

Paramount Group, Inc.
Form 10-Q
August 13, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended: June 30, 2015

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: 001-36746

PARAMOUNT GROUP, INC.

(Exact name of registrant as specified in its charter)

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Maryland 32-0439307
(State or other jurisdiction of (IRS Employer
incorporation or organization) Identification No.)

1633 Broadway, Suite 1801, New York, NY 10019
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (212) 237-3100

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 (Section 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, 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 July 31, 2015, there were 212,111,937 shares of the registrant's common stock outstanding.



Table of Contents

Item	Page Number
Part I. Financial Information	
Item 1. <u>Consolidated Financial Statements</u>	3
<u>Consolidated Balance Sheets (Unaudited) as of June 30, 2015 and December 31, 2014</u>	3
<u>Consolidated Statements of Income of the Company (Unaudited) for the three and six months ended June 30, 2015</u>	4
<u>Combined Consolidated Statements of Income of the Predecessor (Unaudited) for the three and six months ended June 30, 2014</u>	5
<u>Consolidated Statements of Comprehensive Income of the Company (Unaudited) for the three and six months ended June 30, 2015</u>	6
<u>Combined Consolidated Statements of Changes in Equity (Unaudited) of the Company for the six months ended June 30, 2015 and the Predecessor for the six months ended June 30, 2014</u>	7
<u>Combined Consolidated Statements of Cash Flows (Unaudited) of the Company for the six months ended June 30, 2015 and the Predecessor for the six months ended June 30, 2014</u>	8
<u>Notes to Combined Consolidated Financial Statements (Unaudited)</u>	9
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	32
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	49
Item 4. <u>Controls and Procedures</u>	50
Part II. Other Information	
Item 1. <u>Legal Proceedings</u>	51
Item 1A. <u>Risk Factors</u>	51
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	51
Item 3. <u>Defaults Upon Senior Securities</u>	51
Item 4. <u>Mine Safety Disclosures</u>	51
Item 5. <u>Other Information</u>	51
Item 6. <u>Exhibits</u>	51
<u>Signatures</u>	52

PART I – FINANCIAL INFORMATION

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

PARAMOUNT GROUP, INC.

CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

(Amounts in thousands, except share and per share amounts)	The Company	
ASSETS	June 30, 2015	December 31, 2014
Rental property, at cost		
Land	\$2,042,071	\$2,042,071
Buildings and improvements	5,534,885	5,488,168
	7,576,956	7,530,239
Accumulated depreciation and amortization	(162,377)	(81,050)
Rental property, net	7,414,579	7,449,189
Real estate fund investments	335,545	323,387
Investments in unconsolidated joint ventures	6,128	5,749
Cash and cash equivalents	438,088	438,599
Restricted cash	45,737	55,728
Marketable securities	21,524	20,159
Deferred rent receivable	40,308	8,267
Accounts and other receivables, net of allowance of \$406 and \$333 in 2015		
and 2014, respectively	10,781	7,692
Deferred charges, net of accumulated amortization of \$13,002 and \$10,859 in 2015		
and 2014, respectively	49,547	39,165
Intangible assets, net of accumulated amortization of \$103,158 and \$20,509 in 2015		
and 2014, respectively	583,126	669,385
Other assets	9,529	13,121
Total assets	\$8,954,892	\$9,030,441
LIABILITIES AND EQUITY		
Mortgages and notes payable	\$2,853,237	\$2,852,287
Credit facility	-	-
Due to affiliates	27,299	27,299
Loans payable to noncontrolling interests	43,981	42,195
Accounts payable and accrued expenses	96,595	93,472
Deferred income taxes	2,659	2,861
Interest rate swap liabilities	160,473	194,196

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Intangible liabilities, net of accumulated amortization of \$21,064 and \$3,757 in 2015

and 2014, respectively	201,839	219,228
Dividends and distributions payable	25,066	-
Other liabilities	45,922	43,950
Total liabilities	3,457,071	3,475,488
Commitments and contingencies		
Paramount Group, Inc. equity:		
Common stock \$0.01 par value per share; authorized 900,000,000 shares; issued		
and outstanding 212,111,937 and 212,106,718 shares in 2015 and 2014, respectively	2,122	2,122
Additional paid-in-capital	3,893,756	3,851,432
Earnings (less than) in excess of distributions	(5,843)	57,308
Accumulated other comprehensive loss	(493)	-
Paramount Group, Inc. equity	3,889,542	3,910,862
Noncontrolling interests in:		
Consolidated joint ventures and funds	703,596	685,888
Operating Partnership (51,660,088 and 51,543,993 units outstanding in 2015		
and 2014, respectively)	904,683	958,203
Total equity	5,497,821	5,554,953
Total liabilities and equity	\$8,954,892	\$9,030,441

See notes to combined consolidated financial statements (unaudited).

