ZILLOW INC
Form 10-Q
August 06, 2014
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2014

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

Commission File Number: 001-35237

ZILLOW, INC.

(Exact name of registrant as specified in its charter)

Washington	**20-2000033**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**
1301 Second Avenue, Floor 31, Seattle, Washington	**98101**
(Address of principal executive offices)	**(Zip Code)**

(206) 470-7000

https://twitter.com/zillow

(Registrant s telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

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

Large accelerated filer x	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

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

As of July 31, 2014, 34,118,777 shares of Class A common stock and 6,217,447 shares of Class B common stock were outstanding.

ZILLOW, INC.

Quarterly Report on Form 10-Q

For the Three Months Ended June 30, 2014

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As used in this Quarterly Report on Form 10-Q, the terms Zillow, the Company, we, us and our refer to Zillow, unless the context indicates otherwise.

NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q, including Part I, Item 2 (Management s Discussion and Analysis of Financial Condition and Results of Operations), contains forward-looking statements based on our management s beliefs and assumptions and on information currently available to our management. Forward-looking statements include all statements that are not historical facts and generally may be identified by terms such as believe, may, will, estimate, continue, anticipate, intend, could, would, project, plan, expect or the negative or plural of these words expressions.

These forward-looking statements are subject to a number of risks, uncertainties and assumptions, including but not limited to, our ability to successfully integrate and realize the benefits of our past or future strategic acquisitions or investments, including our proposed acquisition of Trulia, Inc.; our ability to maintain and effectively manage an adequate rate of growth; the impact of the real estate industry on our business; our ability to innovate and provide products and services that are attractive to our users and advertisers; our ability to increase awareness of the Zillow brand in a cost-effective manner; our ability to maintain or establish relationships with listings and data providers; our ability to attract consumers to our mobile applications and websites; our ability to compete successfully against existing or future competitors; the reliable performance of our network infrastructure and content delivery process; and our ability to protect our intellectual property. Further discussion of factors that may affect our business and results of operations is included in Part II, Item 1A (Risk Factors) in this Quarterly Report on Form 10-Q. Moreover, we operate in a very competitive and rapidly changing environment. New risks emerge from time to time. It is not possible for our management to predict all risks, nor can we assess the effect of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements we may make. In light of these risks, uncertainties and assumptions, the forward-looking events and circumstances discussed in this report may not occur and actual results could differ materially and adversely from those anticipated or implied in the forward-looking statements.

You should not rely on forward-looking statements as predictions of future events. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee that the future results, levels of activity, performance or events and circumstances reflected in the forward-looking statements will be achieved or occur. Moreover, except as required by law, neither we nor any other person assumes responsibility for the accuracy and completeness of the forward-looking statements, and we undertake no obligation to update publicly any forward-looking statements for any reason after the date of this report to conform these statements to actual results or to changes in our expectations.

WHERE YOU CAN FIND MORE INFORMATION

Our filings with the Securities and Exchange Commission, or SEC, including our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports are available on our website at www.zillow.com, free of charge, as soon as reasonably practicable after the electronic filing of these reports with the SEC. The information contained on our website is not a part of this quarterly report on Form 10-Q.

Investors and others should note that we announce material financial information to our investors using our investor relations website, press releases, SEC filings, and public conference calls and webcasts. We also use the following social media channels as a means of disclosing information about the company, our services, and other matters, and for complying with our disclosure obligations under Regulation FD:

Zillow Twitter Account (https://twitter.com/zillow)

Zillow Facebook Page (https://www.facebook.com/Zillow)

Zillow Company Blog (http://www.zillowblog.com/)

The information we post through these social media channels may be deemed material. Accordingly, investors should monitor these accounts and the blog, in addition to following our investor relations website, press releases, SEC filings, and public conference calls and webcasts. This list may be updated from time to time. The information we post through these channels is not a part of this quarterly report on Form 10-Q.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements (unaudited)

ZILLOW, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share data, unaudited)

	June 30, 2014	December 31, 2013
Assets		
Current assets:		
Cash and cash equivalents	$ 138,289	$ 201,760
Short-term investments	219,777	93,531
Accounts receivable, net of allowance for doubtful accounts of $2,490 and $1,850 at June 30, 2014 and December 31, 2013, respectively	19,885	15,234
Prepaid expenses and other current assets	6,464	4,987
Total current assets	384,415	315,512
Long-term investments	99,806	142,435
Property and equipment, net	34,011	27,408
Goodwill	96,352	93,213
Intangible assets, net	26,455	29,149
Other assets	434	346
Total assets	$ 641,473	$ 608,063
Liabilities and shareholders equity		
Current liabilities:		
Accounts payable	$ 14,279	$ 4,724
Accrued expenses and other current liabilities	12,116	10,601
Accrued compensation and benefits	6,363	4,440
Deferred revenue	14,037	12,298
Deferred rent, current portion	735	546
Total current liabilities	47,530	32,609
Deferred rent, net of current portion	10,248	7,658
Commitments and contingencies (Note 11)		
Shareholders equity:		
Preferred stock, $0.0001 par value; 30,000,000 shares authorized as of June 30, 2014 and December 31, 2013; no shares issued and outstanding as of June 30, 2014 and December 31, 2013		
	3	3

Class A common stock, $0.0001 par value; 600,000,000 shares authorized as of June 30, 2014 and December 31, 2013; 34,045,698 and 32,934,074 shares issued and outstanding as of June 30, 2014 and December 31, 2013, respectively		
Class B common stock, $0.0001 par value; 15,000,000 shares authorized as of June 30, 2014 and December 31, 2013; 6,217,447 and 6,468,892 shares issued and outstanding as of June 30, 2014 and December 31, 2013, respectively	1	1
Additional paid-in capital	684,548	651,913
Accumulated deficit	(100,857)	(84,121)
Total shareholders equity	583,695	567,796
Total liabilities and shareholders equity	$ 641,473	$ 608,063

See accompanying notes to condensed consolidated financial statements.

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ZILLOW, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data, unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Revenue	$ 78,675	$ 46,920	$ 144,918	$ 85,886
Costs and expenses:				
Cost of revenue (exclusive of amortization) (1)	6,793	4,294	12,957	8,424
Sales and marketing	48,075	32,924	82,973	52,718
Technology and development	19,862	11,071	36,832	21,682
General and administrative	14,706	8,978	29,395	17,211
Total costs and expenses	89,436	57,267	162,157	100,035
Loss from operations	(10,761)	(10,347)	(17,239)	(14,149)
Other income	284	115	503	170
Net loss	$ (10,477)	$ (10,232)	$ (16,736)	$ (13,979)
Net loss per share basic and diluted	$ (0.26)	$ (0.30)	$ (0.42)	$ (0.41)
Weighted-average shares outstanding basic and diluted	39,800	34,553	40,314	34,164
(1) Amortization of website development costs and intangible assets included in technology and development	$ 6,857	$ 4,492	$ 13,641	$ 8,700

See accompanying notes to condensed consolidated financial statements.

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ZILLOW, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands, unaudited)

	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
Operating activities		
Net loss	$ (16,736)	$ (13,979)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	16,670	9,934
Share-based compensation expense	15,542	14,613
Loss on disposal of property and equipment	353	668
Bad debt expense	1,225	765
Deferred rent	2,779	(122)
Amortization of bond premium	1,751	210
Changes in operating assets and liabilities:		
Accounts receivable	(5,876)	(5,193)
Prepaid expenses and other assets	(1,565)	(462)
Accounts payable	9,555	2,659
Accrued expenses	3,438	(1,506)
Deferred revenue	1,739	959
Net cash provided by operating activities	28,875	8,546
Investing activities		
Proceeds from maturities of investments	73,885	33,000
Purchases of investments	(159,253)	(56,272)
Purchases of property and equipment	(15,373)	(10,996)
Purchases of intangible assets	(2,132)	(1,707)
Cash paid for acquisition	(3,500)	
Net cash used in investing activities	(106,373)	(35,975)
Financing activities		
Proceeds from exercise of Class A common stock options	14,027	8,941
Net cash provided by financing activities	14,027	8,941
Net decrease in cash and cash equivalents during period	(63,471)	(18,488)
Cash and cash equivalents at beginning of period	201,760	150,040
Cash and cash equivalents at end of period	$ 138,289	$ 131,552
Supplemental disclosures of cash flow information		
Noncash transactions:		
Capitalized share-based compensation	$ 3,086	$ 1,732

Write-off of fully depreciated property and equipment	$ 3,017	$ 792

See accompanying notes to condensed consolidated financial statements.

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ZILLOW, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

Note 1. Organization and Description of Business

Zillow, Inc. was incorporated as a Washington corporation effective December 13, 2004, and we launched the initial version of our website, Zillow.com, in February 2006. Zillow operates the leading real estate and home-related information marketplaces on mobile and the Web, with a complementary portfolio of brands and products to help people find vital information about homes, and connect with local professionals. In addition to our living database of homes, accessible on Zillow.com, we also own and operate Zillow Mobile, our suite of home-related mobile applications, Zillow Mortgage Marketplace, where borrowers connect with lenders to find loans and get competitive mortgage rates, Zillow Digs, our home improvement marketplace where consumers can find visual inspiration and local cost estimates, Zillow Rentals, a marketplace and suite of tools for rental professionals, Postlets, Diverse Solutions, Agentfolio, Mortech, HotPads, StreetEasy and Retsly. Zillow provides products and services to help consumers through every stage of homeownership buying, selling, renting, borrowing and remodeling.

Certain Significant Risks and Uncertainties

We operate in a dynamic industry and, accordingly, can be affected by a variety of factors. For example, we believe that changes in any of the following areas could have a significant negative effect on us in terms of our future financial position, results of operations or cash flows: rates of revenue growth; engagement and usage of our products; scaling and adaptation of existing technology and network infrastructure; competition in our market; management of our growth; acquisitions and investments; qualified employees and key personnel; protection of our brand and intellectual property; changes in government regulation affecting our business; intellectual property infringement and other claims; protection of customers information and privacy concerns; and security measures related to our mobile applications and websites, among other things.

Note 2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying condensed consolidated financial statements include Zillow, Inc. and our wholly-owned subsidiary, Zillow (Canada), Inc. All significant intercompany balances and transactions have been eliminated in consolidation. These condensed consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States (GAAP) and applicable rules and regulations of the Securities and Exchange Commission (SEC) regarding interim financial reporting. Certain information and note disclosures normally included in the financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. Accordingly, these interim condensed consolidated financial statements should be read in conjunction with the audited financial statements and accompanying notes as of and for the year ended December 31, 2013 included in the Company s Annual Report on Form 10-K, which was filed with the SEC on February 18, 2014. The condensed balance sheet as of December 31, 2013, included herein, was derived from the audited financial statements as of that date.

The unaudited condensed consolidated interim financial statements have been prepared on the same basis as the annual financial statements and, in the opinion of management, reflect all adjustments, consisting only of normal recurring adjustments, necessary to present fairly our financial position as of June 30, 2014, our results of operations for the three and six month periods ended June 30, 2014 and 2013, and our cash flows for the six month periods ended June 30, 2014 and 2013. The results of the three and six month periods ended June 30, 2014 are not necessarily indicative of the results to be expected for the year ended December 31, 2014 or for any interim period or for any other future year.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities and the related disclosures at the date of the financial statements, as well as the reported amounts of revenue and expenses during the periods presented. Estimates are used for revenue recognition, the allowance for doubtful accounts, website development costs, goodwill, recoverability of intangible assets with definite lives and other long-lived assets, and for share-based compensation. To the extent there are material differences between these estimates, judgments, or assumptions and actual results, our financial statements will be affected.

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Reclassifications

Certain immaterial reclassifications have been made to conform data for prior periods to the current format.

Recently Issued Accounting Standards

In July 2013, the Financial Accounting Standards Board (FASB) issued guidance on the presentation of certain unrecognized tax benefits in the financial statements. This guidance provides that a liability related to an unrecognized tax benefit must be offset against a deferred tax asset for a net operating loss carryforward, a similar tax loss or a tax credit carryforward if such settlement is required or expected in the event the uncertain tax position is disallowed. This guidance is effective for interim and annual reporting periods beginning after December 15, 2013, with earlier adoption permitted, and may be applied prospectively or retrospectively. We adopted this guidance on January 1, 2014. The adoption of this guidance did not have a significant impact on our financial position, results of operations or cash flows, as we have provided a full valuation allowance against our net deferred tax assets.

