The Company, its directors, officers, employees, shareholders, partners, agents, attorneys, predecessors, successors, parent and subsidiary entities, insurers, affiliates, and assigns, hereby releases Executive and his heirs, executors, successors and assigns, from any and all claims, liabilities and obligations, both known and unknown, that arise out of or are in any way related to events, acts, conduct, or omissions occurring at any time prior to and including the date the Company signs this Release Agreement. This general mutual release includes, but is not limited to: (A) all claims arising out of or in any way related to Executive's employment with the Company or the termination of that employment; (B) all claims related to Executive's compensation or benefits from the Company, including salary, bonuses, commissions, vacation pay, expense reimbursements, severance pay, fringe benefits, stock, stock options, or any other ownership interests in the Company; (C) all claims for breach of contract, wrongful termination, and breach of the implied covenant of good faith and fair dealing; (D) all tort claims, including claims for fraud, defamation, emotional distress, and discharge in violation of public policy; (E) all federal, state, and local statutory claims, including claims for discrimination, harassment, retaliation, attorneys' fees, or other claims arising under the federal Civil Rights Act of 1964 (as amended), the federal Americans with Disabilities Act of 1990, the federal Age Discrimination in Employment Act of 1967 (as amended) ("ADEA"), the federal Employee Retirement Income Security Act of 1974 (as amended), and the California Fair Employment and Housing Act (as amended); and (F) all claims and rights with respect to Executive's right to communicate directly with, cooperate with, or provide information to, any federal, state or local government regulator; provided, however, that nothing in this paragraph shall be construed in any way to release the Company from its obligation to indemnify Executive pursuant to agreement, the Company's bylaws or binding resolutions, or applicable law.

Executive acknowledges that he is knowingly and voluntarily waiving and releasing any rights he may have under the ADEA, and that the consideration given under his Employment Agreement with the Company for the waiver and release in the preceding paragraph hereof is in addition to anything of value to which he was already entitled. Executive further acknowledges

that he has been advised by this writing, as required by the ADEA, that: (A) this waiver and release does not apply to any rights or claims that may arise after the date Executive signs this Release Agreement; (B) Executive should consult with an attorney prior to signing this Release Agreement (although Executive may choose voluntarily not do so); (C) Executive has twenty-one (21) days to consider this Release Agreement (although Executive may choose voluntarily to sign this Release Agreement earlier); (D) Executive has seven (7) days following the date that he signs this Release Agreement to revoke the Release Agreement by providing written notice to an officer of the Company; and (E) this Release Agreement shall not be effective until the date upon which the revocation period has expired, which shall be the eighth day after Executive signs this Release Agreement. Both Executive and the Company acknowledge that each has read and understands Section 1542 of the California Civil Code which reads as follows:

A general release does not extend to claims that the creditor or releasing party does not know or suspect to exist in his or her favor at the time of executing the release and that, if known by him or her, would have materially affected his or her settlement with the debtor or released party.

Both Executive and the Company hereby expressly waive and relinquish all rights and benefits under that section and any law of any jurisdiction of similar effect with respect to each party's release of any claims hereunder.

Notwithstanding anything herein, the Executive acknowledges and agrees that, pursuant to 18 USC Section 1833(b), the Executive will not be held criminally or civilly liable under any federal or state trade secret law for the disclosure of a trade secret that is made: (i) in confidence to a federal, state, or local government official, either directly or indirectly, or to an attorney, and solely for the purpose of reporting or investigating a suspected violation of law; or (ii) in a complaint or other document filed in a lawsuit or other proceeding, if such filing is made under seal.

Mutual Nondisparagement.

(a) Nondisparagement by Executive. At all times following the cessation of the Executive's employment with the Company, the Executive agrees not to make negative comments or statements about, or otherwise criticize or disparage, in any format or through any medium, the Company or any entity controlled by, controlling or under common control with the Company ("Affiliates") or any of the officers, directors, managers, employees, services, operations, investments or products of the Company or any of its Affiliates. For purposes of the foregoing sentence, disparagement shall include, but not be limited to, negative comments or statements intended or reasonably likely to be harmful or disruptive to a person's or entity's respective business, business reputation, business operations, or personal reputation.

(b) Nondisparagement by Designated Company Representatives. At all times following the cessation of the Executive's employment with the Company, the Company agrees not to publish, and agrees to cause the Designated Company Representatives not to make, negative comments or statements about, or otherwise criticize or disparage, in any format or through any medium, the Executive. For purposes of the foregoing sentence, disparagement shall include, but not be limited to, negative comments or statements intended or reasonably likely to be harmful or disruptive to a person's business reputation or personal reputation. For purposes of this sub-section (b), the "Designated Company Representatives" are (i) all executive officers of the Company while serving in such capacity and (ii) all members of the Board of Directors while serving in such capacity.

(c) The foregoing sub-sections (a) and (b) shall not be violated by truthful comments or statements (i) made in response to legal process, in required governmental testimony or filings, in judicial, administrative or arbitral proceedings (including, without limitation, depositions in connection with such proceedings), in compliance with law, administrative rule, or regulation, or made pursuant to a court or administrative order, or in connection with reporting possible violations of federal law or regulation to any governmental agency or entity, or making other disclosures that are protected under the whistleblower provisions of federal law or regulation, (ii) made by members of the Board of Directors in the course of meetings or discussions of the Board of Directors (or any committee thereof) or in communications between members of the Board of Directors and the Executive, and not disclosed to the public, (iii) made by a member of the Board of Directors in the good faith belief that the statements are required for the proper discharge of his or her fiduciary duties, or (iv) made by the Board of Directors in connection with a termination of the Executive for Cause.

[*Signature Page Follows*]

IN WITNESS WHEREOF, the Company has caused this Agreement to be executed by its duly authorized officer, and the Executive has hereunto signed this Agreement, as of the date set forth below.

EXECUTIVE

Name: ______________________________
Christopher J. Abate

Date: ______________________________

COMPANY

Name: ______________________________

Date: ______________________________

GROUP TERMINATION

EXHIBIT B
RELEASE AGREEMENT

Except as otherwise set forth in this Release Agreement or in Sections 7 and 18 of the Employment Agreement between Christopher J. Abate and Redwood Trust, Inc., Christopher J. Abate ("Executive") hereby generally and completely releases the Company and its directors, officers, employees, shareholders, partners, agents, attorneys, predecessors, successors, parent and subsidiary entities, insurers, affiliates, and assigns from any and all claims, liabilities and obligations, both known and unknown, that arise out of or are in any way related to events, acts, conduct, or omissions occurring at any time prior to and including the date Executive signs this Release Agreement. The Company, its directors, officers, employees, shareholders, partners, agents, attorneys, predecessors, successors, parent and subsidiary entities, insurers, affiliates, and assigns, hereby releases Executive and his heirs, executors, successors and assigns, from any and all claims, liabilities and obligations, both known and unknown, that arise out of or are in any way related to events, acts, conduct, or omissions occurring at any time prior to and including the date the Company signs this Release Agreement. This general mutual release includes, but is not limited to: (A) all claims arising out of or in any way related to Executive's employment with the Company or the termination of that employment; (B) all claims related to Executive's compensation or benefits from the Company, including salary, bonuses, commissions, vacation pay, expense reimbursements, severance pay, fringe benefits, stock, stock options, or any other ownership interests in the Company; (C) all claims for breach of contract, wrongful termination, and breach of the implied covenant of good faith and fair dealing; (D) all tort claims, including claims for fraud, defamation, emotional distress, and discharge in violation of public policy; (E) all federal, state, and local statutory claims, including claims for discrimination, harassment, retaliation, attorneys' fees, or other claims arising under the federal Civil Rights Act of 1964 (as amended), the federal Americans with Disabilities Act of 1990, the federal Age Discrimination in Employment Act of 1967 (as amended) ("ADEA"), the federal Employee Retirement Income Security Act of 1974 (as amended), and the California Fair Employment and Housing Act (as amended); and (F) all claims and rights with respect to Executive's right to communicate directly with, cooperate with, or provide information to, any federal, state or local government regulator; provided, however, that nothing in this paragraph shall be construed in any way to release the Company from its obligation to indemnify Executive pursuant to agreement, the Company's bylaws or binding resolutions, or applicable law.

Executive acknowledges that he is knowingly and voluntarily waiving and releasing any rights he may have under the ADEA, and that the consideration given under his Employment Agreement with the Company for the waiver and release in the preceding paragraph hereof is in addition to anything of value to which he was already entitled. Executive further acknowledges

that he has been advised by this writing, as required by the ADEA, that: (A) this waiver and release does not apply to any rights or claims that may arise after the date Executive signs this Release Agreement; (B) Executive should consult with an attorney prior to signing this Release Agreement (although Executive may choose voluntarily not do so); (C) Executive has forty-five (45) days to consider this Release Agreement (although he may choose voluntarily to sign this Release Agreement earlier); (D) Executive has seven (7) days following the date that he signs this Release Agreement to revoke the Release Agreement by providing written notice to an officer of the Company; (E) this Release Agreement shall not be effective until the date upon which the revocation period has expired, which shall be the eighth day after Executive signs this Release Agreement; and (F) Executive has received with this Release Agreement a detailed list of the job titles and ages of all employees who were terminated in this group termination and the ages of all employees of the Company in the same job classification or organizational unit who were not terminated.

Both the Executive and the Company acknowledge that each has read and understands Section 1542 of the California Civil Code which reads as follows:

A general release does not extend to claims that the creditor or releasing party does not know or suspect to exist in his or her favor at the time of executing the release and that, if known by him or her, would have materially affected his or her settlement with the debtor or released party.

Both the Executive and the Company hereby expressly waive and relinquish all rights and benefits under that section and any law of any jurisdiction of similar effect with respect to each party's release of any claims hereunder.

Notwithstanding anything herein, the Executive acknowledges and agrees that, pursuant to 18 USC Section 1833(b), the Executive will not be held criminally or civilly liable under any federal or state trade secret law for the disclosure of a trade secret that is made: (i) in confidence to a federal, state, or local government official, either directly or indirectly, or to an attorney, and solely for the purpose of reporting or investigating a suspected violation of law; or (ii) in a complaint or other document filed in a lawsuit or other proceeding, if such filing is made under seal.

Mutual Nondisparagement.

(a) Nondisparagement by Executive. At all times following the cessation of the Executive's employment with the Company, the Executive agrees not to make negative comments or statements about, or otherwise criticize or disparage, in any format or through any medium, the Company or any entity controlled by, controlling or under common control with the Company ("Affiliates") or any of the officers, directors, managers, employees, services, operations, investments or products of the Company or any of its Affiliates. For purposes of the foregoing sentence, disparagement shall include, but not be limited to, negative comments or statements intended or reasonably likely to be harmful or disruptive to a person's or entity's respective business, business reputation, business operations, or personal reputation.

(b) Nondisparagement by Designated Company Representatives. At all times following the cessation of the Executive's employment with the Company, the Company agrees not to publish, and agrees to cause the Designated Company Representatives not to make, negative comments or statements about, or otherwise criticize or disparage, in any format or through any medium, the Executive. For purposes of the foregoing sentence, disparagement shall include, but not be limited to, negative comments or statements intended or reasonably likely to be harmful or disruptive to a person's business reputation or personal reputation. For purposes of this sub-section (b), the "Designated Company Representatives" are (i) all executive officers of the Company while serving in such capacity and (ii) all members of the Board of Directors while serving in such capacity.

(c) The foregoing sub-sections (a) and (b) shall not be violated by truthful comments or statements (i) made in response to legal process, in required governmental testimony or filings, in judicial, administrative or arbitral proceedings (including, without limitation, depositions in connection with such proceedings), in compliance with law, administrative rule, or regulation, or made pursuant to a court or administrative order, or in connection with reporting possible violations of federal law or regulation to any governmental agency or entity, or making other disclosures that are protected under the whistleblower provisions of federal law or regulation, (ii) made by members of the Board of Directors in the course of meetings or discussions of the Board of Directors (or any committee thereof) or in communications between members of the Board of Directors and the Executive, and not disclosed to the public, (iii) made by a member of the Board of Directors in the good faith belief that the statements are required for the proper discharge of his or her fiduciary duties, or (iv) made by the Board of Directors in connection with a termination of the Executive for Cause.

[*Signature Page Follows*]

IN WITNESS WHEREOF, the Company has caused this Agreement to be executed by its duly authorized officer, and the Executive has hereunto signed this Agreement, as of the date set forth below.

EXECUTIVE

Name: ______________________________
Christopher J. Abate

Date: ______________________________

COMPANY

Name: ______________________________

Date: ______________________________

EXHIBIT C

Section 2870 of California Labor Code

Section 2870 of California Labor Code: Application of provision providing that employee shall assign or offer to assign rights in invention to employer.

a. Any provision and employment agreement which provides that an employee shall assign, or offer to assign, any of his or her rights in an invention to his or her employer shall not apply to an invention that the employee developed entirely on his or her own time without using the employer's equipment, supplies, facilities or trade secret information except for those inventions that either:

1. Relate at the time of conception or reduction to practice of the invention to the employer's business, or actual or demonstrably anticipated research or development of the employer; or

2. Result from any work performed by the employee for the employer.

b. To the extent a provision in an employment agreement purports to require an employee to assign an invention otherwise excluded from being required to be assigned under subdivision (a), the provision is against the public policy of this state and is unenforceable.

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Section 3: EX-10.2 (EXHIBIT 10.2)

EXHIBIT 10.2

THIRD AMENDED AND RESTATED EMPLOYMENT AGREEMENT

This Third Amended and Restated Employment Agreement ("Agreement"), effective as of May 7, 2019 (the "Effective Date"), is entered into by and between **Andrew P. Stone** (the "Executive") and **Redwood Trust, Inc.,** a Maryland corporation (the "Company"), and amends and restates in its entirety that certain Second Amended and Restated Employment Agreement by and between the Executive and the Company effective May 22, 2018 (as subsequently amended, the "Prior Agreement").

The Company desires to establish its right to the continued services of the Executive, in the capacity, on the terms and conditions, and subject to the rights of termination hereinafter set forth, and the Executive is willing to accept such continued employment in such capacity, on such terms and conditions, and subject to such rights of termination.

In consideration of the mutual agreements hereinafter set forth, the Executive and the Company have agreed and do hereby agree as follows:

1. Employment and Responsibilities. During the Term, the Executive shall serve as Executive Vice President and General Counsel of the Company, reporting to the Chief Executive Officer of the Company or his designee, with responsibilities, duties and authority customary for such position. The Executive does hereby accept and agree to such continued employment. The Chief Executive Officer may, from time to time, in his sole discretion, modify, reassign and/or augment the Executive's responsibilities, subject to approval by the Board of Directors of the Company (the "Board"), and any such modification, reassignment and/or augmentation shall be deemed a waiver by the Executive of his rights under Section 6(e)(i) hereof only with his express written consent. Any such modification, reassignment or augmentation of responsibilities shall be in writing. The Executive shall devote such time, energy and skill to the performance of his duties for the Company and for the benefit of the Company as may be necessary or required for the effective conduct and operation of the Company's business. Furthermore, the Executive shall act only in good faith and exercise due diligence and care in the performance of his duties to the Company under this Agreement.

