Empire State Realty Trust, Inc.
Form 10-Q
November 06, 2018

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarterly Period Ended September 30, 2018
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: 001-36105
EMPIRE STATE REALTY TRUST, INC.

(Exact name of Registrant as specified in its charter)

Maryland	37-1645259
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

111 West 33rd Street, 12th Floor
New York, New York 10120
(Address of principal executive offices) (Zip Code)
(212) 687-8700
(Registrant's telephone number, including area code)
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o
Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit 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 definition of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer x	Accelerated filer o
Non-accelerated filer o	Smaller reporting company o
	Emerging growth company o

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. o
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
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class A Common Stock, par value $0.01 per share	173,008,231
Class B Common Stock, par value $0.01 per share	1,038,804
(Class)	(Outstanding on October 30, 2018)

EMPIRE STATE REALTY TRUST, INC.
FORM 10-Q FOR THE QUARTER ENDED SEPTEMBER 30, 2018
TABLE OF CONTENTS

		PAGE
PART 1.	FINANCIAL INFORMATION	
ITEM 1.	FINANCIAL STATEMENTS	
	Condensed Consolidated Balance Sheets as of September 30, 2018 (unaudited) and December 31, 2017	2
	Condensed Consolidated Statements of Income for the three and nine months ended September 30, 2018 and 2017 (unaudited)	3
	Condensed Consolidated Statements of Comprehensive Income (Loss) for the three and nine months ended September 30, 2018 and 2017 (unaudited)	4
	Condensed Consolidated Statements of Stockholders' Equity for the nine months ended September 30, 2018 (unaudited)	5
	Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2018 and 2017 (unaudited)	6
	Notes to Condensed Consolidated Financial Statements (unaudited)	8
ITEM 2.	MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS	28
ITEM 3.	QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK	44
ITEM 4.	CONTROLS AND PROCEDURES	44
PART II.	OTHER INFORMATION	45
ITEM 1.	LEGAL PROCEEDINGS	45
ITEM 1A.	RISK FACTORS	45
ITEM 2.	UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS	45
ITEM 3.	DEFAULTS UPON SENIOR SECURITIES	45
ITEM 4.	MINE SAFETY DISCLOSURES	45
ITEM 5.	OTHER INFORMATION	45
ITEM 6.	EXHIBITS	45
SIGNATURES		46

1

ITEM 1. FINANCIAL STATEMENTS

Empire State Realty Trust, Inc.
Condensed Consolidated Balance Sheets
(amounts in thousands, except share and per share amounts)

	September 30, 2018 (unaudited)	December 31, 2017
ASSETS		
Commercial real estate properties, at cost:		
Land	$ 201,196	$ 201,196
Development costs	7,987	7,986
Building and improvements	2,616,772	2,458,473
	2,825,955	2,667,655
Less: accumulated depreciation	(718,959)	(656,900)
Commercial real estate properties, net	2,106,996	2,010,755
Cash and cash equivalents	229,745	464,344
Restricted cash	54,356	65,853
Short-term investments	400,000	—
Tenant and other receivables, net of allowance of $1,616 and $1,422 in 2018 and 2017, respectively	31,342	28,329
Deferred rent receivables, net of allowance of $22 and $185 in 2018 and 2017, respectively	195,455	178,629
Prepaid expenses and other assets	50,663	61,028
Deferred costs, net	244,441	262,701
Acquired below-market ground leases, net	362,355	368,229
Goodwill	491,479	491,479
Total assets	$ 4,166,832	$ 3,931,347
LIABILITIES AND EQUITY		
Liabilities:		
Mortgage notes payable, net	$ 609,299	$ 717,164
Senior unsecured notes, net	1,045,362	707,895
Unsecured term loan facility, net	264,023	263,662
Unsecured revolving credit facility	—	—
Accounts payable and accrued expenses	128,340	110,849
Acquired below-market leases, net	55,662	66,047
Deferred revenue and other liabilities	32,175	40,907
Tenants’ security deposits	42,520	47,086
Total liabilities	2,177,381	1,953,610
Commitments and contingencies		
Equity:		
Empire State Realty Trust, Inc. stockholders' equity:		
Preferred stock, $0.01 par value per share, 50,000,000 shares authorized, none issued or outstanding	—	—
Class A common stock, $0.01 par value per share, 400,000,000 shares authorized, 168,176,734 shares issued and outstanding and 160,424,575 shares issued and outstanding in 2018 and 2017, respectively	1,681	1,604
Class B common stock, $0.01 par value per share, 50,000,000 shares authorized, 1,044,169 and 1,052,469 shares issued and outstanding in 2018 and 2017, respectively	10	11
Additional paid-in capital	1,165,080	1,128,460

Accumulated other comprehensive loss	(2,229)	(8,555)
Retained earnings	37,004	46,762
Total Empire State Realty Trust, Inc.'s stockholders' equity	1,201,546	1,168,282
Non-controlling interests in operating partnership	779,901	801,451
Private perpetual preferred units, $16.62 per unit liquidation preference, 1,560,360 issued and outstanding in 2018 and 2017	8,004	8,004
Total equity	1,989,451	1,977,737
Total liabilities and equity	$ 4,166,832	$ 3,931,347

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

Empire State Realty Trust, Inc.
Condensed Consolidated Statements of Income
(unaudited)
(amounts in thousands, except per share amounts)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Revenues:				
Rental revenue	$123,621	$122,391	$369,970	$360,348
Tenant expense reimbursement	18,627	20,346	52,626	53,889
Observatory revenue	40,241	39,306	96,691	94,212
Lease termination fees	1,185	1,165	2,164	10,354
Third-party management and other fees	312	345	1,151	1,088
Other revenue and fees	2,416	2,993	9,600	7,338
Total revenues	186,402	186,546	532,202	527,229
Operating expenses:				
Property operating expenses	42,772	41,270	126,375	122,009
Ground rent expenses	2,331	2,331	6,994	6,994
General and administrative expenses	13,148	12,899	39,001	36,566
Observatory expenses	8,854	8,648	23,868	23,079
Real estate taxes	28,284	26,901	81,771	76,001
Depreciation and amortization	42,475	38,490	121,826	119,868
Total operating expenses	137,864	130,539	399,835	384,517
Total operating income	48,538	56,007	132,367	142,712
Other income (expense):				
Interest income	3,485	774	7,209	2,169
Interest expense	(20,658)	(16,890)	(58,774)	(52,109)
Loss on early extinguishment of debt	—	(2,157)	—	(2,157)
Loss from derivative financial instruments	—	—	—	(289)
Income before income taxes	31,365	37,734	80,802	90,326
Income tax expense	(2,135)	(2,245)	(3,330)	(4,333)
Net income	29,230	35,489	77,472	85,993
Private perpetual preferred unit distributions	(234)	(234)	(702)	(702)
Net income attributable to non-controlling interests	(12,654)	(16,449)	(34,009)	(39,916)
Net income attributable to common stockholders	$16,342	$18,806	$42,761	$45,375
Total weighted average shares:				
Basic	167,657	158,102	165,613	157,796
Diluted	297,478	297,871	297,181	298,089
Earnings per share attributable to common stockholders:				
Basic	$0.10	$0.12	$0.26	$0.29
Diluted	$0.10	$0.12	$0.26	$0.29
Dividends per share	$0.105	$0.105	$0.315	$0.315

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Empire State Realty Trust, Inc.
Condensed Consolidated Statements of Comprehensive Income (Loss)
(unaudited)
(amounts in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Net income	$29,230	$35,489	$77,472	$85,993
Other comprehensive income (loss):				
Unrealized gain (loss) on valuation of interest rate swap agreements	3,884	(1,638)	9,827	(14,654)
Less: amount reclassified into interest expense	427	359	1,562	402
Other comprehensive income (loss)	4,311	(1,279)	11,389	(14,252)
Comprehensive income (loss)	33,541	34,210	88,861	71,741
Net income attributable to non-controlling interests and private perpetual preferred unitholders	(12,888)	(16,683)	(34,711)	(40,618)
Other comprehensive (income) loss attributable to non-controlling interests	(1,881)	586	(5,045)	6,670
Comprehensive income (loss) attributable to common stockholders	$18,772	$18,113	$49,105	$37,793

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

Empire State Realty Trust, Inc.
Condensed Consolidated Statements of Stockholders' Equity
For The Nine Months Ended September 30, 2018
(unaudited)
(amounts in thousands)

	Number of Class A Common Shares	Class A Common Stock	Number of Class B Common Shares	Class B Common Stock	Additional Paid-In Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total Stockholders' Equity	Non-controlling Interests	Private Perpetual Preferred Units	Total Equity
Balance at December 31, 2017	160,425	$1,604	1,052	$11	$1,128,460	$(8,555)	$46,762	$1,168,282	$801,451	$8,004	$1,977,737
Issuance of Class A shares	284	3	—	—	4,746	—	—	4,749	—	—	4,749
Conversion of operating partnership units and Class B shares to Class A shares	7,444	74	(8)	(1)	31,605	(18)	—	31,660	(31,660)	—	—
Equity compensation:											
LTIP units	—	—	—	—	—	—	—	—	13,795	—	13,795
Restricted stock, net of forfeitures	24	—	—	—	269	—	—	269	—	—	269
Dividends and distributions	—	—	—	—	—	—	(52,519)	(52,519)	(42,739)	(702)	(95,960)
Net income	—	—	—	—	—	—	42,761	42,761	34,009	702	77,472
Other comprehensive income (loss)	—	—	—	—	—	6,344	—	6,344	5,045	—	11,389
Balance at September 30, 2018	168,177	$1,681	1,044	$10	$1,165,080	$(2,229)	$37,004	$1,201,546	$779,901	$8,004	$1,989,451

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

Empire State Realty Trust, Inc.
Condensed Consolidated Statements of Cash Flows
(unaudited)
(amounts in thousands)

	Nine Months Ended September 30,	
	2018	2017
Cash Flows From Operating Activities		
Net income	$77,472	$85,993
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	121,826	119,868
Amortization of non-cash items within interest expense	5,142	919
Amortization of acquired above- and below-market leases, net	(4,387)	(4,154)
Amortization of acquired below-market ground leases	5,873	5,873
Straight-lining of rental revenue	(16,662)	(20,590)
Equity based compensation	14,064	10,808
Settlement of derivative contracts	—	(6,335)
Unrealized loss from derivative financial instruments	—	2,157
Increase (decrease) in cash flows due to changes in operating assets and liabilities:		
Security deposits	(4,566)	213
Tenant and other receivables	(3,176)	(12,119)
Deferred leasing costs	(18,578)	(21,660)
Prepaid expenses and other assets	20,308	13,672
Accounts payable and accrued expenses	(1,181)	(8,917)
Deferred revenue and other liabilities	(8,732)	9,108
Net cash provided by operating activities	187,403	174,836
Cash Flows From Investing Activities		
Short-term investments	(400,000)	—
Development costs	(1)	(27)
Additions to building and improvements	(169,622)	(157,579)
Net cash used in investing activities	(569,623)	(157,606)

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

Empire State Realty Trust, Inc.
Condensed Consolidated Statements of Cash Flows (continued)
(unaudited)
(amounts in thousands)

	Nine Months Ended September 30,	
	2018	2017
Cash Flows From Financing Activities		
Proceeds from mortgage notes payable	160,000	315,000
Repayment of mortgage notes payable	(265,688)	(344,618)
Proceeds from unsecured senior notes	335,000	—
Proceeds from unsecured revolving credit facility and term loan	—	265,000
Repayments of unsecured revolving credit facility and term loan	—	(265,000)
Proceeds from the sale of common stock	4,749	—
Deferred financing costs	(1,977)	(12,186)
Private perpetual preferred unit distributions	(702)	(702)
Dividends paid to common stockholders	(52,518)	(49,843)
Distributions paid to non-controlling interests in the operating partnership	(42,740)	(44,641)
Net cash provided by (used in) financing activities	136,124	(136,990)
Net decrease in cash and cash equivalents and restricted cash	(246,096)	(119,760)
Cash and cash equivalents and restricted cash—beginning of period	530,197	615,885
Cash and cash equivalents and restricted cash—end of period	$284,101	$496,125
Reconciliation of Cash and Cash Equivalents and Restricted Cash:		
Cash and cash equivalents at beginning of period	$464,344	$554,371
Restricted cash at beginning of period	65,853	61,514
Cash and cash equivalents and restricted cash at beginning of period	$530,197	$615,885
Cash and cash equivalents at end of period	$229,745	$432,105
Restricted cash at end of period	54,356	64,020
Cash and cash equivalents and restricted cash at end of period	$284,101	$496,125
Supplemental disclosures of cash flow information:		
Cash paid for interest	$56,597	$53,918
Cash paid for income taxes	$3,690	$5,004
Non-cash investing and financing activities:		
Building and improvements included in accounts payable and accrued expenses	$92,506	$72,130
Derivative instruments at fair values included in prepaid expenses and other assets	9,944	—
Derivative instruments at fair values included in accounts payable and accrued expenses	—	13,378
Conversion of operating partnership units and Class B shares to Class A shares	31,660	11,087

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

Empire State Realty Trust, Inc.
Notes to Condensed Consolidated Financial Statements
(unaudited)

1. Description of Business and Organization

As used in these condensed consolidated financial statements, unless the context otherwise requires, “we,” “us,” “our,” the “company,” and "ESRT" mean Empire State Realty Trust, Inc. and its consolidated subsidiaries.