In May 2014, the FASB issued guidance on revenue recognition. This guidance provides that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This guidance also requires more detailed disclosures to enable users of financial statements to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. This guidance is effective for interim and annual reporting periods beginning after December 15, 2016, early adoption is not permitted, and must be applied retrospectively or modified retrospectively. We expect to adopt this guidance on January 1, 2017. We have not yet determined the impact the adoption of this guidance will have on our financial position, results of operations or cash flows, if any.

Note 3. Fair Value Measurements

Accounting standards define fair value as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market in an orderly transaction between market participants on the measurement date. The standards also establish a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. There are three levels of inputs that may be used to measure fair value:

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

Level 2 Assets and liabilities valued based on observable market data for similar instruments, such as quoted prices for similar assets or liabilities.

Level 3 Unobservable inputs that are supported by little or no market activity; instruments valued based on the best available data, some of which is internally developed, and considers risk premiums that a market participant would require.

We applied the following methods and assumptions in estimating our fair value measurements:

Cash equivalents Cash equivalents are comprised of highly liquid investments, including money market funds, municipal securities and certificates of deposit with original maturities of less than three months. The fair value measurement of our cash equivalents is based on quoted prices in active markets for identical assets.

Short-term and long-term investments Our investments consist of fixed income securities, which include U.S. government agency securities, corporate notes and bonds, municipal securities, certificates of deposit and commercial paper. Investments with maturities greater than three months but less than one year are classified as short-term investments. Investments with maturities greater than one year are classified as long-term investments. The fair value measurement of these assets is based on observable market-based inputs or inputs that are derived principally from or corroborated by observable market data by correlation or other means. Our short-term and long-term investments are classified as held-to-maturity and are recorded at amortized cost, as we do not intend to sell the investments, and it is not more likely than not that we will be required to sell these investments prior to maturity. The amortized cost of our short-term and long-term investments approximates their fair value.

Of the short-term investments and long-term investments on hand as of June 30, 2014, 68.8% mature on or prior to June 30, 2015, and the remaining 31.2% mature on or prior to June 30, 2016.

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The following tables present the balances of cash equivalents and investments as of the dates presented (in thousands):

	June 30, 2014		
	Total	Level 1	Level 2
Cash equivalents:			
Money market funds	$ 125,685	$ 125,685	$
Short-term investments:			
U.S government agency securities	139,707	139,707	
Corporate notes and bonds	36,086		36,086
Municipal securities	15,952		15,952
Certificates of deposit	14,055		14,055
Commercial paper	13,977		13,977
Long-term investments:			
Corporate notes and bonds	47,394		47,394
U.S. government agency securities	27,768	27,768	
Certificates of deposit	23,197		23,197
Municipal securities	1,447		1,447
Total	$ 445,268	$ 293,160	$ 152,108

	December 31, 2013		
	Total	Level 1	Level 2
Cash equivalents:			
Money market funds	$ 184,941	$ 184,941	$
U.S government agency securities	3,306	3,306	
Short-term investments:			
U.S government agency securities	78,448	78,448	
Commercial paper	3,998		3,998
Corporate notes and bonds	11,085		11,085
Long-term investments:			
U.S government agency securities	112,623	112,623	
Corporate notes and bonds	29,812		29,812
Total	$ 424,213	$ 379,318	$ 44,895

We did not have any Level 3 assets or liabilities measured at fair value on a recurring basis as of June 30, 2014 or December 31, 2013.

Note 4. Property and Equipment, net

The following table presents the detail of property and equipment as of the dates presented (in thousands):

	June 30, 2014	December 31, 2013
Website development costs	$ 55,885	$ 50,408
Computer equipment	10,646	8,238
Leasehold improvements	9,784	7,320
Software	2,759	1,807
Construction-in-progress	5,891	3,289
Office equipment, furniture and fixtures	4,550	3,661
Property and equipment	89,515	74,723
Less: accumulated amortization and depreciation	(55,504)	(47,315)
Property and equipment, net	$ 34,011	$ 27,408

We recorded depreciation expense related to property and equipment (other than website development costs) of $1.7 million and $0.7 million, respectively, during the three months ended June 30, 2014 and 2013, and $3.0 million and $1.2 million, respectively, during the six months ended June 30, 2014 and 2013.

We capitalized $5.5 million and $4.1 million, respectively, in website development costs during the three months ended June 30, 2014 and 2013, and $11.1 million and $8.0 million, respectively, during the six months ended June 30, 2014 and 2013. Amortization expense for website development costs included in technology and development expenses was $4.2 million and $2.8 million, respectively, during the three months ended June 30, 2014 and 2013, and $8.5 million and $5.3 million, respectively, during the six months ended June 30, 2014 and 2013.

Construction-in-progress primarily consists of website development costs that are capitalizable, but for which the associated applications had not been placed in service.

Note 5. Goodwill

The following table presents the change in goodwill from December 31, 2013 through June 30, 2014 (in thousands):

Balance as of December 31, 2013	$ 93,213
Goodwill recorded in connection with an acquisition	3,139
Balance as of June 30, 2014	$ 96,352

In June 2014, Zillow entered into an asset purchase agreement, pursuant to which Zillow acquired substantially all of the operating assets, including intellectual property rights and intangible assets, of the acquiree. The acquisition has been accounted for as a business combination, and assets acquired and liabilities assumed were recorded at their estimated fair values as of the acquisition date, and were not significant. The results of operations related to the acquisition have been included in our consolidated financial statements since the date of acquisition, and are not significant. Pro forma financial information for the acquisition accounted for as a business combination has not been presented, as the effects were not material to our consolidated financial statements. The goodwill recorded in connection with the June 2014 acquisition is deductible for tax purposes.

Note 6. Intangible Assets, net

The following tables present the detail of intangible assets subject to amortization as of the dates presented (in thousands):

	June 30, 2014		
	Cost	Accumulated Amortization	Net
Purchased content	$ 15,100	$ (10,927)	$ 4,173
Developed technology	19,195	(6,148)	13,047
Customer relationships	9,775	(2,824)	6,951
Trademarks	3,261	(977)	2,284
Total	$ 47,331	$ (20,876)	$ 26,455

	December 31, 2013		
	Cost	Accumulated Amortization	Net
Purchased content	$ 12,968	$ (8,846)	$ 4,122
Developed technology	18,835	(4,417)	14,418
Customer relationships	9,775	(1,799)	7,976
Trademarks	3,261	(628)	2,633
Total	$ 44,839	$ (15,690)	$ 29,149

Amortization expense recorded for intangible assets for the three months ended June 30, 2014 and 2013 was $2.6 million and $1.7 million, respectively. Amortization expense recorded for intangible assets for the six months ended June 30, 2014 and 2013 was $5.2 million and $3.4 million, respectively. These amounts are included in technology and development expenses.

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Note 7. Income Taxes

We are subject to federal and state income taxes in the United States and in Canada. During the three and six month periods ended June 30, 2014 and 2013, we did not have reportable taxable income, and we are not projecting reportable taxable income for the year ending December 31, 2014. Therefore, no tax liability or expense has been recorded in the consolidated financial statements. We have provided a full valuation allowance against our net deferred tax assets as of June 30, 2014 and December 31, 2013 because, based on the weight of available evidence, it is more likely than not (a likelihood of more than 50%) that some or all of the deferred tax assets will not be realized. We have accumulated federal tax losses of approximately $236.5 million as of December 31, 2013, which are available to reduce future taxable income. We have accumulated state tax losses of approximately $6.1 million (tax effected) as of December 31, 2013.

Note 8. Shareholders Equity

Our board of directors has the authority to fix and determine and to amend the number of shares of any series of preferred stock that is wholly unissued or to be established and to fix and determine and to amend the designation, preferences, voting powers and limitations, and the relative, participating, optional or other rights, of any series of shares of preferred stock that is wholly unissued or to be established, subject in each case to certain approval rights of holders of our outstanding Class B common stock. There was no preferred stock issued and outstanding as of June 30, 2014 or December 31, 2013.

Our Class A common stock has no preferences or privileges and is not redeemable. Holders of Class A common stock are entitled to one vote for each share.

Our Class B common stock has no preferences or privileges and is not redeemable. At any time after the date of issuance, each share of Class B common stock, at the option of the holder, may be converted into one share of Class A common stock, or automatically converted upon the affirmative vote by or written consent of holders of a majority of the shares of the Class B common stock. During the three and six month periods ended June 30, 2014, 50,000 shares and 251,445 shares of Class B common stock, respectively, were converted into Class A common stock at the option of the holders. During the year ended December 31, 2013, 993,634 shares of Class B common stock were converted into Class A common stock at the option of the holders. Holders of Class B common stock are entitled to 10 votes for each share.

In August 2013, we sold 3,253,522 shares of our Class A common stock, including 753,522 shares of our Class A common stock pursuant to the underwriters option to purchase additional shares, and certain shareholders sold 2,523,486 shares of our Class A common stock, at a price of $82.00 per share. We received net proceeds of $253.9 million after deducting underwriting discounts and commissions and offering expenses payable by us. We received no proceeds from the sale of our Class A common stock by the selling shareholders.

Note 9. Share-Based Awards

On July 19, 2011, our 2011 Incentive Plan (as amended and/or restated from time to time, the 2011 Plan) became effective and replaced our 2005 Equity Incentive Plan. The 2011 Plan contains an evergreen provision, pursuant to which the number of shares of Class A common stock available for issuance under the 2011 Plan can be increased on the first day of each of our fiscal years beginning in 2013 by a number of shares equal to the least of (a) 3.5% of our outstanding Class A common stock and Class B common stock on a fully diluted basis as of the end of our immediately preceding fiscal year, (b) 3,500,000 shares, and (c) a lesser amount determined by our board of directors;

provided, however, that any shares from any increases in previous years that are not actually issued will continue to be available for issuance under the 2011 Plan. The 2011 Plan is administered by the compensation committee of the board of directors. Under the terms of the 2011 Plan, the compensation committee may grant equity awards, including incentive stock options, nonqualified stock options, restricted stock, restricted stock units, or restricted units to employees, officers, directors, consultants, agents, advisors and independent contractors. The compensation committee has also authorized certain senior executive officers to grant equity awards under the 2011 Plan, within limits prescribed by the compensation committee.

Stock Options

All stock options granted from inception through June 30, 2014 are nonqualified stock options, with the exception of substituted incentive stock options for 15,143 shares of Zillow s Class A common stock that were granted in connection with the December 14, 2012 acquisition of HotPads, Inc. Options under the 2011 Plan are granted with an exercise price per share not less than 100% of the fair market value of our Class A common stock on the date of grant, with the exception of substituted stock options granted in connection with acquisitions, and are exercisable at such times and under such conditions as determined by the compensation committee. Under the 2011 Plan, the maximum term of an option is ten years from the date of grant. Any portion of an option that is not vested and exercisable on the date of a participant s termination of service expires on such date. Employees generally forfeit their rights to exercise vested options after 3 months following their termination of employment or 12 months in the event of termination by reason of death, disability or retirement. Options granted under the 2011 Plan are typically granted with seven-year terms and typically vest 25% after 12 months and ratably thereafter over the next 36 months, except for options granted under the Stock Option Grant Program for Nonemployee Directors (Nonemployee Director Awards), which are fully vested and exercisable on the date of grant, and except for certain options that were granted to our chief executive officer in December 2012 and January 2013.

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The following table summarizes stock option activity for the year ended December 31, 2013 and the six months ended June 30, 2014:

	Shares Available for Grant	Number of Shares Subject to Existing Options	Weighted-Average Exercise Price Per Share	Weighted-Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value
Outstanding at January 1, 2013	321,678	5,462,672	$ 14.48	4.48	$ 78,912,364
Authorized increase in plan shares	2,887,064				
Granted	(1,984,157)	2,009,542	43.87		
Exercised		(2,026,829)	9.03		
Forfeited or cancelled	288,679	(288,679)	31.93		
Outstanding at December 31, 2013	1,513,264	5,156,706	27.09	5.43	283,008,505
Authorized increase in plan shares	1,563,827				
Granted	(1,641,789)	1,641,789	88.00		
Exercised		(825,342)	17.00		
Forfeited or cancelled	148,343	(148,343)	52.54		
Outstanding at June 30, 2014	1,583,645	5,824,810	45.06	5.53	571,097,095
Vested and exercisable at June 30, 2014		1,566,583	17.55	3.92	196,414,195

The shares available for grant identified in the above table exclude options for an aggregate of 25,385 shares that were granted in 2013 in substitution of options previously granted by StreetEasy, Inc. (StreetEasy). Pursuant to the terms of the 2011 Plan, such substituted stock option awards do not reduce the number of shares available for future issuance under the 2011 Plan. As of June 30, 2014, the numbers above do not include 77,750 shares of restricted stock and 164,167 restricted stock units outstanding under our 2011 Plan.

