

VORNADO REALTY TRUST
Form 10-Q
August 05, 2013

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark one)

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

For the quarterly period **June 30, 2013**
ended:

Or

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

For the transition period from: _____ **to** _____

Commission File Number: **001-11954**

VORNADO REALTY TRUST

(Exact name of registrant as specified in its charter)

Maryland

22-1657560

Edgar Filing: VORNADO REALTY TRUST - Form 10-Q

(State or other jurisdiction of incorporation or organization)

(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 No

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

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

Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer (Do not check if 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

As of June 30, 2013, 186,991,076 of the registrant's common shares of beneficial interest are outstanding.

PART I.	Financial Information:	Page Number
Item 1.	Financial Statements:	
	Consolidated Balance Sheets (Unaudited) as of June 30, 2013 and December 31, 2012	3
	Consolidated Statements of Income (Unaudited) for the Three and Six Months Ended June 30, 2013 and 2012	4
	Consolidated Statements of Comprehensive Income (Unaudited) for the Three and Six Months Ended June 30, 2013 and 2012	5
	Consolidated Statements of Changes in Equity (Unaudited) for the Six Months Ended June 30, 2013 and 2012	6
	Consolidated Statements of Cash Flows (Unaudited) for the Six Months Ended June 30, 2013 and 2012	8
	Notes to Consolidated Financial Statements (Unaudited)	10
	Report of Independent Registered Public Accounting Firm	39
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations	40
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	82
Item 4.	Controls and Procedures	83
 PART II.	 Other Information:	
Item 1.	Legal Proceedings	84
Item 1A.	Risk Factors	84
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	84
Item 3.	Defaults Upon Senior Securities	84
Item 4.	Mine Safety Disclosures	84
Item 5.	Other Information	84
Item 6.	Exhibits	84

SIGNATURES	85
EXHIBIT INDEX	86

PART I. FINANCIAL INFORMATION**Item 1. Financial Statements**

**VORNADO REALTY TRUST
CONSOLIDATED BALANCE SHEETS
(UNAUDITED)**

(Amounts in thousands, except share and per share amounts)	June 30,	December
ASSETS	2013	31,
		2012
Real estate, at cost:		
Land	\$ 4,209,969	\$ 4,797,773
Buildings and improvements	12,302,151	12,476,372
Development costs and construction in progress	997,381	920,357
Leasehold improvements and equipment	127,491	130,077
Total	17,636,992	18,324,579
Less accumulated depreciation and amortization	(3,246,837)	(3,084,700)
Real estate, net	14,390,155	15,239,879
Cash and cash equivalents	781,655	960,319
Restricted cash	312,071	183,256
Marketable securities	402,935	398,188
Tenant and other receivables, net of allowance for doubtful accounts of \$25,963 and \$37,674	140,938	195,718
Investments in partially owned entities	1,031,644	1,226,256
Investment in Toys "R" Us	417,764	478,041
Real Estate Fund investments	622,124	600,786
Mortgage and mezzanine loans receivable	175,699	225,359
Receivable arising from the straight-lining of rents, net of allowance of \$4,307 and \$3,165	790,358	760,310
Deferred leasing and financing costs, net of accumulated amortization of \$251,202 and \$224,453	412,695	407,500
Identified intangible assets, net of accumulated amortization of \$365,854 and \$346,664	289,110	406,358
Assets related to discontinued operations	63,573	602,000
Other assets	502,510	381,079
	\$ 20,333,231	\$ 22,065,049
LIABILITIES, REDEEMABLE NONCONTROLLING INTERESTS AND EQUITY		
Mortgages payable	\$ 8,582,573	\$ 8,663,326
Senior unsecured notes	1,358,182	1,358,008
Revolving credit facility debt	83,982	1,170,000
Accounts payable and accrued expenses	393,362	484,746
Deferred revenue	486,901	596,067
Deferred compensation plan	111,093	105,200