We are a self-administered and self-managed real estate investment trust ("REIT") that owns, manages, operates, acquires and repositions office and retail properties in Manhattan and the greater New York metropolitan area. As of September 30, 2018, our total portfolio contained 10.1 million rentable square feet of office and retail space. We owned 14 office properties (including three long-term ground leasehold interests) encompassing approximately 9.4 million rentable square feet of office space. Nine of these properties are located in the midtown Manhattan market and aggregate approximately 7.6 million rentable square feet of office space, including the Empire State Building. Our Manhattan office properties also contain an aggregate of 513,437 rentable square feet of retail space on their ground floor and/or contiguous levels. Our remaining five office properties are located in Fairfield County, Connecticut and Westchester County, New York, encompassing in the aggregate approximately 1.9 million rentable square feet. The majority of square footage for these five properties is located in densely populated metropolitan communities with immediate access to mass transportation. Additionally, we have entitled land at the Stamford Transportation Center in Stamford, Connecticut, adjacent to one of our office properties, that will support the development of an approximately 380,000 rentable square foot office building and garage. As of September 30, 2018, our portfolio included four standalone retail properties located in Manhattan and two standalone retail properties located in the city center of Westport, Connecticut, encompassing 205,748 rentable square feet in the aggregate.

We were organized as a Maryland corporation on July 29, 2011 and commenced operations upon completion of our initial public offering and related formation transactions on October 7, 2013. Our operating partnership, Empire State Realty OP, L.P. (the "Operating Partnership"), holds substantially all of our assets and conducts substantially all of our business. As of September 30, 2018, we owned approximately 55.8% of the aggregate operating partnership units in the Operating Partnership. We, as the sole general partner in the Operating Partnership, have responsibility and discretion in the management and control of the Operating Partnership, and the limited partners in the Operating Partnership, in such capacity, have no authority to transact business for, or participate in the management activities of, the Operating Partnership. Accordingly, the Operating Partnership has been consolidated by us. We elected to be taxed as a REIT and operate in a manner that we believe allows us to qualify as a REIT for federal income tax purposes commencing with our taxable year ended December 31, 2013.

2. Summary of Significant Accounting Policies

There have been no material changes to the summary of significant accounting policies included in the section entitled "Summary of Significant Accounting Policies" in our December 31, 2017 Annual Report on Form 10-K.

Basis of Quarterly Presentation and Principles of Consolidation

The accompanying unaudited condensed consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (“GAAP”), for interim financial information, and with the rules and regulations of the Securities and Exchange Commission (the "SEC"). Accordingly, certain information and footnote disclosures required by GAAP for complete financial statements have been condensed or omitted in accordance with such rules and regulations. In the opinion of management, all adjustments and eliminations (including intercompany balances and transactions), consisting of normal recurring adjustments, considered necessary for the fair presentation of the financial statements have been included.

The results of operations for the periods presented are not necessarily indicative of the results that may be expected for the corresponding full years. These financial statements should be read in conjunction with the financial statements and accompanying notes included in the financial statements for the year ended December 31, 2017 contained in our

Annual Report on Form 10-K. We do not consider our business to be subject to material seasonal fluctuations, except that our observatory business is subject to tourism seasonality. During the past ten years, approximately 16.0% to 18.0% of our annual observatory

revenue was realized in the first quarter, 26.0% to 28.0% was realized in the second quarter, 31.0% to 33.0% was realized in the third quarter and 23.0% to 25.0% was realized in the fourth quarter.

We consolidate entities in which we have a controlling financial interest. In determining whether we have a controlling financial interest in a partially owned entity and the requirement to consolidate the accounts of that entity, we consider factors such as ownership interest, board representation, management representation, authority to make decisions, and contractual and substantive participating rights of the partners/members. For variable interest entities ("VIE"), we consolidate the entity if we are deemed to have a variable interest in the entity and through that interest we are deemed the primary beneficiary. The primary beneficiary of a VIE is the entity that has (i) the power to direct the activities that most significantly impact the entity's economic performance and (ii) the obligation to absorb losses of the VIE or the right to receive benefits from the VIE that could be significant to the VIE. The primary beneficiary is required to consolidate the VIE. The Operating Partnership is a variable interest entity of our company, Empire State Realty Trust, Inc. As the Operating Partnership is already consolidated in the financial statements of Empire State Realty Trust, Inc., the identification of this entity as a variable interest entity has no impact on our consolidated financial statements.

We will assess the accounting treatment for each investment we may have in the future. This assessment will include a review of each entity’s organizational agreement to determine which party has what rights and whether those rights are protective or participating. For all VIEs, we will review such agreements in order to determine which party has the power to direct the activities that most significantly impact the entity’s economic performance and benefit. In situations where we or our partner could approve, among other things, the annual budget, or leases that cover more than a nominal amount of space relative to the total rentable space at each property, we would not consolidate the investment as we consider these to be substantive participation rights that result in shared power of the activities that would most significantly impact the performance and benefit of such joint venture investment.

A non-controlling interest in a consolidated subsidiary is defined as the portion of the equity (net assets) in a subsidiary not attributable, directly or indirectly, to a parent. Non-controlling interests are required to be presented as a separate component of equity in the condensed consolidated balance sheets and in the condensed consolidated statements of income by requiring earnings and other comprehensive income to be attributed to controlling and non-controlling interests.

Accounting Estimates

The preparation of the condensed consolidated financial statements in accordance with GAAP requires management to use estimates and assumptions that in certain circumstances affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. Significant items subject to such estimates and assumptions include allocation of the purchase price of acquired real estate properties among tangible and intangible assets, determination of the useful life of real estate properties and other long-lived assets, valuation and impairment analysis of commercial real estate properties and other long-lived assets, estimate of tenant expense reimbursements, valuation of the allowance for doubtful accounts, and valuation of derivative instruments, senior unsecured notes, mortgage notes payable, unsecured term loan and revolving credit facilities, and equity based compensation. These estimates are prepared using management’s best judgment, after considering past, current, and expected events and economic conditions. Actual results could differ from those estimates.

Short-term Investments

Short-term investments include time deposits with original maturities of greater than three months and remaining maturities of less than one year. The fair values of these investments approximate their carrying values.

Reclassification

The prior year balance of other revenues and fees has been reclassified to separately present lease termination fees and interest income and conform to our current year presentation.

Recently Issued or Adopted Accounting Standards

During August 2018, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2018-15, Intangibles-Goodwill and Other-Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract (a consensus of the FASB Emerging Issues Task Force), which contain amendments that align the requirements for

capitalizing implementation costs

incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal use software license). Accordingly, for entities in a hosting arrangement that is a service contract, costs for implementation activities in the application development stage are capitalized depending on the nature of the costs, while costs incurred during the preliminary project and post-implementation stages are expensed as the activities are performed. The amendments in ASU No. 2018-15 also require the entity (customer) to expense the capitalized implementation costs of a hosting arrangement that is a service contract over the term of the hosting arrangement. The amendments are effective for public business entities for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. Early adoption of the amendments is permitted, including adoption in any interim period. The amendments in ASU No. 2018-15 should be applied either retrospectively or prospectively to all implementation costs incurred after the date of adoption. We are evaluating the impact of adopting this new accounting standard on our consolidated financial statements.

During January 2017, the FASB issued ASU No. 2017-04, Intangibles-Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment, which contain amendments that modify the concept of impairment from the condition that exists when the carrying amount of goodwill exceeds its implied fair value to the condition that exists when the carrying amount of a reporting unit exceeds its fair value. An entity no longer will determine goodwill impairment by calculating the implied fair value of goodwill by assigning the fair value of a reporting unit to all of its assets and liabilities as if that reporting unit had been acquired in a business combination. Because these amendments eliminate Step 2 from the goodwill impairment test, they should reduce the cost and complexity of evaluating goodwill for impairment. ASU No. 2017-04 should be applied on a prospective basis and the amendments adopted for the annual or any interim goodwill impairment tests in fiscal years beginning after December 15, 2019. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. We are evaluating the impact of adopting this new accounting standard on our consolidated financial statements.

During January 2017, the FASB issued ASU No. 2017-01, Business Combinations (Topic 805): Clarifying the Definition of a Business, which contain amendments to clarify the definition of a business with the objective of adding guidance to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The amendments in ASU No. 2017-01 provide a screen to determine when an integrated set of assets and activities (collectively referred to as a "set") is not a business. The screen requires that when substantially all of the fair value of the gross assets acquired (or disposed of) is concentrated in a single identifiable asset or a group of similar identifiable assets, the set is not a business. This screen reduces the number of transactions that need to be further evaluated. Real estate acquisitions that do not meet the definition of a business will be accounted for as asset acquisitions and the corresponding acquisition costs will be capitalized rather than expensed. These amendments narrow the definition of the term output so that the term is consistent with how outputs are described in Topic 606, Revenue from Contracts with Customers. ASU No. 2017-01 is effective for annual periods beginning after December 15, 2017, including interim periods within those periods. The amendments are applied prospectively on or after the effective date. No disclosures are required at transition. We believe that acquisitions of real estate properties will generally be considered asset acquisitions.

During November 2016, the FASB issued ASU No. 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash, which contain amendments that require that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. ASU No. 2016-18 is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. We adopted this standard on January 1, 2018 using a retrospective transition method. The adoption did not have a material impact on our consolidated financial statements.

During August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments, which addresses eight specific cash flow issues with the objective of reducing the existing diversity in practice in how certain cash receipts and cash payments are presented and classified in the statement of cash flows. ASU No. 2016-15 is effective for fiscal years beginning after December 15, 2017,

including interim periods within those fiscal years. We adopted this standard on January 1, 2018 using a retrospective transition method. The adoption did not have a material impact on our consolidated financial statements.

During June 2016, the FASB issued ASU No. 2016-13, Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, which contains amendments that replace the incurred loss impairment methodology in current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. ASU No. 2016-13 will be effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Earlier adoption as of the fiscal

years beginning after December 15, 2018, including interim periods within those fiscal years, is permitted. The amendments must be adopted through a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective (that is, a modified retrospective approach). We are evaluating the impact of adopting this new accounting standard on our consolidated financial statements.

