VORNADO REALTY TRUST
Form 10-Q
May 04, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark one)

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)**

OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended: **March 31, 2015**

Or

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)**

OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from: **to**

Commission File Number: **001-11954**

<u>VORNADO REALTY TRUST</u>

(Exact name of registrant as specified in its charter)

Maryland (State or other jurisdiction of incorporation or organization)	**22-1657560** (I.R.S. Employer Identification Number)
888 Seventh Avenue, New York, New York (Address of principal executive offices)	**10019** (Zip Code)

(212) 894-7000

(Registrant's telephone number, including area code)

N/A

(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (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 o

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.

x Large Accelerated Filer	o Accelerated Filer
o Non-Accelerated Filer (Do not check if smaller reporting company)	o 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 o No x

As of March 31, 2015, 188,272,702 of the registrant's common shares of beneficial interest are outstanding.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

VORNADO REALTY TRUST
CONSOLIDATED BALANCE SHEETS
(UNAUDITED)

(Amounts in thousands, except share and per share amounts)	**March 31, 2015**	**December 31, 2014**
ASSETS		
Real estate, at cost:		
Land	$ 3,914,401	$ 3,861,913
Buildings and improvements	11,881,228	11,705,749
Development costs and construction in progress	1,157,180	1,128,037
Leasehold improvements and equipment	127,534	126,659
Total	17,080,343	16,822,358
Less accumulated depreciation and amortization	(3,248,078)	(3,161,633)
Real estate, net	13,832,265	13,660,725
Cash and cash equivalents	1,067,568	1,198,477
Restricted cash	198,672	176,204
Marketable securities	184,991	206,323
Tenant and other receivables, net of allowance for doubtful accounts of $12,456 and $12,210	110,477	109,998
Investments in partially owned entities	1,408,214	1,246,496
Real estate fund investments	554,426	513,973
Receivable arising from the straight-lining of rents, net of allowance of $3,083 and $3,188	816,661	787,271
Deferred leasing and financing costs, net of accumulated amortization of $289,589 and $281,109	478,507	475,158
Identified intangible assets, net of accumulated amortization of $200,330 and $199,821	229,579	225,155
Assets related to discontinued operations	35,342	2,238,474
Other assets	344,349	410,066
	$ 19,261,051	$ 21,248,320
LIABILITIES, REDEEMABLE NONCONTROLLING INTERESTS AND EQUITY		
Mortgages payable	$ 8,316,793	$ 8,263,165
Senior unsecured notes	847,332	1,347,159
Revolving credit facility debt	400,000	-
Accounts payable and accrued expenses	432,970	447,745
Deferred revenue	346,026	358,613
Deferred compensation plan	121,530	117,284
Liabilities related to discontinued operations	11,354	1,511,362
Other liabilities	436,608	375,830
Total liabilities	10,912,613	12,421,158
Commitments and contingencies		
Redeemable noncontrolling interests:		

Class A units - 11,640,982 and 11,356,550 units outstanding	1,303,790	1,336,780
Series D cumulative redeemable preferred unit - 1 unit outstanding	1,000	1,000
Total redeemable noncontrolling interests	1,304,790	1,337,780
Vornado shareholders' equity:		
Preferred shares of beneficial interest: no par value per share; authorized 110,000,000 shares; issued and outstanding 52,678,939 shares	1,277,014	1,277,026
Common shares of beneficial interest: $.04 par value per share; authorized 250,000,000 shares; issued and outstanding 188,272,702 and 187,887,498 shares	7,509	7,493
Additional capital	6,935,205	6,873,025
Earnings less than distributions	(2,006,439)	(1,505,385)
Accumulated other comprehensive income	72,609	93,267
Total Vornado shareholders' equity	6,285,898	6,745,426
Noncontrolling interests in consolidated subsidiaries	757,750	743,956
Total equity	7,043,648	7,489,382
	$ 19,261,051	$ 21,248,320

See notes to consolidated financial statements (unaudited).

VORNADO REALTY TRUST
CONSOLIDATED STATEMENTS OF INCOME
(UNAUDITED)

(Amounts in thousands, except per share amounts)	For the Three Months Ended March 31, 2015	2014
REVENUES:		
Property rentals	$ 500,274	$ 467,140
Tenant expense reimbursements	66,921	59,301
Fee and other income	39,607	35,940
Total revenues	606,802	562,381
EXPENSES:		
Operating	254,493	236,561
Depreciation and amortization	124,122	131,792
General and administrative	58,492	47,502
Acquisition and transaction related costs	1,981	1,285
Total expenses	439,088	417,140
Operating income	167,714	145,241
(Loss) income from partially owned entities	(2,405)	1,979
Income from real estate fund investments	24,089	18,148
Interest and other investment income, net	10,792	11,850
Interest and debt expense	(91,674)	(96,312)
Net gain on disposition of wholly owned and partially owned assets	1,860	9,635
Income before income taxes	110,376	90,541
Income tax expense	(971)	(851)
Income from continuing operations	109,405	89,690
Income from discontinued operations	15,841	8,466
Net income	125,246	98,156
Less net income attributable to noncontrolling interests in:		
Consolidated subsidiaries	(15,882)	(11,579)
Operating Partnership	(5,287)	(3,860)
Net income attributable to Vornado	104,077	82,717
Preferred share dividends	(19,484)	(20,368)
NET INCOME attributable to common shareholders	$ 84,593	$ 62,349
INCOME PER COMMON SHARE - BASIC:		
Income from continuing operations, net	$ 0.37	$ 0.29
Income from discontinued operations, net	0.08	0.04
Net income per common share	$ 0.45	$ 0.33
Weighted average shares outstanding	187,999	187,307
INCOME PER COMMON SHARE - DILUTED:		
Income from continuing operations, net	$ 0.37	$ 0.29
Income from discontinued operations, net	0.08	0.04
Net income per common share	$ 0.45	$ 0.33
Weighted average shares outstanding	189,336	188,240
DIVIDENDS PER COMMON SHARE	$ 0.63	$ 0.73

See notes to consolidated financial statements (unaudited).

VORNADO REALTY TRUST
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(UNAUDITED)

(Amounts in thousands)	For the Three Months Ended March 31, 2015	2014
Net income	$ 125,246	$ 98,156
Other comprehensive income (loss):		
Change in unrealized net (loss) gain on available-for-sale securities	(21,332)	13,125
Pro rata share of other comprehensive income (loss) of nonconsolidated subsidiaries	157	(8,286)
Change in value of interest rate swap and other	(771)	1,611
Comprehensive income	103,300	104,606
Less comprehensive income attributable to noncontrolling interests	(19,881)	(15,800)
Comprehensive income attributable to Vornado	$ 83,419	$ 88,806

See notes to consolidated financial statements (unaudited).