PARAMOUNT GROUP, INC.

CONSOLIDATED STATEMENTS OF INCOME

(UNAUDITED)

	The Company	
	Three Months	Six Months
	Ended	Ended
(Amounts in thousands, except share and per share amounts)	June 30, 2015	June 30, 2015
REVENUES:		
Rental income	\$145,917	\$289,160
Tenant reimbursement income	12,063	25,551
Fee and other income	4,948	9,443
Total revenues	162,928	324,154
EXPENSES:		
Operating	57,781	119,665
Depreciation and amortization	79,421	153,004
General and administrative	9,133	21,746
Acquisition and transaction related costs	8,208	9,347
Total expenses	154,543	303,762
Operating income	8,385	20,392
Income from real estate fund investments	14,072	19,293
Income from unconsolidated joint ventures	2,011	2,986
Unrealized gains on interest rate swaps	21,747	33,725
Interest and other income, net	512	1,366
Interest and debt expense	(42,236)	(84,124)
Net income (loss) before income taxes	4,491	(6,362)
Income tax expense	(1,343)	(1,917)
Net income (loss)	3,148	(8,279)
Less net (income) loss attributable to noncontrolling interests in:		
Consolidated joint ventures and funds	(9,004)	(9,672)
Operating Partnership	1,147	3,511
Net loss attributable to common shareholders	\$(4,709)	\$(14,440)
LOSS PER COMMON SHARE - BASIC:		
Loss per common share	\$(0.02)	\$(0.07)
Weighted average shares outstanding	212,106,718	212,106,718
LOSS PER COMMON SHARE - DILUTED:		
Loss per common share	\$(0.02)	\$(0.07)
Weighted average shares outstanding	212,106,718	212,106,718
DIVIDENDS PER COMMON SHARE	\$0.095	\$0.190

(1)

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⁽¹⁾ Excludes the \$0.039 cash dividend for the 38 day period following the completion of our initial public offering and related formation transactions and ending on December 31, 2014.

See notes to combined consolidated financial statements (unaudited).

4

PARAMOUNT PREDECESSOR

COMBINED CONSOLIDATED STATEMENTS OF INCOME

(UNAUDITED)

(Amounts in thousands)	The Predecessor	
	Three Months Ended June 30, 2014	Six Months Ended June 30, 2014
REVENUES:		
Rental income	\$8,499	\$16,312
Tenant reimbursement income	441	896
Distributions from real estate fund investments	4,744	11,247
Realized and unrealized gains, net	33,750	79,917
Fee and other income	6,400	11,582
Total revenues	53,834	119,954
EXPENSES:		
Operating	4,214	7,753
Depreciation and amortization	2,899	5,566
General and administrative	4,363	12,448
Profit sharing compensation	3,438	8,232
Other	2,634	3,901
Total expenses	17,548	37,900
Operating income	36,286	82,054
Income from unconsolidated joint ventures	903	2,035
Unrealized loss on interest rate swaps	(354)	(196)
Interest and other income, net	997	1,706
Interest and debt expense	(7,988)	(15,787)
Net income before income taxes	29,844	69,812
Income tax expense	(3,842)	(7,105)
Net income	26,002	62,707
Net income attributable to noncontrolling interests	(25,823)	(53,133)
Net income attributable to the Predecessor	\$179	\$9,574

See notes to combined consolidated financial statements (unaudited).

PARAMOUNT GROUP, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(UNAUDITED)

	The Company	
	Three Months Ended June 30, 2015	Six Months Ended June 30, 2015
(Amounts in thousands)		
Net income (loss)	\$3,148	\$(8,279)
Other comprehensive loss:		
Pro rata share of other comprehensive loss of unconsolidated joint ventures	(613)	(613)
Comprehensive income (loss)	2,535	(8,892)
Less comprehensive (income) loss attributable to noncontrolling interests in:		
Consolidated joint ventures and funds	(9,004)	(9,672)
Operating Partnership	1,267	3,631
Comprehensive loss attributable to Paramount Group, Inc.	\$(5,202)	\$(14,933)

See notes to combined consolidated financial statements (unaudited).