During February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842), which requires that a lessee recognize in the statement of financial position a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term. For leases with a term of 12 months or less, a lessee is permitted to make an accounting policy election by class of underlying asset not to recognize lease assets and lease liabilities. ASU No. 2016-02 leaves the accounting for leases by lessors largely unchanged from previous GAAP. ASU No. 2016-02 will be effective for fiscal years beginning after December 15, 2018 and subsequent interim periods. The new standard must be adopted using a modified retrospective transition, and provides for certain practical expedients. Transition will require application of the new guidance at the beginning of the earliest comparative period presented. This ASU is expected to result in the recognition of a right-to-use asset and related liability to account for our future obligations under our ground lease agreements for which we are the lessee. As of September 30, 2018, the remaining contractual payments under our ground lease agreements aggregated $76.3 million. In addition, under ASU 2016-02, lessors may only capitalize incremental direct leasing costs. As a result, we expect that we will no longer capitalize our non-contingent leasing costs and instead will expense these costs as incurred. These costs totaled $4.5 million for the year ended December 31, 2017. During July 2018, the FASB issued ASU No. 2018-10, Codification Improvements to Topic 842, Leases, which contains amendments which are intended to clarify or to correct unintended application of ASU No. 2016-02. Also during July 2018, the FASB issued ASU No. 2018-11, Targeted Improvements to Topic 842, Leases, which provides another transition method in addition to the existing modified retrospective transition method by allowing a cumulative effect adjustment to the opening balance of retained earnings in the period of adoption. The amendments in ASU No. 2018-11 also provide lessors with a practical expedient, by class of underlying asset, to not separate nonlease components from the associated lease component provided that (1) the timing and pattern of transfer are the same for the nonlease components and associated lease component and (2) the lease component, if accounted separately, would be classified as an operating lease. For entities that have not yet adopted ASU No. 2016-02, the effective dates and transition requirements for ASU No. 2018-10 and ASU 2018-11 will be the same as the effective date and transition requirements in ASU No. 2016-02. We continue to evaluate the impact of adopting these new accounting standards on our consolidated financial statements.

During May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers, which replaces all current GAAP guidance related to revenue recognition and eliminates all industry-specific guidance. The new revenue recognition standard provides a unified model to determine when and how revenue is recognized. The core principle is that a company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. We adopted this standard on January 1, 2018 and it did not have a material impact on our consolidated financial statements.

3. Deferred Costs, Acquired Lease Intangibles and Goodwill

Deferred costs, net, consisted of the following as of September 30, 2018 and December 31, 2017 (amounts in thousands):

	September 30, 2018	December 31, 2017
Leasing costs	$ 171,865	$ 164,751
Acquired in-place lease value and deferred leasing costs	218,810	237,364
Acquired above-market leases	53,208	67,415
	443,883	469,530
Less: accumulated amortization	(206,210)	(215,102)
Total deferred costs, net, excluding net deferred financing costs	$ 237,673	$ 254,428

At September 30, 2018 and December 31, 2017, $6.8 million and $8.3 million, respectively, of net deferred financing costs associated with the unsecured revolving credit facility was included in deferred costs, net on the condensed consolidated balance sheet.

Amortization expense related to deferred leasing costs and acquired deferred leasing costs was $6.3 million and $5.8 million for the three months ended September 30, 2018 and 2017, respectively, and $18.4 million and $17.9 million for the nine months ended September 30, 2018 and 2017, respectively. Amortization expense related to acquired lease intangibles was $2.9

million and $4.0 million for the three months ended September 30, 2018 and 2017, respectively, and $9.3 million and $13.0 million for the nine months ended September 30, 2018 and 2017, respectively.

Amortizing acquired intangible assets and liabilities consisted of the following as of September 30, 2018 and December 31, 2017 (amounts in thousands):

	September 30, 2018	December 31, 2017
Acquired below-market ground leases	$ 396,916	$ 396,916
Less: accumulated amortization	(34,561)	(28,687)
Acquired below-market ground leases, net	$ 362,355	$ 368,229

	September 30, 2018	December 31, 2017
Acquired below-market leases	$ (120,568)	$ (132,026)
Less: accumulated amortization	64,906	65,979
Acquired below-market leases, net	$ (55,662)	$ (66,047)

Rental revenue related to the amortization of below-market leases, net of above-market leases, was $1.7 million and $1.6 million for the three months ended September 30, 2018 and 2017, respectively, and $4.4 million and $4.1 million for the nine months ended September 30, 2018 and 2017, respectively.

As of September 30, 2018, we had goodwill of $491.5 million. Goodwill was allocated $227.5 million to the observatory reportable segment and $264.0 million to the real estate segment.

12

4. Debt

Debt consisted of the following as of September 30, 2018 and December 31, 2017 (amounts in thousands):

	Principal Balance		As of September 30, 2018		
	September 30, 2018	December 31, 2017	Stated Rate	Effective Rate[1]	Maturity Date[2]
Mortgage debt collateralized by:					
Fixed rate mortgage debt					
Metro Center	$92,372	$93,948	3.59%	3.66%	11/5/2024
10 Union Square	50,000	50,000	3.70%	3.97%	4/1/2026
1542 Third Avenue	30,000	30,000	4.29%	4.53%	5/1/2027
First Stamford Place[3]	180,000	180,000	4.28%	4.44%	7/1/2027
1010 Third Avenue and 77 West 55th Street	39,177	39,710	4.01%	4.20%	1/5/2028
10 Bank Street	33,988	34,602	4.23%	4.35%	6/1/2032
383 Main Avenue	30,000	30,000	4.44%	4.55%	6/30/2032
1333 Broadway	160,000	66,602	4.21%	4.26%	2/5/2033
1400 Broadway					
(first lien mortgage loan)	—	66,632	—	—	—
(second lien mortgage loan)	—	9,172	—	—	—
111 West 33rd Street					
(first lien mortgage loan)	—	74,045	—	—	—
(second lien mortgage loan)	—	9,369	—	—	—
1350 Broadway	—	37,144	—	—	—
Total mortgage debt	615,537	721,224			
Senior unsecured notes - exchangeable	250,000	250,000	2.63%	3.93%	8/15/2019
Senior unsecured notes:[6]					
Series A	100,000	100,000	3.93%	3.96%	3/27/2025
Series B	125,000	125,000	4.09%	4.12%	3/27/2027
Series C	125,000	125,000	4.18%	4.21%	3/27/2030
Series D	115,000	115,000	4.08%	4.11%	1/22/2028
Series E	160,000	—	4.26%	4.27%	3/22/2030
Series F	175,000	—	4.44%	4.45%	3/22/2033
Unsecured revolving credit facility[6]	—	—	[4]	[4]	8/29/2021
Unsecured term loan facility[6]	265,000	265,000	[5]	[5]	8/29/2022
Total principal	1,930,537	1,701,224			
Unamortized discount, net of unamortized premium	(2,315)	(3,370)			
Deferred financing costs, net	(9,538)	(9,133)			
Total	$1,918,684	$1,688,721			

(1) The effective rate is the yield as of September 30, 2018, including the effects of debt issuance costs and the amortization of the fair value of debt adjustment.

(2) Pre-payment is generally allowed for each loan upon payment of a customary pre-payment penalty.

(3) Represents a $164 million mortgage loan bearing interest at 4.09% and a $16 million loan bearing interest at 6.25%.

(4) At September 30, 2018, the unsecured revolving credit facility bears a floating rate at 30 day LIBOR plus 1.10%. The rate at September 30, 2018 was 3.36%.

(5) The unsecured term loan facility bears a floating rate at 30 day LIBOR plus 1.20%. Pursuant to an interest rate swap agreement, the LIBOR rate is fixed at 2.1485% through maturity. The rate at September 30, 2018 was 3.35%.

(6) At September 30, 2018, we were in compliance with all debt covenants.

Mortgage Debt

During January 2018, we refinanced and increased our mortgage debt on 1333 Broadway from $66.6 million to $160.0 million, due February 2033 with interest fixed at 4.21%. A portion of this increase was applied to release the $75.8 million mortgage lien on 1400 Broadway.

Principal Payments
Aggregate required principal payments at September 30, 2018 are as follows (amounts in thousands):

Year	Amortization	Maturities	Total
2018	$ 925	$—	$925
2019	3,790	250,000	253,790
2020	3,938	—	3,938
2021	4,090	—	4,090
2022	5,628	265,000	270,628
Thereafter	41,744	1,355,422	1,397,166
Total	$ 60,115	$1,870,422	$1,930,537

Deferred Financing Costs
Deferred financing costs, net, consisted of the following at September 30, 2018 and December 31, 2017 (amounts in thousands):

	September 30, 2018	December 31, 2017
Financing costs	$ 25,312	$24,446
Less: accumulated amortization	(9,006)	(7,039)
Total deferred financing costs, net	$ 16,306	$17,407

At September 30, 2018 and December 31, 2017, $6.8 million and $8.3 million, respectively, of net deferred financing costs associated with the unsecured revolving credit facility was included in deferred costs, net on the condensed consolidated balance sheet.
Amortization expense related to deferred financing costs was $1.1 million and $1.0 million for the three months ended September 30, 2018 and 2017, respectively, and $3.1 million and $3.6 million for the nine months ended September 30, 2018 and 2017, respectively, and was included in interest expense.
Unsecured Revolving Credit and Term Loan Facility

During August 2017, through the Operating Partnership, we entered into an amended and restated senior unsecured revolving credit and term loan facility (the “Facility”) with Bank of America, N.A., as administrative agent, Merrill Lynch, Pierce, Fenner & Smith Incorporated and Wells Fargo Securities, LLC as Joint Lead Arrangers and Joint Bookrunners, Wells Fargo, National Association and Capital One, National Association, as co-syndication agents, and the lenders party thereto.

The Facility is in the original principal amount of up to $1.365 billion, which consists of a $1.1 billion revolving credit facility and a $265 million term loan facility. We may request the Facility be increased through one or more increases in the revolving credit facility or one or more increases in the term loan facility or the addition of new pari passu term loan tranches, for a maximum aggregate principal amount not to exceed $1.75 billion.

The initial maturity of the unsecured revolving credit facility is August 2021. We have the option to extend the initial term for up to two additional 6-month periods, subject to certain conditions, including the payment of an extension fee equal to 0.0625% and 0.075% of the then outstanding commitments under the unsecured revolving credit facility on the first and the second extensions, respectively. The term loan facility matures on August 2022. We may prepay the loans under the Facility at any time, subject to reimbursement of the lenders’ breakage and redeployment costs in the case of prepayment of Eurodollar Rate borrowings.

Exchangeable Senior Notes

Issued in August 2014, the $250.0 million 2.625% Exchangeable Senior Notes ("2.625% Exchangeable Senior Notes") are due August 15, 2019. The 2.625% Exchangeable Senior Notes will be exchangeable into cash, shares of Class A

common stock or a combination of cash and shares of Class A common stock, at our election. We have asserted that it is our intent and ability to settle the principal amount of the 2.625% Exchangeable Senior Notes in cash. As of September 30, 2018, the exchange rate of the 2.625% Exchangeable Senior Notes was 51.9443 shares per $1,000 principal amount of notes (equivalent to an initial exchange price of approximately $19.25 per share of Class A common stock), subject to adjustment, as described in the related indenture governing the 2.625% Exchangeable Senior Notes.