VORNADO REALTY TRUST
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
(UNAUDITED)

(Amounts in thousands)	Preferred Shares		Common Shares		Additional	Earnings Less Than	Accumulated Other Comprehensive Income	Non-controlling Interests in Consolidated	Total
	Shares	Amount	Shares	Amount	Capital	Distributions	(Loss)	Subsidiaries	Equity
Balance, December 31, 2014	52,679	$ 1,277,026	187,887	$ 7,493	$ 6,873,025	$ (1,505,385)	$ 93,267	$ 743,956	$ 7,489,382
Net income attributable to Vornado	-	-	-	-	-	104,077	-	-	104,077
Net income attributable to noncontrolling interests in consolidated subsidiaries	-	-	-	-	-	-	-	15,882	15,882
Distribution of Urban Edge Properties	-	-	-	-	-	(464,262)	-	(341)	(464,603)
Dividends on common shares	-	-	-	-	-	(118,447)	-	-	(118,447)
Dividends on preferred shares	-	-	-	-	-	(19,484)	-	-	(19,484)
Common shares issued:									
Upon redemption of Class A units, at redemption value	-	-	210	8	23,485	-	-	-	23,493
Under employees' share option plan	-	-	165	7	11,672	(2,579)	-	-	9,100
Under dividend	-	-	3	-	338	-	-	-	338

reinvestment plan									
Contributions:									
Real estate fund investments	-	-	-	-	-	-	-	51,350	51,350
Distributions:									
Real estate fund investments	-	-	-	-	-	-	-	(52,882)	(52,882)
Other	-	-	-	-	-	-	-	(125)	(125)
Conversion of Series A preferred shares to common shares	-	(12)	1	-	12	-	-	-	-
Deferred compensation shares and options	-	-	7	1	1,324	(359)	-	-	966
Change in unrealized net loss on available-for-sale securities	-	-	-	-	-	-	(21,332)	-	(21,332)
Pro rata share of other comprehensive income of nonconsolidated subsidiaries	-	-	-	-	-	-	157	-	157
Change in value of interest rate swap	-	-	-	-	-	-	(776)	-	(776)
Adjustments to carry redeemable Class A units at redemption value	-	-	-	-	25,349	-	-	-	25,349
Redeemable noncontrolling interests' share of above adjustments	-	-	-	-	-	-	1,288	-	1,288
Other	-	-	-	-	-	-	5	(90)	(85)

Balance, March 31, 2015	52,679	$ 1,277,014	188,273	$ 7,509	$ 6,935,205	$ (2,006,439)	$ 72,609	$ 757,750	$ 7,043,648

See notes to consolidated financial statements (unaudited).

VORNADO REALTY TRUST
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY - CONTINUED
(UNAUDITED)

(Amounts in thousands)	Preferred Shares		Common Shares		Additional	Earnings Less Than	Accumulated Other Comprehensive Income	Non-controlling Interests in Consolidated	Total
	Shares	Amount	Shares	Amount	Capital	Distributions	(Loss)	Subsidiaries	Equity
Balance, December 31, 2013	52,683	$ 1,277,225	187,285	$ 7,469	$ 7,143,840	$ (1,734,839)	$ 71,537	$ 829,512	$ 7,594,744
Net income attributable to Vornado	-	-	-	-	-	82,717	-	-	82,717
Net income attributable to noncontrolling interests in consolidated subsidiaries	-	-	-	-	-	-	-	11,579	11,579
Dividends on common shares	-	-	-	-	-	(136,761)	-	-	(136,761)
Dividends on preferred shares	-	-	-	-	-	(20,368)	-	-	(20,368)
Common shares issued:									
Upon redemption of Class A units, at redemption value	-	-	55	2	5,154	-	-	-	5,156
Under employees' share option plan	-	-	60	2	3,228	-	-	-	3,230
Under dividend reinvestment plan	-	-	5	-	446	-	-	-	446
Distributions:									
	-	-	-	-	-	-	-	(1,950)	(1,950)

Real estate fund investments									
Other	-	-	-	-	-	-	-	(142)	(142)
Deferred compensation shares and options	-	-	7	1	2,118	(340)	-	-	1,779
Change in unrealized net gain on available-for-sale securities	-	-	-	-	-	-	13,125	-	13,125
Pro rata share of other comprehensive loss of nonconsolidated subsidiaries	-	-	-	-	-	-	(8,286)	-	(8,286)
Change in value of interest rate swap	-	-	-	-	-	-	1,610	-	1,610
Adjustments to carry redeemable Class A units at redemption value	-	-	-	-	(136,937)	-	-	-	(136,937)
Redeemable noncontrolling interests' share of above adjustments	-	-	-	-	-	-	(361)	-	(361)
Other	-	-	-	-	(238)	(18)	1	1	(254)
Balance, March 31, 2014	52,683	$ 1,277,225	187,412	$ 7,474	$ 7,017,611	$ (1,809,609)	$ 77,626	$ 839,000	$ 7,409,327

See notes to consolidated financial statements (unaudited).

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VORNADO REALTY TRUST
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	For the Three Months Ended March 31,	
	2015	**2014**
(Amounts in thousands)		
Cash Flows from Operating Activities:		
Net income	$ 125,246	$ 98,156
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization (including amortization of deferred financing costs)	131,112	153,869
Return of capital from real estate fund investments	72,208	-
Net gains on sale of real estate and other	(32,243)	-
Straight-lining of rental income	(29,474)	(13,236)
Net realized and unrealized gains on real estate fund investments	(17,639)	(14,169)
Distributions of income from partially owned entities	15,874	12,966
Other non-cash adjustments	15,865	11,885
Amortization of below-market leases, net	(12,754)	(12,144)
Loss (income) from partially owned entities	2,405	(1,979)
Net gain on disposition of wholly owned and partially owned assets	(1,860)	(9,635)
Impairment losses	256	20,842
Changes in operating assets and liabilities:		
Real estate fund investments	(95,022)	(123)
Accounts receivable, net	975	(7,624)
Prepaid assets	62,658	53,841
Other assets	(13,093)	(18,297)
Accounts payable and accrued expenses	(12,691)	31,554
Other liabilities	(17,307)	3,225
Net cash provided by operating activities	194,516	309,131
Cash Flows from Investing Activities:		
Proceeds from sales of real estate and related investments	334,725	120,270
Development costs and construction in progress	(88,052)	(90,653)
Additions to real estate	(54,466)	(53,103)
Acquisitions of real estate and other	(49,878)	-
Investments in partially owned entities	(23,912)	(16,633)
Proceeds from repayments of mortgage and mezzanine loans receivable and other	16,763	69,347
Distributions of capital from partially owned entities	13,409	1,277
Restricted cash	1,282	52,256
Net cash provided by investing activities	149,871	82,761

See notes to consolidated financial statements (unaudited).

VORNADO REALTY TRUST
CONSOLIDATED STATEMENTS OF CASH FLOWS - CONTINUED
(UNAUDITED)

	For the Three Months Ended March 31,	
	2015	**2014**
(Amounts in thousands)		
Cash Flows from Financing Activities:		
Repayments of borrowings	$ (907,431)	$ (233,198)
Proceeds from borrowings	800,000	600,000
Cash included in the spin-off of Urban Edge Properties	(225,000)	-
Dividends paid on common shares	(118,447)	(136,761)
Distributions to noncontrolling interests	(60,287)	(10,474)
Contributions from noncontrolling interests	51,350	-
Dividends paid on preferred shares	(19,484)	(20,368)
Proceeds received from exercise of employee share options	12,018	3,676
Debt issuance costs	(5,076)	(20,752)
Repurchase of shares related to stock compensation agreements and/or related tax withholdings	(2,939)	(578)
Net cash (used in) provided by financing activities	(475,296)	181,545
Net (decrease) increase in cash and cash equivalents	(130,909)	573,437
Cash and cash equivalents at beginning of period	1,198,477	583,290
Cash and cash equivalents at end of period	$ 1,067,568	$ 1,156,727
Supplemental Disclosure of Cash Flow Information:		
Cash payments for interest, excluding capitalized interest of $8,479 and $13,622	$ 91,702	$ 100,209
Cash payments for income taxes	$ 2,175	$ 1,214
Non-Cash Investing and Financing Activities:		
Non-cash distribution of Urban Edge Properties:		
Assets	$ 1,722,263	$ -
Liabilities	(1,482,660)	-
Equity	(239,603)	-
Transfer of interest in real estate to Pennsylvania Real Estate Investment Trust	(145,313)	-
Accrued capital expenditures included in accounts payable and accrued expenses	87,232	74,424
Financing assumed in acquisitions	62,000	-
Like-kind exchange of real estate:		
Acquisitions	57,722	-
Dispositions	(38,822)	-
Adjustments to carry redeemable Class A units at redemption value	25,349	(136,937)
Receipt of security deposits included in restricted cash and other liabilities	42,346	-
Write-off of fully depreciated assets	(18,790)	(67,204)
	-	59,375

Elimination of a mortgage and mezzanine loan asset and liability

See notes to consolidated financial statements (unaudited).

VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

1. Organization

Vornado Realty Trust ("Vornado") is a fully integrated real estate investment trust ("REIT") and conducts its business through, and substantially all of its interests in properties are held by, Vornado Realty L.P., a Delaware limited partnership (the "Operating Partnership"). Vornado is the sole general partner of, and owned approximately 93.9% of the common limited partnership interest in, the Operating Partnership at March 31, 2015. All references to "we," "us," "our," the "Company" and "Vornado" refer to Vornado Realty Trust and its consolidated subsidiaries, including the Operating Partnership.

On January 15, 2015, we completed the spin-off of substantially all of our retail segment comprised of 79 strip shopping centers, three malls, a warehouse park and $225,000,000 of cash to Urban Edge Properties ("UE") (NYSE: UE). As part of this transaction, we retained 5,717,184 UE operating partnership units (5.4% ownership interest). We are providing transition services to UE for an initial period of up to two years, including information technology, human resources, tax and financial reporting. UE is providing us with leasing and property management services for (i) the Monmouth Mall, (ii) certain small retail properties that we plan to sell, and (iii) our affiliate, Alexander's, Inc. (NYSE: ALX), Rego Park retail assets. Steven Roth, our Chairman and Chief Executive Officer is a member of the Board of Trustees of UE. The spin-off distribution was effected by Vornado distributing one UE common share for every two Vornado common shares. Beginning in the first quarter of 2015, the historical financial results of UE are reflected in our consolidated financial statements as discontinued operations for all periods presented.

2. Basis of Presentation

The accompanying consolidated financial statements are unaudited and include the accounts of Vornado and its consolidated subsidiaries, including the Operating Partnership. All intercompany amounts have been eliminated. In our opinion, all adjustments (which include only normal recurring adjustments) necessary to present fairly the financial position, results of operations and changes in cash flows have been made. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") have been condensed or omitted. These condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q of the SEC and should be read in conjunction with the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K, as amended, for the year ended December 31, 2014, as filed with the SEC.

We have made estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates. The results of operations for the three months ended March 31, 2015 are not necessarily indicative of the operating results for the full year.

Certain prior year balances have been reclassified in order to conform to the current period presentation. Beginning in the three months ended March 31, 2015, the Company classified signage revenue within “property rentals”. For the three months ended March 31, 2014, $9,300,000 related to signage revenue has been reclassified from “fee and other income” to “property rentals” to conform to the current period presentation.

VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(UNAUDITED)

3. Recently Issued Accounting Literature

In April 2014, the Financial Accounting Standards Board ("FASB") issued an update ("ASU 2014-08") *Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity* to ASC Topic 205, *Presentation of Financial Statements* and ASC Topic 360, *Property Plant and Equipment.* Under ASU 2014-08, only disposals that represent a strategic shift that has (or will have) a major effect on the entity's results and operations would qualify as discontinued operations. In addition, ASU 2014-08 expands the disclosure requirements for disposals that meet the definition of a discontinued operation and requires entities to disclose information about disposals of individually significant components that do not meet the definition of discontinued operations. ASU 2014-08 is effective for interim and annual reporting periods in fiscal years that began after December 15, 2014. Upon adoption of this standard on January 1, 2015, individual properties sold in the ordinary course of business are not expected to qualify as discontinued operations. The financial results of UE and certain other retail assets are reflected in our consolidated financial statements as discontinued operations for all periods presented (see Note 8 – *Dispositions*).

In May 2014, the FASB issued an update ("ASU 2014-09") establishing ASC Topic 606, *Revenue from Contracts with Customers*. ASU 2014-09 establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most of the existing revenue recognition guidance. ASU 2014-09 requires an entity to recognize revenue when it transfers 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 and also requires certain additional disclosures. ASU 2014-09 is effective for interim and annual reporting periods in fiscal years that begin after December 15, 2016. We are currently evaluating the impact of the adoption of ASU 2014-09 on our consolidated financial statements.

In June 2014, the FASB issued an update ("ASU 2014-12") to ASC Topic 718, *Compensation – Stock Compensation*. ASU 2014-12 requires an entity to treat performance targets that can be met after the requisite service period of a share based award has ended, as a performance condition that affects vesting. ASU 2014-12 is effective for interim and annual reporting periods in fiscal years that begin after December 15, 2015. We are currently evaluating the impact of the adoption of ASU 2014-12 on our consolidated financial statements.

In February 2015, the FASB issued an update ("ASU 2015-02") *Amendments to the Consolidation Analysis* to ASC Topic 810, *Consolidation*. ASU 2015-02 affects reporting entities that are required to evaluate whether they should consolidate certain legal entities. Specifically, the amendments: (i) modify the evaluation of whether limited partnerships and similar legal entities are variable interest entities ("VIEs") or voting interest entities, (ii) eliminate the presumption that a general partner should consolidate a limited partnership, (iii) affect the consolidated analysis of reporting entities that are involved with VIEs, and (iv) provide a scope exception for certain entities. ASU 2015-02 is effective for interim and annual reporting periods beginning after December 15, 2015. We are currently evaluating the impact of the adoption of ASU 2015-02 on our consolidated financial statements.

In April 2015, the FASB issued an update ("ASU 2015-03") *Simplifying the Presentation of Debt Issuance Costs* to ASC Topic 835, *Interest*. ASU 2015-03 requires that debt issuance costs be presented in the balance sheet as a direct deduction from the carrying amount of the debt liability to which they relate, consistent with debt discounts, as opposed to being presented as assets. ASU 2015-03 is effective for interim and annual reporting periods in fiscal years that begin after December 15, 2015. The adoption of this update on January 1, 2016 will not have a material impact on our consolidated financial statements.

4. Acquisitions

On January 20, 2015, we and one of the Fund's limited partners co-invested with the Fund to buy out the Fund's joint venture partner's 57% interest in the Crowne Plaza Times Square Hotel (see Note 5 – *Vornado Capital Partners Real Estate Fund*).

On March 18, 2015, we acquired the Center Building, a 437,000 square foot office building, located at 33-00 Northern Boulevard in Long Island City, New York, for $142,000,000, including the assumption of an existing $62,000,000, 4.43% mortgage maturing in October 2018.

As of March 31, 2015, we have made a $25,000,000 non-refundable deposit related to an agreement to acquire a property in the Penn Plaza submarket in Manhattan for $355,000,000.

On April 8, 2015, we made an $11,000,000 refundable contribution to a joint venture, in which we will have a 55% interest. The joint venture plans to develop a 173,000 square foot Class-A office building, located on the western side of the High Line at 510 West 22nd Street.

VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(UNAUDITED)

5. Vornado Capital Partners Real Estate Fund (the "Fund")

We are the general partner and investment manager of the Fund, which has an eight-year term and a three-year investment period that ended in July 2013. During the investment period, the Fund was our exclusive investment vehicle for all investments that fit within its investment parameters, as defined. The Fund is accounted for under ASC 946, *Financial Services – Investment Companies* and its investments are reported on its balance sheet at fair value, with changes in value each period recognized in earnings. We consolidate the accounts of the Fund into our consolidated financial statements, retaining the fair value basis of accounting.

On January 20, 2015, we and one of the Fund's limited partners co-invested with the Fund to buy out the Fund's joint venture partner's 57% interest in the Crowne Plaza Times Square Hotel (the "Co-Investment"). The purchase price for the 57% interest was approximately $95,000,000 (our share $39,000,000) which valued the property at approximately $480,000,000. The property is encumbered by a newly placed $310,000,000 mortgage loan bearing interest at LIBOR plus 2.80% which matures in December 2018 with a one-year extension option. Our aggregate ownership interest in the property increased to 33% from 11%. The Co-Investment is included as a component of "real estate fund investments" on our consolidated balance sheets.