Edgar Filing: VORNADO REALTY TRUST - Form 10-Q

Deferred tax liabilities	15,369	15,305
Liabilities related to discontinued operations	2,677	423,163
Other liabilities	436,877	400,938
Total liabilities	11,471,016	13,216,753
Commitments and contingencies		
Redeemable noncontrolling interests:		
Class A units - 11,345,667 and 11,215,682 units outstanding	939,988	898,152
Series D cumulative redeemable preferred units - 1 and 1,800,001 units outstanding	1,000	46,000
Total redeemable noncontrolling interests	940,988	944,152
Vornado shareholders' equity:		
Preferred shares of beneficial interest: no par value per share; authorized 110,000,000 shares; issued and outstanding 52,682,807 and 51,184,609 shares	1,277,455	1,240,278
Common shares of beneficial interest: \$.04 par value per share; authorized 250,000,000 shares; issued and outstanding 186,991,076 and 186,734,711 shares	7,450	7,440
Additional capital	7,190,336	7,195,438
Earnings less than distributions	(1,471,643)	(1,573,275)
Accumulated other comprehensive income (loss)	132,894	(18,946)
Total Vornado shareholders' equity	7,136,492	6,850,935
Noncontrolling interests in consolidated subsidiaries	784,735	1,053,209
Total equity	7,921,227	7,904,144
	\$ 20,333,231	\$ 22,065,049

See notes to consolidated financial statements (unaudited).

VORNADO REALTY TRUST
CONSOLIDATED STATEMENTS OF INCOME
(UNAUDITED)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
(Amounts in thousands, except per share amounts)	2013	2012	2013	2012
REVENUES:				
Property rentals	\$ 545,194	\$ 517,233	\$1,079,050	\$1,026,726
Tenant expense reimbursements	75,659	71,409	152,415	141,906
Cleveland Medical Mart development project	16,990	56,304	29,133	111,363
Fee and other income	48,015	33,037	145,239	66,315
Total revenues	685,858	677,983	1,405,837	1,346,310
EXPENSES:				
Operating Depreciation and amortization	261,080	243,485	520,953	489,462
General and administrative	135,486	128,372	277,570	259,767
Cleveland Medical Mart development project	54,323	46,832	108,905	102,122
Acquisition related costs	15,151	53,935	26,525	106,696
Total expenses	3,350	2,559	3,951	3,244
Operating income	469,390	475,183	937,904	961,291
(Loss) income applicable to Toys "R" Us	216,468	202,800	467,933	385,019
Income from partially owned entities	(36,861)	(19,190)	(35,102)	97,281
Income from Real Estate Fund	1,472	12,563	22,238	32,223
Interest and other investment income	34,470	20,301	51,034	32,063
	26,416	(49,172)	(22,658)	(33,507)

Edgar Filing: VORNADO REALTY TRUST - Form 10-Q

(loss), net				
Interest and debt expense	(121,762)	(124,320)	(243,650)	(254,379)
Net gain (loss) on disposition of wholly owned and partially owned assets	1,005	4,856	(35,719)	4,856
Income before income taxes	121,208	47,838	204,076	263,556
Income tax expense	(2,877)	(7,479)	(3,950)	(14,304)
Income from continuing operations	118,331	40,359	200,126	249,252
Income from discontinued operations	63,990	17,869	271,122	89,240
Net income	182,321	58,228	471,248	338,492
Less net income attributable to noncontrolling interests in:				
Consolidated subsidiaries	(14,930)	(14,721)	(26,216)	(24,318)
Operating Partnership	(8,849)	(1,337)	(22,782)	(16,608)
Preferred unit distributions of the Operating Partnership	(348)	(3,873)	(1,134)	(7,747)
Net income attributable to Vornado	158,194	38,297	421,116	289,819
Preferred share dividends	(20,368)	(17,787)	(42,070)	(35,574)
Preferred unit and share redemptions	8,100	-	(1,130)	-
NET INCOME attributable to common shareholders	\$ 145,926	\$ 20,510	\$ 377,916	\$ 254,245

INCOME PER COMMON SHARE - BASIC:

Income from continuing operations, net	\$ 0.46	\$ 0.02	\$ 0.65	\$ 0.91
Income from discontinued	0.32	0.09	1.37	0.46

operations, net					
Net income per common share	\$ 0.78	\$ 0.11	\$ 2.02	\$ 1.37	
Weighted average shares outstanding	186,931	185,673	186,842	185,521	

INCOME PER COMMON SHARE - DILUTED:

Income from continuing operations, net	\$ 0.46	\$ 0.02	\$ 0.65	\$ 0.91	
Income from discontinued operations, net	0.32	0.09	1.36	0.45	
Net income per common share	\$ 0.78	\$ 0.11	\$ 2.01	\$ 1.36	
Weighted average shares outstanding	187,720	186,342	187,627	186,271	

DIVIDENDS PER COMMON SHARE

	\$ 0.73	\$ 0.69	\$ 1.46	\$ 1.38	
--	---------	---------	---------	---------	--

See notes to consolidated financial statements (unaudited).