The fair value of options granted, excluding Nonemployee Director Awards and certain options granted to the Company s chief executive officer in December 2012 and January 2013, is estimated at the date of grant using the Black-Scholes-Merton option-pricing model, assuming no dividends and with the following assumptions for the periods presented:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Expected volatility	54%	50%	53%-54%	50%-51%
Expected dividend yields				
Risk-free interest rate	1.35%-1.49%	0.59%-1.22%	1.29%-1.52%	0.59%-1.22%
Weighted-average expected life	4.58 years	4.58 years	4.58 years	4.58 years
Weighted-average fair value of options granted	$49.25	$23.22	$39.62	$16.53

In March 2014, stock options for an aggregate of 23,010 shares of our Class A common stock were granted as Nonemployee Director Awards. The fair value of options granted for the Nonemployee Director Awards, $32.60 per share, is estimated at the date of grant using the Black-Scholes-Merton option-pricing model, assuming no dividends, expected volatility of 54%, a risk-free interest rate of 0.69%, and a weighted-average expected life of 3.5 years. During the six months ended June 30, 2014 and 2013, share-based compensation expense recognized in our statements of operations related to Nonemployee Director Awards was $0.8 million and $0.5 million, respectively, and is included in general and administrative expenses. There was no share-based compensation expense recognized in our statements of operations related to Nonemployee Director Awards for the three months ended June 30, 2014 and 2013.

As of June 30, 2014, there was a total of $81.1 million in unrecognized compensation cost related to unvested stock options, which is expected to be recognized over a weighted-average period of 3.3 years.

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Restricted Stock Awards

The following table summarizes restricted stock award activity for the year ended December 31, 2013 and the six months ended June 30, 2014:

	Shares of Restricted Stock	Weighted-Average Grant-Date Fair Value
Unvested outstanding at January 1, 2013	340,103	$ 30.37
Granted	3,673	44.66
Vested	(108,379)	30.94
Forfeited or cancelled	(5,270)	25.92
Unvested outstanding at December 31, 2013	230,127	30.43
Granted	3,255	80.91
Vested	(91,048)	30.90
Forfeited or cancelled		
Unvested outstanding at June 30, 2014	142,334	31.28

The fair value of the outstanding shares of restricted stock awards will be recorded as share-based compensation expense over the vesting period. As of June 30, 2014, there was $4.4 million of total unrecognized compensation cost related to restricted stock awards.

Restricted Stock Units

The following table summarizes activity for restricted stock units for the year ended December 31, 2013 and the six months ended June 30, 2014:

	Restricted Stock Units	Weighted-Average Grant-Date Fair Value
Unvested outstanding at January 1, 2013	295,737	$ 38.76
Granted	97,804	81.12
Vested	(253,384)	42.53
Forfeited or cancelled	(19,034)	59.26
Unvested outstanding at December 31, 2013	121,123	64.07
Granted	96,964	102.12
Vested	(30,407)	67.66
Forfeited or cancelled	(23,513)	76.22

Unvested outstanding at June 30, 2014	164,167	83.20

In April 2014, pursuant to the terms of an Amended and Restated Executive Employment Agreement and a Restricted Stock Unit Award Notice and Restricted Stock Unit Award Agreement entered into between Zillow and an employee, Zillow granted to the employee restricted stock units for 59,320 shares of our Class A common stock, which vest quarterly over four years beginning on the vesting commencement date of March 26, 2014, subject to the recipient s continued full-time employment or service to Zillow. In the event of termination of service or employment by Zillow without cause or upon the resignation by such employee for good reason, the employee will receive 24 months accelerated vesting of the restricted stock units, except that in the event of such a termination in connection with a change in control, the restricted stock units will become fully vested. The employee will be entitled to receive one share of Zillow s Class A common stock for each then outstanding unit that becomes vested. The grant date fair value of the restricted stock units is approximately $5.4 million.

In June 2014, pursuant to the terms of Restricted Stock Unit Award Notices and Restricted Stock Unit Award Agreements entered into between Zillow and certain employees, Zillow granted to the employees restricted stock units for a total of 24,880 shares of our Class A common stock, which vest ratably after each six-month period over two years beginning on the vesting commencement date of June 3, 2014, subject to the recipients continued full-time employment or service to Zillow. In the event of termination of service of employment by Zillow without cause, 50% of the then unvested restricted stock units will become vested units, and the recipient will be entitled to receive one share of Zillow s Class A common stock for each then outstanding unit. The grant date fair value of the restricted stock units is approximately $3.2 million.

The fair value of restricted stock units will be recorded as share-based compensation expense over the vesting period. As of June 30, 2014, there was $13.5 million of total unrecognized compensation cost related to restricted stock units.

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Share-Based Compensation Expense

The following table presents the effects of share-based compensation in our statements of operations during the periods presented (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	**2013**	**2014**	**2013**
Cost of revenue	$ 418	$ 176	$ 791	$ 339
Sales and marketing	1,698	7,777	3,001	9,004
Technology and development	3,056	1,034	5,081	2,068
General and administrative	3,238	1,480	6,669	3,202
Total	$ 8,410	$ 10,467	$ 15,542	$ 14,613

Note 10. Net Loss Per Share

Basic net loss per share is computed by dividing net loss by the weighted-average number of common shares (including Class A common stock and Class B common stock) outstanding during the period. In the calculation of basic net loss per share, undistributed earnings are allocated assuming all earnings during the period were distributed.

Diluted net loss per share is computed by dividing net loss by the weighted-average number of common shares (including Class A common stock and Class B common stock) outstanding during the period and potentially dilutive Class A common stock equivalents, except in cases where the effect of the Class A common stock equivalent would be antidilutive. Potential Class A common stock equivalents consist of Class A common stock issuable upon exercise of stock options and Class A common stock underlying unvested restricted stock awards and unvested restricted stock units using the treasury stock method.

For the periods presented, the following Class A common stock equivalents were excluded from the calculations of diluted net loss per share because their effect would have been antidilutive (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	**2013**	**2014**	**2013**
Class A common stock issuable upon the exercise of stock options	3,012	2,950	3,024	2,899
Class A common stock underlying unvested restricted stock awards and restricted stock units	119	130	114	180
Total Class A common stock equivalents	3,131	3,080	3,138	3,079

In the event of liquidation, dissolution, distribution of assets or winding-up of the Company, the holders of all classes of common stock have equal rights to receive all the assets of the Company after the rights of the holders of outstanding preferred stock have been satisfied. We have not presented net loss per share under the two-class method for our Class A common stock and Class B common stock because it would be the same for each class due to equal dividend and liquidation rights for each class.

Note 11. Commitments and Contingencies
Lease Commitments

We have various operating leases for office space and equipment. In March 2011, we entered into a lease agreement for office space that houses our corporate headquarters in Seattle, Washington (as amended from time to time, the Seattle Lease). Pursuant to the terms of the Seattle Lease, we lease a total of approximately 155,000 square feet, and we are obligated to make escalating monthly lease payments that began in December 2012 and continue through November 2022. In April 2012, we entered into a lease agreement for office space in Irvine, California (as amended from time to time, the Irvine Lease). Pursuant to the terms of the Irvine Lease, we lease a total of approximately 60,000 square feet under which we are obligated to make escalating monthly lease payments which began in August 2012 and continue through July 2022. In November 2012, we entered into an operating lease in San Francisco, California for 18,353 square feet under which we are obligated to make escalating monthly lease payments which began in December 2012 and continue through November 2018. In February 2014, we entered into an operating lease in New York, New York for 13,300 square feet under which we are obligated to make escalating monthly lease payments beginning in August 2014 and continuing through September 2024. In June 2014, we entered into a lease amendment for our operating lease in New York, New York, which increased the rentable area of the premises by 13,300 square feet, for which we are obligated to make escalating monthly lease payments expected to begin in May 2015 and continue through September 2024. We lease additional office space in Chicago, Illinois, Lincoln, Nebraska, and New York, New York.

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Future minimum payments for all operating leases as of June 30, 2014 are as follows (in thousands):

Remainder of 2014	$ 3,237
2015	8,727
2016	9,544
2017	10,769
2018	10,896
All future years	41,284
Total future minimum lease payments	$ 84,457

Rent expense for the three months ended June 30, 2014 and 2013 was $1.6 million and $1.1 million, respectively. Rent expense for the six months ended June 30, 2014 and 2013 was $3.1 million and $2.2 million, respectively.

Purchase Commitments

As of June 30, 2014, we had non-cancelable purchase commitments for content related to our mobile applications and websites totaling $11.4 million. The amounts due for this content as of June 30, 2014 are as follows (in thousands):

Remainder of 2014	$ 2,294
2015	4,650
2016	3,599
2017	817
Total future purchase commitments	$ 11,360

Letters of Credit

We have executed a standby letter of credit of $2.0 million in connection with our Seattle Lease and a standby letter of credit of $0.7 million in connection with the operating lease of our New York offices. The letters of credit are secured by our investments and are effective until 60 days after the expiration date of the lease.

Legal Proceedings

In March 2010, Smarter Agent, LLC (Smarter Agent) filed a complaint against us and multiple other defendants, including HotPads, Inc. (HotPads), for patent infringement in the U.S. District Court for the District of Delaware. The complaint alleges, among other things, that our mobile technology infringes three patents held by Smarter Agent purporting to cover: a Global positioning-based real estate database access device and method, a Position-based information access device and method and a Position-based information access device and method of searching, and seeks an injunction against the alleged infringing activities and an unspecified award for damages. In November 2010, the U.S. Patent and Trademark Office granted our petition for re-examination of the three patents-in-suit, and, to date, all claims of all three patents remain rejected in the re-examination proceedings. In March 2011, the court granted a stay of the litigation pending the completion of the re-examination proceedings. In addition, in October 2011, Smarter Agent filed a substantially similar complaint against Diverse Solutions, Inc. (Diverse Solutions), StreetEasy, and other defendants, for patent infringement in the U.S. District Court for the District of Delaware. On October 31, 2011, we acquired substantially all of the operating assets and certain liabilities of Diverse Solutions, including the Smarter Agent complaint against Diverse Solutions. On December 14, 2012, we acquired HotPads, and took responsibility for the Smarter Agent complaint against HotPads. On August 26, 2013, we acquired StreetEasy, and took responsibility for the Smarter Agent complaint against StreetEasy. We have not recorded an accrual related to these complaints as of June 30, 2014 or December 31, 2013, as we do not believe a material loss is probable. It is a reasonable possibility that a loss may be incurred; however, the possible loss or range of loss is not estimable.

In September 2010, LendingTree, LLC (LendingTree) filed a complaint against us for patent infringement in the U.S. District Court for the Western District of North Carolina. The complaint alleged, among other things, that our website technology infringes two patents purporting to cover a Method and computer network for coordinating a loan over the internet. The complaint sought, among other things, a judgment that we infringed certain patents held by LendingTree, an injunction against the alleged infringing activities and an award for damages. We denied the allegations and asserted defenses and counterclaims seeking declarations that we are not infringing the patents and that the patents are invalid. In March 2014, a federal jury found that Zillow does not infringe the patents and that the patents asserted by LendingTree are invalid. In April, 2014, LendingTree filed two motions for judgment as a matter of law and for a new trial, all of which we opposed. We have not recorded an accrual related to this complaint as of June 30, 2014 or December 31, 2013, as we do not believe a material loss is probable.

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In November 2012, a securities class action lawsuit was filed in the U.S. District Court for the Western District of Washington at Seattle against us and certain of our executive officers seeking unspecified damages. A consolidated amended complaint was filed in June 2013. The complaint purports to state claims for violations of federal securities laws on behalf of a class of those who purchased our common stock between February 15, 2012 and November 6, 2012. The complaint generally alleges, among other things, that during the period between February 15, 2012 and November 6, 2012, we issued materially false and misleading statements regarding our business practices and financial results. In August 2013, we moved to dismiss the lawsuit. That motion to dismiss has been fully briefed and is pending before the Court. We have denied the allegations of wrongdoing, and we will continue to vigorously defend the claims in the lawsuit. We have not recorded an accrual related to this lawsuit as of June 30, 2014 or December 31, 2013, as we do not believe a material loss is probable. It is a reasonable possibility that a loss may be incurred; however, the possible loss or range of loss is not estimable.