2. Term of Agreement. The term of this Agreement (the "Term") shall commence on the Effective Date and shall continue through December 31, 2019; provided, however, that (i) on January 1, 2020 and each succeeding January 1, the Term shall automatically be extended for one additional year unless, not later than three months prior to any such January 1, either party shall have given written notice to the other that it does not wish to extend the Term and (ii) such one year extensions of the Term shall not occur on and after the January 1 of the year in which the Executive will attain age sixty-five (65) but instead the Term shall be extended only until the date of the Executive's sixty-fifth (65th) birthday.

3. Compensation.

(a) Base Salary. The Company shall pay the Executive, and the Executive agrees to accept from the Company, in payment for his services to the Company a base salary (the "Base Salary") at the rate of $400,000 per year, paid in accordance with the customary payroll practices of the Company subject to annual review and increase by the Board in its sole discretion (or by the Board's separately designated Compensation Committee in its sole discretion). For the avoidance of doubt, references to the Board in this Section 3 shall include the Board's separately designated Compensation Committee.

(b) Performance Bonus - Board of Directors' Discretion. The Executive shall be eligible to receive an annual bonus. The Board in its discretion will determine whether such annual bonus will be paid, the amount of such bonus and its form of payment. The Executive's target annual bonus amount is 120% of his Base Salary (the "Target Bonus"). If the Board determines in its discretion that the Executive's performance meets or exceeds the criteria established by the Board for the award of a Target Bonus, the Board may award the Executive the Target Bonus or a higher amount. Likewise, if the Executive's performance does not meet said criteria, the Board may award a lesser amount, or no bonus may be awarded. Unless otherwise provided in this Agreement, the Executive's eligibility to receive any bonus under this Section 3 (b) shall be expressly conditioned on, among other things, the Executive remaining employed with the Company up through any designated distribution date set by the Board.

(c) Equity Incentive Awards. Executive shall be eligible to receive grants of equity-based long-term incentive awards, which may include options to purchase Company stock, performance or restricted stock units and Company restricted stock contributions to Company's deferred compensation plan, or other equity-based awards. Such awards shall be determined in the discretion of the Board. In the event of a Change of Control (as defined in the Redwood Trust, Inc. Executive Deferred Compensation Plan) in which the surviving or acquiring corporation does not assume the Executive's outstanding equity-related awards (including options and equity-based awards granted both before and after the Effective Date) or substitute similar equity-related awards, such equity-related awards shall immediately vest and become exercisable if the Executive's service with the Company has not terminated before the effective date of the Change of Control; provided, however, that the foregoing provision shall only apply if the Company is not the surviving corporation or if shares of the Company's common stock are converted into or exchanged for other securities or cash.

(d) Annual Review. The Executive's performance shall be reviewed at least annually. The performance evaluations shall consider and assess the Executive's performance of his duties and responsibilities, the timely accomplishment of existing performance objectives, his level of efficiency and overall effectiveness and/or other factors or criteria that the Company, in its sole discretion, may deem relevant. The frequency of performance evaluations may vary depending upon, among other things, length of service, past performance, changes in job duties or performance levels. The Board shall, at least annually, review the Executive's entire compensation package to determine whether it continues to meet the Company's compensation objectives. Such annual review will include a determination of (i) whether to increase the Base Salary in accordance with Section 3(a); (ii) the incentive performance bonus to be awarded in accordance with Section 3(b); and (iii) the amount and type of any equity awards granted in accordance with Section 3(c). Positive performance evaluations do not guarantee salary increases or incentive bonuses. Salary increases and incentive bonus awards are solely within the discretion of the Board and may depend upon many factors other than the Executive's performance.

4. Fringe Benefits. The Executive shall be entitled to participate in any benefit programs adopted from time to time by the Company for the benefit of its senior executive employees, and the Executive shall be entitled to receive such other fringe benefits as may be granted to him from time to time by the Board.

(a) Benefit Plans. The Executive shall be entitled to participate in any benefit plans relating to equity-based compensation awards, pension, thrift, profit sharing, life insurance, medical coverage, education, deferred compensation, or other retirement or employee benefits available to other senior executive employees of the Company, subject to any restrictions (including waiting periods) specified in such plans and/or related individual agreements. The Company shall make commercially reasonable efforts to obtain medical and disability insurance, and such other forms of insurance as the Board shall from time to time determine, for its senior executive employees.

(b) Paid Time Off. The Executive shall be entitled to twenty-five (25) days of paid time off ("PTO") per calendar year pursuant to the Company's policies applicable to similarly situated employees of the Company, as in effect from time to time and consistent with the Executive's satisfactory performance of the duties set forth in Section 1; provided, however, that the Executive may only accrue up to a maximum of fifty (50) days of PTO. The Executive may use PTO for any reason, including vacation, sick time, personal time and family illness. Any vacation shall be taken at the reasonable and mutual convenience of the Company and the Executive.

5. Business Expenses. The Company shall reimburse the Executive for any and all necessary, customary and usual expenses, properly receipted in accordance with Company policies, incurred by Executive on behalf of the Company.

6. Termination of Executive's Employment.

(a) Death. If the Executive dies while employed by the Company, his employment shall immediately terminate. The Company's obligation to pay the Executive's Base Salary shall cease as of the date of the Executive's death, and any unpaid Base Salary shall be paid to the Executive's estate. In addition, within fifteen (15) days of the Executive's death, the Company shall pay to the Executive's estate an incentive performance bonus based on Executive's Target Bonus then in effect, prorated for the number of days of employment completed by the Executive during the year of his death. Executive's beneficiaries or his estate shall receive benefits in accordance with the Company's retirement, insurance and other applicable programs and plans then in effect. All stock options or other equity-related awards with time-based vesting, including deferred or restricted stock units, shall vest in full and, in the case of stock options, shall be exercisable for such period as set forth in the applicable award agreement by which such awards are evidenced. All stock options or other equity-related awards with performance-based vesting, including performance stock units, shall remain outstanding and shall continue to be eligible to vest and become payable based on the number of target shares and the performance goals set forth in the applicable award agreement by which such awards are evidenced, with any stock options remaining exercisable for such period as set forth in the applicable award agreement.

(b) Disability. If, as a result of the Executive's incapacity due to physical or mental illness ("Disability"), Executive shall have been absent from the full-time performance of his duties with the Company for six (6) consecutive months, and, within thirty (30) days after written notice is provided to him by the Company, he shall not have returned to the full-time performance of his duties, the Executive's employment under this Agreement may be terminated by the Company for Disability. During any period prior to such termination during which the Executive is absent from the full-time performance of his duties with the Company due to Disability, the Company shall continue to pay the Executive his Base Salary at the rate in effect at the commencement of such period of Disability. Subsequent to such termination, the Executive's benefits shall be determined under the Company's retirement, insurance and other compensation programs then in effect in accordance with the terms of such programs. In addition, within fifteen (15) days of such termination, the Company shall pay to the Executive an incentive performance bonus based on Executive's Target Bonus then in effect, prorated for the number of days of employment completed by the Executive during the year in which his employment terminated. The Executive, the Executive's beneficiaries or his estate shall receive benefits in accordance with the Company's retirement, insurance and other applicable programs and plans then in effect. All stock options or other equity-related awards with time-based vesting, including deferred or restricted stock units, shall vest in full and, in the case of stock options, shall be exercisable for such period as set forth in the applicable award agreement by which such awards are evidenced. All stock options or other equity-related awards with performance-based vesting, including performance stock units, shall remain outstanding and shall continue to be eligible to vest and become payable based on the number of target shares and the performance goals set forth in the applicable award agreement by which such awards are evidenced, with any stock options remaining exercisable for such period as set forth in the applicable award agreement.

(c) Termination By The Company For Cause. The Company may terminate the Executive's employment under this Agreement for Cause, at any time prior to expiration of the Term of the Agreement; provided, however, that prior to any termination of employment for Cause pursuant to subsection (i), (ii), or (iii) below, the Company must first provide written notice describing the reason for such termination of employment (and, with respect to subsections (ii) and (iii) below, such notice may be provided on the same date as the termination date). For purposes of this Agreement, "Cause" shall mean (i) the Executive's material failure to substantially perform the reasonable and lawful duties of his position for the Company, which failure shall continue for thirty (30) days after written notice thereof by the Company to the Executive; (ii) acts or omissions constituting gross negligence, recklessness or willful misconduct on the part of the Executive in respect of the performance of his duties hereunder, his fiduciary obligations or otherwise relating to the business of the Company; (iii) the habitual or repeated neglect of his duties by Executive; (iv) the Executive's conviction of a felony; (v) theft or embezzlement, or attempted theft or embezzlement, of money or tangible or intangible assets or property of the Company or its employees, customers, clients, or others having business relations with the Company; (vi) any act of moral turpitude by Executive injurious to the interest, property, operations, business or reputation of the Company; or (vii) unauthorized use or disclosure of trade secrets or confidential or proprietary information pertaining to Company business.

In the event of a termination under this Section 6(c), the Company will pay only the portion of Base Salary or previously awarded bonus unpaid as of the termination date. Fringe benefits which have accrued and/or vested on the termination date will continue in effect according to their terms.

(d) Termination By The Company Without Cause. The Company may terminate Executive's employment hereunder at any time without Cause upon 30 days written notice to Executive or pay in lieu thereof. In the event of a termination under this Section 6(d), the Executive shall be entitled to the benefits set forth in Section 7.

(e) Termination By The Executive For Good Reason. The Executive shall have the right to terminate this Agreement for Good Reason. For purposes of this Agreement, "Good Reason" shall mean the occurrence, without the Executive's express written consent, of any one or more of the following events:

(i) A material reduction in Executive's responsibilities; title, duties or authority;

(ii) A material reduction in the Executive's Base Salary or a material reduction by the Company in the value of the Executive's total compensation package (salary, bonus opportunity, equity incentive award opportunity and benefits) if such a reduction is not made in proportion to an across-the-board reduction for all senior executives of the Company;

(iii) The relocation of the Executive's principal Company office to a location more than twenty-five (25) miles from its location as of the Effective Date (which location is the Company's headquarters in Mill Valley, California) except for required travel on the Company's business to the extent necessary to fulfill the Executive's obligations under Section 1;

(iv) A failure at any time to renew this Agreement for successive one-year periods pursuant to Section 2;

(v) The complete liquidation of the Company; or

(vi) In the event of a merger, consolidation, transfer, or closing of a sale of all or substantially all the assets of the Company with or to any other individual or entity, the failure of the Company's successor to affirmatively adopt this Agreement or to otherwise comply with its obligations pursuant to Section 13 below.

Notwithstanding the foregoing, the Executive will not be deemed to have resigned for Good Reason for purposes of subclause (i) unless (1) the Executive provides the Company with written notice setting forth in reasonable detail the facts and circumstances claimed by the Executive to constitute Good Reason within ninety (90) days after the date of the occurrence of any event that the Executive knows or should reasonably have known to constitute Good Reason, (2) the Company fails to cure such acts or omissions within thirty (30) days following its receipt of such notice, and (3) the effective date of the Executive's termination for Good Reason occurs no later than thirty (30) days after the expiration of the Company's cure period. In the event of a termination under this Section 6(e), the Executive shall be entitled to the benefits set forth in Section 7.

(f) Termination By The Executive Without Good Reason. The Executive may at any time during the Term terminate his employment hereunder for any reason or no reason by giving the Company notice in writing not less than sixty (60) days in advance of such termination. The Executive shall have no further obligations to the Company after the effective date of termination, as set forth in the notice. In the event of a termination by the Executive under this Section 6(f), the Company will pay only the portion of Base Salary or previously awarded bonus unpaid as of the termination date. Fringe benefits which have accrued and/or vested on the termination date will continue in effect according to their terms.

7. Compensation Upon Termination By the Company without Cause or By The Executive for Good Reason.

(a) If the Executive's employment shall be terminated by the Company without Cause or by the Executive for Good Reason, the Executive shall be entitled to the following benefits:

(i) Payment of Unpaid Base Salary. The Company shall immediately pay the Executive any portion of the Executive's Base Salary through the date of termination or previously awarded bonus not paid prior to the termination date.

(ii) Severance Payment.

(A) In the event such termination is not a CIC Termination (as defined below), then the Company shall provide the Executive (x) an amount equal to two (2) times the Executive's Annual Base Salary as in effect immediately prior to his termination and (y) an amount equal to the Executive's Annual Base Salary in effect immediately prior to his termination prorated for the number of days of employment completed by the Executive during the year in which his employment is terminated.

(B) In the event such termination of employment occurs within three months prior to, on, or within 24 months following a Change of Control (a "CIC Termination"), then instead of providing the payments in Section 7(a)(ii)(A), the Company shall provide the Executive an amount equal to the sum of (x) the Executive's Target Bonus in effect immediately prior to his termination, prorated for the number of days of employment completed by the Executive during the year in which his employment terminated; (y) one (1) times the Executive's Annual Base Salary as in effect immediately prior to his termination; and (z) one (1) times the Executive's Target Bonus in effect immediately prior to his termination. Notwithstanding the foregoing, the maximum aggregate amount that the Company shall pay to the Executive pursuant to this Section 7(a)(ii)(B) is $1,750,000.

(iii) Equity Awards. All stock options or other equity-related awards with time-based vesting, including deferred or restricted stock units, shall vest in full and, in the case of stock options, shall be exercisable for such period as set forth in the applicable award agreement by which such awards are evidenced. If the Executive's employment shall be terminated by the Company without Cause, all stock options or other equity-related awards with performance-based vesting, including performance stock units, shall remain outstanding and shall continue to be eligible to vest and become payable or exercisable based on (x) the performance goals set forth in the applicable award agreement by which such awards are evidenced and (y) a reduced number of target shares adjusted on a pro-rata basis to reflect the number of days of employment completed during the applicable vesting period in which termination occurs, with any stock options remaining exercisable for such period as set forth in the applicable award agreement. If the Executive's employment shall be terminated by the Executive for Good Reason, all stock options or other equity-related awards with performance-based vesting, including performance stock units, shall remain outstanding and shall continue to be eligible to vest and become payable based on the number of target shares and the performance goals set forth in the applicable award agreement by which such awards are evidenced, with any stock options remaining exercisable for such period as set forth in the applicable award agreement.