VORNADO REALTY TRUST
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(UNAUDITED)

(Amounts in thousands)	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2013	2012	2013	2012
Net income	\$ 182,321	\$ 58,228	\$ 471,248	\$ 338,492
Other comprehensive income (loss):				
Change in unrealized net gain (loss) on				
available-for-sale securities	20,348	(233,218)	169,138	(220,525)
Pro rata share of other comprehensive loss of				
nonconsolidated subsidiaries	(19,707)	(4,310)	(23,354)	(26,254)
Change in value of interest rate swap	12,037	(8,388)	14,560	(6,002)
Other	(3)	496	530	373
Comprehensive income (loss)	194,996	(187,192)	632,122	86,084
Less comprehensive income attributable to noncontrolling interests	(24,862)	(4,470)	(59,166)	(32,779)
Comprehensive income (loss) attributable to Vornado	\$ 170,134	\$ (191,662)	\$ 572,956	\$ 53,305

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 Capital	Earnings Less Than Distributions	Other Comprehensive Income	Non-controlling Interests in Consolidated Subsidiaries	Total Equity
	Shares	Amount	Shares	Amount					
Balance, December 31, 2011	42,187	\$ 1,021,660	185,080	\$ 7,373	\$ 7,127,258	\$ (1,401,704)	\$ 73,729	\$ 680,131	\$ 7,508,447
Net income	-	-	-	-	-	289,819	-	24,318	314,137
Dividends on common shares	-	-	-	-	-	(256,119)	-	-	(256,119)
Dividends on preferred shares	-	-	-	-	-	(35,574)	-	-	(35,574)
Common shares issued:									
Upon redemption of Class A units, at redemption value	-	-	303	12	24,964	-	-	-	24,976
Under employees' share option plan	-	-	412	16	8,800	(16,389)	-	-	(7,573)
Under dividend reinvestment plan	-	-	10	1	842	-	-	-	843
Contributions:									
Real Estate Fund	-	-	-	-	-	-	-	108,319	108,319
Other	-	-	-	-	-	-	-	30	30
Distributions:									
Real Estate Fund	-	-	-	-	-	-	-	(44,910)	(44,910)
Conversion of Series A preferred									

Edgar Filing: VORNADO REALTY TRUST - Form 10-Q

shares to common shares	(2)	(105)	3	-	105	-	-	-	-
Deferred compensation shares and options	-	-	7	-	8,484	(339)	-	-	8,145
Change in unrealized net loss on available-for-sale securities	-	-	-	-	-	-	(220,525)	-	(220,525)
Pro rata share of other comprehensive loss of nonconsolidated subsidiaries	-	-	-	-	-	-	(26,254)	-	(26,254)
Change in value of interest rate swap	-	-	-	-	-	-	(6,002)	-	(6,002)
Adjustments to carry redeemable Class A units at redemption value	-	-	-	-	(110,581)	-	-	-	(110,581)
Redeemable noncontrolling interests' share of above adjustments	-	-	-	-	-	-	15,894	-	15,894
Other	-	-	-	-	-	2	373	(3)	372
Balance, June 30, 2012	42,185	\$ 1,021,555	185,815	\$ 7,402	\$ 7,059,872	\$ (1,420,304)	\$ (162,785)	\$ 767,885	\$ 7,273,625

See notes to consolidated financial statements (unaudited).

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

(Amounts in thousands)	Preferred Shares		Common Shares		Additional Capital	Earnings Less Than Distributions	Other Comprehensive Income (Loss)	Non-Accumulated controlling Interests in Consolidated Subsidiaries	Total Equity
	Shares	Amount	Shares	Amount					
Balance, December 31, 2012	51,185	\$ 1,240,278	186,735	\$ 7,440	\$ 7,195,438	\$ (1,573,275)	\$ (18,946)	\$ 1,053,209	\$ 7,904,144
Net income	-	-	-	-	-	421,116	-	26,216	447,332
Dividends on common shares	-	-	-	-	-	(272,825)	-	-	(272,825)
Dividends on preferred shares	-	-	-	-	-	(42,070)	-	-	(42,070)
Issuance of Series L preferred shares	12,000	290,536	-	-	-	-	-	-	290,536
Redemption of Series F and Series H preferred shares	(10,500)	(253,269)	-	-	-	-	-	-	(253,269)
Common shares issued:									
Upon redemption of Class A units, at redemption value	-	-	180	7	14,973	-	-	-	14,980
Under employees' share option plan	-	-	62	3	3,564	-	-	-	3,567
Under dividend reinvestment plan	-	-	11	-	903	-	-	-	903
Contributions:									