PARAMOUNT GROUP, INC. AND PARAMOUNT PREDECESSOR

COMBINED CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(UNAUDITED)

(Amounts in thousands)	Common Shares		Additional Paid in Capital	Earnings (Less than) In Excess of Distributions	Accumulated Other Comprehensive Loss	Predecessor Shareholders' Equity	Noncontrolling Interests in Consolidated Joint Ventures and Funds		Operating Partnership Equity	Total Equity
	Shares	Amount								
The Predecessor Balance as of December 31, 2013	-	\$-	\$-	\$-	\$-	\$321,769	\$1,703,675	\$-	\$2,025,444	
Net income	-	-	-	-	-	9,574	53,133	-	62,707	
Contributions	-	-	-	-	-	1,253	88,804	-	90,057	
Distributions	-	-	-	-	-	(22,323)	(2,183)	-	(24,506)	
Balance as of June 30, 2014	-	\$-	\$-	\$-	\$-	\$310,273	\$1,843,429	\$-	\$2,153,702	
The Company Balance as of December 31, 2014	212,107	\$2,122	\$3,851,432	\$57,308	\$-	\$-	\$685,888	\$958,203	\$5,554,953	
Net (loss) income	-	-	-	(14,440)	-	-	9,672	(3,511)	(8,279)	
Common shares and units issued under										
Omnibus share plan	5	-	(2,131)	-	-	-	-	2,131	-	
Dividends and distributions	-	-	-	(48,573)	-	-	-	(11,819)	(60,392)	
Contributions from noncontrolling interests	-	-	-	-	-	-	14,031	-	14,031	
	-	-	-	-	-	-	(5,673)	-	(5,673)	

Distributions to
noncontrolling

interests									
Pro rata share of other comprehensive									
loss of unconsolidated joint ventures	-	-	-	-	(493)	-		(120)	(613)
Adjustments to noncontrolling interests	-	-	43,981	-	-	-	-	(43,981)	-
Amortization of equity awards	-	-	885	-	-	-	-	3,780	4,665
Other	-	-	(411)	(138)	-	-	(322)	-	(871)
Balance as of June 30, 2015	212,112	\$2,122	\$3,893,756	\$(5,843)	\$(493)	\$-	\$703,596	\$904,683	\$5,497,821

See notes to combined consolidated financial statements (unaudited).

PARAMOUNT GROUP, INC. AND PARAMOUNT PREDECESSOR

COMBINED CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

(Amounts in thousands)	The Company Six Months Ended 30, 2015	The Predecessor Six Months Ended June 30, 2014
CASH FLOWS FROM OPERATING ACTIVITIES		
Net (loss) income	\$(8,279)	\$ 62,707
Adjustments to reconcile net (loss) income to net cash provided by (used in) operating activities:		
Depreciation and amortization	153,004	5,566
Unrealized (gains) losses on interest rate swaps	(33,725)	196
Straight-lining of rental income	(32,042)	90
Realized and unrealized gains, net, on real estate fund investments	(12,136)	(79,917)
Income from unconsolidated joint ventures	(2,986)	(2,035)
Distributions of income from unconsolidated joint ventures	1,993	1,768
Amortization of above and below-market leases, net	(1,762)	-
Amortization of deferred financing costs	1,170	216
Transfer taxes due in connection with the sale of shares by a former joint venture partner	5,872	-
Realized and unrealized gains on marketable securities	(924)	(1,228)
Other non-cash adjustments	8,091	3,756
Changes in operating assets and liabilities:		
Restricted cash	-	2,481
Real estate fund investments	(22)	(164,181)
Accounts and other receivables	(261)	(2,669)
Deferred charges	(12,523)	-
Other assets	2,721	(3,456)
Accounts payable and accrued expenses	(7,635)	(2,945)
Profit sharing payables	-	5,414
Deferred income taxes	(202)	10,043
Other liabilities	1,972	1,693
Net cash provided by (used in) operating activities	62,326	(162,501)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Acquisitions of, and additions to, rental properties	(41,914)	(65,451)
Changes in restricted cash	9,550	253
Distributions of capital from unconsolidated joint ventures	-	1,123
Net cash used in investing activities	(32,364)	(64,075)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Dividends paid to common shareholders and unitholders	(35,325)	-
Contributions from noncontrolling interests	11,203	88,804
Distributions to noncontrolling interests	(5,673)	(2,183)
Contributions from Predecessor shareholders	-	1,253