On March 25, 2015, the Fund completed the sale of 520 Broadway in Santa Monica, CA for $91,650,000. The Fund realized a $24,705,000 net gain over the holding period.

At March 31, 2015, we had six investments with an aggregate fair value of $554,426,000, or $169,832,000 in excess of cost, and had remaining unfunded commitments of $102,324,000, of which our share was $25,581,000. Below is a summary of income from the Fund for the three months ended March 31, 2015 and 2014.

(Amounts in thousands)	For the Three Months Ended March 31,	
	2015	**2014**

Net investment income	$	6,450	$	3,979
Net realized gains on exited investments		24,705		-
Previously recorded unrealized gains on exited investments		(23,279)		-
Net unrealized gains on held investments		16,213		14,169
Income from real estate fund investments		24,089		18,148
Less income attributable to noncontrolling interests		(13,539)		(10,849)
Income from real estate fund investments attributable to Vornado (1)	$	10,550	$	7,299

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(1) Excludes property management, leasing and development fees of $704 and $618 for the three months ended March 31, 2015 and 2014, respectively, which are included as a component of "fee and other income" on our consolidated statements of income.

6. Marketable Securities

Below is a summary of our marketable securities portfolio as of March 31, 2015 and December 31, 2014.

(Amounts in thousands)	As of March 31, 2015			As of December 31, 2014		
	Fair Value	GAAP Cost	Unrealized Gain	Fair Value	GAAP Cost	Unrealized Gain
Equity securities:						
Lexington Realty Trust	$ 181,550	$ 72,549	$ 109,001	$ 202,789	$ 72,549	$ 130,240
Other	3,441	-	3,441	3,534	-	3,534
	$ 184,991	$ 72,549	$ 112,442	$ 206,323	$ 72,549	$ 133,774

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VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(UNAUDITED)

7. Investments in Partially Owned Entities

Toys "R" Us ("Toys")

As of March 31, 2015, we own 32.6% of Toys. We have not guaranteed any of Toys' obligations and are not committed to provide any support to Toys. Pursuant to ASC 323-10-35-20, we discontinued applying the equity method for our Toys' investment when the carrying amount was reduced to zero in the third quarter of 2014. We will resume application of the equity method if, during the period the equity method has been suspended, our share of unrecognized net income exceeds our share of unrecognized net losses.

In the first quarter of 2014, we recognized our share of Toys' fourth quarter net income of $75,196,000 and a corresponding non-cash impairment loss of the same amount.

Below is a summary of Toys' latest available financial information on a purchase accounting basis:

(Amounts in thousands)	Balance as of	
Balance Sheet:	**January 31, 2015**	**November 1, 2014**
Assets	$ 9,958,000	$ 11,267,000
Liabilities	9,014,000	10,377,000
Noncontrolling interests	85,000	82,000
Toys "R" Us, Inc. equity (1)	859,000	808,000
	For the Three Months Ended	
Income Statement:	**January 31, 2015**	**February 1, 2014**
Total revenues	$ 4,983,000	$ 5,267,000
Net income attributable to Toys	193,700	82,500

(1) At March 31, 2015, the carrying amount of our investment in Toys is less than our share of Toys' equity by approximately $279,936. This basis difference results primarily from non-cash impairment losses aggregating $355,953 that we have recognized through March 31, 2015. We have allocated the basis difference primarily to Toys' real estate, which is being amortized over its remaining estimated useful life.

Alexander’s, Inc. (“Alexander’s”) (NYSE: ALX)

As of March 31, 2015, we own 1,654,068 Alexander’s common shares, or approximately 32.4% of Alexander’s common equity. We manage, lease and develop Alexander’s properties pursuant to agreements which expire in March of each year and are automatically renewable.

As of March 31, 2015, the market value (“fair value” pursuant to ASC 820) of our investment in Alexander’s, based on Alexander’s March 31, 2015 closing share price of $456.58, was $755,214,000, or $623,071,000 in excess of the carrying amount on our consolidated balance sheet. As of March 31, 2015, the carrying amount of our investment in Alexander’s exceeds our share of the equity in the net assets of Alexander’s by approximately $41,048,000. The majority of this basis difference resulted from the excess of our purchase price for the Alexander’s common stock acquired over the book value of Alexander’s net assets. Substantially all of this basis difference was allocated, based on our estimates of the fair values of Alexander’s assets and liabilities, to real estate (land and buildings). We are amortizing the basis difference related to the buildings into earnings as additional depreciation expense over their estimated useful lives. This depreciation is not material to our share of equity in Alexander’s net income. The basis difference related to the land will be recognized upon disposition of our investment.

VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(UNAUDITED)

7. Investments in Partially Owned Entities - continued

Alexander's, Inc. ("Alexander's") (NYSE: ALX) - continued

Below is a summary of Alexander's latest available financial information:

(Amounts in thousands)	Balance as of	
Balance Sheet:	**March 31, 2015**	**December 31, 2014**
Assets	$ 1,433,000	$ 1,423,000
Liabilities	1,084,000	1,075,000
Stockholders' equity	349,000	348,000
	For the Three Months Ended March 31,	
Income Statement:	**2015**	**2014**
Total revenues	$ 52,000	$ 49,000
Net income attributable to Alexander's	18,000	15,000

Urban Edge Properties ("UE") (NYSE: UE)

As part of our spin-off of substantially all of our retail segment to UE on January 15, 2015 (see Note 1 – *Organization*), we retained 5,717,184 UE operating partnership units, representing a 5.4% ownership interest in UE. We account for our investment in UE under the equity method and will recognize our share of UE's earnings on a one-quarter lag basis. We are providing transition services to UE for an initial period of up to two years, including information technology, human resources, tax and financial reporting. UE is providing us with leasing and property management services for (i) the Monmouth Mall, (ii) certain small retail properties that we plan to sell, and (iii) our affiliate, Alexander's, Rego Park retail assets.

Pennsylvania Real Estate Investment Trust ("PREIT") (NYSE: PEI)

On March 31, 2015, we transferred the redeveloped Springfield Town Center, a 1,350,000 square foot mall located in Springfield, Fairfax County, Virginia, to PREIT Associates, L.P., which is the operating partnership of PREIT, in exchange for $485,313,000; comprised of $340,000,000 of cash and 6,250,000 PREIT operating partnership units (valued at $145,313,000 or $23.25 per PREIT unit) (See Note 8 – Dispositions). $19,000,000 of tenant improvements and allowances was credited to PREIT as a closing adjustment. As a result of this transaction, we own an 8.1% interest in PREIT. We account for our investment in PREIT under the equity method and will recognize our share of PREIT's earnings on a one-quarter lag basis.

Alexander's, Inc. ("Alexander's") (NYSE: ALX)

VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(UNAUDITED)

7. Investments in Partially Owned Entities – continued

Below are schedules summarizing our investments in, and (loss) income from, partially owned entities.

(Amounts in thousands)	Percentage Ownership at	Balance as of	
Investments:	**March 31, 2015**	**March 31, 2015**	**December 31, 2014**
Partially owned office buildings (1)	Various	$ 766,074	$ 760,749
PREIT Associates	8.1%	144,681	-
Alexander's	32.4%	132,143	131,616
India real estate ventures	4.1%-36.5%	67,159	76,752
Urban Edge	5.4%	25,206	-
Toys	32.6%	-	-
Other investments (2)	Various	272,951	277,379
		$ 1,408,214	$ 1,246,496

(1) Includes interests in 280 Park Avenue, 650 Madison Avenue, One Park Avenue, 666 Fifth Avenue (Office), 330 Madison Avenue and others.

(2) Includes interests in Independence Plaza, Monmouth Mall, 85 Tenth Avenue, Fashion Center Mall, 50-70 West 93rd Street and others.