(iv) Continuation of Fringe Benefits. For a period of up to twelve (12) months (or, in the event of a CIC Termination, twelve (12) months) following the date of Executive's termination of employment with Company, subject to the Executive's valid election to continue healthcare coverage under Section 4980B of the Internal Revenue Code of 1986, as amended (the "Code") and the regulations thereunder, the Company shall continue to provide the Executive and the Executive's eligible dependents with coverage under its group health plans at the same levels and the same cost to the Executive as would have applied if the Executive's employment had not been terminated based on the Employee's elections in effect on the date of termination (the "Continued Coverage"), provided that (1) if any plan pursuant to which such benefits are provided is not, or ceases prior to the expiration of the period of continuation coverage to be, exempt from the application of Section 409A of the Code under Treasury Regulation Section 1.409A-1(a)(5), or (2) the Company is otherwise unable to continue to cover the Executive under its group health plans without penalty under applicable law (including without limitation, Section 2716 of the Public Health Service Act or the Patient Protection and Affordable Care Act), the Company may in its sole discretion provide that (i) the Executive shall pay to the Company, on an after-tax basis, a monthly amount equal to the full premium cost of the Continued Coverage for such month and (ii) within 30 days of such premium payment, the Company shall reimburse the Executive in cash (less required withholding) an amount equal to the sum of (A) the excess of (x) the full premium cost of the Continued Coverage for such month over (y) any premium amount that would have been payable by the Executive if the Executive had been actively employed by the Company for such month and (B) an additional tax "gross up" payment to cover all estimated applicable local, state and federal income and payroll taxes imposed on the Executive with respect to the Continued Coverage. For the twelve (12) month (or, in the event of a CIC Termination, twelve (12) month) period following the termination of the Executive's employment, the Company shall also continue to provide the Executive with all life insurance, disability insurance and other fringe benefits set forth in Section 4 as if the Executive's employment under the Agreement had not been terminated; provided, however, that such life insurance, disability insurance and other fringe benefits shall cease as of the date the Executive receives such coverage from a subsequent employer.

(v) Payment/Benefit Limitation. If any payment or benefit due under this Agreement, together with all other payments and benefits that the Executive receives or is entitled to receive from the Company or any of its subsidiaries, affiliates or related entities, would (if paid or provided) constitute an "excess parachute payment" for purposes of Section 280G of the Code, the amounts otherwise payable and benefits otherwise due under this Agreement will either (i) be delivered in full, or (ii) be limited to the minimum extent necessary to ensure that no portion thereof will fail to be tax-deductible to the Company by reason of Section 280G of the Code (and therefore, no portion thereof will be subject to the excise tax imposed under Section 4999 of the Code), whichever of the foregoing amounts, taking into account applicable federal, state and local income and employment taxes and the excise tax imposed under Section 4999 of the Code, results in the receipt by the Executive, on an after-tax basis, of the greatest amount of payments and benefits, notwithstanding that all or some portion of such payments and/or benefits may be subject to the excise tax imposed under Section 4999 of the Code. Unless otherwise specified in writing by the Executive, in the event that the payments and/or benefits are to be reduced pursuant to this Section 7(a)(v), such payments and benefits shall be reduced such that the reduction of cash compensation to be provided to the Executive as a result of this Section 7 is minimized. In applying this principle, the reduction shall be made in a manner consistent with the requirements of Section 409A of the Code and where two economically equivalent amounts are subject to reduction but payable at different times, such amounts shall be reduced on a pro rata basis but not below zero. All determinations required to be made under this Section 7(a)(v) shall be made by the Company's independent public accounting firm (or such other nationally recognized public accounting firm as may be selected by the Company and to which selection the Executive consents (such consent not to be unreasonably withheld)) which shall provide detailed supporting calculations both to the Company and the Executive within fifteen (15) business days of the receipt of notice from the Executive that there has been a payment or benefit subject to this Section 7(a)(v), or such earlier time as is requested by the Company.

(b) No Mitigation Required; No Other Entitlement To Benefits Under Agreement. The Executive shall not be required in any way to mitigate the amount of any payment provided for in this Section 7, including, without limitation, by seeking other employment, nor shall the amount of any payment provided for in this Section 7 be reduced by any compensation earned by the Executive as the result of employment with another employer after the termination date of employment, or otherwise. Except as set forth in this Section 7, following a termination governed by this Section 7, the Executive shall not be entitled to any other compensation or benefits set forth in this Agreement, except as may be separately negotiated by the parties and approved the Board in writing in conjunction with the termination of Executive’s employment under this Section 7.

(c) Release Agreement. As a condition of receiving any of the payments, vesting and benefits set forth in this Section 7 (other than the payment provided for in sub-section 7(a)(i)), the Executive shall be required to execute a mutual release agreement in the form attached hereto as Exhibit A or Exhibit B, as appropriate, and such release agreement must have become effective in accordance with its terms within 60 days following the termination date. The Company, in its sole discretion, may modify the term of the required release agreement to comply with applicable law and may incorporate the required release agreement into a termination agreement or other agreement with the Executive

(d) Timing of Severance Payments. Notwithstanding any other provision of this Agreement, all severance payments provided under this Agreement in connection with the termination of the employment of the Executive shall be payable in an amount equal to 75% of such payments on the date that is six months after the termination date, and the remaining 25% shall be payable in six equal monthly installments beginning on the date that is seven months after the termination date and continuing on the same date of each of the five months thereafter.

(e) Timing of Bonus Payments. Notwithstanding any other provision of this Agreement, all bonus payments provided under this Agreement in connection with the termination of the employment of the Executive shall be payable on the date that is six months after the termination date.

8. Disputes Relating To Executive’s Termination of Employment For Good Reason. If the Executive resigns his employment with the Company alleging in good faith as the basis for such resignation “Good Reason” as defined in Section 6(e), and if the Company then disputes the Executive’s right to the payment of benefits under Section 7, the Company shall continue to pay the Executive the full compensation (including, without limitation, his Base Salary) in effect at the date the Executive provided written notice of such resignation, and the Company shall continue the Executive as a participant in all compensation, benefit and insurance plans in which the Executive was then a participant, until the earlier of the expiration of the Term or the date the dispute is finally resolved, either by mutual written agreement of the parties or by application of the provisions of Section 11. For the purposes of this Section 8, the Company shall bear the burden of proving that the grounds for the Executive's resignation do not fall within the scope of Section 6(e), and there shall be a rebuttable presumption that the Executive alleged such grounds in good faith.

9. Restrictive Covenant Provisions.

(a) Noncompetition. The Executive agrees that during the Term prior to any termination of his employment hereunder, he will not, directly or indirectly, without the prior written consent of a majority of the non-employee members of the Board, manage, operate, join, control, participate in, or be connected as a stockholder (other than as a holder of shares publicly traded on a stock exchange or the NASDAQ National Market System), partner, or other equity holder with, or as an officer, director or employee of, any real estate or mortgage investment organization whose business strategy is competitive with that of the Company, as determined by a majority of the non-employee members of the Board. It is further expressly agreed that the Company will or would suffer irreparable injury if the Executive were to compete with the Company or any subsidiary or affiliate of the Company in violation of this Agreement and that the Company would by reason of such competition be entitled to injunctive relief in a court of appropriate jurisdiction, and the Executive further consents and stipulates to the entry of such injunctive relief in such a court prohibiting the Executive from competing with the Company or any subsidiary or affiliate of the Company, in the areas of business set forth above, in violation of this Agreement.

(b) Duty To Avoid Conflict Of Interest. During his employment by the Company, Executive agrees not to engage or participate in, directly or indirectly, any activities in conflict with the best interests of the Company. The Company shall be the final decision-maker with regard to any conflict of interest issue.

(c) Right To Company Materials. The Executive agrees that all styles, designs, lists, materials, books, files, reports, correspondence, records, and other documents ("Company Materials") used, prepared, or made available to the Executive shall be and shall remain the property of the Company. Upon the termination of employment or the expiration of this Agreement, the Executive shall immediately return to the Company all Company Materials, and the Executive shall not make or retain any copies thereof.

(d) Nonsolicitation. The Executive promises and agrees that he will not directly or indirectly solicit any of the Company's employees to work for any competing real estate or mortgage investment organization as determined under Section 9 (a) for a period of one (1) year following the occurrence of any event entitling the Executive to payments and benefits, provided the Company makes all such payments when due according to the provisions herein.

(e) Confidential And Proprietary Information.

(1) It is hereby acknowledged that Executive has and shall gain knowledge of trade secrets and confidential information owned by or related to the Company and/or its affiliates including but not limited to the following: (i) the names, lists, buying habits and practices of customers, clients or vendors, (ii) marketing and related information, (iii) relationships with the persons or entities with whom or with which the Company has contracted, (iv) their products, designs, software, developments, improvements and methods of operation, (v) financial condition, profit performance and financial requirements, (vi) the compensation paid to employees, (vii) business plans and the information contained therein, and (viii) all other confidential information of, about or concerning the Company, the manner of operation of the Company and other confidential data of any kind, nature or description relating to the Company (collectively, the "Confidential Information"). Confidential Information does not include information which (A) is or becomes generally available to the public other than as a result of a disclosure by Executive; or (B) becomes available to Executive on a non-confidential basis after the termination or expiration of Executive's obligations under this Agreement from a source other than the Company, provided that such source is not bound by a confidentiality agreement with or other contractual, legal or fiduciary obligation of confidentiality to the Company or any other party with respect to such information; or (C) is independently developed after the termination or expiration of

Executive's obligations under this agreement without reference to the Confidential Information, provided such independent development can reasonably be proven by Executive by written records.

(2) The parties hereby acknowledge that the Confidential Information constitutes important, unique, material and confidential trade secrets which affect the successful activities of the Company, and constitute a substantial part of the assets and goodwill of the Company. In view of the foregoing, Executive agrees that he will not at any time whether during or after the term of this Agreement, except as required in the course of Executive's employment by Company and at its direction and for its sole benefit, in any fashion, form or manner, directly or indirectly (i) use or divulge, disclose, communicate or provide or permit access to any person, firm, partnership, corporation or other entity, any Confidential Information of any kind, nature or description, or (ii) remove from Company's premises any notes or records relating thereto, or copies or facsimiles thereof (whether made by electronic, electrical, magnetic, optical, laser, acoustic or other means).

(3) Promptly upon the request of Company, and immediately upon the termination of Executive's employment, Executive shall not transfer to any third person and shall deliver to Company all Confidential Information, and other property belonging to the Company, including all copies thereof, in the possession or under the control of the Executive.

(4) Executive represents that the performance of all the terms of this Agreement will not conflict with, and will not breach, any other invention assignment agreement, confidentiality agreement, employment agreement or non-competition agreement to which Executive is or has been a party. To the extent that Executive has confidential information or materials of any former employer, Executive acknowledges that the Company has directed Executive to not disclose such confidential information or materials to the Company or any of its employees, and that the Company prohibits Executive from using said confidential information or materials in any work that Executive may perform for the Company. Executive agrees that Executive will not bring with Executive to the Company, and will not use or disclose any confidential, proprietary information, or trade secrets acquired by Executive prior to his employment with the Company. Executive will not disclose to the Company or any of its employees, or induce the Company or any of its employees to use, any confidential or proprietary information or material belonging to any previous employers or others, nor will Executive bring to the Company or use in connection with Executive's work for the Company copies of any software, computer files, or any other copyrighted or trademarked materials except those owned by or licensed to the Company. Executive represents that he is not a party to any other agreement that will interfere with his full compliance with this Agreement. Executive further agrees not to enter into any agreement, whether written or oral, in conflict with the provisions of this Agreement.

(5) Notwithstanding the generality of the foregoing, nothing in this Agreement is intended to prohibit the Executive from filing a charge with, reporting possible violations to, or participating or cooperating with the Securities and Exchange Commission or any other federal, state or local regulatory body or law enforcement agency, including in relation to any whistleblower, anti-discrimination, or anti-retaliation provisions of federal, state or local law or regulation. Pursuant to 18 U.S.C. Section 1833(b), the Executive will not be held criminally or civilly liable under any federal or state trade secret law for the disclosure of a trade secret that is made: (x) in confidence to a federal, state or local government official, either directly or indirectly, or to an attorney, and solely for the purpose of reporting or investigating a suspected violation of law; or (y) in a complaint or other document filed in a lawsuit or other proceeding, if such filing is made under seal.

(f) Inventions. Any and all inventions, discoveries or improvements that Executive has conceived or made or may conceive or make during the period of employment relating to or in any way pertaining to or connected with the systems, products, computer programs, software, apparatus or methods employed, manufactured or constructed by the Company or to systems, products, apparatus or methods with respect to which the Company engages in, requests or anticipates research or development, shall be promptly and fully disclosed and described by Executive to the Company and shall be the sole and exclusive property of the Company, and Executive shall assign, and hereby does assign to the Company Executive's entire right, title and interest in and to all such inventions, discoveries or improvements as well as any modifications or improvements thereto that may be made.

The obligations outlined in this Section 9(f) do not apply to any invention that qualifies fully under California Labor Code Section 2870 (a copy of which is attached hereto as Exhibit C) or to any rights Executive may have acquired in connection with an invention, discovery or improvement that was developed entirely on Executive's own time for which no equipment, supplies, facilities or trade secret information of the Company was used and (a) that does not relate directly or indirectly to the business of the Company or to the Company's actual or demonstrable anticipated research or development, or (b) that does not result from any work performed by Executive for the Company.

(g) Maryland Law. The Executive agrees, in accordance with Maryland law, to first offer to the Company corporate opportunities learned of solely as a result of his service as an officer of the Company.

(h) Breach. It is expressly agreed that each breach of this Section 9 is a distinct and material breach of this Agreement and that solely a monetary remedy would be inadequate, impracticable and extremely difficult to prove, and that each such breach would cause the Company irreparable harm. It is further agreed that, in addition to any and all remedies available at law or equity (including money damages), either party shall be entitled to temporary and permanent injunctive relief to enforce the provisions of this Section, without the necessity of proving actual damages. It is further agreed that either party shall be entitled to seek such equitable relief in any forum, including a court of law, notwithstanding the provisions of Section 11. Either party may pursue any of the remedies described herein concurrently or consecutively in any order as to any such breach or violation, and the pursuit of one of such remedies at any time will not be deemed an election of remedies or waiver of the right to pursue any of the other such remedies. Any breach of this Section 9 shall immediately terminate any obligations by the Company to provide Executive with severance and continued benefits pursuant to Section 6 or 7 of this Agreement.

(i) Unenforceability. Should any portion of this Section 9 be deemed unenforceable because of its scope, duration or effect, and only in such event, then the parties expressly consent and agree to such limitation on scope, duration or effect as may be finally adjudicated as enforceable, to give this Section 9 its maximum permissible scope, duration and effect.

10. Notices. All notices and other communications under this Agreement shall be in writing and shall be given by fax or first class mail, certified or registered with return receipt requested, and shall be deemed to have been duly given three (3) days after mailing or twenty-four (24) hours after transmission of a fax to the respective persons named below:

If to the Company: Redwood Trust, Inc.
Attn: Chief Executive Officer
One Belvedere Place, Suite 300
Mill Valley, CA 94941
Phone: (415) 389-7373
Fax: (415) 381-1773

If to the Executive: Andrew P. Stone
c/o Redwood Trust, Inc.
One Belvedere Place, Suite 300
Mill Valley, CA 94941
Phone: (415) 389-7373
Fax: (415) 381-1773

Either party may change such party’s address for notices by notice duly given pursuant hereto.