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Distributions to Predecessor shareholders	-	(22,323)
Proceeds from loans payable to noncontrolling interests	-	39,075
Repayment of mortgage notes and loans payable	(678)	(1,877)
Offering costs	-	(9,577)
Net cash (used in) provided by financing activities	(30,473)	93,172
Net decrease in cash and cash equivalents	(511)	(133,404)
Cash and cash equivalents at beginning of period	438,599	307,161
Cash and cash equivalents at end of period	\$438,088	\$ 173,757

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:

Cash payments for interest	\$78,860	\$ 10,665
Cash payments for income taxes	\$1,213	\$ 5,168

NON-CASH TRANSACTIONS:

Dividends and distributions declared but not yet paid	\$25,066	\$ -
Contributions from non controlling interests called but not yet received	2,828	-
(Purchases) sale of marketable securities	(441)	6,946

See notes to combined consolidated financial statements (unaudited).

8

PARAMOUNT GROUP, INC. AND PARAMOUNT PREDECESSOR

NOTES TO COMBINED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

1. Organization and Business

As used in these consolidated and combined financial statements, unless indicated otherwise, all references to “we,” “us,” “our,” the “Company,” and “Paramount” refer to Paramount Group, Inc. and its consolidated subsidiaries, including Paramount Group Operating Partnership LP, upon completion of the Formation Transactions (as more fully described below) and the initial public offering of common stock.

We are a fully-integrated real estate investment trust (“REIT”) focused on owning, operating, managing, acquiring and redeveloping high-quality, Class A office properties in select central business district submarkets of New York City, Washington, D.C. and San Francisco. As of June 30, 2015, our portfolio consisted of 12 Class A office properties aggregating approximately 10.4 million square feet that had an occupancy rate of 92.9%.

We were incorporated in Maryland as a corporation on April 14, 2014 to continue the business of our Predecessor, as defined, and did not have any meaningful operations until the acquisition of substantially all of the assets of our Predecessor and the assets of the Property Funds, as defined, that it controlled, as well as the interests of unaffiliated third parties in certain properties. Our properties were acquired through a series of Formation Transactions (the “Formation Transactions”) concurrently with our initial public offering of 150,650,000 common shares at a public offering price of \$17.50 per share on November 24, 2014 (the “Offering”).

We conduct our business through, and substantially all of our interests are held by, Paramount Group Operating Partnership LP, a Delaware limited partnership (the “Operating Partnership”). We are the sole general partner of, and owned approximately 80.4% of, the Operating Partnership as of June 30, 2015.

Our Predecessor

Our Predecessor is not a legal entity but a combination of entities under common control as they were entities controlled by members of the Otto family that held various assets, including interests in (i) 15 private equity real estate funds controlled by our Predecessor (which included nine primary funds and six parallel funds) (collectively,

the “Funds”) that owned interests in 12 properties, (ii) a wholly-owned property, Waterview, in Rosslyn, Virginia and (iii) three partially owned properties in New York, NY (See note 4, Investments in Unconsolidated Joint Ventures).

Below is a summary of the 15 private equity real estate funds that were controlled by our Predecessor prior to the completion of the Formation Transactions.

The following funds are collectively referred to herein as the “Property Funds”:

- ¶Paramount Group Real Estate Fund I, L.P. (“Fund I”)
- ¶Paramount Group Real Estate Fund II, L.P. (“Fund II”)
- ¶Paramount Group Real Estate Fund III, L.P. (“Fund III”)
- ¶Paramount Group Real Estate Fund IV, L.P. (“Fund IV”)
- ¶PGREF IV Parallel Fund (Cayman), L.P. (“Fund IV Cayman”)
- ¶Paramount Group Real Estate Fund V (CIP), L.P. (“Fund V CIP”)
- ¶Paramount Group Real Estate Fund V (Core), L.P. (“Fund V Core”)
- ¶PGREF V (Core) Parallel Fund (Cayman), L.P. (“Fund V Cayman”)
- ¶Paramount Group Real Estate Fund VII, LP (“Fund VII”)
- ¶Paramount Group Real Estate Fund VII-H, LP (“Fund VII-H”)