Edgar Filing: VORNADO REALTY TRUST - Form 10-Q

Real Estate Fund	-	-	-	-	-	-	-	18,781	18,781
Other	-	-	-	-	-	-	-	15,186	15,186
Distributions:									
Real Estate Fund	-	-	-	-	-	-	-	(43,145)	(43,145)
Other	-	-	-	-	-	-	-	(120,051)	(120,051)
Conversion of Series A preferred shares to common shares	(2)	(90)	3	-	90	-	-	-	-
Deferred compensation shares and options	-	-	-	-	4,786	(305)	-	-	4,481
Change in unrealized net gain on available-for-sale securities	-	-	-	-	-	-	169,138	-	169,138
Pro rata share of other comprehensive loss of nonconsolidated subsidiaries	-	-	-	-	-	-	(23,354)	-	(23,354)
Change in value of interest rate swap	-	-	-	-	-	-	14,560	-	14,560
Adjustments to carry redeemable Class A units at redemption value	-	-	-	-	(29,393)	-	-	-	(29,393)
Redeemable noncontrolling interests' share of above adjustments	-	-	-	-	-	-	(9,034)	-	(9,034)
Preferred share redemptions	-	-	-	-	-	(1,130)	-	-	(1,130)
Deconsolidation of partially owned entity	-	-	-	-	-	-	-	(165,427)	(165,427)

Edgar Filing: VORNADO REALTY TRUST - Form 10-Q

Other	-	-	-	-	(25)	(3,154)	530	(34)	(2,683)
Balance, June 30, 2013	52,683	\$ 1,277,455	186,991	\$ 7,450	\$ 7,190,336	\$ (1,471,643)	\$ 132,894	\$ 784,735	\$ 7,921,227

See notes to consolidated financial statements (unaudited).

7

VORNADO REALTY TRUST
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	For the Six Months	
	Ended	
	June 30,	
	2013	2012
(Amounts in thousands)		
Cash Flows from Operating Activities:		
Net income	\$ 471,248	\$ 338,492
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization (including amortization of deferred financing costs)	289,643	285,617
Net gains on sale of real estate	(267,994)	(72,713)
Return of capital from Real Estate Fund investments	56,664	-
Net unrealized gain on Real Estate Fund investments	(47,109)	(27,979)
Other non-cash adjustments	42,339	20,993
Non-cash impairment loss on J.C. Penney common shares	39,487	-
Net loss (gain) on disposition of wholly owned and partially owned assets	35,719	(4,856)
Straight-lining of rental income	(32,730)	(43,124)
Amortization of below-market leases, net	(28,511)	(26,457)
Distributions of income from partially owned entities	23,774	34,613
Loss from the mark-to-market of J.C. Penney derivative position	13,475	57,687
Equity in net loss (income) of partially owned entities, including Toys "R" Us	12,864	(129,504)
Impairment losses	4,007	13,511
Changes in operating assets and liabilities:		
Real Estate Fund investments	(30,893)	(85,867)
Accounts receivable, net	53,821	(8,971)
Prepaid assets	(104,149)	(100,012)
Other assets	(35,570)	(18,582)
Accounts payable and accrued expenses	(50,690)	25,940
Other liabilities	(595)	5,076
Net cash provided by operating activities	444,800	263,864
Cash Flows from Investing Activities:		
Proceeds from sales of real estate and related investments	648,167	370,037
	281,991	17,963

Distributions of capital from partially owned entities		
Proceeds from the sale of LNR	240,474	-
Proceeds from sales of marketable securities	160,715	58,460
Additions to real estate	(113,060)	(83,368)
Funding of J.C. Penney derivative collateral	(98,447)	(70,000)
Development costs and construction in progress	(85,550)	(58,069)
Return of J.C. Penney derivative collateral	85,450	24,950
Investments in partially owned entities	(59,472)	(57,237)
Acquisitions of real estate and other	(53,992)	(32,156)
Proceeds from repayments of mortgage and mezzanine loans receivable and other	47,950	1,994
Restricted cash	16,596	(14,658)
Investment in mortgage and mezzanine loans receivable and other	(137)	(145)
Proceeds from the repayment of loan to officer	-	13,123
Net cash provided by investing activities	1,070,685	170,894

See notes to consolidated financial statements (unaudited).