For the three and nine months ended September 30, 2018, total interest expense related to the 2.625% Exchangeable Senior Notes was $2.4 million and $7.3 million, respectively, consisting of (i) the contractual interest expense of $1.6 million and $4.9 million, respectively, (ii) the additional non-cash interest expense of $0.7 million and $2.0 million, respectively, relating to the accretion of the debt discount, and (iii) the amortization of deferred financing costs of $0.1 million and $0.4 million, respectively. For the three and nine months ended September 30, 2017, total interest expense related to the 2.625% Exchangeable Senior Notes was $2.4 million and $7.3 million, respectively, consisting of (i) the contractual interest expense of $1.6 million and $4.9 million, respectively, (ii) the additional non-cash interest expense of $0.7 million and $2.0 million, respectively, relating to the accretion of the debt discount, and (iii) the amortization of deferred financing costs of $0.1 million and $0.4 million, respectively.

Senior Unsecured Notes

During December 2017, we entered into an agreement to issue and sell an aggregate principal amount of $450.0 million of senior unsecured notes consisting of $115.0 million of 4.08% Series D Senior Notes due 2028, $160.0 million of 4.26% Series E Senior Notes due 2030, and $175.0 million of 4.44% Series F Senior Notes due 2033. We issued and sold the Series D Senior Notes in December 2017 and the Series E and F Senior Notes in March 2018. In connection with the March 2018 issuance of the notes, we repaid our mortgage indebtedness on 111 West 33rd Street and 1350 Broadway, before their maturity dates in early April 2018.

5. Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses consisted of the following as of September 30, 2018 and December 31, 2017 (amounts in thousands):

	September 30, 2018	December 31, 2017
Accrued capital expenditures	$ 92,506	$ 71,769
Accounts payable and accrued expenses	31,841	32,509
Interest rate swap agreements liability	—	436
Accrued interest payable	3,447	5,687
Due to affiliated companies	546	448
Total accounts payable and accrued expenses	$ 128,340	$ 110,849

6. Financial Instruments and Fair Values

Derivative Financial Instruments

We use derivative financial instruments primarily to manage interest rate risk and such derivatives are not considered speculative. These derivative instruments are typically in the form of interest rate swap and forward agreements and the primary objective is to minimize interest rate risks associated with investing and financing activities. The counterparties of these arrangements are major financial institutions with which we may also have other financial relationships. We are exposed to credit risk in the event of non-performance by these counterparties; however, we currently do not anticipate that any of the counterparties will fail to meet their obligations.

We have agreements with our derivative counterparties that contain a provision where if we either default or are capable of being declared in default on any of our indebtedness, then we could also be declared in default on our

derivative obligations. As of September 30, 2018, we did not have any derivatives in a net liability position.

As of September 30, 2018 and December 31, 2017, we had interest rate LIBOR swaps with an aggregate notional value of $515.0 million and $265.0 million, respectively. The notional value does not represent exposure to credit, interest rate

or market risks. As of September 30, 2018, the fair value of our derivative instruments amounted to $9.9 million which is included in prepaid expenses and other assets on the condensed consolidated balance sheet. As of December 31, 2017, the fair value of our derivative instruments amounted to $(0.4) million which was included in accounts payable and accrued expenses on the condensed consolidated balance sheet. These interest rate swaps have been designated as cash flow hedges and hedge the future cash outflows on our exchangeable senior notes and also on our term loan facility that is subject to a floating interest rate. As of September 30, 2018 and 2017, our cash flow hedges are deemed highly effective and a net unrealized gain (loss) of $4.3 million and $(1.3) million for the three months ended September 30, 2018 and 2017, respectively, and a net unrealized gain (loss) of $11.4 million and $(14.3) million for the nine months ended September 30, 2018 and 2017, respectively, are reflected in the condensed consolidated statements of comprehensive income. Amounts reported in accumulated other comprehensive income (loss) related to derivatives will be reclassified to interest expense as interest payments are made on the debt. We estimate that $(2.3) million of the current balance held in accumulated other comprehensive income (loss) will be reclassified into interest expense within the next 12 months relating to interest rate swap contracts in effect as of September 30, 2018.

As of September 30, 2018 and December 31, 2017, the deferred net losses from terminated hedges amounted to $14.1 million and $15.1 million, respectively, which are included in accumulated other comprehensive income (loss) related to derivatives. We will reclassify into earnings, as an increase to interest expense, approximately $1.5 million within the next 12 months related to the deferred losses from the terminated hedges. For the nine months ended September 30, 2017, we recognized a loss of $0.3 million from derivative financial instruments, incurred in connection with the partial termination and re-designation of related cash flow hedges on a $20.0 million notional amount.

The table below summarizes the terms of agreements and the fair values of our derivative financial instruments as of September 30, 2018 and December 31, 2017 (dollar amounts in thousands):

						September 30, 2018		December 31, 2017	
Derivative	Notional Amount	Receive Rate	Pay Rate	Effective Date	Expiration Date	Asset	Liability	Asset	Liability
Interest rate swap	$265,000	1 Month LIBOR	2.1485%	August 31, 2017	August 24, 2022	$ 7,300	$ —	$ —	$ (436)
Interest rate swap	125,000	3 Month LIBOR	2.9580%	July 1, 2019	July 1, 2026	1,316	—	—	—
Interest rate swap	125,000	3 Month LIBOR	2.9580%	July 1, 2019	July 1, 2026	1,328	—	—	—
						$ 9,944	$ —	$ —	$ (436)

The table below shows the effect of our derivative financial instruments designated as cash flow hedges on accumulated other comprehensive income (loss) for the three and nine months ended September 30, 2018 and 2017 (amounts in thousands):

Effects of Cash Flow Hedges	Three Months Ended September 30, 2018	September 30, 2017	Nine Months Ended September 30, 2018	September 30, 2017
Amount of gain (loss) recognized in other comprehensive income (loss)	$3,884	$ (1,638)	$9,827	$(14,654)
Amount of gain (loss) reclassified from accumulated other comprehensive income (loss) into interest expense	(427)	(359)	(1,562)	(402)

The table below shows the effect of our derivative financial instruments designated as cash flow hedges on the condensed consolidated statements of income for the three and nine months ended September 30, 2018 and 2017 (amounts in thousands):

	Three Months Ended	Nine Months Ended
Effects of Cash Flow Hedges		

	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Total interest (expense) presented in the condensed consolidated statements of income in which the effects of cash flow hedges are recorded	$(20,658)	$(16,890)	$(58,774)	$(52,109)
Amount of gain (loss) reclassified from accumulated other comprehensive income (loss) into interest expense	(427)	(359)	(1,562)	(402)

Fair Valuation

The estimated fair values at September 30, 2018 and December 31, 2017 were determined by management, using available market information and appropriate valuation methodologies. Considerable judgment is necessary to interpret market data and develop estimated fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts we could realize on disposition of the financial instruments. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

The fair value of our senior unsecured notes - exchangeable was derived from quoted prices in active markets and is classified as Level 2 since trading volumes are low.

The fair value of derivative instruments is determined using widely accepted valuation techniques, including discounted cash flow analysis on the expected cash flows of each derivative. Although the majority of the inputs used to value our derivatives fall within Level 2 of the fair value hierarchy, the credit valuation adjustments associated with our derivatives utilize Level 3 inputs, such as estimates of current credit spreads to evaluate the likelihood of default by ourselves and our counterparties. The impact of such credit valuation adjustments, determined based on the fair value of each individual contract, was not significant to the overall valuation. As a result, all of our derivatives were classified as Level 2 of the fair value hierarchy.

The fair value of our mortgage notes payable, senior unsecured notes - Series A, B, C, D, E and F, and unsecured term loan facility which are determined using Level 3 inputs, are estimated by discounting the future cash flows using current interest rates at which similar borrowings could be made to us.

The following tables summarize the carrying and estimated fair values of our financial instruments as of September 30, 2018 and December 31, 2017 (amounts in thousands):

	September 30, 2018				
		Estimated Fair Value			
	Carrying Value	Total	Level 1	Level 2	Level 3
Interest rate swaps included in prepaid expenses and other assets	$9,944	$9,944	$ —	$9,944	$ —
Interest rate swaps included in accounts payable and accrued expenses	—	—	—	—	—
Mortgage notes payable	609,299	574,238	—	—	574,238
Senior unsecured notes - Exchangeable	247,114	251,563	—	251,563	—
Senior unsecured notes - Series A, B, C, D, E and F	798,248	773,375	—	—	773,375
Unsecured term loan facility	264,023	265,000	—	—	265,000

	December 31, 2017				
		Estimated Fair Value			
	Carrying Value	Total	Level 1	Level 2	Level 3
Interest rate swaps included in prepaid expenses and other assets	$ —	$ —	$ —	$ —	$ —
Interest rate swaps included in accounts payable and accrued expenses	436	436	—	436	—
Mortgage notes payable	717,643	707,300	—	—	707,300
Senior unsecured notes - Exchangeable	242,737	275,723	275,723	—	—
Senior unsecured notes - Series A, B, C and D	463,656	460,352	—	—	460,352
Unsecured term loan facility	263,692	265,000	—	—	265,000

Disclosure about the fair value of financial instruments is based on pertinent information available to us as of September 30, 2018 and December 31, 2017. Although we are not aware of any factors that would significantly affect the

reasonable fair value amounts, such amounts have not been comprehensively revalued for purposes of these financial statements since that date and current estimates of fair value may differ significantly from the amounts presented herein.

7. Rental Income

We lease various spaces to tenants over terms ranging from one to 21 years. Certain leases have renewal options for additional terms. The leases provide for base monthly rentals and reimbursements for real estate taxes, escalations linked to the consumer price index or common area maintenance known as operating expense escalation. Operating expense reimbursements are reflected in our condensed consolidated statements of income as tenant expense reimbursement.

8. Commitments and Contingencies

Legal Proceedings

Except as described below, as of September 30, 2018, we were not involved in any material litigation, nor, to our knowledge, was any material litigation threatened against us or our properties, other than routine litigation arising in the ordinary course of business such as disputes with tenants. We believe that the costs and related liabilities, if any, which may result from such actions will not materially affect our condensed consolidated financial position, operating results or liquidity.

As previously disclosed, in October 2014, 12 former investors in Empire State Building Associates L.L.C. (“ESBA”), which prior to the initial public offering of our company (the "Offering"), owned the fee title to the Empire State Building, filed an arbitration with the American Arbitration Association against Peter L. Malkin, Anthony E. Malkin, Thomas N. Keltner, Jr., and our subsidiary ESRT MH Holdings LLC, the former supervisor of ESBA, as respondents. The statement of claim (also filed later in federal court in New York for the expressed purpose of tolling the statute of limitations) alleges breach of fiduciary duty and related claims in connection with the Offering and formation transactions and seeks monetary damages and declaratory relief. These investors had opted out of a prior class action bringing similar claims that was settled with court approval. The respondents filed an answer and counterclaims. In March 2015, the federal court action was stayed on consent of all parties pending the arbitration. Arbitration hearings for a select number of sessions started in May 2016 and concluded in August 2018. Post-hearing briefing is currently scheduled to be completed by January 17, 2019.

The respondents believe the allegations in the arbitration are entirely without merit, and they intend to continue to defend them vigorously.

Pursuant to indemnification agreements which were made with our directors, executive officers and chairman emeritus as part of our formation transactions, Anthony E. Malkin, Peter L. Malkin and Thomas N. Keltner, Jr. have defense and indemnity rights from us with respect to this arbitration.

Unfunded Capital Expenditures

At September 30, 2018, we estimate that we will incur approximately $91.5 million of capital expenditures (including tenant improvements and leasing commissions) on our properties pursuant to existing lease agreements. We expect to fund these capital expenditures with operating cash flow, additional property level mortgage financings, our unsecured credit facility, cash on hand and other borrowings. Future property acquisitions may require substantial capital investments for refurbishment and leasing costs. We expect that these financing requirements will be met in a similar fashion.