11. Resolution of Disputes. To ensure the rapid and economical resolution of disputes that may arise in connection with the Executive’s employment with the Company, the Executive and the Company agree that any and all disputes, claims, or causes of action, in law or equity, arising from or relating to the enforcement, breach, performance, or interpretation of this Agreement, the Executive’s employment, or the termination of the Executive’s employment (“Arbitrable Claims”) shall be submitted to confidential mediation in San Francisco, California conducted by a mutually agreeable mediator from Judicial Arbitration and Mediation Services (“JAMS”) or its successor under the JAMS Rules of Practice and Procedure then in effect, which can be found at www.jamsadr.com/adr-rules-procedures. The cost of JAMS’ mediation fees shall be paid by the Company. In the event that mediation is unsuccessful in resolving the Arbitrable Claims, the Arbitrable Claims shall be resolved, to the fullest extent permitted by law, by final, binding and confidential arbitration in San Francisco, California conducted by JAMS or its successor, under the then applicable rules of JAMS.

The Executive acknowledges that by agreeing to this arbitration procedure, both the Executive and the Company waive the right to resolve any such dispute through a trial by jury or judge or administrative proceeding.

The arbitrator shall: (a) have the authority to compel adequate discovery for the resolution of the dispute and to award such relief as would otherwise be permitted by law; and (b) issue a written arbitration decision including the arbitrator’s essential findings and conclusions and a statement of the award. The arbitrator shall be authorized to award any or all remedies that the Executive or the Company would be entitled to seek in a court of law, including, without limitation, the award of attorneys’ fees based on a determination of the extent to which each party has prevailed as to the material issues raised in determination of the dispute. The Company shall pay all JAMS’ arbitration fees in excess of those which would be required if the dispute were decided in a court of law. Nothing in this Agreement is intended to prevent either the Executive or the Company from obtaining injunctive relief in court to prevent irreparable harm pending the conclusion of any such mediation or arbitration.

12. [Reserved]

13. Assignment; Successors. This Agreement is personal in its nature, and neither of the parties hereto shall, without the consent of the other, assign or transfer this Agreement or any rights or obligations hereunder; provided, however, that, in the event of the merger, consolidation, transfer, or sale of all or substantially all of the assets of the Company with or to any other individual or entity, this Agreement shall, subject to the provisions hereof, be binding upon and inure to the benefit of such successor and such successor shall discharge and perform all the promises, covenants, duties, and obligations of the Company hereunder.

14. Governing Law. This Agreement and the legal relations thus created between the parties hereto shall be governed by and construed under and in accordance with the laws of the State of California.

15. Entire Agreement; Headings. This Agreement embodies the entire agreement of the parties with respect to the subject matter hereof and supersedes in their entirety all other or prior agreements, whether oral or written, with respect thereto, including but not limited to the Prior Agreement, but excluding the plans, programs and equity award agreements under which compensation and benefits are provided pursuant to Sections 3 and 4 hereof to the extent such plans and programs and equity award agreements are not inconsistent with this Agreement. Section headings in this Agreement are included herein for convenience of reference only and shall not constitute a part of this Agreement for any other purpose.

16. Waiver; Modification. Failure to insist upon strict compliance with any of the terms, covenants, or conditions hereof shall not be deemed a waiver of such term, covenant, or condition, nor shall any waiver or relinquishment of, or failure to insist upon strict compliance with, any right or power hereunder at any one or more times be deemed a waiver or relinquishment of such right or power at any other time or times. This Agreement shall not be modified in any respect except by a writing executed by each party hereto.

17. Severability. In the event that a court of competent jurisdiction determines that any portion of this Agreement is in violation of any statute or public policy, only the portions of this Agreement that violate such statute or public policy shall be stricken. All portions of this Agreement that do not violate any statute or public policy shall continue in full force and effect. Further, any court order striking any portion of this Agreement shall modify the stricken terms as narrowly as possible to give as much effect as possible to the intentions of the parties under this Agreement.

18. Indemnification. The Company shall indemnify and hold Executive harmless to the maximum extent permitted by Section 2-418 of the Maryland General Corporations Law or its successor statute, or if greater, by the Company's Bylaws, by any applicable resolution of the Board or by the terms providing the most extensive indemnification contained in any written agreement between the Company and any director or officer of the Company. The Company shall make Executive a named beneficiary under all director and officer liability policies maintained by the Company from time to time for the benefit of its directors and officers, entitled to all benefits provided thereunder to persons serving in a comparable role as an officer of the Company.

19. Section 409A. Any payments under this Agreement subject to Section 409A of the Code that are subject to execution of a waiver and release which may be executed and/or revoked in a calendar year following the calendar year in which the payment event (such as a termination of employment) occurs shall commence payment only in the calendar year in which the consideration period or, if applicable, release revocation period ends, as necessary to comply with Section 409A of the Code. Notwithstanding anything to the contrary in this Agreement, no compensation or benefits shall be paid to the Executive during the six (6)-month period following the Executive's "separation from service" from the Company (within the meaning of Section 409A of the Code, a "Separation from Service") if the Company determines that paying such amounts at the time or times indicated in this Agreement would be a prohibited distribution under Section 409A(a)(2)(B)(i) of the Code. If the payment of any such amounts is delayed as a result of the previous sentence, then on the first day of the seventh month following the date of Separation from Service (or such earlier date upon which such amount can be paid under Section 409A without resulting in a prohibited distribution, including as a result of the Executive's death), the Company shall pay the Executive a lump-sum amount equal to the cumulative amount that would have otherwise been payable to the Executive during such period. Any right to a series of installment payments pursuant to this Agreement is to be treated as a right to a series of separate payments. To the extent permitted under Section 409A of the Code, any separate payment or benefit under this Agreement or otherwise shall not be deemed "nonqualified deferred compensation" subject to Section 409A of the Code to the extent provided in the exceptions in Treasury Regulation Section 1.409A-1(b)(4), Section 1.409A-1(b)(9) or any other applicable exception or provision of Section 409A. All payments of nonqualified deferred compensation subject to Section 409A to be made upon a termination of employment under this Agreement may only be made upon the Executive's "separation from service" from the Company

20. Counterparts. This Agreement may be executed in several counterparts, each of which shall be deemed to be an original but all of which together will constitute one and the same instrument.

21. Successor Sections. References herein to sections or rules of the Code shall be deemed to include any successor sections or rules.

[*Signature Page Follows*]

IN WITNESS WHEREOF, the Company has caused this Agreement to be executed by its duly authorized officer, and the Executive has hereunto signed this Agreement, as of the Effective Date.

REDWOOD TRUST, INC.

By: /s/ Christopher J. Abate

Christopher J. Abate
Chief Executive Officer

EXECUTIVE

/s/ Andrew P. Stone

Andrew P. Stone

EXHIBIT A
RELEASE AGREEMENT

Except as otherwise set forth in this Release Agreement or in Sections 7 and 18 of the Employment Agreement between Andrew P. Stone and Redwood Trust, Inc., Andrew P. Stone ("Executive") hereby generally and completely releases the Company and its directors, officers, employees, shareholders, partners, agents, attorneys, predecessors, successors, parent and subsidiary entities, insurers, affiliates, and assigns from any and all claims, liabilities and obligations, both known and unknown, that arise out of or are in any way related to events, acts, conduct, or omissions occurring at any time prior to and including the date Executive signs this Release Agreement. The Company, its directors, officers, employees, shareholders, partners, agents, attorneys, predecessors, successors, parent and subsidiary entities, insurers, affiliates, and assigns, hereby releases Executive and his heirs, executors, successors and assigns, from any and all claims, liabilities and obligations, both known and unknown, that arise out of or are in any way related to events, acts, conduct, or omissions occurring at any time prior to and including the date the Company signs this Release Agreement. This general mutual release includes, but is not limited to: (A) all claims arising out of or in any way related to Executive's employment with the Company or the termination of that employment; (B) all claims related to Executive's compensation or benefits from the Company, including salary, bonuses, commissions, vacation pay, expense reimbursements, severance pay, fringe benefits, stock, stock options, or any other ownership interests in the Company; (C) all claims for breach of contract, wrongful termination, and breach of the implied covenant of good faith and fair dealing; (D) all tort claims, including claims for fraud, defamation, emotional distress, and discharge in violation of public policy; (E) all federal, state, and local statutory claims, including claims for discrimination, harassment, retaliation, attorneys' fees, or other claims arising under the federal Civil Rights Act of 1964 (as amended), the federal Americans with Disabilities Act of 1990, the federal Age Discrimination in Employment Act of 1967 (as amended) ("ADEA"), the federal Employee Retirement Income Security Act of 1974 (as amended), and the California Fair Employment and Housing Act (as amended); and (F) all claims and rights with respect to Executive's right to communicate directly with, cooperate with, or provide information to, any federal, state or local government regulator; provided, however, that nothing in this paragraph shall be construed in any way to release the Company from its obligation to indemnify Executive pursuant to agreement, the Company's bylaws or binding resolutions, or applicable law.

Executive acknowledges that he is knowingly and voluntarily waiving and releasing any rights he may have under the ADEA, and that the consideration given under his Employment Agreement with the Company for the waiver and release in the preceding paragraph hereof is in addition to anything of value to which he was already entitled. Executive further acknowledges

that he has been advised by this writing, as required by the ADEA, that: (A) this waiver and release does not apply to any rights or claims that may arise after the date Executive signs this Release Agreement; (B) Executive should consult with an attorney prior to signing this Release Agreement (although Executive may choose voluntarily not do so); (C) Executive has twenty-one (21) days to consider this Release Agreement (although Executive may choose voluntarily to sign this Release Agreement earlier); (D) Executive has seven (7) days following the date that he signs this Release Agreement to revoke the Release Agreement by providing written notice to an officer of the Company; and (E) this Release Agreement shall not be effective until the date upon which the revocation period has expired, which shall be the eighth day after Executive signs this Release Agreement. Both Executive and the Company acknowledge that each has read and understands Section 1542 of the California Civil Code which reads as follows:

A general release does not extend to claims that the creditor or releasing party does not know or suspect to exist in his or her favor at the time of executing the release and that, if known by him or her, would have materially affected his or her settlement with the debtor or released party.

Both Executive and the Company hereby expressly waive and relinquish all rights and benefits under that section and any law of any jurisdiction of similar effect with respect to each party's release of any claims hereunder.

Notwithstanding anything herein, the Executive acknowledges and agrees that, pursuant to 18 USC Section 1833(b), the Executive will not be held criminally or civilly liable under any federal or state trade secret law for the disclosure of a trade secret that is made: (i) in confidence to a federal, state, or local government official, either directly or indirectly, or to an attorney, and solely for the purpose of reporting or investigating a suspected violation of law; or (ii) in a complaint or other document filed in a lawsuit or other proceeding, if such filing is made under seal.

Mutual Nondisparagement.

(a) Nondisparagement by Executive. At all times following the cessation of the Executive's employment with the Company, the Executive agrees not to make negative comments or statements about, or otherwise criticize or disparage, in any format or through any medium, the Company or any entity controlled by, controlling or under common control with the Company ("Affiliates") or any of the officers, directors, managers, employees, services, operations, investments or products of the Company or any of its Affiliates. For purposes of the foregoing sentence, disparagement shall include, but not be limited to, negative comments or statements intended or reasonably likely to be harmful or disruptive to a person's or entity's respective business, business reputation, business operations, or personal reputation.

(b) Nondisparagement by Designated Company Representatives. At all times following the cessation of the Executive's employment with the Company, the Company agrees not to publish, and agrees to cause the Designated Company Representatives not to make, negative comments or statements about, or otherwise criticize or disparage, in any format or through any medium, the Executive. For purposes of the foregoing sentence, disparagement shall include, but not be limited to, negative comments or statements intended or reasonably likely to be harmful or disruptive to a person's business reputation or personal reputation. For purposes of this sub-section (b), the "Designated Company Representatives" are (i) all executive officers of the Company while serving in such capacity and (ii) all members of the Board of Directors while serving in such capacity.

(c) The foregoing sub-sections (a) and (b) shall not be violated by truthful comments or statements (i) made in response to legal process, in required governmental testimony or filings, in judicial, administrative or arbitral proceedings (including, without limitation, depositions in connection with such proceedings), in compliance with law, administrative rule, or regulation, or made pursuant to a court or administrative order, or in connection with reporting possible violations of federal law or regulation to any governmental agency or entity, or making other disclosures that are protected under the whistleblower provisions of federal law or regulation, (ii) made by members of the Board of Directors in the course of meetings or discussions of the Board of Directors (or any committee thereof) or in communications between members of the Board of Directors and the Executive, and not disclosed to the public, (iii) made by a member of the Board of Directors in the good faith belief that the statements are required for the proper discharge of his or her fiduciary duties, or (iv) made by the Board of Directors in connection with a termination of the Executive for Cause.

[*Signature Page Follows*]

IN WITNESS WHEREOF, the Company has caused this Agreement to be executed by its duly authorized officer, and the Executive has hereunto signed this Agreement, as of the date set forth below.

EXECUTIVE

Name: ______________________________
Andrew P. Stone

Date: ______________________________

COMPANY

Name: ______________________________

Date: ______________________________

EXHIBIT B
RELEASE AGREEMENT

Except as otherwise set forth in this Release Agreement or in Sections 7 and 18 of the Employment Agreement between Andrew P. Stone and Redwood Trust, Inc., Andrew P. Stone ("Executive") hereby generally and completely releases the Company and its directors, officers, employees, shareholders, partners, agents, attorneys, predecessors, successors, parent and subsidiary entities, insurers, affiliates, and assigns from any and all claims, liabilities and obligations, both known and unknown, that arise out of or are in any way related to events, acts, conduct, or omissions occurring at any time prior to and including the date Executive signs this Release Agreement. The Company, its directors, officers, employees, shareholders, partners, agents, attorneys, predecessors, successors, parent and subsidiary entities, insurers, affiliates, and assigns, hereby releases Executive and his heirs, executors, successors and assigns, from any and all claims, liabilities and obligations, both known and unknown, that arise out of or are in any way related to events, acts, conduct, or omissions occurring at any time prior to and including the date the Company signs this Release Agreement. This general mutual release includes, but is not limited to: (A) all claims arising out of or in any way related to Executive's employment with the Company or the termination of that employment; (B) all claims related to Executive's compensation or benefits from the Company, including salary, bonuses, commissions, vacation pay, expense reimbursements, severance pay, fringe benefits, stock, stock options, or any other ownership interests in the Company; (C) all claims for breach of contract, wrongful termination, and breach of the implied covenant of good faith and fair dealing; (D) all tort claims, including claims for fraud, defamation, emotional distress, and discharge in violation of public policy; (E) all federal, state, and local statutory claims, including claims for discrimination, harassment, retaliation, attorneys' fees, or other claims arising under the federal Civil Rights Act of 1964 (as amended), the federal Americans with Disabilities Act of 1990, the federal Age Discrimination in Employment Act of 1967 (as amended) ("ADEA"), the federal Employee Retirement Income Security Act of 1974 (as amended), and the California Fair Employment and Housing Act (as amended); and (F) all claims and rights with respect to Executive's right to communicate directly with, cooperate with, or provide information to, any federal, state or local government regulator; provided, however, that nothing in this paragraph shall be construed in any way to release the Company from its obligation to indemnify Executive pursuant to agreement, the Company's bylaws or binding resolutions, or applicable law.