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

	For the Six Months Ended	
	June 30,	
	2013	2012
(Amounts in thousands)		
Cash Flows from Financing		
Activities:		
Repayments of borrowings	\$ (2,800,441)	\$ (1,507,220)
Proceeds from borrowings	1,583,357	1,225,000
Purchases of outstanding preferred units and shares	(299,400)	-
Proceeds from the issuance of preferred shares	290,536	-
Dividends paid on common shares	(272,825)	(256,119)
Distributions to noncontrolling interests	(181,510)	(69,367)
Dividends paid on preferred shares	(42,451)	(35,576)
Contributions from noncontrolling interests	33,967	108,349
Debt issuance and other costs	(9,520)	(14,648)
Proceeds received from exercise of employee share options	4,470	9,667
Repurchase of shares related to stock compensation agreements and/or related tax withholdings	(332)	(30,034)
Net cash used in financing activities	(1,694,149)	(569,948)
Net decrease in cash and cash equivalents	(178,664)	(135,190)
Cash and cash equivalents at beginning of period	960,319	606,553
Cash and cash equivalents at end of period	\$ 781,655	\$ 471,363

Supplemental Disclosure of**Cash Flow Information:**

Cash payments for interest, excluding capitalized interest of \$17,492 and \$361	\$ 235,588	\$ 251,434
--	------------	------------

Cash payments for income taxes	\$	4,732	\$	6,494
--------------------------------	----	-------	----	-------

Non-Cash Investing and Financing Activities:

Change in unrealized net gain (loss) on available-for-sale securities	\$	169,138	\$	(220,525)
Adjustments to carry redeemable Class A units at redemption value		(29,393)		(110,581)
Common shares issued upon redemption of Class A units, at redemption value		14,980		24,976
Decrease in assets and liabilities resulting from the deconsolidation of Independence Plaza:				
Real estate, net		(852,166)		-
Notes and mortgages payable		(322,903)		-
Cash restricted for like kind exchange of real estate		(155,810)		-
L.A. Mart seller financing		-		35,000
Write-off of fully depreciated assets		(47,598)		(131,770)

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 94.0% of the common limited partnership interest in the Operating Partnership at June 30, 2013. All references to “we,” “us,” “our,” the “Company” and “Vornado” refer to Vornado Realty Trust and its consolidated subsidiaries, including the Operating Partnership.

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 Securities and Exchange Commission (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, for the year ended December 31, 2012, 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 and six months ended June 30, 2013 are not necessarily indicative of the operating results for the full year. Certain prior year balances have been reclassified in order to conform to current year presentation.

3. Recently Issued Accounting Literature

In February 2013, the Financial Accounting Standards Board (“FASB”) issued an update (“ASU 2013-02”) to Accounting Standards Codification (“ASC”) Topic 220, *Comprehensive Income* (“Topic 220”). ASU 2013-02 requires additional disclosures regarding significant reclassifications out of each component of accumulated other comprehensive income, including the effect on the respective line items of net income for amounts that are required to be reclassified into net income in their entirety and cross-references to other disclosures providing additional information for amounts that are not required to be reclassified into net income in their entirety. The adoption of this update as of January 1, 2013, did not have a material impact on our consolidated financial statements, but resulted in additional disclosures (see Note 13 - *Accumulated Other Comprehensive Income*).

In June 2013, the FASB issued an update (“ASU 2013-08”) to ASC Topic 946, *Financial Services - Investment Companies* (“Topic 946”). ASU 2013-08 amends the guidance in Topic 946 for determining whether an entity qualifies as an investment company and requires certain additional disclosures. ASU 2013-08 is effective for interim and annual reporting periods in fiscal years that begin after December 15, 2013. We are currently evaluating the impact, if any, of ASU 2013-08 on our real estate fund and our consolidated financial statements.