In March 2014, Move, Inc., the National Association of Realtors and three related entities, filed a complaint against us and Errol Samuelson, our Chief Industry Development Officer, in the Superior Court of the State of Washington in King County, alleging, among other things, that Zillow and Mr. Samuelson misappropriated plaintiffs trade secrets in connection with Mr. Samuelson joining Zillow in March 2014. The complaint seeks, among other things, an injunction against the alleged misappropriations and Mr. Samuelson working for us, as well as unspecified damages. In April 2014, the court denied the plaintiffs motion for a preliminary injunction prohibiting Mr. Samuelson from working for us. Plaintiffs renewed their motion for a preliminary injunction and on June 30, 2014, the court granted that request and entered a preliminary injunction. We have filed a motion requesting that the court reconsider that decision and narrow the preliminary injunction. We deny the allegations of any wrongdoing and intend to vigorously defend the claims in the lawsuit. We have not recorded an accrual related to these complaints as of June 30, 2014, as we do not believe a material loss is probable.

In addition to the matters discussed above, from time to time, we are involved in litigation and claims that arise in the ordinary course of business. Although we cannot be certain of the outcome of any litigation and claims, nor the amount of damages and exposure that we could incur, we currently believe that the final disposition of such matters will not have a material effect on our financial position, results of operations or cash flow. Regardless of the outcome, litigation can have an adverse impact on us because of defense and settlement costs, diversion of management resources and other factors.

Note 12. Segment Information and Revenue

We have one reportable segment. Our reportable segment has been identified based on how our chief operating decision-maker manages our business, makes operating decisions and evaluates operating performance. The chief executive officer acts as the chief operating decision-maker and reviews financial and operational information on an entity-wide basis. We have one business activity and there are no segment managers who are held accountable for operations, operating results or plans for levels or components. Accordingly, we have determined that we have a single reporting segment and operating unit structure.

The chief executive officer reviews information about revenue categories, including marketplace revenue and display revenue. The following table presents our revenue categories during the periods presented (in thousands):

	Three Months Ended	**Six Months Ended June 30,**

	June 30,			
	2014	2013	2014	2013
Marketplace revenue:				
Real estate	$ 56,051	$ 30,637	$ 102,646	$ 56,746
Mortgages	6,565	5,814	13,694	10,723
Total Marketplace revenue	62,616	36,451	116,340	67,469
Display revenue	16,059	10,469	28,578	18,417
Total revenue	$ 78,675	$ 46,920	$ 144,918	$ 85,886

Note 13. Subsequent Events

On July 28, 2014, Zillow, Zebra Holdco, Inc., a Washington corporation (HoldCo), and Trulia, Inc., a Delaware corporation (Trulia) entered into an Agreement and Plan of Merger (the Merger Agreement), pursuant to which Zillow agreed to acquire Trulia. Trulia s mobile and web products provide buyers, sellers, renters and real estate professionals with tools and information for the home search process and provide agents with an end-to-end technology platform that enables them to find and serve clients.

The Merger Agreement provides that, upon the terms and subject to the conditions set forth therein, (i) a newly-organized Washington corporation, and wholly owned subsidiary of HoldCo (Zillow Merger Sub), will merge with and into Zillow (the Zillow Merger), with Zillow as the surviving entity, and (ii) a newly-organized Delaware corporation, and wholly-owned subsidiary

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of HoldCo (Trulia Merger Sub), will merge with and into Trulia (the Trulia Merger and, together with the Zillow Merger, the Mergers), with Trulia as the surviving entity. As a result of the Mergers, both Zillow and Trulia will become wholly-owned subsidiaries of HoldCo. Pursuant to the terms of the Merger Agreement, at the effective time of the Zillow Merger (the Zillow Merger Effective Time), (i) each share of Zillow s Class A common stock will be converted into the right to receive one share of Class A common stock of HoldCo (HoldCo Class A Common Stock), and (ii) each share of Zillow s Class B common stock will be converted into the right to receive one share of Class B common stock of HoldCo. The Merger Agreement provides that, at the Zillow Merger Effective Time, all Zillow equity awards as of immediately prior to the Zillow Merger Effective Time will be assumed by HoldCo.

The consummation of the Zillow Merger and the Trulia Merger are each subject to customary conditions, including: (a) approval of the Merger Agreement by Zillow s shareholders and Trulia s stockholders; (b) expiration or termination of the waiting period under Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended; (c) absence of any applicable restraining order or injunction prohibiting the Mergers; (d) effectiveness of a registration statement on Form S-4; (e) absence of a material adverse effect with respect to each of Zillow and Trulia; (f) accuracy of the representations and warranties of each party, subject to specified materiality thresholds; (g) performance in all material respects by each party of its obligations under the Merger Agreement; (h) authorization for listing the HoldCo Class A Common Stock on the NASDAQ Global Select Market; and (i) with respect to Zillow, the absence of certain legal proceedLIGN="bottom">)

The following table presents the unaudited revenues and income from continuing operations for Cherry Creek, Plaza 25 and Lake Vista Pointe on a pro forma basis as if the Predecessor had completed the acquisition of the properties as of January 1, 2013:

	Nine months ended September 30, 2014	**Nine months ended September 30, 2013**
Total revenues as reported by City Office REIT, Inc. and Predecessor	$ 26,374,089	$ 14,625,527
Plus: Cherry Creek		5,186,771
Plaza 25	1,672,163	2,964,289
Lake Vista Pointe	1,879,889	2,591,968
Proforma total revenues	**$ 29,926,141**	**$ 25,368,555**
	$ 2,099,972	$ 2,108,319

Total operating income as reported by the City Office REIT, Inc. and Predecessor				
Property acquisition costs		1,551,347		(1,551,347)
Plus: Cherry Creek				527,261
Plaza 25		(91,120)		(161,531)
Lake Vista Pointe		289,237		398,246
Proforma operating income	**$**	**3,849,436**	**$**	**1,320,948**

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4. Lease Intangibles

Lease intangibles and the value of assumed lease obligations as of September 30, 2014 and December 31, 2013 were comprised as follows:

September 30, 2014	**Above Market Leases**	**In Place Leases**	**Leasing Commissions**	**Total**	**Below Market Leases**	**Below Market Ground Lease**	**Total**
Cost	$ 6,980,813	$ 22,370,372	$ 12,535,456	$ 41,886,641	$ (746,219)	$ (138,218)	$ (884,437)
Accumulated amortization	(3,131,678)	(8,604,160)	(3,155,524)	(14,891,362)	215,986	19,217	235,203
	$ 3,849,135	$ 13,766,212	$ 9,379,932	$ 26,995,279	$ (530,233)	$ (119,001)	$ (649,234)

December 31, 2013	**Above Market Leases**	**In Place Leases**	**Leasing Commissions**	**Total**	**Below Market Leases**	**Below Market Ground Lease**	**Total**
Cost	$ 3,043,030	$ 14,885,115	$ 5,447,198	$ 23,375,343	$ (168,904)	$ (138,218)	$ (307,122)
Accumulated Amortization	(1,306,326)	(6,536,311)	(1,781,143)	(9,623,780)	123,567	16,209	139,776
	$ 1,736,704	$ 8,348,804	$ 3,666,055	$ 13,751,563	$ (45,337)	$ (122,009)	$ (167,346)

The Company has adjusted acquired lease intangibles and accounts payable and accrued liabilities as of December 31, 2013 in the amount of $649,192 to conform with the current period presentation as of September 30, 2014. There was no impact to net income resulting from this adjustment.

The estimated aggregate amortization expense for lease intangibles for the five succeeding years and in the aggregate are as follows:

2014	$ 1,650,514
2015	6,343,804
2016	5,860,838
2017	3,605,134
2018	2,430,107
Thereafter	6,455,648
	$ 26,346,045

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5. Debt

The following table summarizes the secured indebtedness as of September 30, 2014 and December 31, 2013:

Property	September 30, 2014	December 31, 2013	Interest Rate as of September 30, 2014	Maturity
Revolving Credit Facility (1)	$ 6,400,000	$	LIBOR +2.75%(2)	April 2016
AmberGlen Mortgage Loan (3)	25,262,516		4.38%	May 2019
Midland Life Insurance (4)	95,000,000		4.34%	May 2021
Lake Vista Pointe (5)	18,460,000		4.28%	July 2018
Washington Group Plaza (5)	34,481,789	34,949,159	3.85%	July 2018
City Center (6)		22,333,938		June 2014
Central Fairwinds (7)		10,000,000		October 2015
Corporate Parkway (7)		19,133,333		April 2016
AmberGlen (8)		23,500,000		July 2017
Total	$ 179,604,305	$ 109,916,430		

All interest rates are fixed interest rates with the exception of the revolving credit facility (Revolving Credit Facility) as explained in footnote 1 below.

(1) *The Revolving Credit Facility currently has $30 million authorized with $26.4 million available immediately. In addition, the Revolving Credit Facility has an accordion feature that will permit us to borrow up to $150 million, subject to additional collateral availability and lender approval. The Revolving Credit Facility bears an interest rate of LIBOR plus 2.75% and requires the Company to maintain a fixed charge coverage ratio of no less than 1.60x. The Revolving Credit Facility is cross-collateralized by Central Fairwinds and Plaza 25.*

(2) *As of September 30, 2014, the 3 Month LIBOR rate was 0.27%.*

(3) *Following the Formation Transactions, on April 29, 2014, we entered into a new mortgage loan in relation to the AmberGlen property for $25.4 million. The loan bears an interest rate of 4.38% and matures on May 1, 2019. The Company is required to maintain a minimum net worth of $25 million and a minimum liquidity of $2 million.*

(4) *The loan is cross-collateralized by Corporate Parkway, Cherry Creek and City Center. Interest only until February 2016 then interest payable monthly plus principal based on 360 months of amortization. The loan bears a fixed interest rate of 4.34% and matures on May 6, 2021.*

(5) *Interest payable monthly plus principal based on 360 months of amortization.*

(6) *Interest payable monthly plus monthly principal payment of $20,000. This loan was extinguished on April 21, 2014 in relation to the Formation Transaction.*

(7) *Interest only payable monthly, principal due on maturity. This loan was extinguished on April 21, 2014 in relation to the Formation Transactions.*

(8) *This AmberGlen loan was refinanced on April 29, 2014 with the new AmberGlen loan discussed in footnote (3) above.*

On June 13, 2014, in connection with the addition of Plaza 25 as an additional collateral property, the Company, through its Operating Partnership, exercised a portion of the accordion feature of the Revolving Credit Facility and entered into an amendment to the credit agreement, thereby increasing the aggregate principal maximum amount available for borrowing under the Revolving Credit Facility to $30 million.

The scheduled principal repayments of mortgage payable as of September 30, 2014 are as follows:

2014	$ 259,621
2015	1,065,209
2016	8,420,590
2017	2,873,753
2018	34,836,409
Thereafter	132,148,723
	$ 179,604,305

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6. Fair Value of Financial Instruments

Fair value measurements are based on assumptions that market participants would use in pricing an asset or a liability. The hierarchy for inputs used in measuring fair value is as follows:

Level 1 Inputs	quoted prices in active markets for identical assets or liabilities
Level 2 Inputs	observable inputs other than quoted prices in active markets for identical assets and liabilities
Level 3 Inputs	unobservable inputs

Financial assets whose fair values are measured on a recurring basis consist only of an interest rate swap. The fair value of the interest rate swap is calculated based on Level 2 inputs.

As of September 30, 2014, the Company did not have any hedges or derivatives. As of December 31, 2013, the Predecessor had not designated its interest rate swap as a hedge. This derivative was not speculative and was used to manage the Predecessor s exposure to interest rate movements and other identified risks, but the Predecessor elected not to designate these instruments in hedging relationships based on the provisions in ASC 815-10. The changes in fair value of derivatives not designated in hedging relationships have been recognized in earnings. The interest rate swap was subsequently terminated upon completion of the IPO. The interest rate derivative outstanding as at December 31, 2013 was as follows:

Property	Type of Instrument	Notional amount	Maturity date	Effective rate	Fair Value as of December 31, 2013
City Center	Interest Rate Swap	$ 15,000,000		6.0%	$

The fair value of the Central Fairwinds earn-out (note 9) was derived by making assumptions on the timing of the lease up of vacant space and the net effective rents of those new leases and then applying an 8% discount rate to the resulting cash-flows to obtain a present value. The earn-out valuation assumes that approximately 17,000 square feet of additional leasing is completed between the date of the valuation and the end of the calculation period which would take the existing occupancy from 76% signed and committed at September 30, 2014 to 89% by September 2016 and stabilized at that level thereafter. The average net effective rent and incremental operating costs per square foot is assumed to be $14 and $4 respectively.