(Amounts in thousands)	Percentage Ownership at	For the Three Months Ended March 31,	
Our Share of Net (Loss) Income:	**March 31, 2015**	**2015**	**2014**
Partially owned office buildings (1)	Various	$ (9,296)	$ (2,395)
Alexander's:			
Equity in net income	32.4%	5,594	4,759
Management, leasing and development fees		2,097	1,626
		7,691	6,385
Toys:			
Equity in net income	32.6%	-	75,196
Non-cash impairment losses		-	(75,196)
Management fees		1,454	1,847
		1,454	1,847
Urban Edge (2)	5.4%	584	-
India real estate ventures	4.1%-36.5%	(109)	(137)

Other investments [3]	Various	(2,729)	(3,721)
		$ (2,405)	$ 1,979

(1) Includes interests in 280 Park Avenue, 650 Madison Avenue, One Park Avenue, 666 Fifth Avenue (Office), 330 Madison Avenue and others.

(2) Represents fees earned pursuant to our transition services agreement with UE.

(3) Includes interests in Independence Plaza, Monmouth Mall, 85 Tenth Avenue, Fashion Center Mall, 50-70 West 93rd Street and others.

VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(UNAUDITED)

8. Dispositions

Discontinued Operations

On January 15, 2015, we completed the spin-off of substantially all of our retail segment comprised of 79 strip shopping centers, three malls, a warehouse park and $225,000,000 of cash to UE (NYSE: UE) (see Note 1 – *Organization*).

On March 13, 2015, we sold our lease position in Geary Street, CA for $34,189,000, which resulted in a net gain of $21,376,000.

On March 31, 2015, we transferred the redeveloped Springfield Town Center, a 1,350,000 square foot mall located in Springfield, Fairfax County, Virginia, to PREIT (see Note 7 – *Investments in Partially Owned Entities*). The financial statement gain was $7,823,000, of which $7,192,000 was recognized in the first quarter of 2015 and the remaining $631,000 was deferred based on our ownership interest in PREIT. On March 31, 2018, we will be entitled to additional consideration of 50% of the increase in the value of Springfield Town Center, if any, over $465,000,000, calculated utilizing a 5.5% capitalization rate. In the first quarter of 2014, we recorded a non-cash impairment loss of $20,000,000 on Springfield Town Center which is included in “income from discontinued operations” on our consolidated statements of income.

During the first quarter of 2015, we sold five residual retail properties, in separate transactions, for an aggregate of $10,731,000, which resulted in net gains of $3,675,000.

We have reclassified the revenues and expenses of the properties discussed above to “income from discontinued operations” and the related assets and liabilities to “assets related to discontinued operations” and “liabilities related to discontinued operations” for all of the periods presented in the accompanying consolidated financial statements. The net gains resulting from the sale of these properties are included in “income from discontinued operations” on our consolidated statements of income. The tables below set forth the assets and liabilities related to discontinued operations at March 31, 2015 and December 31, 2014 and their combined results of operations and cash flows for the three months ended March 31, 2015 and 2014.

	Balance as of	
(Amounts in thousands)	March 31, 2015	December 31, 2014
Assets related to discontinued operations:		
Real estate, net	$ 27,199	$ 2,028,677
Other assets	8,143	209,797
	$ 35,342	$ 2,238,474
Liabilities related to discontinued operations:		
Mortgages payable	-	1,288,535
Other liabilities (primarily deferred revenue in 2014)	11,354	222,827
	$ 11,354	$ 1,511,362

	For the Three Months Ended March 31,	
(Amounts in thousands)	2015	2014
Income from discontinued operations		
Total revenues	$ 19,958	$ 106,563
Total expenses	13,373	76,025
	6,585	30,538
Net gain on sale of lease position in Geary Street, CA	21,376	-
Net gains on sale of real estate	10,867	-
Transaction related costs	(22,645)	(499)
Impairment losses	(256)	(20,842)
Pretax income from discontinued operations	15,927	9,197
Income tax expense	(86)	(731)
Income from discontinued operations	$ 15,841	$ 8,466
Cash flows related to discontinued operations:		
Cash flows from operating activities	$ (36,672)	$ 15,535
Cash flows from investing activities	310,069	(30,397)

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VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(UNAUDITED)

9. Identified Intangible Assets and Liabilities

The following summarizes our identified intangible assets (primarily acquired in-place and above-market leases) and liabilities (primarily acquired below-market leases) as of March 31, 2015 and December 31, 2014.

	Balance as of	
(Amounts in thousands)	March 31, 2015	December 31, 2014
Identified intangible assets:		
Gross amount	$ 429,909	$ 424,976
Accumulated amortization	(200,330)	(199,821)
Net	$ 229,579	$ 225,155
Identified intangible liabilities (included in deferred revenue):		
Gross amount	$ 620,891	$ 657,976
Accumulated amortization	(304,929)	(329,775)
Net	$ 315,962	$ 328,201

Amortization of acquired below-market leases, net of acquired above-market leases, resulted in an increase to rental income of $12,450,000 and $9,712,000 for the three months ended March 31, 2015 and 2014, respectively. Estimated annual amortization of acquired below-market leases, net of acquired above-market leases, for each of the five succeeding years commencing January 1, 2016 is as follows:

(Amounts in thousands)	
2016	$ 36,804
2017	34,829
2018	33,546
2019	23,514
2020	21,505

Amortization of all other identified intangible assets (a component of depreciation and amortization expense) was $6,185,000 and $8,891,000 for the three months ended March 31, 2015 and 2014, respectively. Estimated annual amortization of all other identified intangible assets including acquired in-place leases, customer relationships, and third party contracts for each of the five succeeding years commencing January 1, 2016 is as follows:

(Amounts in thousands)		
2016	$	22,523
2017		17,692
2018		13,373
2019		11,425
2020		10,651

We are a tenant under ground leases for certain properties. Amortization of these acquired below-market leases, net of above-market leases resulted in an increase to rent expense of $458,000 for the three months ended March 31, 2015 and 2014. Estimated annual amortization of these below-market leases, net of above-market leases for each of the five succeeding years commencing January 1, 2016 is as follows:

(Amounts in thousands)		
2016	$	1,832
2017		1,832
2018		1,832
2019		1,832
2020		1,832

VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(UNAUDITED)

10. Debt

On January 1, 2015, we redeemed all of the $500,000,000 principal amount of our outstanding 4.25% senior unsecured notes, which were scheduled to mature on April 1, 2015, at a redemption price of 100% of the principal amount plus accrued interest through December 31, 2014.

On April 1, 2015, we completed a $308,000,000 refinancing of RiverHouse Apartments, a three building, 1,670 unit rental complex located in Arlington, VA. The loan is interest-only at LIBOR plus 1.28% and matures in 2025. We realized net proceeds of approximately $43,000,000. The property was previously encumbered by a 5.43%, $195,000,000 mortgage maturing in April 2015 and a $64,000,000 mortgage at LIBOR plus 1.53% maturing in 2018.

The following is a summary of our debt:

(Amounts in thousands)	**Interest Rate at March 31, 2015**	**Balance at March 31, 2015**	**Balance at December 31, 2014**
Mortgages Payable:			
Fixed rate	4.46%	$ 6,553,924	$ 6,499,396
Variable rate	2.21%	1,762,869	1,763,769
	3.99%	$ 8,316,793	$ 8,263,165
Unsecured Debt:			
Senior unsecured notes	3.68%	$ 847,332	$ 1,347,159
Revolving credit facility debt	1.23%	400,000	-
	3.39%	$ 1,247,332	$ 1,347,159

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VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(UNAUDITED)

11. Redeemable Noncontrolling Interests

Redeemable noncontrolling interests on our consolidated balance sheets are comprised primarily of Class A Operating Partnership units that are held by third parties and are recorded at the greater of their carrying amount or redemption value at the end of each reporting period. Changes in the value from period to period are charged to "additional capital" in our consolidated statements of changes in equity. Below is a table summarizing the activity of redeemable noncontrolling interests.