Executive acknowledges that he is knowingly and voluntarily waiving and releasing any rights he may have under the ADEA, and that the consideration given under his Employment Agreement with the Company for the waiver and release in the preceding paragraph hereof is in addition to anything of value to which he was already entitled. Executive further acknowledges

that he has been advised by this writing, as required by the ADEA, that: (A) this waiver and release does not apply to any rights or claims that may arise after the date Executive signs this Release Agreement; (B) Executive should consult with an attorney prior to signing this Release Agreement (although Executive may choose voluntarily not do so); (C) Executive has forty-five (45) days to consider this Release Agreement (although he may choose voluntarily to sign this Release Agreement earlier); (D) Executive has seven (7) days following the date that he signs this Release Agreement to revoke the Release Agreement by providing written notice to an officer of the Company; (E) this Release Agreement shall not be effective until the date upon which the revocation period has expired, which shall be the eighth day after Executive signs this Release Agreement; and (F) Executive has received with this Release Agreement a detailed list of the job titles and ages of all employees who were terminated in this group termination and the ages of all employees of the Company in the same job classification or organizational unit who were not terminated.

Both the Executive and the Company acknowledge that each has read and understands Section 1542 of the California Civil Code which reads as follows:

A general release does not extend to claims that the creditor or releasing party does not know or suspect to exist in his or her favor at the time of executing the release and that, if known by him or her, would have materially affected his or her settlement with the debtor or released party.

Both the Executive and the Company hereby expressly waive and relinquish all rights and benefits under that section and any law of any jurisdiction of similar effect with respect to each party's release of any claims hereunder.

Notwithstanding anything herein, the Executive acknowledges and agrees that, pursuant to 18 USC Section 1833(b), the Executive will not be held criminally or civilly liable under any federal or state trade secret law for the disclosure of a trade secret that is made: (i) in confidence to a federal, state, or local government official, either directly or indirectly, or to an attorney, and solely for the purpose of reporting or investigating a suspected violation of law; or (ii) in a complaint or other document filed in a lawsuit or other proceeding, if such filing is made under seal.

Mutual Nondisparagement.

(a) Nondisparagement by Executive. At all times following the cessation of the Executive's employment with the Company, the Executive agrees not to make negative comments or statements about, or otherwise criticize or disparage, in any format or through any medium, the Company or any entity controlled by, controlling or under common control with the Company ("Affiliates") or any of the officers, directors, managers, employees, services, operations, investments or products of the Company or any of its Affiliates. For purposes of the foregoing sentence, disparagement shall include, but not be limited to, negative comments or statements intended or reasonably likely to be harmful or disruptive to a person's or entity's respective business, business reputation, business operations, or personal reputation.

(b) Nondisparagement by Designated Company Representatives. At all times following the cessation of the Executive's employment with the Company, the Company agrees not to publish, and agrees to cause the Designated Company Representatives not to make, negative comments or statements about, or otherwise criticize or disparage, in any format or through any medium, the Executive. For purposes of the foregoing sentence, disparagement shall include, but not be limited to, negative comments or statements intended or reasonably likely to be harmful or disruptive to a person's business reputation or personal reputation. For purposes of this sub-section (b), the "Designated Company Representatives" are (i) all executive officers of the Company while serving in such capacity and (ii) all members of the Board of Directors while serving in such capacity.

(c) The foregoing sub-sections (a) and (b) shall not be violated by truthful comments or statements (i) made in response to legal process, in required governmental testimony or filings, in judicial, administrative or arbitral proceedings (including, without limitation, depositions in connection with such proceedings), in compliance with law, administrative rule, or regulation, or made pursuant to a court or administrative order, or in connection with reporting possible violations of federal law or regulation to any governmental agency or entity, or making other disclosures that are protected under the whistleblower provisions of federal law or regulation, (ii) made by members of the Board of Directors in the course of meetings or discussions of the Board of Directors (or any committee thereof) or in communications between members of the Board of Directors and the Executive, and not disclosed to the public, (iii) made by a member of the Board of Directors in the good faith belief that the statements are required for the proper discharge of his or her fiduciary duties, or (iv) made by the Board of Directors in connection with a termination of the Executive for Cause.

[*Signature Page Follows*]

IN WITNESS WHEREOF, the Company has caused this Agreement to be executed by its duly authorized officer, and the Executive has hereunto signed this Agreement, as of the date set forth below.

EXECUTIVE

Name: ______________________________
Andrew P. Stone

Date: ______________________________

COMPANY

Name: ______________________________

Date: ______________________________

EXHIBIT C
Section 2870 of California Labor Code

Section 2870 of California Labor Code: Application of provision providing that employee shall assign or offer to assign rights in invention to employer.

a. Any provision and employment agreement which provides that an employee shall assign, or offer to assign, any of his or her rights in an invention to his or her employer shall not apply to an invention that the employee developed entirely on his or her own time without using the employer's equipment, supplies, facilities or trade secret information except for those inventions that either:

1. Relate at the time of conception or reduction to practice of the invention to the employer's business, or actual or demonstrably anticipated research or development of the employer; or

2. Result from any work performed by the employee for the employer.

b. To the extent a provision in an employment agreement purports to require an employee to assign an invention otherwise excluded from being required to be assigned under subdivision (a), the provision is against the public policy of this state and is unenforceable.

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Section 4: EX-10.3 (EXHIBIT 10.3)

EXHIBIT 10.3

FIRST AMENDED AND RESTATED EMPLOYMENT AGREEMENT

This Amended and Restated Employment Agreement ("Agreement"), effective as of May 7, 2019 (the "Effective Date"), is entered into by and between **Dashiell I. Robinson** (the "Executive") and **Redwood Trust, Inc.,** a Maryland corporation (the "Company"), and amends and restates in its entirety that certain Employment Agreement by and between the Executive and the Company dated as of August 8, 2017, which became effective as of September 28, 2017 (as subsequently amended, the "Prior Agreement").

The Company desires to establish its right to the continued services of the Executive, in the capacity, on the terms and conditions, and subject to the rights of termination hereinafter set forth, and the Executive is willing to accept such continued employment in such capacity, on such terms and conditions, and subject to such rights of termination.

In consideration of the mutual agreements hereinafter set forth, the Executive and the Company have agreed and do hereby agree as follows:

1. Employment and Responsibilities. During the Term, the Executive shall serve as President of the Company, reporting to the Chief Executive Officer of the Company or his designee, with responsibilities, duties and authority customary for such position, including, without limitation, business and strategic development and implementation, as well as management and oversight of the Chief Investment Officer and the Chief Financial Officer (with the Chief Investment Officer and Chief Financial Officer reporting directly to the Executive). The Executive does hereby accept and agree to such continued employment. The Chief Executive Officer may, from time to time, in his sole discretion, modify, reassign and/or augment the Executive's responsibilities, subject to approval by the Board of Directors of the Company (the "Board"), and any such modification, reassignment and/or augmentation shall be deemed a waiver by the Executive of his rights under Section 6(e)(i) hereof only with his express written consent. Any such modification, reassignment or augmentation of responsibilities shall be in writing. The Executive shall devote such time, energy and skill to the performance of his duties for the Company and for the benefit of the Company as may be necessary or required for the effective conduct and operation of the Company's business. Furthermore, the Executive shall act only in good faith and exercise due diligence and care in the performance of his duties to the Company under this Agreement.

2. Term of Agreement. The term of this Agreement (the "Term") shall commence on the Effective Date and shall continue through December 31, 2019; provided, however, that (i) on January 1, 2020 and each succeeding January 1, the Term shall automatically be extended for one additional year unless, not later than three months prior to any such January 1, either party shall have given written notice to the other that it does not wish to extend the Term and (ii) such one year extensions of the Term shall not occur on and after the January 1 of the year in which the Executive will attain age sixty-five (65) but instead the Term shall be extended only until the date of the Executive's sixty-fifth (65th) birthday.

3. Compensation.

(a) Base Salary. The Company shall pay the Executive, and the Executive agrees to accept from the Company, in payment for his services to the Company a base salary (the "Base Salary") at the rate of $600,000 per year, paid in accordance with the customary payroll practices of the Company subject to annual review and increase by the Board in its sole discretion (or by the Board's separately designated Compensation Committee in its sole discretion). For the avoidance of doubt, references to the Board in this Section 3 shall include the Board's separately designated Compensation Committee.

(b) Performance Bonus - Board of Directors' Discretion. The Executive shall be eligible to receive an annual bonus. The Board in its discretion will determine whether such annual bonus will be paid, the amount of such bonus and its form of payment. The Executive's target annual bonus amount is 165% of his Base Salary (the "Target Bonus"). If the Board determines in its discretion that the Executive's performance meets or exceeds the criteria established by the Board for the award of a Target Bonus, the Board may award the Executive the Target Bonus or a higher amount. Likewise, if the Executive's performance does not meet said criteria, the Board may award a lesser amount, or no bonus may be awarded. Unless otherwise provided in this Agreement, the Executive's eligibility to receive any bonus under this Section 3(b) shall be expressly conditioned on, among other things, the Executive remaining employed with the Company up through any designated distribution date set by the Board.

(c) Equity Incentive Awards. Executive shall be eligible to receive grants of equity-based long-term incentive awards, which may include options to purchase Company stock, performance or restricted stock units and Company restricted stock contributions to Company's deferred compensation plan, or other equity-based awards. Such awards shall be determined in the discretion of the Board. In the event of a Change of Control (as defined in the Redwood Trust, Inc. Executive Deferred Compensation Plan) in which the surviving or acquiring corporation does not assume the Executive's outstanding equity-related awards (including options and equity-based awards granted both before and after the Effective Date) or substitute similar equity-related awards, such equity-related awards shall immediately vest and become exercisable if the Executive's service with the Company has not terminated before the effective date of the Change of Control; provided, however, that the foregoing provision shall only apply if the Company is not the surviving corporation or if shares of the Company's common stock are converted into or exchanged for other securities or cash.

(d) Annual Review. The Executive's performance shall be reviewed at least annually. The performance evaluations shall consider and assess the Executive's performance of his duties and responsibilities, the timely accomplishment of existing performance objectives, his level of efficiency and overall effectiveness and/or other factors or criteria that the Company, in its sole discretion, may deem relevant. The frequency of performance evaluations may vary depending upon, among other things, length of service, past performance, changes in job duties or performance levels. The Board shall, at least annually, review the Executive's entire compensation package to determine whether it continues to meet the Company's compensation objectives. Such annual review will include a determination of (i) whether to increase the Base Salary in accordance with Section 3(a); (ii) the incentive performance bonus to be awarded in accordance with Section 3(b); and (iii) the amount and type of any equity awards granted in accordance with Section 3(c). Positive performance evaluations do not guarantee salary increases or incentive bonuses. Salary increases and incentive bonus awards are solely within the discretion of the Board and may depend upon many factors other than the Executive's performance.

4. Fringe Benefits. The Executive shall be entitled to participate in any benefit programs adopted from time to time by the Company for the benefit of its senior executive employees, and the Executive shall be entitled to receive such other fringe benefits as may be granted to him from time to time by the Board.

(a) Benefit Plans. The Executive shall be entitled to participate in any benefit plans relating to equity-based compensation awards, pension, thrift, profit sharing, life insurance, medical coverage, education, deferred compensation, or other retirement or employee benefits available to other senior executive employees of the Company, subject to any restrictions (including waiting periods) specified in such plans and/or related individual agreements. The Company shall make commercially reasonable efforts to obtain medical and disability insurance, and such other forms of insurance as the Board shall from time to time determine, for its senior executive employees.

(b) Paid Time Off. The Executive shall be entitled to twenty-five (25) days of paid time off (“PTO”) per calendar year pursuant to the Company’s policies applicable to similarly situated employees of the Company, as in effect from time to time and consistent with the Executive’s satisfactory performance of the duties set forth in Section 1; provided, however, that the Executive may only accrue up to a maximum of fifty (50) days of PTO. The Executive may use PTO for any reason, including vacation, sick time, personal time and family illness. Any vacation shall be taken at the reasonable and mutual convenience of the Company and the Executive.

5. Business Expenses. The Company shall reimburse the Executive for any and all necessary, customary and usual expenses, properly receipted in accordance with Company policies, incurred by Executive on behalf of the Company.

6. Termination of Executive’s Employment.

(a) Death. If the Executive dies while employed by the Company, his employment shall immediately terminate. The Company’s obligation to pay the Executive’s Base Salary shall cease as of the date of the Executive’s death, and any unpaid Base Salary shall be paid to the Executive’s estate. In addition, within fifteen (15) days of the Executive’s death, the Company shall pay to the Executive’s estate an incentive performance bonus based on Executive’s Target Bonus then in effect, prorated for the number of days of employment completed by the Executive during the year of his death. Executive’s beneficiaries or his estate shall receive benefits in accordance with the Company’s retirement, insurance and other applicable programs and plans then in effect. All stock options or other equity-related awards with time-based vesting, including deferred or restricted stock units, shall vest in full and, in the case of stock options, shall be exercisable for such period as set forth in the applicable award agreement by which such awards are evidenced. All stock options or other equity-related awards with performance-based vesting, including performance stock units, shall remain outstanding and shall continue to be eligible to vest and become payable based on the number of target shares and the performance goals set forth in the applicable award agreement by which such awards are evidenced, with any stock options remaining exercisable for such period as set forth in the applicable award agreement.

(b) Disability. If, as a result of the Executive’s incapacity due to physical or mental illness (“Disability”), Executive shall have been absent from the full-time performance of his duties with the Company for six (6) consecutive months, and, within thirty (30) days after written notice is provided to him by the Company, he shall not have returned to the full-time performance of his duties, the Executive’s employment under this Agreement may be terminated by the Company for Disability. During any period prior to such termination during which the Executive is absent from the full-time performance of his duties with the Company due to Disability, the Company shall continue to pay the Executive his Base Salary at the rate in effect at the commencement of such period of Disability. Subsequent to such termination, the Executive’s benefits shall be determined under the Company’s retirement, insurance and other compensation programs then in effect in accordance with the terms of such programs. In addition, within fifteen (15) days of such termination, the Company shall pay to the Executive an incentive performance bonus based on Executive’s Target Bonus then in effect, prorated for the number of days of employment completed by the Executive during the year in which his employment terminated. The Executive, the Executive’s beneficiaries or his estate shall receive benefits in accordance with the Company’s retirement, insurance and other applicable programs and plans then in effect. All stock options or other equity-related awards with time-based vesting, including deferred or restricted stock units, shall vest in full and, in the case of stock options, shall be exercisable for such period as set forth in the applicable award agreement by which such awards are evidenced. All stock options or other equity-related awards with performance-based vesting, including performance stock units, shall remain outstanding and shall continue to be eligible to vest and become payable based on the number of target shares and the performance goals set forth in the applicable award agreement by which such awards are evidenced, with any stock options remaining exercisable for such period as set forth in the applicable award agreement.