As of September 30, 2014, the estimated fair value of the earn-out liability is $8.0 million. The change in fair value for the three months ended September 30, 2014 was $1.0 million.

Level 3 sensitivity analysis:

The Company applies judgment in determining unobservable inputs used to calculate the fair value of Level 3 instruments. Level 3 instruments held by the Company include the earn-out. The unobservable inputs used in the valuation of the earn-out primarily include the net effective rent assumptions. A sensitivity analysis has been performed to determine the potential gain or loss by varying the significant unobservable inputs by increasing or decreasing them by 10%. The impact of applying these other reasonably possible inputs is a potential loss of $0.1 million and a potential gain of $0.1 million. This potential gain or loss would be recorded through profit and loss.

Fair Values of Financial Instruments Not Carried at Fair Value

With the exception of fixed rate mortgage loans payable, the carrying amounts of the Predecessor s financial instruments approximate their fair value. The Predecessor determines the fair value of its fixed rate mortgage loan payable based on a discounted cash flow analysis using a discount rate that approximates the current borrowing rates for instruments of similar maturities. Based on this, the Company has determined that the fair value of these instruments was $172,700,000 and $88,500,000 as of September 30, 2014 and December 31, 2013, respectively. Although the Predecessor has determined the majority of the inputs used to value its fixed rate debt fall within Level 2 of the fair value hierarchy, the credit valuation adjustments associated with its fixed rate debt utilize Level 3 inputs, such as estimates of current credit spreads. Accordingly, mortgage loans payable have been classified as Level 3 fair value measurements.

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7. Related Party Transactions

Formation Transactions

The formation transactions were completed on April 21, 2014 through the contribution of the initial properties by Second City Capital Partners II, Limited Partnership, Second City General Partner II, Limited Partnership, Gibralt US, Inc., GCC Amberglen Investments Limited Partnership and Daniel Rapaport (collectively the Second City Group). The Second City Group received as consideration for its contribution approximately $19.4 million in cash in accordance with the terms of its contribution agreement to acquire various noncontrolling interests and eliminate economic incentives in the initial properties. Additional payments to the Second City Group included $4.9 million for reimbursement of IPO costs and $1.8 million for working capital. On May 9, 2014, subsequent to the underwriters exercise of the overallotment option, net proceeds of $9.1 million was paid to the Second City Group to redeem 479,305 common units and 248,095 common stock.

Property Management Fees

Three of the properties (City Center, Central Fairwinds and AmberGlen) engaged related parties to perform asset and property management services for a fee ranging from 1.75% to 3.5% of gross revenue.

Prior to the Formation Transactions, the property manager of Washington Group Plaza was also entitled to an additional incentive commission equal to the lesser of (a) 15% of net operating income in excess of $5 million in 2013, $5.45 million in 2014 and $5.6 million in 2015; or (b) 1% of all monthly gross revenue. The asset and management agreement has an initial term of three years and will automatically renew for successive two year periods. This agreement can be terminated by the Company or the property manager upon thirty days prior written notice to the other party.

Deferred Offering and Financing Costs

Deferred offering and financing costs directly associated with the IPO and Formation Transactions of $4.9 million were reimbursed to Second City Capital Partners II, Limited Partnership, (Second City) upon the closing of the IPO.

8. Future Minimum Rent Schedule

Future minimum lease payments to be received as of September 30, 2014 under noncancellable operating leases for the next five years and thereafter are as follows:

2014	$ 8,532,363
2015	35,048,004
2016	28,542,171
2017	20,887,708
2018	17,401,040
Thereafter	65,593,200
	$ 176,004,486

The above minimum lease payments to be received do not include reimbursements from tenants for certain operating expenses and real estate taxes and do not include early termination payments provided for in certain leases.

Two state government tenants currently have the exercisable right to terminate their lease if the state does not appropriate rent in its annual budgets. The Company has determined that the occurrence of the government tenant not appropriating the rent in its annual budget is a remote contingency and accordingly recognizes lease revenue on a straight-line basis over the respective lease term. These tenants represent approximately 44.0% of the Company s total future minimum lease payments as of September 30, 2014.

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9. Commitments and Contingencies

Earn-Out

As part of the Formation Transactions and contribution agreement with respect to the Central Fairwinds property (which is currently approximately 76.0% leased, including committed tenants), the Company is obligated to make additional payments to Second City (each, an Earn-Out Payment). Earn-Out Payments are contingent on the property reaching certain specified occupancy levels through new leases to qualified tenants and exceeding a net operating income threshold, which grows annually. Second City will be entitled to receive an Earn-Out Payment (net of the associated leasing costs and inclusive of leasing commissions and tenant improvements/allowances and free rent) as and when the occupancy of Central Fairwinds reaches each of 70%, 80% and 90% (each, an Earn-Out Threshold) based on the incremental cash flow generated by new leases and a 7.75% stabilized capitalization rate. The Company will make any additional Earn-Out Payment within 30 days of the end of the Earn-Out Term based on new qualified leases entered into since the achievement of the last Earn-Out Threshold. Earn-Out Payments will be subject to a claw-back if a qualified tenant defaults in the payment of rent and is not replaced with another qualified tenant (see note 6).

As of September 30, 2014, the estimated fair value of the earn-out liability is $8.0 million. The change in fair value for the three months ended September 30, 2014 was $1.0 million.

Property Management Fees

Prior to the Formation Transactions, Washington Group Plaza engaged a related party to perform asset and management services for base and incentive fees as discussed in note 7.

Other

The Company is obligated under certain tenant leases to fund tenant improvements and the expansion of the underlying leased properties.

Under various federal, state and local laws, ordinances and regulations relating to the protection of the environment, a current or previous owner or operator of real estate may be liable for the cost of removal or remediation of certain hazardous or toxic substances disposed, stored, generated, released, manufactured or discharged from, on, at, under, or in a property. As such, the Company may be potentially liable for costs associated with any potential environmental remediation at any of its formerly or currently owned properties.

The Company believes that it is in compliance in all material respects with all federal, state and local ordinances and regulations regarding hazardous or toxic substances. Management is not aware of any environmental liability that it believes would have a material adverse impact on the Company s financial position or results of operations. Management is unaware of any instances in which the Company would incur significant environmental costs if any or all properties were sold, disposed of or abandoned. However, there can be no assurance that any such non-compliance, liability, claim or expenditure will not arise in the future.

The Company is involved from time to time in lawsuits and other disputes which arise in the ordinary course of business. As of September 30, 2014 management believes that these matters will not have a material adverse effect, individually or in the aggregate, on the Company s financial position or results of operations.

10. Earnings per Share

The following table shows the amounts used in computing the Company s basic and diluted earnings per share. As of the three and nine months ended September 30, 2014, there is no dilution to earnings per share.

	Three Months Ended September 30, 2014		Nine Months Ended September 30, 2014	
Numerator for loss per share basic and diluted				
Net loss	$	(2,373,873)	$	(3,237,974)
Less: Net loss attributable to noncontrolling interests in properties		(87,296)		(8,326)
Less: Net loss attributable to Predecessor				(1,973,197)
Less: Net loss attributable to Operating Partnership unitholders noncontrolling interests		693,971		1,508,097
Numerator for loss per share basic and diluted	$	(1,767,198)	$	(3,711,400)
Denominator for loss per share basic and diluted		8,192,915		8,133,940
Basic and diluted loss per share	$	(0.22)	$	(0.46)

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11. Stockholder s Equity

The Company issued 5,800,000 shares in conjunction with the IPO resulting in net proceeds of $63.4 million after deducting the underwriters discount and offering expenses. The underwriters of the IPO exercised their overallotment option to purchase an additional 782,150 shares of the Company s common stock resulting in additional net proceeds to us of $9.1 million after deducting underwriting discounts.

Noncontrolling Interests

Noncontrolling interests in the Company represent common units of the Operating Partnership held by the Predecessor s prior investors. Noncontrolling interests consisted of 3,251,904 Operating Partnership units and represented approximately 28.4% of the Operating Partnership as of September 30, 2014. Operating Partnership units and shares of common stock have essentially the same economic characteristics, as they share equally in the total net income or loss distributions of the Operating Partnership. Beginning on or after the date which is 12 months after the later of the completion of this offering or the date on which a person first became a holder of common units, each limited partner and assignees of limited partners will have the right, subject to the terms and conditions set forth in the partnership agreement, to require the Operating Partnership to redeem all or a portion of the common units held by such limited partner or assignee in exchange for a cash amount per common unit equal to the value of one share of common stock, determined in accordance with and subject to adjustment under the partnership agreement. The Company has the sole option at its discretion to redeem the common units by issuing common stock on a one-for-one basis. The Operating Partnership unitholders are entitled to share in cash distributions from the Operating Partnership in proportion to its percentage ownership of common units.

Restricted Stock Units

The Company has an equity incentive plan (Equity Incentive Plan) for certain officers, directors, advisors and personnel, and, with approval of the board of directors, for subsidiaries, the Advisor and their respective affiliates. The Equity Incentive Plan provides for grants of restricted common stock, restricted stock units, phantom shares, stock options, dividend equivalent rights and other equity-based awards (including LTIP Units), subject to the total number of shares available for issuance under the plan. The Equity Incentive Plan is administered by the compensation committee of the board of directors (the plan administrator).

The maximum number of shares of common stock that may be issued under the Equity Incentive Plan is 1,263,580 shares. To the extent an award granted under the Equity Incentive Plan expires or terminates, the shares subject to any portion of the award that expires or terminates without having been exercised or paid, as the case may be, will again become available for the issuance of additional awards.

On April 21, 2014, 352,272 restricted stock units (RSUs) were granted to the Company s executive officers and one of the directors at a grant date fair value of $12.50 totaling $4.4 million. During the three months ended September 30, 2014 an additional 30,100 RSUs were granted to directors and non-executive employees of the Advisor. The awards will vest in three equal, annual installments on each of the first three anniversaries of the date of grant. For the three and nine months ended September 30, 2014, the Company recognized net compensation expense of $0.4 million and $0.7 million respectively related to the RSU s.

A RSU award represents the right to receive shares of the Company s common stock in the future, after the applicable vesting criteria, determined by the plan administrator, has been satisfied. The holder of an award of RSU has no rights as a stockholder until shares of common stock are issued in settlement of vested restricted stock units. The plan administrator may provide for a grant of dividend equivalent rights in connection with the grant of RSU; provided, however, that if the restricted stock units do not vest solely upon satisfaction of continued employment or service, any payment in respect to the related dividend equivalent rights will be held by the Company and paid when, and only to the extent that, the related RSU vest.

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12. Subsequent Events

On November 7, 2014, the Company, through its Operating Partnership, entered into the Agreement of Purchase and Sale to acquire a property in Orlando, Florida for $26.5 million.

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

The following discussion and analysis is based on, and should be read in conjunction with, the condensed consolidated and combined financial statements and the related notes thereto of the City Office REIT, Inc. and the City Office Predecessor (as defined in this section) for the periods ended September 30, 2014 and September 30, 2013.

References to we, our, us, and the Company refer to City Office REIT, Inc., a Maryland corporation, together with our consolidated subsidiaries, including City Office REIT Operating Partnership L.P., a Maryland limited partnership, of which we are the sole general partner and which we refer to in this section as our Operating Partnership, except where it is clear from the context that the term only means City Office REIT, Inc.. References to the City Office Predecessor are to the real estate activity and holdings of the entities that own the historical interests in the AmberGlen, Central Fairwinds, City Center, Cherry Creek, Corporate Parkway and Washington Group Plaza properties.