Ground Leases

Aggregate required payments on ground leases at September 30, 2018 were as follows (amounts in thousands):

2018	$380
2019	1,518
2020	1,518
2021	1,518

2022	1,518
Thereafter	69,816
	$76,268

Concentration of Credit Risk

Financial instruments that subject us to credit risk consist primarily of cash and cash equivalents, restricted cash, short-term investments, tenant and other receivables and deferred rent receivables. At September 30, 2018, we held on deposit at various major financial institutions cash and cash equivalents, restricted cash and short-term investment balances in excess of amounts insured by the Federal Deposit Insurance Corporation.

Asset Retirement Obligations

We are required to accrue costs that we are legally obligated to incur on retirement of our properties which result from acquisition, construction, development and/or normal operation of such properties. Retirement includes sale, abandonment or disposal of a property. Under that standard, a conditional asset retirement obligation represents a legal obligation to perform an asset retirement activity in which the timing and/or method of settlement is conditional on a future event that may or may not be within a company's control and a liability for a conditional asset retirement obligation must be recorded if the fair value of the obligation can be reasonably estimated. Environmental site assessments and investigations have identified asbestos or asbestos-containing building materials in certain of our properties. As of September 30, 2018, management has no plans to remove or alter these properties in a manner that would trigger federal and other applicable regulations for asbestos removal, and accordingly, the obligations to remove the asbestos or asbestos-containing building materials from these properties have indeterminable settlement dates. As such, we are unable to reasonably estimate the fair value of the associated conditional asset retirement obligation. However, ongoing asbestos abatement, maintenance programs and other required documentation are carried out as required and related costs are expensed as incurred.

Other Environmental Matters

Certain of our properties have been inspected for soil contamination due to pollutants, which may have occurred prior to our ownership of these properties or subsequently in connection with its development and/or its use. Required remediation to such properties has been completed, and as of September 30, 2018, management believes that there are no obligations related to environmental remediation other than maintaining the affected sites in conformity with the relevant authority's mandates and filing the required documents. All such maintenance costs are expensed as incurred. We expect that resolution of the environmental matters relating to the above will not have a material impact on our business, assets, consolidated financial condition, results of operations or liquidity. However, we cannot be certain that we have identified all environmental liabilities at our properties, that all necessary remediation actions have been or will be undertaken at our properties or that we will be indemnified, in full or at all, in the event that such environmental liabilities arise.

Insurance Coverage

We carry insurance coverage on our properties of types and in amounts with deductibles that we believe are in line with coverage customarily obtained by owners of similar properties.

9. Equity

Shares and Units

An operating partnership unit of the Operating Partnership ("OP Unit") and a share of our common stock have essentially the same economic characteristics as they receive the same per unit profit distributions of the Operating Partnership. On the one-year anniversary of issuance, an OP Unit may be tendered for redemption for cash; however, we have sole and absolute discretion, and sufficient authorized common stock, to exchange OP Units for shares of common stock on a one-for-one basis instead of cash.

Long-term incentive plan ("LTIP") units are a special class of partnership interests in the Operating Partnership. Each LTIP unit awarded will be deemed equivalent to an award of one share of stock under the First Amended and Restated Empire State Realty Trust, Inc. and Empire State Realty OP, L.P. 2013 Equity Incentive Plan ("2013 Plan"), reducing the availability for other equity awards on a one-for-one basis. The vesting period for LTIP units, if any, will be determined at the time of issuance. Under the terms of the LTIP units, the Operating Partnership will revalue for tax purposes its assets upon the occurrence of certain specified events, and any increase in valuation from the time of

grant until such event will be allocated first to the holders of LTIP units to equalize the capital accounts of such holders with the capital accounts of OP unitholders. Subject to any agreed upon exceptions, once vested and having achieved parity with OP unitholders, LTIP units are convertible into OP Units in the Operating Partnership on a one-for-one basis.

LTIP units subject to time based vesting, whether vested or not, receive the same per unit distributions as OP units, which equal per share dividends (both regular and special) on our common stock. Performance based LTIP units receive 10% of such distributions currently, unless and until such LTIP units are earned based on performance, at which time they will receive the accrued and unpaid 90% and will commence receiving 100% of such distributions thereafter.

The following is net income attributable to common stockholders and the issuance of our Class A shares in exchange for the conversion of OP Units into common stock (amounts in thousands):

	Three Months Ended, September		Nine Months Ended, September	
	30, 2018	September 30, 2017	30, 2018	September 30, 2017
Net income attributable to common stockholders	$16,342	$ 18,806	$42,761	$ 45,375
Increase in additional paid-in capital for the conversion of OP Units into common stock	5,765	1,953	31,605	11,087
Change from net income attributable to common stockholders and transfers from non-controlling interests	$22,107	$ 20,759	$74,366	$ 56,462

As of September 30, 2018, there were 303,333,599 OP Units outstanding, of which 169,220,903, or 55.8%, were owned by us and 134,112,696, or 44.2%, were owned by other partners, including certain directors, officers and other members of executive management.

Dividends and Distributions

Total dividends paid to common stockholders were $17.7 million and $52.5 million for the three and nine months ended September 30, 2018, respectively, and $16.7 million and $49.8 million for the three and nine months ended September 30, 2017, respectively. Total distributions paid to OP unitholders, excluding inter-company distributions, were $14.1 million and $42.7 million for the three and nine months ended September 30, 2018, respectively, and $14.8 million and $44.6 million for the three and nine months ended September 30, 2017, respectively. Total distributions paid to preferred unitholders were $0.2 million and $0.7 million for the three and nine months ended September 30, 2018, respectively, and $0.2 million and $0.7 million for the three and nine months ended September 30, 2017, respectively.

Incentive and Share-Based Compensation

The 2013 Plan provides for grants to directors, employees and consultants consisting of stock options, restricted stock, dividend equivalents, stock payments, performance shares, LTIP units, stock appreciation rights and other incentive awards. An aggregate of 12.2 million shares of our common stock is authorized for issuance under awards granted pursuant to the 2013 Plan, and as of September 30, 2018, 4.3 million shares of common stock remain available for future issuance.

In March 2018, we made grants of LTIP units to executive officers under the 2013 Plan. At such time, we granted to executive officers a total of 386,876 LTIP units that are subject to time-based vesting and 1,737,917 LTIP units that are subject to performance-based vesting, with fair market values of $6.1 million for the time-based vesting awards and $9.6 million for the performance-based vesting awards. In March 2018, we made grants of LTIP units and restricted stock to certain other employees under the 2013 Plan. At such time, we granted to certain other employees a total of 67,449 LTIP units and 39,608 shares of restricted stock that are subject to time-based vesting and 223,950 LTIP units that are subject to performance-based vesting, with fair market values of $1.7 million for the time-based vesting awards and $1.1 million for the performance-based vesting awards. The awards subject to time-based vesting vest ratably over four years from January 1, 2018, subject generally to the grantee's continued employment. The first installment vests on January 1, 2019 and the remainder will vest thereafter in three equal annual installments. The vesting of the LTIP units subject to performance-based vesting is based on the achievement of absolute and relative total stockholder return hurdles over a three-year performance period, commencing on January 1, 2018. Following the completion of the three-year performance period, our compensation committee will determine the number of LTIP

units to which the grantee is entitled based on our performance relative to the performance hurdles set forth in the LTIP unit award agreements the grantee entered into in connection with the award grant. These units then vest in two installments, with the first installment vesting on January 1, 2021 and the second installment vesting on January 1, 2022, subject generally to the grantee's continued employment on those dates.

In 2017, our board of directors determined to reinforce the alignment of our executive officers' interests with that of stockholders by designing a new bonus election program, under which named executive officers could elect to receive their annual incentive bonus in any combination of (i) cash or vested LTIP's at the face amount of such bonus or (ii) time-vesting

LTIP's which would vest over three years, subject to continued employment, at 125% of such face amount. In February 2018, we made grants of LTIP units to executive officers under the 2013 Plan in connection with the 2017 bonus election program. We granted to executive officers a total of 238,609 LTIP units that are subject to time based vesting with a fair market value of $4.0 million. Of these LTIP units, 25,158 LTIP units vested immediately on the grant date and 213,451 LTIP units vest ratably over three years from January 1, 2018, subject generally to the grantee's continued employment. The first installment vests on January 1, 2019 and the remainder will vest thereafter in two equal annual installments.

In May 2018, we made grants of LTIP units to our non-employee directors under the 2013 Plan. At such time, we granted a total of 65,000 LTIP units that are subject to time-based vesting with fair market values of $1.0 million. The awards vest ratably over three years from the date of the grant, subject generally to the director's continued service on our Board of Directors.

Share-based compensation is measured at the fair value of the award on the date of grant and recognized as an expense on a straight-line basis over the vesting period. For the performance-based LTIP units and restricted stock awards, the fair value of the awards was estimated using a Monte Carlo Simulation model. Our stock price, along with the prices of the comparative indexes, is assumed to follow the Geometric Brownian Motion Process. Geometric Brownian Motion is a common assumption when modeling in financial markets, as it allows the modeled quantity (in this case the stock price) to vary randomly from its current value and take any value greater than zero. The volatilities of the returns on our stock price and the comparative indexes were estimated based on implied volatilities and historical volatilities using a six-year look-back period. The expected growth rate of the stock prices over the performance period is determined with consideration of the risk free rate as of the grant date. For LTIP unit awards that are time-based, the fair value of the awards was estimated based on the fair value of our stock at the grant date discounted for the restriction period during which the LTIP units cannot be redeemed or transferred and the uncertainty regarding if, and when, the book capital account of the LTIP units will equal that of the common units. For restricted stock awards that are time-based, we estimate the stock compensation expense based on the fair value of the stock at the grant date.

LTIP units and restricted stock issued during the nine months ended September 30, 2018 were valued at $23.6 million. The weighted-average per unit or share fair value was $8.54 for grants issued in 2018. The per unit or share granted in 2018 was estimated on the respective dates of grant using the following assumptions: an expected life of 5.6 years, a dividend rate of 2.30%, a risk-free interest rate of 2.50%, and an expected price volatility of 17.0%.

No other stock options, dividend equivalents, or stock appreciation rights were issued or outstanding in 2018.

The following is a summary of restricted stock and LTIP unit activity for the nine months ended September 30, 2018:

	Restricted Stock	LTIP Units	Weighted Average Grant Fair Value
Unvested balance at December 31, 2017	90,791	3,588,609	$ 11.20
Vested	(30,693)	(492,877)	14.58
Granted	39,608	2,719,801	8.54
Forfeited or unearned	(7,811)	(103,490)	8.52
Unvested balance at September 30, 2018	91,895	5,712,043	$ 9.68

The LTIP unit and restricted stock awards will immediately vest upon the later of (i) the date the grantee attains the age of 60 and (ii) the date on which grantee has first completed ten years of continuous service with our company or its affiliates. For award agreements that qualify, we recognize noncash compensation expense on the grant date for the time-based awards and ratably over the vesting period for the performance-based awards, and accordingly, we recognized $0.4 million and $1.7 million for the three and nine months ended September 30, 2018, respectively, and $0.2 million and $0.9 million for the three and nine months ended September 30, 2017, respectively. Unrecognized compensation expense was $1.2 million at September 30, 2018, which will be recognized over a weighted average period of 2.2 years.

For the remainder of the LTIP unit and restricted stock awards, we recognize noncash compensation expense ratably over the vesting period, and accordingly, we recognized noncash compensation expense of $4.5 million and $12.4 million for the three and nine months ended September 30, 2018, respectively, and $3.7 million and $9.9 million for the three and nine months ended September 30, 2017, respectively. Unrecognized compensation expense was $32.0 million at September 30, 2018, which will be recognized over a weighted average period of 2.3 years.