VORNADO REALTY TRUST**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)****(UNAUDITED)****4. Vornado Capital Partners Real Estate Fund (the “Fund”)**

We are the general partner and investment manager of our \$800,000,000 Fund, to which we committed \$200,000,000. The Fund has an eight-year term and a three-year investment period which 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 the AICPA Investment Company Guide 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.

At June 30, 2013, the Fund had ten investments with an aggregate fair value of \$622,124,000, or \$114,751,000 in excess of cost, and had remaining unfunded commitments of \$246,582,000, of which our share was \$61,645,000. Below is a summary of income from the Fund for the three and six months ended June 30, 2013 and 2012.

	For the Three Months		For the Six Months	
(Amounts in thousands)	Ended June 30, 2013	2012	Ended June 30, 2013	2012
Net investment income (loss)	\$ 877	\$ (834)	\$ 3,925	\$ 4,084
Net unrealized gains	33,593	21,135	47,109	27,979
Income from Real Estate Fund	34,470	20,301	51,034	32,063
Less (income)	(14,359)	(12,306)	(23,899)	(20,239)

attributable
to
noncontrolling
interests
Income
from
Real
Estate
Fund
attributable
to
Vornado

(1) \$ 20,111 \$ 7,995 \$ 27,135 \$ 11,824

(1) Excludes management, leasing and development fees of \$827 and \$717 for the three months ended June 30, 2013 and 2012, respectively, and \$1,676 and \$1,420 for the six months ended June 30, 2013 and 2012, respectively, which are included as a component of "fee and other income" on our consolidated statements of income.

5. Mortgage and Mezzanine Loans Receivable

As of June 30, 2013 and December 31, 2012, the carrying amount of mortgage and mezzanine loans receivable was \$175,699,000 and \$225,359,000, respectively. These loans have a weighted average interest rate of 10.8% and 10.3% at June 30, 2013 and December 31, 2012, respectively, and have maturities ranging from August 2014 to May 2016.

On March 27, 2013, we transferred, at par, a 25% participation in a mortgage loan on 701 Seventh Avenue to a third party for \$59,375,000 in cash. We acquired this participation in October 2012, together with a 25% interest in a mezzanine loan on the property. The transfer did not qualify for sale accounting given our continuing interest in the mezzanine loan. Accordingly, we continue to include the 25% participation in the mortgage loan in "Mortgage and Mezzanine Loans Receivable" and have recorded a \$59,375,000 liability in "Other Liabilities" on our consolidated balance sheet.

On April 17, 2013, a \$50,091,000 mezzanine loan that was scheduled to mature in August 2015, was repaid. In connection therewith, we received net proceeds of \$55,358,000, including prepayment penalties, which resulted in income of \$5,267,000, included in "interest and other investment income (loss)" on our consolidated statement of income.

VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

6. Marketable Securities and Derivative Instruments

Our portfolio of marketable securities is comprised of equity securities that are classified as available for sale. Available for sale securities are presented on our consolidated balance sheets at fair value. Unrealized gains and losses resulting from the mark-to-market of these securities are included in “other comprehensive income (loss).” Realized gains and losses are recognized in earnings only upon the sale of the securities and are recorded based on the weighted average cost of such securities.

Investment in J.C. Penney Company, Inc. (“J.C. Penney”) (NYSE: JCP)

On March 4, 2013, we sold 10,000,000 J.C. Penney common shares at a price of \$16.03 per share, or \$160,300,000 in the aggregate, resulting in a net loss of \$36,800,000, which is included in “net gain (loss) on disposition of wholly owned and partially owned assets” on our consolidated statement of income. In addition, in the first quarter of 2013, we wrote down the remaining 8,584,010 J.C. Penney common shares we own to fair value and recorded a \$39,487,000 impairment loss, which is included in “interest and other investment income (loss), net” on our consolidated statement of income.

As of June 30, 2013, we own an economic interest in 13,400,000 J.C. Penney common shares, or 6.1% of its outstanding common shares. Below are the details of our investment.

We own 8,584,010 common shares at a GAAP cost of \$15.11, per share, or \$129,704,000 in the aggregate. As of June 30, 2013, these shares have an aggregate fair value of \$146,615,000, based on J.C. Penney’s closing share price of \$17.08 per share.