(c) Termination By The Company For Cause. The Company may terminate the Executive's employment under this Agreement for Cause, at any time prior to expiration of the Term of the Agreement; provided, however, that prior to any termination of employment for Cause pursuant to subsection (i), (ii), or (iii) below, the Company must first provide written notice describing the reason for such termination of employment (and, with respect to subsections (ii) and (iii) below, such notice may be provided on the same date as the termination date). For purposes of this Agreement, "Cause" shall mean (i) the Executive's material failure to substantially perform the reasonable and lawful duties of his position for the Company, which failure shall continue for thirty (30) days after written notice thereof by the Company to the Executive; (ii) acts or omissions constituting gross negligence, recklessness or willful misconduct on the part of the Executive in respect of the performance of his duties hereunder, his fiduciary obligations or otherwise relating to the business of the Company; (iii) the habitual or repeated neglect of his duties by Executive; (iv) the Executive's conviction of a felony; (v) theft or embezzlement, or attempted theft or embezzlement, of money or tangible or intangible assets or property of the Company or its employees, customers, clients, or others having business relations with the Company; (vi) any act of moral turpitude by Executive injurious to the interest, property, operations, business or reputation of the Company; or (vii) unauthorized use or disclosure of trade secrets or confidential or proprietary information pertaining to Company business.

In the event of a termination under this Section 6(c), the Company will pay only the portion of Base Salary or previously awarded bonus unpaid as of the termination date. Fringe benefits which have accrued and/or vested on the termination date will continue in effect according to their terms.

(d) Termination By The Company Without Cause. The Company may terminate Executive's employment hereunder at any time without Cause upon 30 days written notice to Executive or pay in lieu thereof. In the event of a termination under this Section 6(d), the Executive shall be entitled to the benefits set forth in Section 7.

(e) Termination By The Executive For Good Reason. The Executive shall have the right to terminate this Agreement for Good Reason. For purposes of this Agreement, "Good Reason" shall mean the occurrence, without the Executive's express written consent, of any one or more of the following events:

(i) A material reduction in Executive's responsibilities, title, duties or authority;

(ii) A material reduction in the Executive's Base Salary or a material reduction by the Company in the value of the Executive's total compensation package (salary, bonus opportunity, equity incentive award opportunity and benefits) if such a reduction is not made in proportion to an across-the-board reduction for all senior executives of the Company;

(iii) The relocation of the Executive's principal Company office to a location more than twenty-five (25) miles from its location as of the Effective Date (which location is the Company's headquarters in Mill Valley, California), except for required travel on the Company's business to the extent necessary to fulfill the Executive's obligations under Section 1;

(iv) A failure at any time to renew this Agreement for successive one-year periods pursuant to Section 2;

(v) The complete liquidation of the Company;

(vi) In the event of a merger, consolidation, transfer, or closing of a sale of all or substantially all the assets of the Company with or to any other individual or entity, the failure of the Company's successor to affirmatively adopt this Agreement or to otherwise comply with its obligations pursuant to Section 13 below; or

(vii) As set forth in Section 6(i) of that certain letter agreement between the Company and the Executive dated August 8, 2017 (the "Side Letter").

Notwithstanding the foregoing, the Executive will not be deemed to have resigned for Good Reason for purposes of subclause (i) unless (1) the Executive provides the Company with written notice setting forth in reasonable detail the facts and circumstances claimed by the Executive to constitute Good Reason within ninety (90) days after the date of the occurrence of any event that the Executive knows or should reasonably have known to constitute Good Reason, (2) the Company fails to cure such acts or omissions within thirty (30) days following its receipt of such notice, and (3) the effective date of the Executive's termination for Good Reason occurs no later than thirty (30) days after the expiration of the Company's cure period. In the event of a termination under this Section 6(e), the Executive shall be entitled to the benefits set forth in Section 7.

(f) Termination By The Executive Without Good Reason. The Executive may at any time during the Term terminate his employment hereunder for any reason or no reason by giving the Company notice in writing not less than sixty (60) days in advance of such termination. The Executive shall have no further obligations to the Company after the effective date of termination, as set forth in the notice. In the event of a termination by the Executive under this Section 6(f), the Company will pay only the portion of Base Salary or previously awarded bonus unpaid as of the termination date. Fringe benefits which have accrued and/or vested on the termination date will continue in effect according to their terms.

7. Compensation Upon Termination By the Company without Cause or By The Executive for Good Reason.

(a) If the Executive's employment shall be terminated by the Company without Cause or by the Executive for Good Reason, the Executive shall be entitled to the following benefits:

(i) Payment of Unpaid Base Salary. The Company shall immediately pay the Executive any portion of the Executive's Base Salary through the date of termination or previously awarded bonus not paid prior to the termination date.

(ii) Severance Payment.

(A) In the event such termination is not a CIC Termination (as defined below), then the Company shall provide the Executive (x) an amount equal to two (2) times the Executive's Annual Base Salary as in effect immediately prior to his termination and (y) an amount equal to the Executive's Annual Base Salary in effect immediately prior to his termination, pro-rated for the number of days of employment completed by the Executive during the year in which his employment is terminated.

(B) In the event such termination of employment occurs within three months prior to, on, or within 24 months following a Change of Control (a "CIC Termination"), then instead of providing the payments in Section 7(a)(ii)(A), the Company shall provide the Executive an amount equal to the sum of (x) the Executive's Target Bonus in effect immediately prior to his termination, prorated for the number of days of employment completed by the Executive during the year in which his employment terminated; (y) one-and-one-half (1.5) times the Executive's Annual Base Salary as in effect immediately prior to his termination; and (z) one-and-one-half (1.5) times the Executive's Target Bonus in effect immediately prior to his termination. Notwithstanding the foregoing, the maximum aggregate amount that the Company shall pay to the Executive pursuant to this Section 7(a)(ii)(B) is $4,000,000.

(iii) Equity Awards. All stock options or other equity-related awards with time-based vesting, including deferred or restricted stock units, shall vest in full and, in the case of stock options, shall be exercisable for such period as set forth in the applicable award agreement by which such awards are evidenced. If the Executive's employment shall be terminated by the Company without Cause, all stock options or other equity-related awards with performance-based vesting, including performance stock units, shall remain outstanding and shall continue to be eligible to vest and become payable or exercisable based on (x) the performance goals set forth in the applicable award agreement by which such awards are evidenced and (y) a reduced number of target shares adjusted on a pro-rata basis to reflect the number of days of employment completed during the applicable vesting period in which termination occurs, with any stock options remaining exercisable for such period as set forth in the applicable award agreement. If the Executive's employment shall be terminated by the Executive for Good Reason, all stock options or other equity-related awards with performance-based vesting, including performance stock units, shall remain outstanding and shall continue to be eligible to vest and become payable based on the number of target shares and the performance goals set forth in the applicable award agreement by which such awards are evidenced, with any stock options remaining exercisable for such period as set forth in the applicable award agreement.

(iv) Continuation of Fringe Benefits. For a period of up to twelve (12) months (or, in the event of a CIC Termination, eighteen (18) months) following the date of Executive's termination of employment with Company, subject to the Executive's valid election to continue healthcare coverage under Section 4980B of the Internal Revenue Code of 1986, as amended (the "Code") and the regulations thereunder, the Company shall continue to provide the Executive and the Executive's eligible dependents with coverage under its group health plans at the same levels and the same cost to the Executive as would have applied if the Executive's employment had not been terminated based on the Employee's elections in effect on the date of termination (the "Continued Coverage"), provided that (1) if any plan pursuant to which such benefits are provided is not, or ceases prior to the expiration of the period of continuation coverage to be, exempt from the application of Section 409A of the Code under Treasury Regulation Section 1.409A-1(a)(5), or (2) the Company is otherwise unable to continue to cover the Executive under its group health plans without penalty under applicable law (including without limitation, Section 2716 of the Public Health Service Act or the Patient Protection and Affordable Care Act), the Company may in its sole discretion provide that (i) the Executive shall pay to the Company, on an after-tax basis, a monthly amount equal to the full premium cost of the Continued Coverage for such month and (ii) within 30 days of such premium payment, the Company shall reimburse the Executive in cash (less required withholding) an amount equal to the sum of (A) the excess of (x) the full premium cost of the Continued Coverage for such month over (y) any premium amount that would have been payable by the Executive if the Executive had been actively employed by the Company for such month and (B) an additional tax "gross up" payment to cover all estimated applicable local, state and federal income and payroll taxes imposed on the Executive with respect to the Continued Coverage. For the twelve (12) month (or, in the event of a CIC Termination, eighteen (18) month) period following the termination of the Executive's employment, the Company shall also continue to provide the Executive with all life insurance, disability insurance and other fringe benefits set forth in Section 4 as if the Executive's employment under the Agreement had not been terminated; provided, however, that such life insurance, disability insurance and other fringe benefits shall cease as of the date the Executive receives such coverage from a subsequent employer.

(v) **Payment/Benefit Limitation**. If any payment or benefit due under this Agreement, together with all other payments and benefits that the Executive receives or is entitled to receive from the Company or any of its subsidiaries, affiliates or related entities, would (if paid or provided) constitute an "excess parachute payment" for purposes of Section 280G of the Code, the amounts otherwise payable and benefits otherwise due under this Agreement will either (i) be delivered in full, or (ii) be limited to the minimum extent necessary to ensure that no portion thereof will fail to be tax-deductible to the Company by reason of Section 280G of the Code (and therefore, no portion thereof will be subject to the excise tax imposed under Section 4999 of the Code), whichever of the foregoing amounts, taking into account applicable federal, state and local income and employment taxes and the excise tax imposed under Section 4999 of the Code, results in the receipt by the Executive, on an after-tax basis, of the greatest amount of payments and benefits, notwithstanding that all or some portion of such payments and/or benefits may be subject to the excise tax imposed under Section 4999 of the Code. Unless otherwise specified in writing by the Executive, in the event that the payments and/or benefits are to be reduced pursuant to this Section 7(a)(v), such payments and benefits shall be reduced such that the reduction of cash compensation to be provided to the Executive as a result of this Section 7 is minimized. In applying this principle, the reduction shall be made in a manner consistent with the requirements of Section 409A of the Code and where two economically equivalent amounts are subject to reduction but payable at different times, such amounts shall be reduced on a pro rata basis but not below zero. All determinations required to be made under this Section 7(a)(v) shall be made by the Company's independent public accounting firm (or such other nationally recognized public accounting firm as may be selected by the Company and to which selection the Executive consents (such consent not to be unreasonably withheld)) which shall provide detailed supporting calculations both to the Company and the Executive within fifteen (15) business days of the receipt of notice from the Executive that there has been a payment or benefit subject to this Section 7(a)(v), or such earlier time as is requested by the Company.

(b) No Mitigation Required; No Other Entitlement To Benefits Under Agreement. The Executive shall not be required in any way to mitigate the amount of any payment provided for in this Section 7, including, without limitation, by seeking other employment, nor shall the amount of any payment provided for in this Section 7 be reduced by any compensation earned by the Executive as the result of employment with another employer after the termination date of employment, or otherwise. Except as set forth in this Section 7, following a termination governed by this Section 7, the Executive shall not be entitled to any other compensation or benefits set forth in this Agreement, except as may be separately negotiated by the parties and approved the Board in writing in conjunction with the termination of Executive's employment under this Section 7.

(c) Release Agreement. As a condition of receiving any of the payments, vesting and benefits set forth in this Section 7 (other than the payment provided for in sub-section 7(a)(i)), the Executive shall be required to execute a mutual release agreement in the form attached hereto as Exhibit A or Exhibit B, as appropriate, and such release agreement must have become effective in accordance with its terms within 60 days following the termination date. The Company, in its sole discretion, may modify the term of the required release agreement to comply with applicable law and may incorporate the required release agreement into a termination agreement or other agreement with the Executive.

(d) Timing of Severance Payments. Notwithstanding any other provision of this Agreement, all severance payments provided under this Agreement in connection with the termination of the employment of the Executive shall be payable in an amount equal to 75% of such payments on the date that is six months after the termination date, and the remaining 25% shall be payable in six equal monthly installments beginning on the date that is seven months after the termination date and continuing on the same date of each of the five months thereafter.

(e) Timing of Bonus Payments. Notwithstanding any other provision of this Agreement, all bonus payments provided under this Agreement in connection with the termination of the employment of the Executive shall be payable on the date that is six months after the termination date.

8. Disputes Relating To Executive's Termination of Employment For Good Reason. If the Executive resigns his employment with the Company alleging in good faith as the basis for such resignation "Good Reason" as defined in Section 6(e), and if the Company then disputes the Executive's right to the payment of benefits under Section 7, the Company shall continue to pay the Executive the full compensation (including, without limitation, his Base Salary) in effect at the date the Executive provided written notice of such resignation, and the Company shall continue the Executive as a participant in all compensation, benefit and insurance plans in which the Executive was then a participant, until the earlier of the expiration of the Term or the date the dispute is finally resolved, either by mutual written agreement of the parties or by application of the provisions of Section 11. For the purposes of this Section 8, the Company shall bear the burden of proving that the grounds for the Executive's resignation do not fall within the scope of Section 6(e), and there shall be a rebuttable presumption that the Executive alleged such grounds in good faith.

9. Restrictive Covenant Provisions.

(a) Noncompetition. The Executive agrees that during the Term prior to any termination of his employment hereunder, he will not, directly or indirectly, without the prior written consent of a majority of the non-employee members of the Board, manage, operate, join, control, participate in, or be connected as a stockholder (other than as a holder of shares publicly traded on a stock exchange or the NASDAQ National Market System), partner, or other equity holder with, or as an officer, director or employee of, any real estate or mortgage investment organization whose business strategy is competitive with that of the Company, as determined by a majority of the non-employee members of the Board. It is further expressly agreed that the Company will or would suffer irreparable injury if the Executive were to compete with the Company or any subsidiary or affiliate of the Company in violation of this Agreement and that the Company would by reason of such competition be entitled to injunctive relief in a court of appropriate jurisdiction, and the Executive further consents and stipulates to the entry of such injunctive relief in such a court prohibiting the Executive from competing with the Company or any subsidiary or affiliate of the Company, in the areas of business set forth above, in violation of this Agreement.

(b) Duty To Avoid Conflict Of Interest. During his employment by the Company, Executive agrees not to engage or participate in, directly or indirectly, any activities in conflict with the best interests of the Company. The Company shall be the final decision-maker with regard to any conflict of interest issue.

(c) Right To Company Materials. The Executive agrees that all styles, designs, lists, materials, books, files, reports, correspondence, records, and other documents ("Company Materials") used, prepared, or made available to the Executive shall be and shall remain the property of the Company. Upon the termination of employment or the expiration of this Agreement, the Executive shall immediately return to the Company all Company Materials, and the Executive shall not make or retain any copies thereof.

(d) Nonsolicitation. The Executive promises and agrees that he will not directly or indirectly solicit any of the Company's employees to work for any competing real estate or mortgage investment organization as determined under Section 9 (a) for a period of one (1) year following the occurrence of any event entitling the Executive to payments and benefits, provided the Company makes all such payments when due according to the provisions herein.

(e) Confidential And Proprietary Information.