Earnings Per Share

Earnings per share for the three and nine months ended September 30, 2018 and 2017 is computed as follows (amounts in thousands, except per share amounts):

	Three Months Ended,		Nine Months Ended,	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Numerator - Basic:				
Net income	$29,230	$ 35,489	$77,472	$ 85,993
Private perpetual preferred unit distributions	(234)	(234)	(702)	(702)
Net income attributable to non-controlling interests	(12,654)	(16,449)	(34,009)	(39,916)
Earnings allocated to unvested shares	(10)	(11)	(26)	(28)
Net income attributable to common stockholders - basic	$16,332	$ 18,795	$42,735	$ 45,347
Numerator - Diluted:				
Net income	$29,230	$ 35,489	$77,472	$ 85,993
Private perpetual preferred unit distributions	(234)	(234)	(702)	(702)
Earnings allocated to unvested shares	(10)	(11)	(26)	(28)
Net income attributable to common stockholders - diluted	$28,986	$ 35,244	$76,744	$ 85,263
Denominator:				
Weighted average shares outstanding - basic	167,657	158,102	165,613	157,796
Operating partnership units	129,821	138,287	131,567	138,593
Effect of dilutive securities:				
Stock-based compensation plans	—	762	1	848
Exchangeable senior notes	—	720	—	852
Weighted average shares outstanding - diluted	297,478	297,871	297,181	298,089
Earnings per share:				
Basic	$0.10	$ 0.12	$0.26	$ 0.29
Diluted	$0.10	$ 0.12	$0.26	$ 0.29

There were 541,947 and 458,698 antidilutive shares and LTIP units for the three and nine months ended September 30, 2018, respectively, and 954,533 and 840,092 antidilutive shares and LTIP units for the three and nine months ended September 30, 2017, respectively.

10. Related Party Transactions

Supervisory Fee Revenue

We earned supervisory fees from entities affiliated with Anthony E. Malkin, our Chairman and Chief Executive Officer, of $0.2 million and $0.3 million for the three months ended September 30, 2018 and 2017, respectively, and $0.9 million and $0.9 million for the nine months ended September 30, 2018 and 2017, respectively. These fees are included within third-party management and other fees.

Property Management Fee Revenue

We earned property management fees from entities affiliated with Anthony E. Malkin of $0.1 million and $0.1 million for the three months ended September 30, 2018 and 2017, respectively, and $0.3 million and $0.2 million for the nine months ended September 30, 2018 and 2017, respectively. These fees are included within third-party management and other fees.

Other

We receive rent generally at market rental rate for 5,351 square feet of leased space from entities affiliated with Anthony E. Malkin at one of our properties. Under the lease, the tenant has the right to cancel such lease without special payment on 90 days' notice. We also have a shared use agreement with such tenant, to occupy a portion of the leased premises as the office location for Peter L. Malkin, our chairman emeritus and employee, utilizing approximately 15% of the space, for which we pay an allocable pro rata share of the cost to such tenant. We also have agreements with these entities to provide them with general computer-related support. Total revenue aggregated $0.1 million and $0.1 million for the three months ended September 30, 2018 and 2017, respectively, and $0.3 million and $0.3 million for the nine months ended September 30, 2018 and 2017, respectively.

One of our directors, James D. Robinson IV, is a general partner in an investment fund, which owns more than a 10% economic and voting interest in one of our tenants, OnDeck Capital, with an annualized rent of $4.1 million as of September 30, 2018.

11. Segment Reporting

We have identified two reportable segments: (1) real estate and (2) observatory. Our real estate segment includes all activities related to the ownership, management, operation, acquisition, redevelopment, repositioning and disposition of our real estate assets. Our observatory segment includes the operation of the 86th and 102nd floor observatories at the Empire State Building. These two lines of businesses are managed separately because each business requires different support infrastructures, provides different services and has dissimilar economic characteristics such as investments needed, stream of revenues and marketing strategies. We account for intersegment sales and rent as if the sales or rent were to third parties, that is, at current market prices.

The following tables provide components of segment profit for each segment for the three and nine months ended September 30, 2018 and 2017 (amounts in thousands):

	Three Months Ended September 30, 2018			
	Real Estate	Observatory	Intersegment Elimination	Total
Revenues:				
Rental revenue	$123,621	$—	$ —	$123,621
Intercompany rental revenue	23,805	—	(23,805)	—
Tenant expense reimbursement	18,627	—	—	18,627
Observatory revenue	—	40,241	—	40,241
Lease termination fees	1,185	—	—	1,185
Third-party management and other fees	312	—	—	312
Other revenue and fees	2,416	—	—	2,416
Total revenues	169,966	40,241	(23,805)	186,402
Operating expenses:				
Property operating expenses	42,772	—	—	42,772
Intercompany rent expense	—	23,805	(23,805)	—
Ground rent expense	2,331	—	—	2,331
General and administrative expenses	13,148	—	—	13,148
Observatory expenses	—	8,854	—	8,854
Real estate taxes	28,284	—	—	28,284
Depreciation and amortization	42,458	17	—	42,475
Total operating expenses	128,993	32,676	(23,805)	137,864
Total operating income	40,973	7,565	—	48,538
Other income (expense):				
Interest income	3,485	—	—	3,485
Interest expense	(20,658)	—	—	(20,658)
Income before income taxes	23,800	7,565	—	31,365
Income tax expense	(277)	(1,858)	—	(2,135)
Net income	$23,523	$5,707	$ —	$29,230
Segment assets	$3,904,454	$262,378	$ —	$4,166,832
Expenditures for segment assets	$52,613	$14,507	$ —	$67,120

	Three Months Ended September 30, 2017			
	Real Estate	Observatory	Intersegment Elimination	Total
Revenues:				
Rental revenue	$122,391	$—	$ —	$122,391
Intercompany rental revenue	23,301	—	(23,301)	—
Tenant expense reimbursement	20,346	—	—	20,346
Observatory revenue	—	39,306	—	39,306
Lease termination fees	1,165	—	—	1,165
Third-party management and other fees	345	—	—	345
Other revenue and fees	2,993	—	—	2,993
Total revenues	170,541	39,306	(23,301)	186,546
Operating expenses:				
Property operating expenses	41,270	—	—	41,270
Intercompany rent expense	—	23,301	(23,301)	—
Ground rent expense	2,331	—	—	2,331
General and administrative expenses	12,899	—	—	12,899
Observatory expenses	—	8,648	—	8,648
Real estate taxes	26,901	—	—	26,901
Depreciation and amortization	38,473	17	—	38,490
Total operating expenses	121,874	31,966	(23,301)	130,539
Total operating income	48,667	7,340	—	56,007
Other income (expense):				
Interest income	774	—	—	774
Interest expense	(16,890)	—	—	(16,890)
Loss on early extinguishment of debt	(2,157)	—	—	(2,157)
Income before income taxes	30,394	7,340	—	37,734
Income tax expense	(264)	(1,981)	—	(2,245)
Net income	$30,130	$5,359	$ —	$35,489
Segment assets	$3,582,935	$265,999	$ —	$3,848,934
Expenditures for segment assets	$40,320	$13,411	$ —	$53,731

	Nine Months Ended September 30, 2018			
	Real Estate	Observatory	Intersegment Elimination	Total
Revenues:				
Rental revenue	$369,970	$ —	$ —	$369,970
Intercompany rental revenue	59,356	—	(59,356)	—
Tenant expense reimbursement	52,626	—	—	52,626
Observatory revenue	—	96,691	—	96,691
Lease termination fees	2,164	—	—	2,164
Third-party management and other fees	1,151	—	—	1,151
Other revenue and fees	9,600	—	—	9,600
Total revenues	494,867	96,691	(59,356)	532,202
Operating expenses:				
Property operating expenses	126,375	—	—	126,375
Intercompany rent expense	—	59,356	(59,356)	—
Ground rent expense	6,994	—	—	6,994
General and administrative expenses	39,001	—	—	39,001
Observatory expenses	—	23,868	—	23,868
Real estate taxes	81,771	—	—	81,771
Depreciation and amortization	121,775	51	—	121,826
Total operating expenses	375,916	83,275	(59,356)	399,835
Total operating income	118,951	13,416	—	132,367
Other income (expense):				
Interest income	7,209	—	—	7,209
Interest expense	(58,774)	—	—	(58,774)
Income before income taxes	67,386	13,416	—	80,802
Income tax expense	(852)	(2,478)	—	(3,330)
Net income	$66,534	$ 10,938	$ —	$77,472
Expenditures for segment assets	$148,429	$ 41,930	$ —	$190,359

	Nine Months Ended September 30, 2017			
	Real Estate	Observatory	Intersegment Elimination	Total
Revenues:				
Rental revenue	$360,348	$ —	$ —	$360,348
Intercompany rental revenue	57,354	—	(57,354)	—
Tenant expense reimbursement	53,889	—	—	53,889
Observatory revenue	—	94,212	—	94,212
Lease termination fees	10,354	—	—	10,354
Third-party management and other fees	1,088	—	—	1,088
Other revenue and fees	7,338	—	—	7,338
Total revenues	490,371	94,212	(57,354)	527,229
Operating expenses:				
Property operating expenses	122,009	—	—	122,009
Intercompany rent expense	—	57,354	(57,354)	—
Ground rent expense	6,994	—	—	6,994
General and administrative expenses	36,566	—	—	36,566
Observatory expenses	—	23,079	—	23,079
Real estate taxes	76,001	—	—	76,001
Depreciation and amortization	119,764	104	—	119,868
Total operating expenses	361,334	80,537	(57,354)	384,517
Total operating income	129,037	13,675	—	142,712
Other income (expense):				
Interest income	2,169	—	—	2,169
Interest expense	(52,109)	—	—	(52,109)
Loss on early extinguishment of debt	(2,157)	—	—	(2,157)
Loss from derivative financial instruments	(289)	—	—	(289)
Income before income taxes	76,651	13,675	—	90,326
Income tax expense	(960)	(3,373)	—	(4,333)
Net income	$75,691	$ 10,302	$ —	$85,993
Expenditures for segment assets	$142,854	$ 20,261	$ —	$163,115

12. Subsequent Events

None.

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

Unless the context otherwise requires or indicates, references in this section to "we," "our," and "us" refer to our company and its consolidated subsidiaries. The following discussion related to our consolidated financial statements should be read in conjunction with the financial statements and the notes thereto appearing elsewhere in this Quarterly Report on Form 10-Q and in our Annual Report on Form 10-K for the year ended December 31, 2017.

FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). We intend these forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995 and are including this statement for purposes of complying with those safe harbor provisions. You can identify forward-looking statements by the use of forward-looking terminology such as "believes," "expects," "may," "will," "should," "seeks," "approximately," "intends," "plans," "estimates," "contemplates," "aims," "continues," "would" or "anticipates" or the these words and phrases or similar words or phrases. In particular, statements pertaining to our capital resources, portfolio performance, dividend policy and results of operations contain forward-looking statements. Likewise, all of our statements regarding anticipated growth in our portfolio from operations, acquisitions and anticipated market conditions, demographics and results of operations are forward-looking statements.

Forward-looking statements are subject to substantial risks and uncertainties, many of which are difficult to predict and are generally beyond our control, and you should not rely on them as predictions of future events. Forward-looking statements depend on assumptions, data or methods which may be incorrect or imprecise, and we may not be able to realize them. We do not guarantee that the transactions and events described will happen as described (or that they will happen at all).