(Amounts in thousands)	
Balance at December 31, 2013	$ 1,003,620
Net income	3,860
Other comprehensive income	361
Distributions	(8,383)
Redemption of Class A units for common shares, at redemption value	(5,156)
Adjustments to carry redeemable Class A units at redemption value	136,937
Other, net	9,592
Balance at March 31, 2014	$ 1,140,831
Balance at December 31, 2014	$ 1,337,780
Net income	5,287
Other comprehensive loss	(1,288)
Distributions	(7,280)
Redemption of Class A units for common shares, at redemption value	(23,493)
Adjustments to carry redeemable Class A units at redemption value	(25,349)
Other, net	19,133
Balance at March 31, 2015	$ 1,304,790

As of March 31, 2015 and December 31, 2014, the aggregate redemption value of redeemable Class A units was $1,303,790,000 and $1,336,780,000, respectively.

Redeemable noncontrolling interests exclude our Series G-1 through G-4 convertible preferred units and Series D-13 cumulative redeemable preferred units, as they are accounted for as liabilities in accordance with ASC 480, *Distinguishing Liabilities and Equity*, because of their possible settlement by issuing a variable number of Vornado common shares. Accordingly, the fair value of these units is included as a component of "other liabilities" on our consolidated balance sheets and aggregated $55,097,000 as of March 31, 2015 and December 31, 2014. Changes in the value from period to period, if any, are charged to "interest and debt expense" on our consolidated statements of income.

VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(UNAUDITED)

12. Accumulated Other Comprehensive Income (“AOCI”)

The following tables set forth the changes in accumulated other comprehensive income (loss) by component.

		For the Three Months Ended March 31, 2014			
(Amounts in thousands)	Total	Securities available-for-sale	Pro rata share of nonconsolidated subsidiaries' OCI	Interest rate swap	Other
Balance as of December 31, 2013	$ 71,537	$ 119,309	$ (11,501)	$ (31,882)	$ (4,389)
OCI before reclassifications	6,089	13,125	(8,286)	1,610	(360)
Amounts reclassified from AOCI	-	-	-	-	-
Net current period OCI	6,089	13,125	(8,286)	1,610	(360)
Balance as of March 31, 2014	$ 77,626	$ 132,434	$ (19,787)	$ (30,272)	$ (4,749)

		For the Three Months Ended March 31, 2015			
(Amounts in thousands)	Total	Securities available-for-sale	Pro rata share of nonconsolidated subsidiaries' OCI	Interest rate swap	Other
Balance as of December 31, 2014	$ 93,267	$ 133,774	$ (8,992)	$ (25,803)	$ (5,712)
OCI before reclassifications	(20,658)	(21,332)	157	(776)	1,293
Amounts reclassified from AOCI	-	-	-	-	-
Net current period OCI	(20,658)	(21,332)	157	(776)	1,293
Balance as of March 31, 2015	$ 72,609	$ 112,442	$ (8,835)	$ (26,579)	$ (4,419)

VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(UNAUDITED)

13. Variable Interest Entities (“VIEs”)

At March 31, 2015 and December 31, 2014, we have unconsolidated VIEs comprised of our investments in the entities that own One Park Avenue, Independence Plaza and the Warner Building. We do not consolidate these entities because we are not the primary beneficiary and the nature of our involvement in the activities of these entities does not give us power over decisions that significantly affect these entities’ economic performance. We account for our investment in these entities under the equity method. As of March 31, 2015 and December 31, 2014, the net carrying amounts of our investment in these entities were $286,876,000 and $286,783,000, respectively, and our maximum exposure to loss in these entities is limited to our investment. We did not have any consolidated VIEs as of March 31, 2015 and December 31, 2014.

14. Fair Value Measurements

ASC 820, *Fair Value Measurement and Disclosures* defines fair value and establishes a framework for measuring fair value. The objective of fair value is to determine the price that would be received upon the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (the exit price). ASC 820 establishes a fair value hierarchy that prioritizes observable and unobservable inputs used to measure fair value into three levels: Level 1 – quoted prices (unadjusted) in active markets that are accessible at the measurement date for assets or liabilities; Level 2 – observable prices that are based on inputs not quoted in active markets, but corroborated by market data; and Level 3 – unobservable inputs that are used when little or no market data is available. The fair value hierarchy gives the highest priority to Level 1 inputs and the lowest priority to Level 3 inputs. In determining fair value, we utilize valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible, as well as consider counterparty credit risk in our assessment of fair value. Considerable judgment is necessary to interpret Level 2 and 3 inputs in determining the fair value of our financial and non-financial assets and liabilities. Accordingly, our fair value estimates, which are made at the end of each reporting period, may be different than the amounts that may ultimately be realized upon sale or disposition of these assets.

Financial Assets and Liabilities Measured at Fair Value on a Recurring Basis

Financial assets and liabilities that are measured at fair value on our consolidated balance sheets consist of (i) marketable securities, (ii) real estate fund investments, (iii) the assets in our deferred compensation plan (for which there is a corresponding liability on our consolidated balance sheet), (iv) mandatorily redeemable instruments (Series G-1 through G-4 convertible preferred units and Series D-13 cumulative redeemable preferred units), and (v) an interest rate swap. The tables below aggregate the fair values of these financial assets and liabilities by their levels in the fair value hierarchy at March 31, 2015 and December 31, 2014, respectively.

		As of March 31, 2015		
(Amounts in thousands)	**Total**	**Level 1**	**Level 2**	**Level 3**
Marketable securities	$ 184,991	$ 184,991	$ -	$ -
Real estate fund investments (75% of which is attributable to noncontrolling interests)	554,426	-	-	554,426
Deferred compensation plan assets (included in other assets)	121,530	56,694	-	64,836
Total assets	$ 860,947	$ 241,685	$ -	$ 619,262
Mandatorily redeemable instruments (included in other liabilities)	$ 55,097	$ 55,097	$ -	$ -
Interest rate swap (included in other liabilities)	26,574	-	26,574	-
Total liabilities	$ 81,671	$ 55,097	$ 26,574	$ -
		As of December 31, 2014		
(Amounts in thousands)	**Total**	**Level 1**	**Level 2**	**Level 3**
Marketable securities	$ 206,323	$ 206,323	$ -	$ -
Real estate fund investments (75% of which is attributable to noncontrolling interests)	513,973	-	-	513,973
Deferred compensation plan assets (included in other assets)	117,284	53,969	-	63,315
Total assets	$ 837,580	$ 260,292	$ -	$ 577,288
Mandatorily redeemable instruments (included in other liabilities)	$ 55,097	$ 55,097	$ -	$ -
Interest rate swap (included in other liabilities)	25,797	-	25,797	-
Total liabilities	$ 80,894	$ 55,097	$ 25,797	$ -

VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(UNAUDITED)

14. Fair Value Measurements – continued

Financial Assets and Liabilities Measured at Fair Value on a Recurring Basis - continued

Real Estate Fund Investments

At March 31, 2015, we had six investments with an aggregate fair value of $554,426,000, or $169,832,000 in excess of cost. These investments are classified as Level 3. We use a discounted cash flow valuation technique to estimate the fair value of each of these investments, which is updated quarterly by personnel responsible for the management of each investment and reviewed by senior management at each reporting period. The discounted cash flow valuation technique requires us to estimate cash flows for each investment over the anticipated holding period, which currently ranges from 0.8 to 5.8 years. Cash flows are derived from property rental revenue (base rents plus reimbursements) less operating expenses, real estate taxes and capital and other costs, plus projected sales proceeds in the year of exit. Property rental revenue is based on leases currently in place and our estimates for future leasing activity, which are based on current market rents for similar space plus a projected growth factor. Similarly, estimated operating expenses and real estate taxes are based on amounts incurred in the current period plus a projected growth factor for future periods. Anticipated sales proceeds at the end of an investment's expected holding period are determined based on the net cash flow of the investment in the year of exit, divided by a terminal capitalization rate, less estimated selling costs.