Cautionary Statement Regarding Forward Looking Statements

This quarterly report on Form 10-Q, including Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations, contains both historical and forward-looking statements. All statements, other than statements of historical fact are, or may be deemed to be, forward looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These forward looking statements are not based on historical facts, but rather reflect our current expectations and projections about our future results, performance, prospects and opportunities. We have tried to identify these forward looking statements by using words including anticipate, believe, expect, intend, may, mi plan, estimate, project, should, will, result and similar terms and phrases. These forward looking statements a subject to a number of known and unknown risks, uncertainties and other factors that are difficult to predict and which could cause our actual future results, performance, prospects or opportunities to differ materially from those expressed in, or implied by, these forward looking statements. These risks, uncertainties and other factors include, among others: changes in the real estate industry and in performance of the financial markets; competition in the leasing market; the demand for and market acceptance of our properties for rental purposes; the amount and growth of our expenses; tenant financial difficulties and general economic conditions, including interest rates, as well as economic conditions in our geographic markets; defaults or non-renewal of leases; risks associated with joint venture partners; the risks associated with the ownership and development of real property, including risks related to natural disasters; risks associated with property acquisitions, the failure to acquire or sell properties as and when anticipated; the outcome of claims and litigation involving or affecting the Company; the ability to satisfy conditions necessary to close pending transactions; our failure to maintain our status as real estate investment trust, or REIT; and other factors described in our news releases and filings with the Securities and Exchange Commission (the SEC), including but not limited to our reports on Form 8-K. The forward looking statements included in this report are made only as of the date of this report, and except as otherwise required by federal securities law, we do not have any obligation to publicly update or revise any forward looking statements to reflect subsequent events or circumstances.

Overview

Company

The Company was organized in the state of Maryland on November 26, 2013. On April 21, 2014, Company completed its initial public offering (IPO) of shares of the Company s common stock. The Company contributed the net proceeds of the IPO to our Operating Partnership in exchange for common units in our Operating Partnership.

Both the Company and our Operating Partnership commenced operations upon completion of the IPO and certain related formation transactions (the Formation Transactions).

The Company s interest in the Operating Partnership entitles the Company to share in distributions from, and allocations of profits and losses of, our Operating Partnership in proportion to the Company s percentage ownership of common units. As the sole general partner of our Operating Partnership, the Company has the exclusive power under the partnership agreement to manage and conduct our Operating Partnership s business, subject to limited approval and voting rights of the limited partners.

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On April 21, 2014, the Company closed the IPO, pursuant to which it sold 5,800,000 shares of common stock to the public at a public offering price of $12.50 per share. The Company raised $72.5 million in gross proceeds, resulting in net proceeds to us of approximately $63.4 million after deducting approximately $5.1 million in underwriting discounts and approximately $4.0 million in other expenses relating to the IPO. On May 9, 2014, the underwriters of the IPO exercised their overallotment option to purchase an additional 782,150 shares of the Company s common stock at the IPO price of $12.50 a share resulting in additional gross proceeds of approximately $9.8 million. The net proceeds to the Company were $9.1 million after deducting approximately $0.7 million in underwriting discounts. The Company s common stock began trading on the New York Stock Exchange under the symbol CIO on April 15, 2014.

Pursuant to the Formation Transactions and exercise of the underwriters over-allotment option, our Operating Partnership acquired a 100% interest in each of the Washington Group Plaza, Cherry Creek and Corporate Parkway properties and acquired an approximate 76% economic interest in the AmberGlen property, 90% interest in the Central Fairwinds property and 95% interest in the City Center property. These initial property interests were contributed in exchange for 3,731,209 common units, 1,610,765 shares of our common stock and $19.4 million of cash. On May 9, 2014, subsequent to the exercise of the underwriters overallotment option, 479,305 common units and 248,095 common stock were redeemed for $9.1 million in cash.

The Company intends to elect to be taxed and operate in a manner that will allow it to qualify as a REIT commencing with its taxable year ending December 31, 2014. Subject to qualification as a REIT, the Company will be permitted to deduct distributions paid to its stockholders, eliminating the U.S. federal taxation of income represented by such distributions at the Company level. REITs are subject to a number of organizational and operational requirements. If the Company fails to qualify as a REIT in any taxable year, the Company will be subject to U.S. federal income tax (including any applicable alternative minimum tax) on its taxable income at regular corporate tax rates.

Pursuant to the JOBS Act, the Company qualifies as an emerging growth company (EGC). An EGC may choose to take advantage of the extended private company transition period provided for complying with new or revised accounting standards that may be issued by the Financial Accounting Standards Board (FASB) or the SEC. The Company has elected to opt out of such extended transition period. This election is irrevocable.

Indebtedness

In connection with the IPO and the related formation transactions, the Company, through our Operating Partnership, extinguished the mortgage loan secured by the Central Fairwinds property and completed a refinancing of three properties (Cherry Creek, City Center and Corporate Parkway) with a new $95 million non-recourse mortgage loan and proceeds from the IPO. On April 29, 2014, the Company, through its Operating Partnership, completed a $25.4 million refinancing of the AmberGlen property. Following the formation transactions, the Washington Group Plaza property remained subject to the existing mortgage loan. On June 13, 2014, in connection with the addition of Plaza 25 as an additional collateral security under the secured credit facility (Secured Credit Facility), we, through our Operating Partnership, exercised a portion of the accordion feature of the Secured Credit Facility and entered into an amendment to the credit agreement, thereby increasing the aggregate principal maximum amount available for borrowing under the Secured Credit Facility to $30 million.

For additional information regarding the new mortgage loan, the AmberGlen Mortgage loan, the Washington Mortgage loan and the Secured Credit Facility, please refer to Liquidity and Capital Resources below.

Revenue Base

Upon completion of the IPO and the related Formation Transactions, we owned six office complexes comprised of 16 office buildings with a total of approximately 1.85 million square feet of NRA. As of September 30, 2014, our initial properties were approximately 91% leased (or 93% after giving effect to committed leases, the terms of which have not yet commenced).

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Office Leases

Historically, most leases for our initial properties were on a full-service gross or net lease basis, and we expect to continue to use such leases in the future. A full-service gross lease generally has a base year expense stop, whereby we pay a stated amount of expenses as part of the rent payment while future increases (above the base year stop) in property operating expenses are billed to the tenant based on such tenant s proportionate square footage in the property. The property operating expenses are reflected in operating expenses, however only the increased property operating expenses above the base year stop recovered from tenants are reflected as tenant recoveries in the statements of operations. In a net lease, the tenant is typically responsible for all property taxes and operating expenses. As such, the base rent payment does not include any operating expenses, but rather all such expenses are billed to or paid by the tenant. The full amount of the expenses for this lease type is reflected in operating expenses, and the reimbursement is reflected in tenant recoveries. The tenants in the Corporate Parkway property and the Lake Vista Pointe property have net leases. We are also a lessor for a fee simple ground lease at the AmberGlen property. All of our remaining leases are full-service gross leases.

Interest Rate Contracts

As of September 30, 2014, the Company did not have any interest rate contracts.

Factors That May Influence Our Operating Results and Financial Condition

Business and Strategy

We focus on owning and acquiring office properties in select target markets. Our target markets generally possess favorable economic growth trends, growing populations with above-average employment growth forecasts, a large number of government offices, large international, national and regional employers across diversified industries, are generally low-cost centers for business operations, and exhibit favorable occupancy trends. We utilize our Advisor s market-specific knowledge and relationships as well as the expertise of local real estate operators and our investment partners to identify acquisition opportunities that we believe will offer cash flow stability and long-term value appreciation. Our target markets are attractive, among other reasons, because we believe that ownership is often concentrated among local real estate operators that typically do not benefit from the same access to capital as public REITs and there is a relatively low level of participation of large institutional investors. We believe that these factors result in attractive pricing levels and risk-adjusted returns.

Rental Revenue and Tenant Recoveries

The amount of net rental revenue generated by our properties will depend principally on our ability to maintain the occupancy rates of currently leased space and to lease currently available space and space that becomes available from lease terminations. As of September 30, 2014, our properties were approximately 92% leased (or 93% when giving effect to committed leases, the terms of which have not yet commenced). The amount of rental revenue generated also depends on our ability to maintain or increase rental rates at our properties. We believe that the average rental rates for the portfolio of our properties are generally in-line or slightly below the current average quoted market rates. Negative trends in one or more of these factors could adversely affect our rental revenue in future periods. Future economic downturns or regional downturns affecting our markets or submarkets or downturns in our tenants industries that impair our ability to renew or re-let space and the ability of our tenants to fulfill their lease commitments, as in the case of tenant bankruptcies, could adversely affect our ability to maintain or increase rental rates at our properties. In addition, growth in rental revenue will also partially depend on our ability to acquire additional properties that meet our investment criteria.

Operating Expenses

Our operating expenses generally consist of utilities, property and ad valorem taxes, insurance and site maintenance costs. Increases in these expenses over tenants   base years are generally passed along to tenants in our full-service gross leased properties and are generally paid in full by tenants in our net leased properties. As a public

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company, we estimate that our annual general and administrative expenses will increase due to increased legal, insurance, accounting and other expenses related to corporate governance, SEC reporting and other compliance matters, compared to the period prior to the IPO.

Conditions in Our Markets

Positive or negative changes in economic or other conditions in the markets we operate in, including state budgetary shortfalls, employment rates, natural hazards and other factors, may impact our overall performance.

Summary of Significant Accounting Policies

The interim financial statements follow the same policies and procedures as outlined in the audited combined financial statements of the Predecessor for the year ended December 31, 2013, included in the Company s final prospectus dated April 14, 2014.

Results of Operations

Comparison of Three Months Ended September 30, 2014 to Three Months Ended September 30, 2013

The three months ended September 30, 2014 include the combined results of the Company whereas the comparable three-month period in 2013 pertain to the results of the City Office Predecessor and accordingly may not be directly comparable due to the impact of the Formation Transactions on April 21, 2014. In the forthcoming comparison, we have highlighted the impact of the IPO and formation transactions where applicable.

Revenue

Total Revenue. Revenue includes net rental income, including parking, signage and other income, as well as the recovery of operating costs and property taxes from tenants. Total revenues increased $3.2 million, or 46%, to $10.0 million for the three-month period ended September 30, 2014 compared to $6.8 million in the corresponding period in 2013. Revenue increased by $1.0 million from the acquisition of the Plaza 25 property in September 2014 and $0.6 million from the acquisition of Lake Vista Pointe in July 2014. $1.7 million of the increase is a result of the consolidation of the Cherry Creek property. In January 2014, we acquired the remaining 57.7% of the property we did not already own to bring our ownership to 100%, whereas previously the property was accounted for using the equity method. AmberGlen, City Center and Central Fairwinds revenues were relatively unchanged in comparison to the prior year. The remaining properties were relatively unchanged as a small increase in rental income at AmberGlen due to increased occupancy offset a decrease at Corporate Parkway due to the straight line rent calculation.

Rental Income. Rental income includes net rental income, income from a ground lease and lease termination income. Total rental income increased $2.8 million, or 45%, to $9.0 million for the three-month period ended September 30, 2014 compared to $6.2 million for the three-month period ended September 30, 2013. The increase in rental income was primarily due to the acquisitions described above. The acquisition of the Plaza 25, Lake Vista Pointe and Cherry Creek properties contributed an additional $0.9 million, $0.4 million, and $1.6 million in rental income, respectively. The remaining properties were relatively unchanged as a small increase in rental income at AmberGlen due to increased occupancy offset a decrease at Corporate Parkway due to the straight line rent calculation.

Expense Reimbursement. Total expense reimbursement increased $0.4 million, or 108%, to $0.8 million for the three-month period ended September 30, 2014 compared to $0.4 million for the same period in 2013, primarily due to the acquisition of the Plaza 25, Lake Vista Pointe and Cherry Creek properties described above.

Other. Other revenue includes parking, signage and other miscellaneous income. Total other revenues remained relatively unchanged for the three-month period ended September 30, 2014 compared to the corresponding period in 2013.

Operating Expenses

Total Operating Expenses. Total operating expenses consists of property operating expenses, as well as insurance, property taxes, property management fees, acquisition costs, base management fees, stock-based compensation, general and administrative expenses and depreciation and amortization. Total operating expenses increased by $4.3 million, or 85%, to $9.4 million for the three-month period ended September 30, 2014, from $5.1 million for the same period in 2013, primarily due to the acquisitions described above. Total operating expenses increased by $1.0 million, $0.6 million and $1.4 million, respectively, from the acquisition of the Plaza 25 property in June 2014, the acquisition of the Lake Vista Pointe property and the consolidation of the Cherry Creek property beginning January 2014. AmberGlen, City Center, Corporate Parkway, Washington Group Plaza and Central Fairwinds operating expenses were unchanged in comparison to the prior year. The remaining $1.3 million increase relates to stock-based compensation, base management fees and general and administrative expenses in relation to the formation of the Company on April 21, 2014.