The following factors, among others, could cause actual results and future events to differ materially from those set forth or contemplated in the forward-looking statements:

- changes in our industry, the real estate markets, either nationally or in Manhattan or the greater New York metropolitan area;
- reduced demand for office or retail space;
- decreased rental rates or increased vacancy rates;
- defaults on, early terminations of, or non-renewal of leases by tenants;
- insolvency of a major tenant or a significant number of smaller tenants;
- our failure to redevelop and reposition properties, or to execute any planned capital project, successfully or on the anticipated timeline or at the anticipated costs;
- difficulties in identifying properties to acquire and completing acquisitions;
- risks of real estate development and capital projects, including construction delays and cost overruns;
- inability to manage our properties and our growth effectively;
- declining real estate valuations and impairment charges;
- termination or expiration of our ground leases;
- changes in real estate and zoning laws and increases in real property tax rates;
- increased operating costs;
- misunderstanding of our competition;
- new office or observatory development in our market;
- fluctuations in attendance at the observatory;
- changes in domestic or international tourism, including geopolitical events and currency exchange rates;
- changes in technology and market competition, which affect utilization of our broadcast or other facilities;

- changes in our business strategy;
- resolution of legal proceedings involving the company;
- general volatility of the capital and credit markets and the market price of our Class A common stock and our publicly-traded OP Units;
- availability, terms and deployment of capital;
- our leverage;
- fluctuations in interest rates;
- inability to continue to raise additional debt or equity financing on attractive terms, or at all;
- our failure to generate sufficient cash flows to service our outstanding indebtedness;

- inability to make distributions to our securityholders in the future;
- impact of changes in governmental regulations, tax law and rates and similar matters;
- failure to continue to qualify as a real estate investment trust, or REIT;
- lack, or insufficient amounts, of insurance;
- a future terrorist event in the U.S.;
- environmental uncertainties and risks related to climate change, rising sea levels, adverse weather conditions and natural disasters;
- inability to comply with applicable laws, rules and regulations;
- damages resulting from security breaches through cyberattacks, cyber intrusions or otherwise, as well as other significant disruptions of our technology (IT) networks related systems; and
- other factors discussed under “Item 1A, Risk Factors” of our Annual Report on Form 10-K for the year ended December 31, 2017 and additional factors that may be contained in any filing we make with the SEC, including Part II, Item 1A of our Quarterly Reports on Form 10-Q.

While forward-looking statements reflect our good faith beliefs, they are not guarantees of future performance. We disclaim any obligation to publicly update or revise any forward-looking statement to reflect changes in underlying assumptions or factors, of new information, data or methods, future events or other changes after the date of this Quarterly Report on Form 10-Q, except as required by applicable law. The risks set forth above are not exhaustive. For a further discussion of these and other factors that could impact our future results, performance or transactions, see the sections entitled “Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2017 which we filed with the SEC. You should not place undue reliance on any forward-looking statements, which are based only on information currently available to us.

Overview

We are a self-administered and self-managed real estate investment trust ("REIT") that owns, manages, operates, acquires and repositions office and retail properties in Manhattan and the greater New York metropolitan area.

Highlights for the three months ended September 30, 2018 included:

- Achieved net income attributable to the Company of $16.3 million and Core Funds From Operations of $73.0 million.
- Occupancy and leased percentages at September 30, 2018:
- Total portfolio was 88.4% occupied; including signed leases not commenced (“SLNC”), the total portfolio was 92.1% leased.
- Manhattan office portfolio (excluding the retail component of these properties) was 88.3% occupied; including SLNC, the Manhattan office portfolio was 93.0% leased.
- Retail portfolio was 90.8% occupied; including SLNC, the retail portfolio was 90.8% leased.
- Empire State Building was 94.0% occupied; including SLNC, was 94.3% leased.
- Signed 43 leases, representing 354,099 rentable square feet across the total portfolio, and achieved a 24.1% increase in mark-to-market rent over previous fully escalated rents portfolio-wide on new, renewal, and expansion leases.
- Signed 24 new leases representing 281,844 rentable square feet for the Manhattan office portfolio (excluding the retail component of these properties), and achieved an increase of 27.3% in mark-to-market rent over previous fully escalated rents.
- Opened the new Observatory entrance on August 22, 2018, which is the first phase of the fully reimagined Observatory visitor experience.
- Increased Empire State Building Observatory revenue for the third quarter 2018 by 2.4% to $40.2 million from $39.3 million in the third quarter 2017.
- Authorized a $500 million stock and publicly traded operating partnership unit repurchase program through December 31, 2019.
- Declared a dividend of $0.105 per share.

As of September 30, 2018, our total portfolio contained 10.1 million rentable square feet of office and retail space. We owned 14 office properties (including three long-term ground leasehold interests) encompassing approximately 9.4 million rentable square feet of office space. Nine of these properties are located in the midtown Manhattan market and aggregate approximately 7.6 million rentable square feet of office space, including the Empire State Building. Our Manhattan office properties also contain an aggregate of 513,437 rentable square feet of premier retail space on their ground floor and/or contiguous levels. Our remaining five office properties are located in Fairfield County, Connecticut and Westchester County, New York, encompassing in the aggregate approximately 1.9 million rentable square feet. The majority of square footage for these five properties is located in densely populated metropolitan communities with immediate access to mass transportation. Additionally, we have entitled land at the Stamford Transportation Center in Stamford, Connecticut, adjacent to one of our office properties, that will support the development of an approximately 380,000 rentable square foot office building and garage. As of September 30, 2018, our portfolio included four standalone retail properties located in Manhattan and two standalone retail properties located in the city center of Westport, Connecticut, encompassing 205,748 rentable square feet in the aggregate.

The Empire State Building is our flagship property. The Empire State Building provides us with a diverse source of revenue through its office and retail leases, observatory operations and broadcasting licenses and related leased space. Our observatory operations are a separate reporting segment. Our observatory operations are subject to regular patterns of tourist activity in Manhattan. During the past ten years, approximately 16.0% to 18.0% of our annual observatory revenue was realized in the first quarter, 26.0% to 28.0% was realized in the second quarter, 31.0% to 33.0% was realized in the third quarter, and 23.0% to 25.0% was realized in the fourth quarter.

The components of the Empire State Building revenue are as follows (dollars in thousands):

	Nine Months Ended September 30,					
	2018			2017		
Office leases	$98,597	40.9	%	$94,320	40.5	%
Retail leases	5,549	2.3	%	5,554	2.4	%
Tenant reimbursements & other income	21,660	9.0	%	19,354	8.3	%
Observatory operations	96,691	40.1	%	94,212	40.4	%
Broadcasting licenses and leases	18,501	7.7	%	19,654	8.4	%
Total	$240,998	100.0	%	$233,094	100.0	%

We have been undertaking a comprehensive redevelopment and repositioning strategy of our Manhattan office properties. This strategy is designed to improve the overall value and attractiveness of our properties and has contributed significantly to our tenant repositioning efforts, which seek to increase our occupancy; raise our rental rates; increase our rentable square feet; increase our aggregate rental revenue; lengthen our average lease term; increase our average lease size; and improve our tenant credit quality. These improvements include restored, renovated and upgraded or new lobbies; elevator modernization; renovated public areas and bathrooms; refurbished or new windows; upgrade and standardization of retail storefront and signage; façade restorations; modernization of building-wide systems; and enhanced tenant amenities. We have also aggregated smaller spaces in order to offer larger blocks of office space, including multiple floors, that are attractive to larger, higher credit-quality tenants and to offer new, pre-built suites with improved layouts. This strategy has shown what we believe to be attractive results to date, and we believe has the potential to improve our operating margins and cash flows in the future. We believe we will continue to enhance our tenant base and improve rents as our pre-redevelopment leases continue to expire and be re-leased. From 2002 through September 30, 2018, we have invested a total of approximately $854.5 million (excluding tenant improvement costs and leasing commissions) in our Manhattan office properties pursuant to this program. We intend to fund these capital improvements through a combination of operating cash flow, cash on hand, and borrowings.

During the second quarter 2017, we commenced a multi-year capital project at the Empire State Building which we believe will improve convenience for office tenants and their visitors, increase the value of our 34th Street facing retail space, enhance the Observatory visitor experience, and increase Observatory revenue per capita.

In the first phase, we relocated the present Observatory entrance, previously located on Fifth Avenue, to a new, larger, dedicated entrance for Observatory visitors at the western side of the Empire State Building on 34th Street. The new entrance eliminates Observatory visitor flow into the Fifth Avenue lobby and streamline such visitor exit from that lobby, thereby reducing Observatory traffic in such lobby by more than 50% and improving Fifth Avenue access for our office tenants and their visitors. We believe the resulting new traffic pattern will increase the value of all of our 34th Street facing retail space and enhance office and Observatory convenience.

We anticipate that we will invest approximately $160 million in total over three years to complete all phases of this project. Expenditures, which began during the second quarter 2017, were $78.5 million through September 30, 2018. This investment is an outcome of continually looking at ways to innovate and enhance the office and retail tenant and visitor experience at the Empire State Building.

The elevator servicing the 102nd floor observatory was closed to visitors during the first quarter of 2018 for planned replacement of the machinery and a new glass cab for the elevator which serves it. We have more work to do on the 102nd floor component of our Observatory upgrade program and we anticipate that we will close the 102nd floor in early 2019 for as long as nine months. Revenue for the 102nd floor observatory was $11.4 million in 2017.

The Greater New York Metropolitan Area office market is soft, and we compete with properties that have been redeveloped recently or have planned redevelopment. We expect to spend approximately $40 million over 2018 through 2020 on these well-maintained and well-located properties' common areas and amenities to ensure competitiveness and protect our market position. Expenditures, which began during the second quarter 2018, were $6.1 million through September 30, 2018.

As of September 30, 2018, excluding principal amortization, we have approximately $250.0 million of debt maturing in 2019, and we had total debt outstanding of approximately $1.9 billion, with a weighted average interest rate of 3.84% (excluding discount), a weighted average maturity of 8.3 years and 100.0% of which is fixed-rate indebtedness. As of September 30, 2018, we had cash and cash equivalents and short-term investments of $629.7 million. Our consolidated net debt to total market capitalization was approximately 20.4% as of September 30, 2018.

Results of Operations

Overview

The discussion below relates to our financial condition and results of operations for the three and nine months ended September 30, 2018 and 2017, respectively.

Three Months Ended September 30, 2018 Compared to the Three Months Ended September 30, 2017

The following table summarizes our historical results of operations for the three months ended September 30, 2018 and 2017 (dollars in thousands):

	Three Months Ended September 30,			
	2018	2017	Change	%
Revenues:				
Rental revenue	$123,621	$122,391	$1,230	1.0 %
Tenant expense reimbursement	18,627	20,346	(1,719)	(8.4)%
Observatory revenue	40,241	39,306	935	2.4 %
Lease termination fees	1,185	1,165	20	1.7 %
Third-party management and other fees	312	345	(33)	(9.6)%
Other revenues and fees	2,416	2,993	(577)	(19.3)%
Total revenues	186,402	186,546	(144)	(0.1)%
Operating expenses:				
Property operating expenses	42,772	41,270	(1,502)	(3.6)%
Ground rent expenses	2,331	2,331	—	— %
General and administrative expenses	13,148	12,899	(249)	(1.9)%
Observatory expenses	8,854	8,648	(206)	(2.4)%
Real estate taxes	28,284	26,901	(1,383)	(5.1)%
Depreciation and amortization	42,475	38,490	(3,985)	(10.4)%
Total operating expenses	137,864	130,539	(7,325)	(5.6)%
Operating income	48,538	56,007	(7,469)	(13.3)%
Other income (expense):			—	
Interest income	3,485	774	2,711	350.3 %
Interest expense	(20,658)	(16,890)	(3,768)	(22.3)%
Loss on early extinguishment of debt	—	(2,157)	2,157	100.0 %
Income before income taxes	31,365	37,734	(6,369)	(16.9)%
Income tax expense	(2,135)	(2,245)	110	4.9 %
Net income	29,230	35,489	(6,259)	(17.6)%
Private perpetual preferred unit distributions	(234)	(234)	—	— %
Net income attributable to non-controlling interests	(12,654)	(16,449)	3,795	23.1 %
Net income attributable to common stockholders	$16,342	$18,806	$(2,464)	(13.1)%

Rental Revenue

The increase in rental income was primarily attributable to increased rental rates.