The fair value of each property is calculated by discounting the future cash flows (including the projected sales proceeds), using an appropriate discount rate and then reduced by the property's outstanding debt, if any, to determine the fair value of the equity in each investment. Significant unobservable quantitative inputs used in determining the fair value of each investment include capitalization rates and discount rates. These rates are based on the location, type and nature of each property, and current and anticipated market conditions, which are derived from original underwriting assumptions, industry publications and from the experience of our Acquisitions and Capital Markets departments. Significant unobservable quantitative inputs in the table below were utilized in determining the fair value of these real estate fund investments at March 31, 2015 and December 31, 2014.

Unobservable Quantitative Input	Range		Weighted Average (based on fair value of investments)	
	March 31, 2015	December 31, 2014	March 31, 2015	December 31, 2014
Discount rates	12.0% to 14.5%	12.0% to 17.5%	13.4%	13.7%
Terminal capitalization rates	4.8% to 6.5%	4.7% to 6.5%	5.5%	5.3%

The above inputs are subject to change based on changes in economic and market conditions and/or changes in use or timing of exit. Changes in discount rates and terminal capitalization rates result in increases or decreases in the fair values of these investments. The discount rates encompass, among other things, uncertainties in the valuation models with respect to terminal capitalization rates and the amount and timing of cash flows. Therefore, a change in the fair value of these investments resulting from a change in the terminal capitalization rate, may be partially offset by a change in the discount rate. It is not possible for us to predict the effect of future economic or market conditions on our estimated fair values.

The table below summarizes the changes in the fair value of real estate fund investments that are classified as Level 3, for the three months ended March 31, 2015 and 2014.

	Real Estate Fund Investments For the Three Months Ended March 31,	
(Amounts in thousands)	2015	2014
Beginning balance	$ 513,973	$ 667,710
Purchases	95,000	123
Dispositions / Distributions	(72,186)	-
Net unrealized gains	16,213	14,169
Net realized gains	1,426	-
Ending balance	$ 554,426	$ 682,002

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VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(UNAUDITED)

14. Fair Value Measurements – continued

Financial Assets and Liabilities Measured at Fair Value on a Recurring Basis - continued

Deferred Compensation Plan Assets

Deferred compensation plan assets that are classified as Level 3 consist of investments in limited partnerships and investment funds, which are managed by third parties. We receive quarterly financial reports from a third-party administrator, which are compiled from the quarterly reports provided to them from each limited partnership and investment fund. The quarterly reports provide net asset values on a fair value basis which are audited by independent public accounting firms on an annual basis. The third-party administrator does not adjust these values in determining our share of the net assets and we do not adjust these values when reported in our consolidated financial statements.

The table below summarizes the changes in the fair value of deferred compensation plan assets that are classified as Level 3, for the three months ended March 31, 2015 and 2014.

	Deferred Compensation Plan Assets For the Three Months Ended March 31,	
(Amounts in thousands)	**2015**	**2014**
Beginning balance	$ 63,315	$ 68,782
Purchases	624	1,644
Sales	(438)	(5,124)
Realized and unrealized gain	1,335	2,172
Other, net	-	153
Ending balance	$ 64,836	$ 67,627

Fair Value Measurements on a Nonrecurring Basis

Assets measured at fair value on a nonrecurring basis on our consolidated balance sheets consist primarily of real estate assets required to be measured for impairment at December 31, 2014. The fair value of our real estate assets was determined using widely accepted valuation techniques, including (i) discounted cash flow analysis, which considers, among other things, leasing assumptions, growth rates, discount rates and terminal capitalization rates, (ii) income capitalization approach, which considers prevailing market capitalization rates, and (iii) comparable sales activity.

	As of December 31, 2014			
(Amounts in thousands)	**Total**	**Level 1**	**Level 2**	**Level 3**
Real estate assets	$ 4,848	$ -	$ -	$ 4,848

VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(UNAUDITED)

14. Fair Value Measurements – continued

Financial Assets and Liabilities not Measured at Fair Value

Financial assets and liabilities that are not measured at fair value on our consolidated balance sheets include cash equivalents (primarily money market funds, which invest in obligations of the United States government), mortgage and mezzanine loans receivable and our secured and unsecured debt. Estimates of the fair value of these instruments are determined by the standard practice of modeling the contractual cash flows required under the instrument and discounting them back to their present value at the appropriate current risk adjusted interest rate, which is provided by a third-party specialist. For floating rate debt, we use forward rates derived from observable market yield curves to project the expected cash flows we would be required to make under the instrument. The fair value of cash equivalents and borrowings under our revolving credit facility is classified as Level 1, and the fair value of our mortgage and mezzanine loans receivable is classified as Level 3. The fair value of our secured and unsecured debt are classified as Level 2. The table below summarizes the carrying amounts and fair value of these financial instruments as of March 31, 2015 and December 31, 2014.

	As of March 31, 2015		**As of December 31, 2014**	
(Amounts in thousands)	**Carrying Amount**	**Fair Value**	**Carrying Amount**	**Fair Value**
Cash equivalents	$ 526,218	$ 526,000	$ 749,418	$ 749,000
Mortgage and mezzanine loans receivable	-	-	16,748	17,000
	$ 526,218	$ 526,000	$ 766,166	$ 766,000
Debt:				
Mortgages payable	$ 8,316,793	$ 8,334,000	$ 8,263,165	$ 8,224,000
Senior unsecured notes	847,332	898,000	1,347,159	1,385,000
Revolving credit facility debt	400,000	400,000	-	-
	$ 9,564,125	$ 9,632,000	$ 9,610,324	$ 9,609,000

15. Incentive Compensation

Our 2010 Omnibus Share Plan (the “Plan”) provides for grants of incentive and non-qualified stock options, restricted stock, restricted Operating Partnership units and Out-Performance Plan awards to certain of our employees and officers. We account for all stock-based compensation in accordance with ASC 718, *Compensation – Stock Compensation*. Stock-based compensation expense was $20,142,000 and $11,024,000 in the three months ended March 31, 2015 and 2014, respectively.

VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(UNAUDITED)

16. Fee and Other Income

The following table sets forth the details of fee and other income:

(Amounts in thousands)	For the Three Months Ended March 31, 2015	2014
BMS cleaning fees	$ 22,633	$ 18,956
Management and leasing fees	4,192	5,828
Lease termination fees	3,747	3,577
Other income	9,035	7,579
	$ 39,607	$ 35,940

Management and leasing fees include management fees from Interstate Properties, a related party, of $139,000 and $134,000 for the three months ended March 31, 2015 and 2014, respectively. The above table excludes fee income from partially owned entities, which is typically included in "(loss) income from partially owned entities" (see Note 7 – *Investments in Partially Owned Entities*).

17. Interest and Other Investment Income, Net

The following table sets forth the details of interest and other investment income:

(Amounts in thousands)	For the Three Months Ended March 31, 2015	2014
Dividends and interest on marketable securities	$ 3,203	$ 3,106
Mark-to-market of investments in our deferred compensation plan (1)	2,859	4,400
Interest on mezzanine loans receivable	1,674	2,384
Other, net	3,056	1,960
	$ 10,792	$ 11,850

(1) This income is entirely offset by the expense resulting from the mark-to-market of the deferred compensation plan liability, which is included in "general and administrative"

expense.

18. Interest and Debt Expense

The following table sets forth the details of interest and debt expense:

(Amounts in thousands)	For the Three Months Ended March 31, 2015	2014
Interest expense	$ 95,328	$ 105,512
Amortization of deferred financing costs	7,456	4,422
Capitalized interest and debt expense	(11,110)	(13,622)
	$ 91,674	$ 96,312

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VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(UNAUDITED)

19. Income Per Share

The following table provides a reconciliation of both net income and the number of common shares used in the computation of (i) basic income per common share - which includes the weighted average number of common shares outstanding without regard to dilutive potential common shares, and (ii) diluted income per common share - which includes the weighted average common shares and dilutive share equivalents. Dilutive share equivalents may include our Series A convertible preferred shares, employee stock options and restricted share awards.