Property Operating Expenses. Property operating expenses are comprised mainly of building common area and maintenance expenses, as well as certain expenses that are not recoverable from tenants, the majority of which are related to costs necessary to maintain the appearance and marketability of vacant space. In the normal course of business, property expenses fluctuate and are impacted by various factors including, but not limited to, occupancy levels, weather, utility costs, repairs, maintenance and re-leasing costs. Property operating expenses increased $1.0 million, or 53%, to $2.8 million for the three-month period ended September 30, 2014 compared to $1.8 million for the same period in 2013. The increase in property operating expenses was primarily due to the acquisitions described above. The acquisition of the Plaza 25, Lake Vista Pointe and Cherry Creek properties contributed an additional $0.3 million, $0.1 million and $0.6 million in additional property operating expenses, respectively.

Insurance. Insurance costs increased $0.1 million, or 16%, to $0.2 million for the three-month period ended September 30, 2014 compared to $0.1 million for the three-month period ended September 30, 2013 primarily due to the acquisition of the Plaza 25 and Lake Vista Pointe properties and the consolidation of the Cherry Creek property.

Property Taxes. Property taxes increased $0.3 million, or 64%, to $0.8 million for the three-month period ended September 30, 2014 compared to $0.5 million for the three-month period ended September 30, 2013. The increase is attributable to the acquisition of the Plaza 25 and Lake Vista Pointe properties and the consolidation of the Cherry Creek property.

Property Management Fees. Property management fees increased $0.1 million, or 57%, to $0.2 million for the three-month period ended September 30, 2014 compared to $0.1 million for the three-month period ended September 30, 2013, primarily due to the addition of the Plaza 25, Lake Vista Pointe and Cherry Creek properties.

Acquisition Costs. The acquisition costs in the current period of $0.4 million are related to the Lake Vista Pointe acquisition whereas in the prior period, there were no acquisitions.

Base Management Fee. Base management fee was $0.2 million for the three-month period ended September 30, 2014 representing the fee paid to our Advisor.

Stock-Based Compensation. Stock-based compensation was $0.4 million for the three-month period ended June 30, 2014 representing the amortization of the management equity grants issued as part of the Formation Transactions.

General and Administrative. General and administrative expenses were $0.4 million for the three-month period ended June 30, 2014 representing the public company costs incurred during the quarter which did not exist for the

Predecessor.

Depreciation and Amortization. Depreciation and amortization increased $1.6 million, or 60%, to $4.1 million for the three-month period ended September 30, 2014 compared to $2.5 million for the same period in 2013, primarily due to the addition of the Plaza 25, Lake Vista Pointe and Cherry Creek properties.

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Other Expense (Income)

Interest Expense, Net. Interest expense increased $0.4 million, or 22%, to $2.0 million for the three-month period ended September 30, 2014, compared to $1.7 million, for the corresponding period in 2013. Interest expense increased $0.2 million, and $0.6 million, respectively, due to interest expense associated with the Lake Vista Pointe, and Cherry Creek property debt. The Plaza 25 property was acquired with cash from proceeds of the IPO and as a result did not lead to an increase in interest expense. Interest expense on the Secured Credit Facility was $0.1 million. These increases were offset by the pay-off of the Central Fairwinds debt at the IPO which resulted in savings of $0.2 million and lower financings costs of $0.1 million on each of AmberGlen, City Center and Corporate Parkway due to the debt refinancings at the IPO.

Change in Fair Value of Earn-Out. Change in fair value of earn-out was $0.9 million for the three-month period ended September 30, 2014 representing the change in the estimated fair value of the earn-out liability on the Central Fairwinds property due to the leasing activity that occurred at the property during the period.

Comparison of Nine Months Ended September 30, 2014 to Nine Months Ended September 30, 2013

The nine months ended September 30, 2014 include the combined results of the Company for the period from April 21, 2014 through September 30, 2014, and the results of the City Office Predecessor for the period from January 1, 2014 through April 20, 2014. The comparable nine-month period in 2013 pertain to the results of the City Office Predecessor only and accordingly may not be directly comparable due to the impact of the Formation Transactions on April 21, 2014. The Company incurred a loss of $5.2 million since the date of IPO on April 21, 2014, which includes the loss on early extinguishment of City Office Predecessor debt of $1.7 million. In the forthcoming comparison, we have highlighted the impact of the IPO and formation transactions where applicable.

Revenue

Total Revenue. Revenue includes net rental income, including parking, signage and other income, as well as the recovery of operating costs and property taxes from tenants. Total revenues increased $11.8 million, or 80%, to $26.4 million for the nine month period ended September 30, 2014 compared to $14.6 million in the corresponding period in 2013. Revenue increased by $0.8 million from the acquisition of the Corporate Parkway property in May 2013, $3.5 million from the acquisition of the Washington Group Plaza property in June 2013 and $1.3 million from the acquisition of the Plaza 25 property in June 2014, $0.7 million from the acquisition of the Lake Vista Pointe property in July 2015. AmberGlen increased total revenues by $0.3 million due to the increased occupancy at the property over the prior year. The remaining $5.2 million increase is a result of the consolidation of the Cherry Creek property. In January 2014, we acquired the remaining 57.7% of the property we did not already own to bring our ownership to 100%, whereas previously the property was accounted for using the equity method. AmberGlen, City Center and Central Fairwinds revenues were relatively unchanged in comparison to the prior year.

Rental Income. Rental income includes net rental income, income from a ground lease and lease termination income. Total rental income increased $11.1 million, or 85%, to $24.0 million for the nine month period ended September 30, 2014 compared to $12.9 million for the nine month period ended September 30, 2013. The increase in rental income was primarily due to the acquisitions described above. The acquisition of the Corporate Parkway, Washington Group Plaza, Plaza 25, Lake Pointe Vista and Cherry Creek properties contributed an additional $0.8 million, $3.4 million, $1.2 million, $0.5 million and $4.8 million in rental income, respectively. AmberGlen increased total revenues by $0.4 million due to the increased occupancy at the property over the prior year.

Expense Reimbursement. Total expense reimbursement increased $0.7 million, or 64%, to $1.8 million for the nine month period ended September 30, 2014 compared to $1.1 million for the same period in 2013, primarily due to the acquisition of the Washington Group Plaza, Plaza 25, Lake Vista Pointe and Cherry Creek properties described above. The Corporate Parkway property, which was acquired in May 2013, is a net lease and does not have any expense reimbursements.

Other. Other revenue includes parking, signage and other miscellaneous income. Total other revenues were unchanged at $0.6 million for the nine month period ended September 30, 2014 as compared to the corresponding period in 2013. The Corporate Parkway property, which was acquired in May 2013, is a net lease and does not have any other income and minimal other income was generated by Washington Group Plaza, Plaza 25, Lake Vista Pointe and Cherry Creek.

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Operating Expenses

Total Operating Expenses. Total operating expenses consists of property operating expenses, as well as insurance, property taxes, property management fees, acquisition costs, base management fees, stock-based compensation, and general and administrative expenses and depreciation and amortization. Total operating expenses increased by $11.8 million, or 94%, to $24.3 million for the nine month period ended September 30, 2014, from $12.5 million for the same period in 2013, primarily due to the acquisitions described above. Total operating expenses increased by $2.7 million, $1.4 million, $0.6 million and $4.7 million, respectively, from the acquisition of the Washington Group Plaza property in June 2013, the acquisition of the Plaza 25 property in June 2014, the acquisition of the Lake Vista Pointe property in July 2014 and the consolidation of the Cherry Creek property beginning January 2014. The Corporate Parkway property, which was acquired in May 2013, is a net lease and does not have any significant operating expenses. AmberGlen, City Center and Central Fairwinds operating expenses were relatively unchanged in comparison to the prior year. The remaining increase relates to stock-based compensation, base management fees and general and administrative expenses in relation to the formation of the Company on April 21, 2014.

Property Operating Expenses. Property operating expenses are comprised mainly of building common area and maintenance expenses, as well as certain expenses that are not recoverable from tenants, the majority of which are related to costs necessary to maintain the appearance and marketability of vacant space. In the normal course of business, property expenses fluctuate and are impacted by various factors including, but not limited to, occupancy levels, weather, utility costs, repairs, maintenance and re-leasing costs. Property operating expenses increased $3.3 million, or 82%, to $7.3 million for the nine month period ended September 30, 2014 compared to $4.0 million for the same period in 2013. The increase in property operating expenses was primarily due to the acquisitions described above. The acquisition of the Washington Group Plaza, Plaza 25, Lake Vista Pointe and Cherry Creek properties contributed an additional $1.2 million, $0.4 million, $0.1 million and $1.5 million in additional property operating expenses, respectively.

Insurance. Insurance costs increased $0.1 million, or 31%, to $0.5 million for the nine month period ended September 30, 2014 compared to $0.4 million for the nine month period ended September 30, 2013 primarily due to the acquisition of the Washington Group Plaza, Corporate Parkway, Plaza 25 and Lake Vista Pointe properties and the consolidation of the Cherry Creek property.

Property Taxes. Property taxes increased $0.8 million, or 75%, to $1.8 million for the nine month period ended September 30, 2014 compared to $1.0 million for the nine month period ended September 30, 2013 primarily due to the acquisition of the Washington Group Plaza, Corporate Parkway, Plaza 25 and Lake Vista Pointe properties and the consolidation of the Cherry Creek property.

Property Management Fees. Property management fees increased $0.2 million, or 56%, to $0.6 million for the nine month period ended September 30, 2014 compared to $0.4 million for the nine month period ended September 30, 2013, primarily due to the additions noted above.

Acquisition Costs. Acquisition costs increased $0.1 million, or 5%, to $1.6 million for the nine month period ended September 30, 2014 compared to $1.5 million for the nine month period ended September 30, 2013. The acquisition costs in the current year are related to the Plaza 25, Lake Vista Pointe and Cherry Creek acquisitions whereas in the prior year, the acquisition costs related to Washington Group Plaza and Corporate Parkway properties.

Base Management Fee. Base Management Fee was $0.4 million for the nine month period ended September 30, 2014 representing the fee paid to our Advisor.

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Stock-Based Compensation. Stock-based compensation was $0.7 million for the nine month period ended September 30, 2014 representing the amortization of the management equity grants issued as part of the Formation Transactions.

General and Administrative. General and administrative expenses were $0.8 million for the nine month period ended September 30, 2014 representing the public company costs incurred since the completion of an initial public offering.

Depreciation and Amortization. Depreciation and amortization increased $5.4 million, or 103%, to $10.6 million for the nine month period ended September 30, 2014 compared to $5.2 million for the same period in 2013, primarily due to the addition of the Corporate Parkway, Washington Group Plaza, Plaza 25, Lake Vista Pointe and Cherry Creek properties.

Other Expense (Income)

Interest Expense, Net. Interest expense increased $5.1 million, or 137%, to $8.8 million for the nine month period ended September 30, 2014, compared to $3.7 million for the corresponding period in 2013. Interest expense increased $0.7 million, $0.6 million, $0.2 million and $2.9 million, respectively, due to interest expense associated with the Corporate Parkway, Washington Group Plaza, Lake Pointe Vista and Cherry Creek property debt. Amortization of deferred financing fees increased $0.9 million over the prior period due to the accelerated amortization on the Cherry Creek bridge loan incurred by the City Office Predecessor. The loss on early extinguishment of City Office Predecessor debt is a result of the write-off of deferred amortization expense and prepayment penalties of $1.7 million related to the City Center, Central Fairwinds, Corporate Parkway and AmberGlen debt as part of the Formation Transactions.

Change in Fair Value of Earn-Out. Change in fair value of earn-out was $1.0 million for the nine month period ended September 30, 2014 representing the change in the estimated fair value of the earn-out liability on the Central Fairwinds property.

Gain on Equity Investment. Gain on equity investment is related to the purchase in January 2014 of the remaining 57.7% of Cherry Creek property that we did not already own. As a result of this transaction, a gain of $4.5 million was recorded.

Equity in Income of Unconsolidated Entity. Equity in income of unconsolidated entity is related to the Cherry Creek property in which the City Office Predecessor owned 42.3% as of December 31, 2013. In January 2014, we acquired the remaining 57.7% of the property we did not already own to bring our ownership to 100% and thus began consolidating the property results.

Liquidity and Capital Resources

Analysis of Liquidity and Capital Resources

The Company had approximately $8.9 million of cash and cash equivalents and $13.2 million of restricted cash as of September 30, 2014. In addition, the Company drew down $6.4 million under the Secured Credit Facility in connection with is purchase of the Lake Vista Pointe property. It will continue to use the Secured Credit Facility, among other things, to finance the acquisition of other properties, to provide funds for tenant improvements and capital expenditures and to provide for working capital and other corporate purposes.