(1) It is hereby acknowledged that Executive has and shall gain knowledge of trade secrets and confidential information owned by or related to the Company and/or its affiliates including but not limited to the following: (i) the names, lists, buying habits and practices of customers, clients or vendors, (ii) marketing and related information, (iii) relationships with the persons or entities with whom or with which the Company has contracted, (iv) their products, designs, software, developments, improvements and methods of operation, (v) financial condition, profit performance and financial requirements, (vi) the compensation paid to employees, (vii) business plans and the information contained therein, and (viii) all other confidential information of, about or concerning the Company, the manner of operation of the Company and other confidential data of any kind, nature or description relating to the Company (collectively, the “Confidential Information”). Confidential Information does not include information which (A) is or becomes generally available to the public other than as a result of a disclosure by Executive; or (B) becomes available to Executive on a non-confidential basis after the termination or expiration of Executive’s obligations under this Agreement from a source other than the Company, provided that such source is not bound by a confidentiality agreement with or other contractual, legal or fiduciary obligation of confidentiality to the Company or any other party with respect to such information; or (C) is independently developed after the termination or expiration of Executive’s obligations under this agreement without reference to the Confidential Information, provided such independent development can reasonably be proven by Executive by written records.

(2) The parties hereby acknowledge that the Confidential Information constitutes important, unique, material and confidential trade secrets which affect the successful activities of the Company, and constitute a substantial part of the assets and goodwill of the Company. In view of the foregoing, Executive agrees that he will not at any time whether during or after the term of this Agreement, except as required in the course of Executive’s employment by Company and at its direction and for its sole benefit, in any fashion, form or manner, directly or indirectly (i) use or divulge, disclose, communicate or provide or permit access to any person, firm, partnership, corporation or other entity, any Confidential Information of any kind, nature or description, or (ii) remove from Company’s premises any notes or records relating thereto, or copies or facsimiles thereof (whether made by electronic, electrical, magnetic, optical, laser, acoustic or other means).

(3) Promptly upon the request of Company, and immediately upon the termination of Executive’s employment, Executive shall not transfer to any third person and shall deliver to Company all Confidential Information, and other property belonging to the Company, including all copies thereof, in the possession or under the control of the Executive.

(4) Executive represents that the performance of all the terms of this Agreement will not conflict with, and will not breach, any other invention assignment agreement, confidentiality agreement, employment agreement or non-competition agreement to which Executive is or has been a party. To the extent that Executive has confidential information or materials of any former employer, Executive acknowledges that the Company has directed Executive to not disclose such confidential information or materials to the Company or any of its employees, and that the Company prohibits Executive from using said confidential information or materials in any work that Executive may perform for the Company. Executive agrees that Executive will not bring with Executive to the Company, and will not use or disclose any confidential, proprietary information, or trade secrets acquired by Executive prior to his employment with the Company. Executive will not disclose to the Company or any of its employees, or induce the Company or any of its employees to use, any confidential or proprietary information or material belonging to any previous employers or others, nor will Executive bring to the Company or use in connection with Executive’s work for the Company copies of any software, computer files, or any other copyrighted or trademarked materials except those owned by or licensed to the Company. Executive represents that he is not a party to any other agreement that will interfere with his full compliance with this Agreement. Executive further agrees not to enter into any agreement, whether written or oral, in conflict with the provisions of this Agreement.

(5) Notwithstanding the generality of the foregoing, nothing in this Agreement is intended to prohibit the Executive from filing a charge with, reporting possible violations to, or participating or cooperating with the Securities and Exchange Commission or any other federal, state or local regulatory body or law enforcement agency, including in relation to any whistleblower, anti-discrimination, or anti-retaliation provisions of federal, state or local law or regulation. Pursuant to 18 U.S.C. Section 1833(b), the Executive will not be held criminally or civilly liable under any federal or state trade secret law for the disclosure of a trade secret that is made: (x) in confidence to a federal, state or local government official, either directly or indirectly, or to an attorney, and solely for the purpose of reporting or investigating a suspected violation of law; or (y) in a complaint or other document filed in a lawsuit or other proceeding, if such filing is made under seal.

(f) Inventions. Any and all inventions, discoveries or improvements that Executive has conceived or made or may conceive or make during the period of employment relating to or in any way pertaining to or connected with the systems, products, computer programs, software, apparatus or methods employed, manufactured or constructed by the Company or to systems, products, apparatus or methods with respect to which the Company engages in, requests or anticipates research or development, shall be promptly and fully disclosed and described by Executive to the Company and shall be the sole and exclusive property of the Company, and Executive shall assign, and hereby does assign to the Company Executive's entire right, title and interest in and to all such inventions, discoveries or improvements as well as any modifications or improvements thereto that may be made.

The obligations outlined in this Section 9(f) do not apply to any invention that qualifies fully under California Labor Code Section 2870 (a copy of which is attached hereto as Exhibit C) or to any rights Executive may have acquired in connection with an invention, discovery or improvement that was developed entirely on Executive's own time for which no equipment, supplies, facilities or trade secret information of the Company was used and (a) that does not relate directly or indirectly to the business of the Company or to the Company's actual or demonstrable anticipated research or development, or (b) that does not result from any work performed by Executive for the Company.

(g) Maryland Law. The Executive agrees, in accordance with Maryland law, to first offer to the Company corporate opportunities learned of solely as a result of his service as an officer of the Company.

(h) Breach. It is expressly agreed that each breach of this Section 9 is a distinct and material breach of this Agreement and that solely a monetary remedy would be inadequate, impracticable and extremely difficult to prove, and that each such breach would cause the Company irreparable harm. It is further agreed that, in addition to any and all remedies available at law or equity (including money damages), either party shall be entitled to temporary and permanent injunctive relief to enforce the provisions of this Section, without the necessity of proving actual damages. It is further agreed that either party shall be entitled to seek such equitable relief in any forum, including a court of law, notwithstanding the provisions of Section 11. Either party may pursue any of the remedies described herein concurrently or consecutively in any order as to any such breach or violation, and the pursuit of one of such remedies at any time will not be deemed an election of remedies or waiver of the right to pursue any of the other such remedies. Any breach of this Section 9 shall immediately terminate any obligations by the Company to provide Executive with severance and continued benefits pursuant to Section 6 or 7 of this Agreement.

(i) Unenforceability. Should any portion of this Section 9 be deemed unenforceable because of its scope, duration or effect, and only in such event, then the parties expressly consent and agree to such limitation on scope, duration or effect as may be finally adjudicated as enforceable, to give this Section 9 its maximum permissible scope, duration and effect.

10. Notices. All notices and other communications under this Agreement shall be in writing and shall be given by fax or first class mail, certified or registered with return receipt requested, and shall be deemed to have been duly given three (3) days after mailing or twenty-four (24) hours after transmission of a fax to the respective persons named below:

If to the Company:	Redwood Trust, Inc. Attn: Chief Executive Officer One Belvedere Place, Suite 300 Mill Valley, CA 94941 Phone: (415) 389-7373 Fax: (415) 381-1773
If to the Executive:	Dashiell I. Robinson c/o Redwood Trust, Inc. One Belvedere Place, Suite 300 Mill Valley, CA 94941 Phone: (415) 389-7373 Fax: (415) 381-1773

Either party may change such party's address for notices by notice duly given pursuant hereto.

11. Resolution of Disputes. To ensure the rapid and economical resolution of disputes that may arise in connection with the Executive's employment with the Company, the Executive and the Company agree that any and all disputes, claims, or causes of action, in law or equity, arising from or relating to the enforcement, breach, performance, or interpretation of this Agreement, the Executive's employment, or the termination of the Executive's employment ("Arbitrable Claims") shall be submitted to confidential mediation in San Francisco, California conducted by a mutually agreeable mediator from Judicial Arbitration and Mediation Services ("JAMS") or its successor under the JAMS Rules of Practice and Procedure then in effect, which can be found at www.jamsadr.com/adr-rules-procedures. The cost of JAMS' mediation fees shall be paid by the Company. In the event that mediation is unsuccessful in resolving the Arbitrable Claims, the Arbitrable Claims shall be resolved, to the fullest extent permitted by law, by final, binding and confidential arbitration in San Francisco, California conducted by JAMS or its successor, under the then applicable rules of JAMS.

The Executive acknowledges that by agreeing to this arbitration procedure, both the Executive and the Company waive the right to resolve any such dispute through a trial by jury or judge or administrative proceeding.

The arbitrator shall: (a) have the authority to compel adequate discovery for the resolution of the dispute and to award such relief as would otherwise be permitted by law; and (b) issue a written arbitration decision including the arbitrator's essential findings and conclusions and a statement of the award. The arbitrator shall be authorized to award any or all remedies that the Executive or the Company would be entitled to seek in a court of law, including, without limitation, the award of attorneys' fees based on a determination of the extent to which each party has prevailed as to the material issues raised in determination of the dispute. The Company shall pay all JAMS' arbitration fees in excess of those which would be required if the dispute were decided in a court of law. Nothing in this Agreement is intended to prevent either the Executive or the Company from obtaining injunctive relief in court to prevent irreparable harm pending the conclusion of any such mediation or arbitration.

12. [Reserved]

13. Assignment; Successors. This Agreement is personal in its nature, and neither of the parties hereto shall, without the consent of the other, assign or transfer this Agreement or any rights or obligations hereunder; provided, however, that, in the event of the merger, consolidation, transfer, or sale of all or substantially all of the assets of the Company with or to any other individual or entity, this Agreement shall, subject to the provisions hereof, be binding upon and inure to the benefit of such successor and such successor shall discharge and perform all the promises, covenants, duties, and obligations of the Company hereunder.

14. Governing Law. This Agreement and the legal relations thus created between the parties hereto shall be governed by and construed under and in accordance with the laws of the State of California.

15. Entire Agreement; Headings. This Agreement, together with the Side Letter, embodies the entire agreement of the parties with respect to the subject matter hereof and supersedes in their entirety all other or prior agreements, whether oral or written, with respect thereto, including but not limited to the Prior Agreement, but excluding the plans, programs and equity award agreements under which compensation and benefits are provided pursuant to Sections 3 and 4 hereof to the extent such plans and programs and equity award agreements are not inconsistent with this Agreement. Section headings in this Agreement are included herein for convenience of reference only and shall not constitute a part of this Agreement for any other purpose.

16. Waiver; Modification. Failure to insist upon strict compliance with any of the terms, covenants, or conditions hereof shall not be deemed a waiver of such term, covenant, or condition, nor shall any waiver or relinquishment of, or failure to insist upon strict compliance with, any right or power hereunder at any one or more times be deemed a waiver or relinquishment of such right or power at any other time or times. This Agreement shall not be modified in any respect except by a writing executed by each party hereto.

17. Severability. In the event that a court of competent jurisdiction determines that any portion of this Agreement is in violation of any statute or public policy, only the portions of this Agreement that violate such statute or public policy shall be stricken. All portions of this Agreement that do not violate any statute or public policy shall continue in full force and effect. Further, any court order striking any portion of this Agreement shall modify the stricken terms as narrowly as possible to give as much effect as possible to the intentions of the parties under this Agreement.

18. Indemnification. The Company shall indemnify and hold Executive harmless to the maximum extent permitted by Section 2-418 of the Maryland General Corporations Law or its successor statute, or if greater, by the Company's Bylaws, by any applicable resolution of the Board or by the terms providing the most extensive indemnification contained in any written agreement between the Company and any director or officer of the Company. The Company shall make Executive a named beneficiary under all director and officer liability policies maintained by the Company from time to time for the benefit of its directors and officers, entitled to all benefits provided thereunder to persons serving in a comparable role as an officer of the Company.

19. Section 409A. Any payments under this Agreement subject to Section 409A of the Code that are subject to execution of a waiver and release which may be executed and/or revoked in a calendar year following the calendar year in which the payment event (such as a termination of employment) occurs shall commence payment only in the calendar year in which the consideration period or, if applicable, release revocation period ends, as necessary to comply with Section 409A of the Code. Notwithstanding anything to the contrary in this Agreement, no compensation or benefits shall be paid to the Executive during the six (6)-month period following the Executive's "separation from service" from the Company (within the meaning of Section 409A of the Code, a "Separation from Service") if the Company determines that paying such amounts at the time or times indicated in this Agreement would be a prohibited distribution under Section 409A(a)(2)(B)(i) of the Code. If the payment of any such amounts is delayed as a result of the previous sentence, then on the first day of the seventh month following the date of Separation from Service (or such earlier date upon which such amount can be paid under Section 409A without resulting in a prohibited distribution, including as a result of the Executive's death), the Company shall pay the Executive a lump-sum amount equal to the cumulative amount that would have otherwise been payable to the Executive during such period. Any right to a series of installment payments pursuant to this Agreement is to be treated as a right to a series of separate payments. To the extent permitted under Section 409A of the Code, any separate payment or benefit under this Agreement or otherwise shall not be deemed "nonqualified deferred compensation" subject to Section 409A of the Code to the extent provided in the exceptions in Treasury Regulation Section 1.409A-1(b)(4), Section 1.409A-1(b)(9) or any other applicable exception or provision of Section 409A. All payments of nonqualified deferred compensation subject to Section 409A to be made upon a termination of employment under this Agreement may only be made upon the Executive's "separation from service" from the Company.

20. Counterparts. This Agreement may be executed in several counterparts, each of which shall be deemed to be an original but all of which together will constitute one and the same instrument.

21. Successor Sections. References herein to sections or rules of the Code shall be deemed to include any successor sections or rules.

[*Signature Page Follows*]

IN WITNESS WHEREOF, the Company has caused this Agreement to be executed by its duly authorized officer, and the Executive has hereunto signed this Agreement, as of the Effective Date.

REDWOOD TRUST, INC.

By: /s/ Christopher J. Abate

Christopher J. Abate
Chief Executive Officer

EXECUTIVE

/s/ Dashiell I. Robinson

Dashiell I. Robinson

EXHIBIT A
RELEASE AGREEMENT

Except as otherwise set forth in this Release Agreement or in Sections 7 and 18 of the Employment Agreement between Dashiell I. Robinson and Redwood Trust, Inc., Dashiell I. Robinson ("Executive") hereby generally and completely releases the Company and its directors, officers, employees, shareholders, partners, agents, attorneys, predecessors, successors, parent and subsidiary entities, insurers, affiliates, and assigns from any and all claims, liabilities and obligations, both known and unknown, that arise out of or are in any way related to events, acts, conduct, or omissions occurring at any time prior to and including the date Executive signs this Release Agreement. The Company, its directors, officers, employees, shareholders, partners, agents, attorneys, predecessors, successors, parent and subsidiary entities, insurers, affiliates, and assigns, hereby releases Executive and his heirs, executors, successors and assigns, from any and all claims, liabilities and obligations, both known and unknown, that arise out of or are in any way related to events, acts, conduct, or omissions occurring at any time prior to and including the date the Company signs this Release Agreement. This general mutual release includes, but is not limited to: (A) all claims arising out of or in any way related to Executive's employment with the Company or the termination of that employment; (B) all claims related to Executive's compensation or benefits from the Company, including salary, bonuses, commissions, vacation pay, expense reimbursements, severance pay, fringe benefits, stock, stock options, or any other ownership interests in the Company; (C) all claims for breach of contract, wrongful termination, and breach of the implied covenant of good faith and fair dealing; (D) all tort claims, including claims for fraud, defamation, emotional distress, and discharge in violation of public policy; (E) all federal, state, and local statutory claims, including claims for discrimination, harassment, retaliation, attorneys' fees, or other claims arising under the federal Civil Rights Act of 1964 (as amended), the federal Americans with Disabilities Act of 1990, the federal Age Discrimination in Employment Act of 1967 (as amended) ("ADEA"), the federal Employee Retirement Income Security Act of 1974 (as amended), and the California Fair Employment and Housing Act (as amended); and (F) all claims and rights with respect to Executive's right to communicate directly with, cooperate with, or provide information to, any federal, state or local government regulator; provided, however, that nothing in this paragraph shall be construed in any way to release the Company from its obligation to indemnify Executive pursuant to agreement, the Company's bylaws or binding resolutions, or applicable law.