PARAMOUNT GROUP, INC. AND PARAMOUNT PREDECESSOR

NOTES TO COMBINED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

The following fund was formed to acquire, develop and manage the residential development project at 75 Howard Street:

•Paramount Group Residential Development Fund, LP (“Residential Fund”)

The following funds are collectively referred to herein as the “Alternative Investment Funds”:

•Paramount Group Real Estate Special Situations Fund, L.P. (“PGRESS”)

•Paramount Group Real Estate Special Situations Fund–H, L.P. (“PGRESS-H”)

•Paramount Group Real Estate Special Situations Fund–A, L.P. (“PGRESS-A”)

- Paramount Group Real Estate Fund VIII, L.P. (“Fund VIII”)

The Property Funds and Residential Fund owned interests in the following properties:

- 1633 Broadway, New York, NY
- 60 Wall Street, New York, NY
- 900 Third Avenue, New York, NY
- 31 West 52nd Street, New York, NY
- 1301 Avenue of the Americas, New York, NY
- One Market Plaza, San Francisco, CA
- 50 Beale Street, San Francisco, CA
- 75 Howard Street, San Francisco, CA
- Liberty Place, Washington, D.C.
- 1899 Pennsylvania Avenue, Washington, D.C.
- 2099 Pennsylvania Avenue, Washington, D.C.
- 425 Eye Street, Washington, D.C.

PARAMOUNT GROUP, INC. AND PARAMOUNT PREDECESSOR

NOTES TO COMBINED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

2. Basis of Presentation and Significant Accounting Policies

Basis of Presentation

The accompanying consolidated and combined financial statements include the accounts of Paramount and its consolidated subsidiaries, including the Operating Partnership. All significant inter-company amounts have been eliminated. In our opinion, all adjustments (which include only normal recurring adjustments) necessary to present fairly the financial position, result of operations and changes in the 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 consolidated and combined financial statements have been prepared in accordance with the instructions to Form 10-Q of the Securities and Exchange Commission (“SEC”) and should be read in conjunction with the consolidated and combined financial statements and notes thereto included in our Annual Report on Form 10-K 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 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, 2015 are not necessarily indicative of the operating results for the full year.

Our Predecessor’s combined financial statements included all the accounts of our Predecessor, including its interests in (i) the Funds, (ii) Waterview and (iii) the three partially-owned properties. Our Predecessor evaluated each of the Funds pursuant to the control model of Accounting Standards Codification (“ASC”) 810-20, Consolidation—Control of Partnerships and Similar Entities and concluded that based on its rights and responsibilities as the sole managing member of the general partner it should consolidate each of the Funds. With the exception of the Residential Fund, which is carried at historical cost, each of the Funds qualify as investment companies pursuant to Financial Services—Investment Companies (“ASC 946”); accordingly, the underlying real estate investments are carried at fair value, which was retained in consolidation by our Predecessor.

Upon completion of the Offering and the Formation Transactions, we acquired substantially all of the assets of our Predecessor and all of the assets of the Property Funds that it controlled, other than their interests in 60 Wall Street, 50

Beale Street, and a residual 2.0% interest in One Market Plaza. In addition, as part of the Formation Transactions, we also acquired the interests of certain unaffiliated third parties in 1633 Broadway, 31 West 52nd Street and 1301 Avenue of the Americas. These transactions were accounted for as transactions among entities under common control. However, since the assets that we acquired from our Predecessor are no longer held by funds which qualify for investment company accounting, we account for these assets following the Formation Transactions using historical cost accounting. As a result, our consolidated financial statements following the Formation Transactions, differ significantly from, and are not comparable with, the historical financial position and results of operations of our Predecessor.

PARAMOUNT GROUP, INC. AND PARAMOUNT PREDECESSOR

NOTES TO COMBINED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Significant Accounting Policies

There were no material changes to our significant accounting policies disclosed in our Annual Report on Form 10-K for the year ended December 31, 2014.