We also own an economic interest in 4,815,990 common shares through a forward contract at a weighted average strike price of \$29.27 per share, or \$140,947,000 in the aggregate. The forward contract may be settled, at our election, in cash or common shares, in whole or in part, at any time prior to October 8, 2022. The counterparty may accelerate settlement, in whole or in part, on October 8, 2014, or any anniversary thereof, or in the event we were to receive a credit downgrade. The forward contract strike price per share increases at an annual rate of LIBOR plus 95

basis points during the first two years of the contract and LIBOR plus 80 basis points thereafter. The contract is a derivative instrument that does not qualify for hedge accounting treatment. Gains and losses from the mark-to-market of the underlying common shares are recognized in “interest and other investment income (loss), net” on our consolidated statements of income. In the three and six months ended June 30, 2013, we recognized income of \$9,065,000 and a loss of \$13,475,000, respectively, from the mark-to-market of the underlying common shares, and as of June 30, 2013, have funded \$69,377,000 in connection with this derivative position. In the three and six months ended June 30, 2012, we recognized losses of \$58,732,000 and \$57,687,000, respectively, from the mark-to-market of the underlying common shares.

As of June 30, 2013, the aggregate economic net loss on our investment in J.C. Penney, including shares sold, was \$201,119,000.

Investment in Lexington Realty Trust (“Lexington”) (NYSE: LXP)

From the inception of our investment in Lexington in 2008, until the first quarter of 2013, we accounted for that investment under the equity method because of our ability to exercise significant influence over Lexington’s operating and financial policies. As a result of Lexington’s common share issuances, our ownership interest has been reduced over time from approximately 17.2% to 8.8% at March 31, 2013. In the first quarter of 2013, we concluded that we no longer have the ability to exercise significant influence over Lexington’s operating and financial policies, and began accounting for this investment as a marketable equity security – available for sale, in accordance with Accounting Standards Codification (“ASC”) Topic 320, *Investments – Debt and Equity Securities*.

Below is a summary of our marketable securities portfolio as of June 30, 2013 and December 31, 2012.

(Amounts in thousands)	As of June 30, 2013			As of December 31, 2012		
	Fair Value	GAAP Cost	Unrealized Gain	Fair Value	GAAP Cost	Unrealized Gain
Equity securities:						
Lexington	\$ 215,718	\$ 72,549	\$ 143,169	\$ -	\$ -	\$ -
J.C. Penney	146,615	129,704	16,911	366,291	366,291	-
Other	40,602	12,112	28,490	31,897	12,465	19,432
	\$ 402,935	\$ 214,365	\$ 188,570	\$ 398,188	\$ 378,756	\$ 19,432

12

VORNADO REALTY TRUST

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

7. Investments in Partially Owned Entities

Toys "R" Us ("Toys")

As of June 30, 2013, we own 32.6% of Toys. We account for our investment in Toys under the equity method and record our share of Toys' net income or loss on a one-quarter lag basis because Toys' fiscal year ends on the Saturday nearest January 31, and our fiscal year ends on December 31. The business of Toys is highly seasonal. Historically, Toys' fourth quarter net income accounts for more than 80% of its fiscal year net income.

In the fourth quarter of 2012, we recorded a \$40,000,000 non-cash impairment loss on our investment in Toys and disclosed, that if current facts don't change, our share of Toys' undistributed income, which in accordance with the equity method of accounting, would increase the carrying amount of our investment above fair value, would require an offsetting impairment loss.

In the first quarter of 2013, we recognized our share of Toys' fourth quarter net income of \$78,542,000 and a corresponding non-cash impairment loss of the same amount.

As of June 30, 2013, the carrying amount of our investment in Toys is less than our share of Toys' equity by approximately \$146,215,000. This basis difference resulted primarily from the non-cash impairment losses aggregating \$118,542,000 that were recognized in 2012 and 2013. We have allocated the basis difference to Toys' intangible assets (primarily trade names and trademarks). The basis difference is not being amortized and will be recognized upon disposition of our investment.

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

(Amounts in thousands)

	Balance as of	
	May 4, 2013	October 27, 2012
Balance Sheet:		
Assets	\$ 11,303,000	\$ 12,953,000
Liabilities	9,475,000	11,190,000
Noncontrolling interests	67,000	44,000
Toys “R” Us, Inc. equity	1,761,000	1,719,000
	For the Three Months Ended	For the Six Months Ended
	May 4,	April 28,
Income Statement:	2013	2012