Executive acknowledges that he is knowingly and voluntarily waiving and releasing any rights he may have under the ADEA, and that the consideration given under his Employment Agreement with the Company for the waiver and release in the preceding paragraph hereof is in addition to anything of value to which he was already entitled. Executive further acknowledges that he has been advised by this writing, as required by the ADEA, that: (A) this waiver and release does not apply to any rights or claims that may arise after the date Executive signs this Release Agreement; (B) Executive should consult with an attorney prior to signing this Release Agreement (although Executive may choose voluntarily not do so); (C) Executive has twenty-one (21) days to consider this Release Agreement (although Executive may choose voluntarily to sign this Release Agreement earlier); (D) Executive has seven (7) days following the date that he signs this Release Agreement to revoke the Release Agreement by providing written notice to an officer of the Company; and (E) this Release Agreement shall not be effective until the date upon which the revocation period has expired, which shall be the eighth day after Executive signs this Release Agreement. Both Executive and the Company acknowledge that each has read and understands Section 1542 of the California Civil Code which reads as follows:

A general release does not extend to claims that the creditor or releasing party does not know or suspect to exist in his or her favor at the time of executing the release and that, if known by him or her, would have materially affected his or her settlement with the debtor or released party.

Both Executive and the Company hereby expressly waive and relinquish all rights and benefits under that section and any law of any jurisdiction of similar effect with respect to each party’s release of any claims hereunder.

Notwithstanding anything herein, the Executive acknowledges and agrees that, pursuant to 18 USC Section 1833(b), the Executive will not be held criminally or civilly liable under any federal or state trade secret law for the disclosure of a trade secret that is made: (i) in confidence to a federal, state, or local government official, either directly or indirectly, or to an attorney, and solely for the purpose of reporting or investigating a suspected violation of law; or (ii) in a complaint or other document filed in a lawsuit or other proceeding, if such filing is made under seal.

Mutual Nondisparagement.

(a) Nondisparagement by Executive. At all times following the cessation of the Executive's employment with the Company, the Executive agrees not to make negative comments or statements about, or otherwise criticize or disparage, in any format or through any medium, the Company or any entity controlled by, controlling or under common control with the Company ("Affiliates") or any of the officers, directors, managers, employees, services, operations, investments or products of the Company or any of its Affiliates. For purposes of the foregoing sentence, disparagement shall include, but not be limited to, negative comments or statements intended or reasonably likely to be harmful or disruptive to a person’s or entity’s respective business, business reputation, business operations, or personal reputation.

(b) Nondisparagement by Designated Company Representatives. At all times following the cessation of the Executive's employment with the Company, the Company agrees not to publish, and agrees to cause the Designated Company Representatives not to make, negative comments or statements about, or otherwise criticize or disparage, in any format or through any medium, the Executive. For purposes of the foregoing sentence, disparagement shall include, but not be limited to, negative comments or statements intended or reasonably likely to be harmful or disruptive to a person’s business reputation or personal reputation. For purposes of this sub-section (b), the “Designated Company Representatives” are (i) all executive officers of the Company while serving in such capacity and (ii) all members of the Board of Directors while serving in such capacity.

(c) The foregoing sub-sections (a) and (b) shall not be violated by truthful comments or statements (i) made in response to legal process, in required governmental testimony or filings, in judicial, administrative or arbitral proceedings (including, without limitation, depositions in connection with such proceedings), in compliance with law, administrative rule, or regulation, or made pursuant to a court or administrative order, or in connection with reporting possible violations of federal law or regulation to any governmental agency or entity, or making other disclosures that are protected under the whistleblower provisions of federal law or regulation, (ii) made by members of the Board of Directors in the course of meetings or discussions of the Board of Directors (or any committee thereof) or in communications between members of the Board of Directors and the Executive, and not disclosed to the public, (iii) made by a member of the Board of Directors in the good faith belief that the statements are required for the proper discharge of his or her fiduciary duties, or (iv) made by the Board of Directors in connection with a termination of the Executive for Cause.

[*Signature Page Follows*]

IN WITNESS WHEREOF, the Company has caused this Agreement to be executed by its duly authorized officer, and the Executive has hereunto signed this Agreement, as of the date set forth below.

EXECUTIVE

Name: ______________________________

Dashiell I. Robinson

Date: ______________________________

COMPANY

Name: ______________________________

Date: ______________________________

EXHIBIT B
RELEASE AGREEMENT

Except as otherwise set forth in this Release Agreement or in Sections 7 and 18 of the Employment Agreement between Dashiell I. Robinson and Redwood Trust, Inc., Dashiell I. Robinson ("Executive") hereby generally and completely releases the Company and its directors, officers, employees, shareholders, partners, agents, attorneys, predecessors, successors, parent and subsidiary entities, insurers, affiliates, and assigns from any and all claims, liabilities and obligations, both known and unknown, that arise out of or are in any way related to events, acts, conduct, or omissions occurring at any time prior to and including the date Executive signs this Release Agreement. The Company, its directors, officers, employees, shareholders, partners, agents, attorneys, predecessors, successors, parent and subsidiary entities, insurers, affiliates, and assigns, hereby releases Executive and his heirs, executors, successors and assigns, from any and all claims, liabilities and obligations, both known and unknown, that arise out of or are in any way related to events, acts, conduct, or omissions occurring at any time prior to and including the date the Company signs this Release Agreement. This general mutual release includes, but is not limited to: (A) all claims arising out of or in any way related to Executive's employment with the Company or the termination of that employment; (B) all claims related to Executive's compensation or benefits from the Company, including salary, bonuses, commissions, vacation pay, expense reimbursements, severance pay, fringe benefits, stock, stock options, or any other ownership interests in the Company; (C) all claims for breach of contract, wrongful termination, and breach of the implied covenant of good faith and fair dealing; (D) all tort claims, including claims for fraud, defamation, emotional distress, and discharge in violation of public policy; (E) all federal, state, and local statutory claims, including claims for discrimination, harassment, retaliation, attorneys' fees, or other claims arising under the federal Civil Rights Act of 1964 (as amended), the federal Americans with Disabilities Act of 1990, the federal Age Discrimination in Employment Act of 1967 (as amended) ("ADEA"), the federal Employee Retirement Income Security Act of 1974 (as amended), and the California Fair Employment and Housing Act (as amended); and (F) all claims and rights with respect to Executive's right to communicate directly with, cooperate with, or provide information to, any federal, state or local government regulator; provided, however, that nothing in this paragraph shall be construed in any way to release the Company from its obligation to indemnify Executive pursuant to agreement, the Company's bylaws or binding resolutions, or applicable law.

Executive acknowledges that he is knowingly and voluntarily waiving and releasing any rights he may have under the ADEA, and that the consideration given under his Employment Agreement with the Company for the waiver and release in the preceding paragraph hereof is in addition to anything of value to which he was already entitled. Executive further acknowledges that he has been advised by this writing, as required by the ADEA, that: (A) this waiver and release does not apply to any rights or claims that may arise after the date Executive signs this Release Agreement; (B) Executive should consult with an attorney prior to signing this Release Agreement (although Executive may choose voluntarily not do so); (C) Executive has forty-five (45) days to consider this Release Agreement (although he may choose voluntarily to sign this Release Agreement earlier); (D) Executive has seven (7) days following the date that he signs this Release Agreement to revoke the Release Agreement by providing written notice to an officer of the Company; (E) this Release Agreement shall not be effective until the date upon which the revocation period has expired, which shall be the eighth day after Executive signs this Release Agreement; and (F) Executive has received with this Release Agreement a detailed list of the job titles and ages of all employees who were terminated in this group termination and the ages of all employees of the Company in the same job classification or organizational unit who were not terminated.

Both the Executive and the Company acknowledge that each has read and understands Section 1542 of the California Civil Code which reads as follows:

A general release does not extend to claims that the creditor or releasing party does not know or suspect to exist in his or her favor at the time of executing the release and that, if known by him or her, would have materially affected his or her settlement with the debtor or released party.

Both the Executive and the Company hereby expressly waive and relinquish all rights and benefits under that section and any law of any jurisdiction of similar effect with respect to each party's release of any claims hereunder.

Notwithstanding anything herein, the Executive acknowledges and agrees that, pursuant to 18 USC Section 1833(b), the Executive will not be held criminally or civilly liable under any federal or state trade secret law for the disclosure of a trade secret that is made: (i) in confidence to a federal, state, or local government official, either directly or indirectly, or to an attorney, and solely for the purpose of reporting or investigating a suspected violation of law; or (ii) in a complaint or other document filed in a lawsuit or other proceeding, if such filing is made under seal.

Mutual Nondisparagement.

(a) Nondisparagement by Executive. At all times following the cessation of the Executive's employment with the Company, the Executive agrees not to make negative comments or statements about, or otherwise criticize or disparage, in any format or through any medium, the Company or any entity controlled by, controlling or under common control with the Company ("Affiliates") or any of the officers, directors, managers, employees, services, operations, investments or products of the Company or any of its Affiliates. For purposes of the foregoing sentence, disparagement shall include, but not be limited to, negative comments or statements intended or reasonably likely to be harmful or disruptive to a person's or entity's respective business, business reputation, business operations, or personal reputation.

(b) Nondisparagement by Designated Company Representatives. At all times following the cessation of the Executive's employment with the Company, the Company agrees not to publish, and agrees to cause the Designated Company Representatives not to make, negative comments or statements about, or otherwise criticize or disparage, in any format or through any medium, the Executive. For purposes of the foregoing sentence, disparagement shall include, but not be limited to, negative comments or statements intended or reasonably likely to be harmful or disruptive to a person's business reputation or personal reputation. For purposes of this sub-section (b), the "Designated Company Representatives" are (i) all executive officers of the Company while serving in such capacity and (ii) all members of the Board of Directors while serving in such capacity.

(c) The foregoing sub-sections (a) and (b) shall not be violated by truthful comments or statements (i) made in response to legal process, in required governmental testimony or filings, in judicial, administrative or arbitral proceedings (including, without limitation, depositions in connection with such proceedings), in compliance with law, administrative rule, or regulation, or made pursuant to a court or administrative order, or in connection with reporting possible violations of federal law or regulation to any governmental agency or entity, or making other disclosures that are protected under the whistleblower provisions of federal law or regulation, (ii) made by members of the Board of Directors in the course of meetings or discussions of the Board of Directors (or any committee thereof) or in communications between members of the Board of Directors and the Executive, and not disclosed to the public, (iii) made by a member of the Board of Directors in the good faith belief that the statements are required for the proper discharge of his or her fiduciary duties, or (iv) made by the Board of Directors in connection with a termination of the Executive for Cause.

[*Signature Page Follows*]

IN WITNESS WHEREOF, the Company has caused this Agreement to be executed by its duly authorized officer, and the Executive has hereunto signed this Agreement, as of the date set forth below.

EXECUTIVE

Name: ______________________________
Dashiell I. Robinson

Date: ______________________________

COMPANY

Name: ______________________________

Date: ______________________________

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EXHIBIT C
Section 2870 of California Labor Code

Section 2870 of California Labor Code: Application of provision providing that employee shall assign or offer to assign rights in invention to employer.

a. Any provision and employment agreement which provides that an employee shall assign, or offer to assign, any of his or her rights in an invention to his or her employer shall not apply to an invention that the employee developed entirely on his or her own time without using the employer's equipment, supplies, facilities or trade secret information except for those inventions that either:

1. Relate at the time of conception or reduction to practice of the invention to the employer's business, or actual or demonstrably anticipated research or development of the employer; or

2. Result from any work performed by the employee for the employer.

b. To the extent a provision in an employment agreement purports to require an employee to assign an invention otherwise excluded from being required to be assigned under subdivision (a), the provision is against the public policy of this state and is unenforceable.

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Section 5: EX-31.1 (EXHIBIT 31.1)

EXHIBIT 31.1

CHIEF EXECUTIVE OFFICER CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Christopher J. Abate, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Redwood Trust, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over the financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and we have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 9, 2019	/s/ Christopher J. Abate
	Christopher J. Abate
	Chief Executive Officer

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Section 6: EX-31.2 (EXHIBIT 31.2)

EXHIBIT 31.2

CHIEF FINANCIAL OFFICER CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Collin L. Cochrane, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Redwood Trust, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to

make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over the financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and we have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 9, 2019	/s/ Collin L. Cochrane
	Collin L. Cochrane
	Chief Financial Officer

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Section 7: EX-32.1 (EXHIBIT 32.1)

EXHIBIT 32.1

CERTIFICATION

Pursuant to 18 U.S.C. §1350, the undersigned officer of Redwood Trust, Inc. (the "Registrant") hereby certifies that the Registrant's Quarterly Report on Form 10-Q for the three months ended March 31, 2019 (the "Quarterly Report") fully complies with the requirements of Section 13(a) or 15 (d), as applicable, of the Securities Exchange Act of 1934 and that the information contained in the Quarterly Report fairly presents, in all material respects, the financial condition and results of operations of the Registrant.

Date: May 9, 2019	/s/ Christopher J. Abate
	Christopher J. Abate
	Chief Executive Officer

The foregoing certification is being furnished solely pursuant to 18 U.S.C. §1350 and is not being filed as part of the Quarterly Report or as a separate disclosure document.

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Section 8: EX-32.2 (EXHIBIT 32.2)

EXHIBIT 32.2

CERTIFICATION

Pursuant to 18 U.S.C. §1350, the undersigned officer of Redwood Trust, Inc. (the “Registrant”) hereby certifies that the Registrant’s Quarterly Report on Form 10-Q for the three months ended March 31, 2019 (the “Quarterly Report”) fully complies with the requirements of Section 13(a) or 15 (d), as applicable, of the Securities Exchange Act of 1934 and that the information contained in the Quarterly Report fairly presents, in all material respects, the financial condition and results of operations of the Registrant.

Date: May 9, 2019	/s/ Collin L. Cochrane
	Collin L. Cochrane
	Chief Financial Officer

The foregoing certification is being furnished solely pursuant to 18 U.S.C. §1350 and is not being filed as part of the Quarterly Report or as a separate disclosure document.

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