Segment Reporting

Upon completion of the Offering and Formation Transactions, we acquired substantially all of the assets of our Predecessor and substantially all of the assets of the Property Funds that it controlled. Our business, post the Formation Transactions, is comprised of one reportable segment. We have determined that our properties have similar economic characteristics to be aggregated into one reportable segment (operating, leasing and managing office properties). Our determination was based primarily on our method of internal reporting. Our Predecessor historically operated an integrated business that consisted of three reportable segments, (i) Owned Properties, (ii) Managed Funds and (iii) a Management Company. The Owned Properties segment consisted of properties in which our Predecessor had a direct or indirect ownership interest, other than properties that it owned through its private equity real estate funds. The Managed Funds segment consisted of the private equity real estate funds. In addition, our Predecessor included a Management Company that performed property management and asset management services and certain general and administrative level functions, including legal and accounting, as a separate reportable segment.

Recently Issued Accounting Literature

In May 2014, the FASB issued an update ("ASU 2014-09") 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 modifies the evaluation of whether limited partnerships and similar legal entities are VIEs or voting interest entities, eliminates the presumption that a general partner should consolidate a limited partnership and affects the consolidation analysis of reporting entities that are involved with VIEs, particularly those that have fee arrangements and related party relationships. ASU 2015-02 is effective for fiscal years that begin 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 – Imputation of Interest. ASU 2015-03 requires an entity to present debt issuance costs in the balance sheet as a direct deduction from the related debt liability rather than as an asset. Amortization of the costs is reported as interest expense. 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.

PARAMOUNT GROUP, INC. AND PARAMOUNT PREDECESSOR

NOTES TO COMBINED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

3. Real Estate Fund Investments

Real estate fund investments are presented at fair value on our consolidated balance sheets and are comprised of (i) Property Funds and (ii) Alternative Investment Funds.

The Company

Below is a summary of the fair value of fund investments on our consolidated balance sheet.

(Amounts in thousands) Balance Sheet	As of	
	June 30, 2015	December 31, 2014
Real Estate Fund Investments:		
Property Funds	\$ 193,081	\$ 183,216
Alternative Investment Funds	142,464	140,171
Total	\$ 335,545	\$ 323,387

Below is a summary of the fair value of fund investments on our consolidated statement of income.

(Amounts in thousands) Income Statement	Three Months Ended June 30, 2015	Six Months Ended June 30, 2015
Investment income	\$ 2,853	\$ 7,348
Investment expenses	45	191
Net investment income	2,808	7,157
Net unrealized gains	11,264	12,136
Income from real estate fund investments	\$ 14,072	\$ 19,293

Property Funds

The purpose of the Property Funds is to invest in office buildings and related facilities primarily in New York City, Washington, D.C. and San Francisco. As of June 30, 2015, the Property Funds were comprised of (i) Fund II, (ii)

Fund III, (iii) Fund VII and (iv) Fund VII-H.

The following is a summary of the investments of our Property Funds.

	% Ownership	As of June 30, 2015		
		60 Wall Street	One Market Plaza	50 Beale Street
Fund II	10.0	% 46.3	% -	-
Fund III	3.1	% 16.0	% 2.0	% -
Fund VII/VII-H ⁽¹⁾	7.2	% -	-	42.8 %
Total Property Funds		62.3 %	2.0 %	42.8 %
Other Investors		37.7 %	98.0 % ⁽²⁾	57.2 %
Total		100.0 %	100.0 %	100.0 %

⁽¹⁾As of June 30, 2015, Fund VII and Fund VII-H had an aggregate of \$57,600,000 of committed capital that had not yet been invested. On July 10, 2015, Fund VII and Fund VII-H entered into an agreement to acquire 670 Broadway, a 77,480 square foot office building located in the NoHo submarket of Manhattan, for \$112,000,000.

⁽²⁾Includes a 49.0% direct ownership interest held by us.

PARAMOUNT GROUP, INC. AND PARAMOUNT PREDECESSOR

NOTES TO COMBINED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Alternative Investment Funds

The purpose of the Alternative Investment Funds is to invest primarily in real estate related debt and preferred equity investments. As of June 30, 2015, the Alternative Investment Funds were comprised of (i) PGRESS, (ii) PGRESS-H, (iii) PGRESS-A and (iv) Fund VIII, which had an aggregate of \$580,200,000 of committed capital (including \$95,200,000 of capital which was committed in the second quarter), of which we have invested \$51,000,000.

The following is a summary of the investments of our Alternative Investment Funds.