Our short-term liquidity requirements primarily consist of operating expenses and other expenditures associated with our properties, distributions to our limited partners and distributions to our stockholders required to qualify for REIT status, capital expenditures and, potentially, acquisitions. We expect to meet our short-term liquidity requirements through net cash provided by operations, reserves established from existing cash, the proceeds from this offering and borrowings under our Secured Credit Facility.

Our long-term liquidity needs consist primarily of funds necessary for the repayment of debt at maturity, property acquisitions and non-recurring capital improvements. We expect to meet our long-term liquidity requirements with net cash from operations, long-term secured and unsecured indebtedness and the issuance of equity and debt securities. We also may fund property acquisitions and non-recurring capital improvements using our Secured Credit Facility pending permanent financing.

We believe we have access to multiple sources of capital to fund our long-term liquidity requirements, including the incurrence of additional debt and the issuance of additional equity securities. However, we cannot assure you that this is or will continue to be the case. Our ability to incur additional debt is dependent on a number of factors, including our degree of leverage, the value of our unencumbered assets and borrowing restrictions that may be imposed by lenders. Our ability to access the equity capital markets is dependent on a number of factors as well, including general market conditions for REITs and market perceptions about the Company.

Consolidated Indebtedness as of September 30, 2014

As of September 30, 2014, the Company had approximately $179.6 million of outstanding consolidated indebtedness all of which is fixed rate debt. The following table sets forth information as of September 30, 2014 with respect to the Company s outstanding indebtedness.

Debt	**September 30, 2014**	**Interest Rate as of September 30, 2013**	**Maturity Date**
Secured Credit Facility (1)	$ 6,400,000	LIBOR(2) +2.75%(2)	April 2016
AmberGlen (3)	25,262,516	4.38%	May 2019
Midland Life Insurance (4)	95,000,000	4.34%	May 2021
Lake Vista Pointe (5)	18,460,000	4.28%	July 2024
Washington Group Plaza (5)	34,481,789	3.85%	July 2018
Total	**$ 179,604,305**		

(1) The Revolving Credit Facility currently has $30 million authorized with $26.4 million available immediately. In addition, the Revolving Credit Facility has an accordion feature that will permit us to borrow up to $150 million, subject to additional collateral availability and lender approval. The Revolving Credit Facility bears an interest rate of LIBOR plus 2.75% and requires the Company to maintain a fixed charge coverage ratio of no less than 1.60x. The Revolving Credit Facility is cross-collateralized by Central Fairwinds and Plaza 25.

(2) As of September 30, 2014, the 3 Month LIBOR rate was 0.27%.

(3) Following the Formation Transactions, on April 29, 2014, we entered into a new mortgage loan in relation to the AmberGlen property for $25.4 million. The loan bears an interest rate of 4.38% and matures on May 1, 2019. The Company is required to maintain a minimum net worth of $25 million and a minimum liquidity of $2 million.

(4) The loan is cross-collateralized by Corporate Parkway, Cherry Creek and City Center. Interest only until February 2016 then interest payable monthly plus principal based on 360 months of amortization. The loan bears a fixed interest rate of 4.34% and matures on May 6, 2021.

(5) Interest payable monthly plus principal based on 360 months of amortization.

Contractual Obligations and Other Long-Term Liabilities

The following table provides information with respect to the Company s commitments as of September 30, 2014, including any guaranteed or minimum commitments under contractual obligations. The table does not reflect available debt extension options.

	Payments Due by Period				
Contractual Obligation	**Total**	**2014**	**2015-2016**	**2017-2018**	**More than 5 years**
Principal payments on mortgage loans	$ 179,604,305	$ 259,621	$ 9,485,799	$ 37,710,162	$ 132,148,723
Interest payments	43,554,799	1,816,151	14,421,821	13,448,934	13,867,893
Tenant- related commitments	4,175,280	3,045,101	130,179		1,000,000
Total	$ 227,334,384	$ 5,120,873	$ 24,037,799	$ 51,159,096	$ 147,016,616

Cash Flows

Comparison of Period Ended September 30, 2014 to Period Ended September 30, 2013

Cash and cash equivalents were $8.9 million and $7.6 million as of September 30, 2014 and September 30, 2013, respectively.

Cash flow from operating activities. Net cash provided by (used in) operating activities decreased by $0.4 million to $6.0 million for the period ended September 30, 2014 compared to $6.4 million for the same period in 2013. The decrease was primarily attributable to the loss on early extinguishment of debt, offset by changes in rents receivable.

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Cash flow to investing activities. Net cash used in investing activities decreased by $7.6 million to $65.7 million for the period ended September 30, 2014 compared to $73.3 million for the same period in 2013. The net cash used in investing activities in 2014 was used to acquire Plaza 25, Lake Vista Pointe and the remaining 57.7% ownership in the Cherry Creek property, complete tenant improvements and associated costs to acquire equipment and enhance capital assets.

Cash flow from financing activities. Net cash provided by financing activities decreased by $9.9 million to $61.4 million for the period ended September 30, 2014 compared to $71.3 million for the period ended September 30, 2013. Cash flow from financing activities is primarily derived from the proceeds from the sale of common stock, and the re-financing and mortgage proceeds on new financing as part of the formation transactions, offset by mortgage payments during the period.

Off-Balance Sheet Arrangements

As of September 30, 2014, we did not have any off-balance sheet arrangements.

Inflation

Substantially all of our office leases provide for separate real estate tax and operating expense escalations. In addition, most of the leases provide for fixed rent increases. We believe that inflationary increases may be at least partially offset by the contractual rent increases and expense escalations described above.

Quantitative and Qualitative Disclosures about Market Risk

Our future income, cash flows and fair values relevant to financial instruments are dependent upon prevailing market interest rates. Market risk refers to the risk of loss from adverse changes in market prices and interest rates. We may use derivative financial instruments to manage or hedge interest rate risks related to borrowings. We do not use derivatives for trading or speculative purposes and only enter into contracts with major financial institutions based upon their credit rating and other factors. We have entered, and we will only enter into, contracts with major financial institutions based on their credit rating and other factors. As of September 30, 2014, the Company did not have any outstanding derivatives.

Interest risk amounts are our management s estimates based on the Company s capital structure and were determined by considering the effect of hypothetical interest rates on our financial instruments. These analyses do not consider the effect of any change in overall economic activity that could occur in that environment nor the change to the capital structure as a result of the IPO and Formation Transactions. We may take actions to further mitigate our exposure to changes in interest rates. However, due to the uncertainty of the specific actions that would be taken and their possible effects, these analyses assume no changes in the Company s financial structure.

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Item 3. Quantitative and Qualitative Disclosures about Market Risk

Our future income, cash flows and fair values relevant to financial instruments are dependent upon prevailing market interest rates. Market risk refers to the risk of loss from adverse changes in market prices and interest rates. We have used, and will use, derivative financial instruments to manage or hedge interest rate risks related to borrowings. We do not use derivatives for trading or speculative purposes and only enter into contracts with major financial institutions based upon their credit rating and other factors. We have entered, and we will only enter into, contracts with major financial institutions based on their credit rating and other factors. As of September 30, 2014, the Company did not have any outstanding derivatives.

As of September 30, 2014, approximately $173.2 million, or 96.4%, of our debt had fixed interest rates and approximately $6.4 million, or 3.6%, had variable interest rates. The variable rate indebtedness relates to borrowings under the Secured Credit Facility.

The variable rate component of our consolidated indebtedness is LIBOR-based. Assuming no increase in the amount of our variable rate debt as of September 30, 2014, if LIBOR were to increase by 100 basis points, the increase in interest expense on our variable rate debt would decrease our future earnings and cash flows by approximately $0.1 million annually. If LIBOR were to decrease by 100 basis points, interest expense on our variable rate debt would decrease by approximately $0.1 million annually.

Interest risk amounts are our management s estimates based on the Company s capital structure and were determined by considering the effect of hypothetical interest rates on our financial instruments. These analyses do not consider the effect of any change in overall economic activity that could occur in that environment nor the change to the capital structure as a result of the IPO and Formation Transactions. We may take actions to further mitigate our exposure to changes in interest rates. However, due to the uncertainty of the specific actions that would be taken and their possible effects, these analyses assume no changes in the Company s financial structure.

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Item 4. Controls and Procedures

We maintain disclosure controls and procedures (as such term is defined in Rule 13a-15(e) and 15d-15(e) under the Exchange Act of 1934, as amended (the Exchange Act)), that are designed to ensure that information required to be disclosed in our reports under the Exchange Act is processed, recorded, summarized and reported within the time periods specified in the rules and regulations of the SEC and that such information is accumulated and communicated to 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.

We have carried out an evaluation, under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer, regarding the effectiveness of our disclosure controls and procedures as of September 30, 2014, the end of the period covered by the report. Based on the foregoing, our Chief Executive Officer and Chief Financial Officer have concluded, as of September 30, 2014, that our disclosure controls and procedures were effective in ensuring that information required to be disclosed by us in reports filed or submitted under the Exchange Act (i) is processed, recorded, summarized and reported within the time periods specified in the SEC s rules and forms and (ii) is accumulated and communicated to our management, including our Chief Executive Officer and our Chief Financial Officer, as appropriate to allow for timely decisions regarding required disclosure.

No changes to our internal control over financial reporting were identified in connection with the evaluation referenced above that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We and our subsidiaries are, from time to time, parties to litigation arising from the ordinary course of their business. Our management does not believe that any such litigation will materially affect our financial position or operations.

Item 1A. Risk Factors

There have been no material changes from the risk factors disclosed in the section entitled Risk Factors of our final prospectus dated April 14, 2014.

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

On April 21, 2014, in connection with the Formation Transactions, we issued to certain prior investors in our properties an aggregate of 5,590,069 common units of limited partnership interest in our Operating Partnership (OP Units) with an aggregate value of approximately $69.9 million based on the IPO price. The issuance of such units was effected in reliance upon exemptions from registration provided by Section 4(2) of the Securities Act and Regulation D of the Securities Act. Pursuant to the partnership agreement of our Operating Partnership, limited partners of our Operating Partnership will have the right, commencing one year from the date of issuance of such units, to require our Operating Partnership to redeem part or all of their OP Units for cash equal to the then-current market value of an equal number of our common shares, or, at our election, for common shares on a one-for-one basis, subject to certain adjustments and the restrictions on ownership and transfer of our shares set forth in our charter.

On April 21, 2014, we closed the IPO, pursuant to which we sold 5,800,000 shares of our common stock to the public at a public offering price of $12.50 per share. We raised $72.5 million in gross proceeds, resulting in net proceeds to us of approximately $63.4 million after deducting approximately $5.1 million in underwriting discounts and approximately $4.0 million in other expenses relating to the IPO. On May 9, 2014, the underwriters of the IPO exercised their overallotment option to purchase an additional 782,150 shares of our common stock at the IPO price of $12.50 a share resulting in additional gross proceeds to us of approximately $9.8 million resulting in net proceeds to us of $9.1 million after deducting approximately $0.7 million in underwriting discounts.

All of the 6,582,150 shares of our common stock were sold pursuant to our registration statement on Form S-11, as amended (File No. 333-193219), that was declared effective by the SEC on April 14, 2014. Janney Montgomery Scott LLC, Wunderlich Securities, Inc. and Oppenheimer & Co. Inc. served as joint book-running managers for the offering and as representatives of the underwriters.

We contributed the net proceeds of the IPO to our Operating Partnership in exchange for OP Units, and our Operating Partnership used the net proceeds received from us as described below:

- approximately $19.4 million to acquire interests in our initial properties, including the payment of transaction expenses in connection with the contribution of our initial properties in the formation transactions;

- approximately $6.5 million to repay portions of certain mortgage loans;
- approximately $36.1 million for general working capital purposes, including payment of expenses associated with our Formation Transactions, future acquisitions and creating reserves for capital expenditures, tenant improvements and leasing commissions.

We used all of the additional net proceeds from the exercise of the overallotment option to redeem a portion of the common stock and OP Units issued to certain Second City entities in the Formation Transactions at the IPO price.

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There has been no material change in our planned use of proceeds from our IPO as described in the final prospectus filed with the SEC pursuant to Rule 424(b).

Item 3. Defaults Upon Senior Securities

None.

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Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

Exhibit number	Description
31.1	Certification of Periodic Report by Chief Executive Officer under Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Periodic Report by Chief Financial Officer under Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

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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.

CITY OFFICE REIT, INC.

Date: November 13, 2014

By: /s/ James Farrar
James Farrar
Chief Executive Officer

Date: November 13, 2014

By: /s/ Anthony Maretic
Anthony Maretic
Chief Financial Officer

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