(Amounts in thousands, except per share amounts)	For the Three Months Ended March 31, 2015	2014
Numerator:		
Income from continuing operations, net of income attributable to noncontrolling interests	$ 89,166	$ 74,743
Income from discontinued operations, net of income attributable to noncontrolling interests	14,911	7,974
Net income attributable to Vornado	104,077	82,717
Preferred share dividends	(19,484)	(20,368)
Net income attributable to common shareholders	84,593	62,349
Earnings allocated to unvested participating securities	(19)	(30)
Numerator for diluted income per share	$ 84,574	$ 62,319
Denominator:		
Denominator for basic income per share – weighted average shares	187,999	187,307
Effect of dilutive securities[(1)]:		
Employee stock options and restricted share awards	1,337	933
Denominator for diluted income per share – weighted average shares and assumed conversions	189,336	188,240

INCOME PER COMMON SHARE – BASIC:				
Income from continuing operations, net	$	0.37	$	0.29
Income from discontinued operations, net		0.08		0.04
Net income per common share	$	0.45	$	0.33
INCOME PER COMMON SHARE – DILUTED:				
Income from continuing operations, net	$	0.37	$	0.29
Income from discontinued operations, net		0.08		0.04
Net income per common share	$	0.45	$	0.33

(1) The effect of dilutive securities in the three months ended March 31, 2015 and 2014 excludes an aggregate of 11,488 and 11,326 weighted average common share equivalents, respectively, as their effect was anti-dilutive.

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VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(UNAUDITED)

20. Commitments and Contingencies

Insurance

We maintain general liability insurance with limits of $300,000,000 per occurrence and all risk property and rental value insurance with limits of $2.0 billion per occurrence, with sub-limits for certain perils such as floods. Our California properties have earthquake insurance with coverage of $180,000,000 per occurrence, subject to a deductible in the amount of 5% of the value of the affected property, up to a $180,000,000 annual aggregate. We maintain coverage for terrorism acts with limits of $4.0 billion per occurrence and in the aggregate, and $2.0 billion per occurrence and in the aggregate for terrorism involving nuclear, biological, chemical and radiological ("NBCR") terrorism events, as defined by Terrorism Risk Insurance Program Reauthorization Act, which expires in December 2020.

Penn Plaza Insurance Company, LLC ("PPIC"), our wholly owned consolidated subsidiary, acts as a re-insurer with respect to a portion of all risk property and rental value insurance and a portion of our earthquake insurance coverage, and as a direct insurer for coverage for NBCR acts. Coverage for acts of terrorism (excluding NBCR acts) is fully reinsured by third party insurance companies and the Federal government with no exposure to PPIC. For NBCR acts, PPIC is responsible for a deductible of $2,480,000 and 15% of the balance of a covered loss (16% effective January 1, 2016) and the Federal government is responsible for the remaining 85% of a covered loss (84% effective January 1, 2016). We are ultimately responsible for any loss incurred by PPIC.

We continue to monitor the state of the insurance market and the scope and costs of coverage for acts of terrorism. However, we cannot anticipate what coverage will be available on commercially reasonable terms in the future.

Our debt instruments, consisting of mortgage loans secured by our properties which are non-recourse to us, senior unsecured notes and revolving credit agreements contain customary covenants requiring us to maintain insurance. Although we believe that we have adequate insurance coverage for purposes of these agreements, we may not be able to obtain an equivalent amount of coverage at reasonable costs in the future. Further, if lenders insist on greater coverage than we are able to obtain it could adversely affect our ability to finance our properties and expand our portfolio.

Other Commitments and Contingencies

We are from time to time involved in legal actions arising in the ordinary course of business. In our opinion, after consultation with legal counsel, the outcome of such matters is not expected to have a material adverse effect on our financial position, results of operations or cash flows.

Each of our properties has been subjected to varying degrees of environmental assessment at various times. The environmental assessments did not reveal any material environmental contamination. However, there can be no assurance that the identification of new areas of contamination, changes in the extent or known scope of contamination, the discovery of additional sites, or changes in cleanup requirements would not result in significant costs to us.

Our mortgage loans are non-recourse to us. However, in certain cases we have provided guarantees or master leased tenant space. These guarantees and master leases terminate either upon the satisfaction of specified circumstances or repayment of the underlying loans. As of March 31, 2015, the aggregate dollar amount of these guarantees and master leases is approximately $349,000,000.

At March 31, 2015, $39,632,000 of letters of credit were outstanding under one of our revolving credit facilities. Our revolving credit facilities contain financial covenants that require us to maintain minimum interest coverage and maximum debt to market capitalization ratios, and provide for higher interest rates in the event of a decline in our ratings below Baa3/BBB. Our revolving credit facilities also contain customary conditions precedent to borrowing, including representations and warranties, and also contain customary events of default that could give rise to accelerated repayment, including such items as failure to pay interest or principal.

As of March 31, 2015, we expect to fund additional capital to certain of our partially owned entities aggregating approximately $78,000,000.

VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

(UNAUDITED)

21. Segment Information

As a result of the spin-off of substantially all of our Retail Properties segment (see Note 8 - *Dispositions*), the remaining retail properties no longer meet the criteria to be a separate reportable segment. In addition, as a result of our investment in Toys being reduced to zero, we suspended equity method accounting for our investment in Toys (see Note 7 - *Investments in Partially Owned Entities*) and the Toys segment no longer meets the criteria to be a separate reportable segment. Accordingly, effective January 1, 2015, the Retail Properties segment and Toys have been reclassified to the Other segment. We have also reclassified the prior period segment financial results to conform to the current period presentation. Below is a summary of net income and a reconciliation of net income to EBITDA[(1)] by segment for the three months ended March 31, 2015 and 2014.

(Amounts in thousands)	For the Three Months Ended March 31, 2015			
	Total	**New York**	**Washington, DC**	**Other**
Total revenues	$ 606,802	$ 399,513	$ 133,968	$ 73,321
Total expenses	439,088	252,760	92,997	93,331
Operating income (loss)	167,714	146,753	40,971	(20,010)
(Loss) income from partially owned entities	(2,405)	(5,663)	131	3,127
Income from real estate fund investments	24,089	-	-	24,089
Interest and other investment income, net	10,792	1,862	13	8,917
Interest and debt expense	(91,674)	(45,351)	(18,160)	(28,163)
Net gain on disposition of wholly owned and partially owned assets	1,860	-	-	1,860
Income (loss) before income taxes	110,376	97,601	22,955	(10,180)
Income tax (expense) benefit	(971)	(943)	674	(702)
Income (loss) from continuing operations	109,405	96,658	23,629	(10,882)
Income from discontinued operations	15,841	-	-	15,841
Net income	125,246	96,658	23,629	4,959
Less net income attributable to noncontrolling interests	(21,169)	(1,506)	-	(19,663)
Net income (loss) attributable to Vornado	104,077	95,152	23,629	(14,704)
Interest and debt expense[(2)]	114,675	58,667	21,512	34,496

Depreciation and amortization(2)	156,450	94,124	40,752	21,574
Income tax (benefit) expense (2)	(739)	1,002	(2,636)	895
EBITDA(1)	$ 374,463	$ 248,945 (3)	$ 83,257 (4)	$ 42,261 (5)

(Amounts in thousands)	For the Three Months Ended March 31, 2014			
	Total	**New York**	**Washington, DC**	**Other**
Total revenues	$ 562,381	$ 361,184	$ 135,278	$ 65,919
Total expenses	417,140	237,734	89,572	89,834
Operating income (loss)	145,241			