(Amounts in thousands)		%	Interest/ Dividend		As of	
Fund	Investment Type	Ownership	Rate	Initial Maturity	June 30, 2015	December 31, 2014
Fund VIII	Mezzanine Loan	1.7%	8.3%	Jan-2022	\$46,747	\$45,947
PGRESS Funds	Preferred Equity Investments	4.9% - 5.4%	10.3% - 15.0%	Sep-2015 - Feb-2019	95,717	94,224
					\$142,464	\$140,171

The Predecessor

Below is a summary of realized and unrealized gains from real estate fund investments on our consolidated statement of income.

(Amounts in thousands)	Three Months Ended June 30, 2014	Six Months Ended June 30, 2014
Income Statement		
Realized gains on real estate fund investments	\$-	\$-

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Unrealized gains on real estate fund investments	33,750	79,917
Realized and unrealized gains, net	\$33,750	\$79,917

Asset Management Fees

Our predecessor earned asset management fees from the Funds it managed. Asset management fees and expenses related to Funds included in the combined consolidated statement of income are eliminated in combination and consolidation. The limited partners' share of such fees are reflected as a reduction of net income attributable to noncontrolling interests, which results in a corresponding increase in net income attributable to our Predecessor.

Below is a summary of the asset management fees earned by our Predecessor.

(Amounts in thousands)	Three Months Ended June 30, 2014	Six Months Ended June 30, 2014
Income Statement		
Gross asset management fees	\$ 7,527	\$ 14,937
Eliminated fees ⁽¹⁾	(392)	(782)
Net asset management fees	\$ 7,135	\$ 14,155

⁽¹⁾Eliminated fees reflect a reduction in asset management fees from the general partner interest in each of the Funds.

PARAMOUNT GROUP, INC. AND PARAMOUNT PREDECESSOR

NOTES TO COMBINED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

The following tables summarize the income statements for the three and six months ended June 30, 2014 for each of the Property Funds' underlying investments.

(Amounts in thousands)

Statements of Income	Property Funds' Underlying Investments for the Three Months Ended June 30, 2014								
	1633 Broadway Ave	900 Third Ave	31 West 52nd St	1301 Ave of the Americas	One Market Plaza	Liberty Place	1899 Penn. Ave	2099 Penn. Ave	425 Eye St
Revenues:									
Rental income	\$37,251	\$8,982	\$18,122	\$27,139	\$17,910	\$1,690	\$1,940	\$43	\$2,642
Tenant reimbursement income	3,096	751	1,300	2,318	273	563	967	1	83
Fee and other income	702	168	1,333	1,087	681	9	28	7	(179)
Total revenue	41,049	9,901	20,755	30,544	18,864	2,262	2,935	51	2,546
Expenses:									
Building operating	13,268	4,038	5,774	13,008	6,836	1,086	1,348	1,143	1,390
Related party management fees	784	261	329	427	177	61	66	1	79
Operating	14,052	4,299	6,103	13,435	7,013	1,147	1,414	1,144	1,469
Depreciation and amortization	2,780	2,144	5,545	9,341	8,682	-	940	-	1,398
General and administrative	10	24	7	24	281	11	11	12	107
Total expenses	16,842	6,467	11,655	22,800	15,976	1,158	2,365	1,156	2,974
Operating income (loss)	24,207	3,434	9,100	7,744	2,888	1,104	570	(1,105)	(428)
Unrealized gain on interest rate swaps	5,665	1,169	1,686	2,872	3,529	-	-	-	-
Interest and debt expense	(12,894)	(3,696)	(5,564)	(15,379)	(13,334)	(945)	(1,129)	(1,380)	(1,301)
Unrealized depreciation on investment in real estate	-	-	-	-	-	(459)	-	(520)	-
Net income (loss) before taxes	16,978	907	5,222	(4,763)	(6,917)	(300)	(559)	(3,005)	(1,729)
Income tax benefit (expense)	-	-	-	-	-	(29)	114	-	24
Net income (loss)	\$16,978	\$907	\$5,222	\$(4,763)	\$(6,917)	\$(329)	\$(445)	\$(3,005)	\$(1,705)

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(Amounts in thousands)	Property Funds' Underlying Investments for the Six Months Ended							
	June 30, 2014							
		31						
	900	West	1301 Ave	One		1899	2099	425
	1633	52nd	of the	Market	Liberty	Penn.	Penn.	Eye
Statements of Income	Broadway	St	Americas	Plaza	Place	Ave	Ave	St