Tenant Expense Reimbursement

The decrease in tenant expense reimbursements was due to a reduction in broadcasting expense reimbursements.

Observatory Revenue

Observatory revenues were higher primarily due to an improvement in our ticket mix and higher per person average ticket price.

Lease Termination Fees

Lease termination fees were consistent with 2017.

Third-Party Management and Other Fees

Third-party management fees were consistent with 2017.

Other Revenues and Fees
The decrease in other revenues and fees is primarily attributable to a real estate tax refund received in the third quarter 2017.
Property Operating Expenses
The increase in property operating expenses was primarily due to increased utility costs and higher labor costs.
Ground Rent Expenses
Ground rent expense was consistent with 2017.
General and Administrative Expenses
The increase in general and administrative expenses was primarily due to increased equity compensation expense.
Observatory Expenses
Observatory expenses increased primarily due to higher consulting fees and higher marketing costs.
Real Estate Taxes
The increase in real estate taxes was primarily due to higher assessed values for multiple properties.

Depreciation and Amortization

The increase in depreciation and amortization was attributable to the accelerated depreciation of retired assets including those relating to a tenant relocation as well as to additional depreciation on assets newly placed in service during the quarter.
Interest Income
Interest income increased primarily due to higher interest rates on cash balances.
Interest Expense
Interest expense increased due to higher outstanding principal balances.

Loss on Early Extinguishment of Debt

There was no loss on early extinguishment of debt in the three months ended September 30, 2018.
Income Taxes
The decrease in income tax expense was attributable to lower federal tax rates.

Nine Months Ended September 30, 2018 Compared to the Nine Months Ended September 30, 2017

The following table summarizes our historical results of operations for the nine months ended September 30, 2018 and 2017 (dollars in thousands):

	Nine Months Ended September 30,			
	2018	2017	Change	%
Revenues:				
Rental revenue	$369,970	$360,348	$9,622	2.7 %
Tenant expense reimbursement	52,626	53,889	(1,263)	(2.3)%
Observatory revenue	96,691	94,212	2,479	2.6 %
Lease termination fees	2,164	10,354	(8,190)	(79.1)%
Third-party management and other fees	1,151	1,088	63	5.8 %
Other revenues and fees	9,600	7,338	2,262	30.8 %
Total revenues	532,202	527,229	4,973	0.9 %
Operating expenses:				
Property operating expenses	126,375	122,009	(4,366)	(3.6)%
Ground rent expenses	6,994	6,994	—	— %
General and administrative expenses	39,001	36,566	(2,435)	(6.7)%
Observatory expenses	23,868	23,079	(789)	(3.4)%
Real estate taxes	81,771	76,001	(5,770)	(7.6)%
Depreciation and amortization	121,826	119,868	(1,958)	(1.6)%
Total operating expenses	399,835	384,517	(15,318)	(4.0)%
Operating income	132,367	142,712	(10,345)	(7.2)%
Other income (expense):				
Interest income	7,209	2,169	5,040	232.4 %
Interest expense	(58,774)	(52,109)	(6,665)	(12.8)%
Loss on early extinguishment of debt	—	(2,157)	2,157	100.0 %
Loss from derivative financial instruments	—	(289)	289	100.0 %
Income before income taxes	80,802	90,326	(9,524)	(10.5)%
Income tax expense	(3,330)	(4,333)	1,003	23.1 %
Net income	77,472	85,993	(8,521)	(9.9)%
Private perpetual preferred unit distributions	(702)	(702)	—	— %
Net income attributable to non-controlling interests	(34,009)	(39,916)	5,907	14.8 %
Net income attributable to common stockholders	$42,761	$45,375	$(2,614)	(5.8)%

Rental Revenue

The increase in rental income was primarily attributable to increased rental rates.

Tenant Expense Reimbursement

The decrease in tenant expense reimbursements was due to a reduction in broadcasting expense reimbursements.

Observatory Revenue

Observatory revenues were higher primarily due to an improvement in our ticket mix and higher per person average ticket price, partially offset by the scheduled closure of the 102nd floor observation deck in the first quarter 2018 for replacement of original elevator machinery.

Lease Termination Fees

The nine months ended September 30, 2017 included significantly higher lease termination fees, whereas the nine months ended September 30, 2018 had reduced lease termination fees.

34

Third-Party Management and Other Fees

Third-party management fees were consistent with 2017.

Other Revenues and Fees

The increase in other revenues and fees for the nine months ended September 30, 2018 was primarily due to a $2.8 million settlement with a former broadcast tenant.

Property Operating Expenses

The increase in property operating expenses was primarily due to higher repairs and maintenance costs and higher labor costs.

Ground Rent Expenses

Ground rent expense was consistent with 2017.

General and Administrative Expenses

The increase in general and administrative expenses was primarily due to increased equity compensation expense.

Observatory Expenses

Observatory expenses increased primarily due to higher payroll and marketing costs.

Real Estate Taxes

The increase in real estate taxes was primarily due to higher assessed values for multiple properties.

Depreciation and Amortization

The increase in depreciation and amortization was primarily due to depreciation of assets newly placed in service together with the accelerated depreciation of retired assets, partially offset by lower amortization of purchase accounting deferred leasing costs associated with 2013 and 2014 acquisitions as these costs become fully amortized.

Interest Income

Interest income increased primarily due to higher interest rates on cash balances.

Interest Expense

Interest expense increased due to higher outstanding principal balances.

Loss on Early Extinguishment of Debt

There was no loss on early extinguishment of debt in the nine months ended September 30, 2018.

Loss from Derivative Financial Instruments

There were no interest rate swaps or cash flow hedges terminated during the nine months ended September 30, 2018.

Income Taxes

The decrease in income tax expense was attributable to lower federal tax rates.

Liquidity and Capital Resources

Liquidity is a measure of our ability to meet potential cash requirements, including ongoing commitments to repay borrowings, fund and maintain our assets and operations, including lease-up costs, fund our redevelopment and repositioning programs, acquire properties, make distributions to our securityholders and fulfill other general business needs. Based on the historical experience of our management and our business strategy, in the foreseeable future we anticipate we will generate positive cash flows from operations. In order to qualify as a REIT, we are required under the Internal Revenue Code of 1986 to distribute to our stockholders, on an annual basis, at least 90% of our REIT taxable income, determined without regard to the deduction for dividends paid and excluding net capital gains. We expect to make quarterly distributions to our securityholders.

While we may be able to anticipate and plan for certain liquidity needs, there may be unexpected increases in uses of cash that are beyond our control and which would affect our financial condition and results of operations. For example, we may be required to comply with new laws or regulations that cause us to incur unanticipated capital expenditures for our properties, thereby increasing our liquidity needs. Even if there are no material changes to our anticipated liquidity requirements, our sources of liquidity may be fewer than, and the funds available from such sources may be less than, anticipated or needed. Our primary sources of liquidity will generally consist of cash on hand and cash generated from our operating activities, debt issuances and unused borrowing capacity under our unsecured revolving credit facility. We expect to meet our short-term liquidity requirements, including distributions, operating expenses, working capital, debt service, and capital expenditures from cash flows from operations, cash on hand, debt issuances, and available borrowing capacity under our unsecured revolving credit facility. The availability of these borrowings is subject to the conditions set forth in the applicable loan agreements. We expect to meet our long-term capital requirements, including acquisitions, redevelopments and capital expenditures through our cash flows from operations, cash on hand, our unsecured revolving credit facility, mortgage financings, debt issuances, common and/or preferred equity issuances and asset sales. Our properties require periodic investments of capital for individual lease related tenant improvements allowances, general capital improvements and costs associated with capital expenditures. Our overall leverage will depend on our mix of investments and the cost of leverage. Our charter does not restrict the amount of leverage that we may use.

At September 30, 2018, we had approximately $629.7 million available in cash and cash equivalents and short-term investments and there was $1.1 billion available under our unsecured revolving credit facility.

Through August 2021, Q REIT Holding LLC, a Qatar Financial Centre limited liability company and a wholly owned subsidiary of the Qatar Investment Authority, a governmental authority of the State of Qatar (“QREIT”, together with any eligible transferee, “QIA”) will have a right of first offer to co-invest with us as a joint venture partner in real estate investment opportunities initiated by us where we have elected, at our discretion, to seek out a joint venture partner. The right of first offer period will be extended for 30 months so long as at least one joint venture transaction is consummated by us and QIA during the initial term, and will be extended for a further 30-month term if at least one more joint venture transaction is
consummated during such initial extension period.

As of September 30, 2018, we had approximately $1.9 billion of total consolidated indebtedness outstanding, with a weighted average interest rate of 3.84% (excluding discounts) and a weighted average maturity of 8.3 years. As of September 30, 2018, exclusive of principal amortization, we have approximately $250.0 million of debt maturing in 2019. Our consolidated net debt to total market capitalization was approximately 20.4% as of September 30, 2018.

During January 2018, we refinanced and increased our mortgage debt on 1333 Broadway from $66.6 million to $160.0 million, due February 2033 with interest fixed at 4.21%. A portion of this increase was applied to release the $75.8 million mortgage lien on 1400 Broadway.

During December 2017, we entered into an agreement to issue and sell an aggregate principal amount of $450 million of our senior unsecured notes in a private placement, of which $115 million was sold and purchased in December 2017 and $335 million was sold and purchased in March 2018. We used the net proceeds from the March 2018 issuance to repay our mortgage indebtedness on 111 West 33rd Street and 1350 Broadway, before their maturity dates in early April 2018 and to add to cash balances.

Unsecured Revolving Credit and Term Loan Facility

During August 2017, through the Operating Partnership, we entered into an amended and restated senior unsecured revolving credit and term loan facility. This unsecured revolving credit and term loan facility is comprised of a $1.1 billion revolving credit facility and a $265 million term loan facility. The unsecured revolving credit and term loan facility contains

an accordion feature that would allow us to increase the maximum aggregate principal amount to $1.75 billion under specified circumstances.

The initial maturity of the unsecured revolving credit facility is August 2021. We have the option to extend the initial term for up to two additional six-month periods, subject to certain conditions, including the payment of an extension fee equal to 0.0625% and 0.075% of the then outstanding commitments under the unsecured revolving credit facility on the first and the second extensions, respectively. The term loan facility matures on August 2022.

The unsecured revolving credit facility includes the following financial covenants: (i) maximum leverage ratio of total indebtedness to total asset value (as defined in the agreement) of the loan parties and their consolidated subsidiaries will not exceed 60%, (ii) consolidated secured indebtedness will not exceed 40% of total asset value, (iii) tangible net worth will not be less than $1.2 billion plus 75% of net equity proceeds received by the Operating Partnership (other than proceeds received within ninety days after the redemption, retirement or repurchase of ownership or equity interests in the Operating Partnership up to the amount paid by the Operating Partnership in connection with such redemption, retirement or repurchase, where, the net effect is that the Operating Partnership shall not have increased its net worth as a result of any such proceeds), (iv) adjusted EBITDA (as defined in the unsecured revolving credit facility) to consolidated fixed charges will not be less than 1.50x, (v) the aggregate net operating income with respect to all unencumbered eligible properties to the portion of interest expense attributable to unsecured indebtedness will not be less than 1.75x, and (vi) the ratio of total unsecured indebtedness to unencumbered asset value will not exceed 60%.

As of September 30, 2018, we were in compliance with the covenants (dollars in thousands):

Financial covenant	Required	September 30, 2018	In Compliance
Maximum total leverage	< 60%	29.0 %	Yes
Maximum secured debt	< 40%	9.2 %	Yes
Minimum fixed charge coverage	> 1.50x	3.9x	Yes
Minimum unencumbered interest coverage	> 1.75x	5.1x	Yes
Maximum unsecured leverage	< 60%	25.8 %	Yes
Minimum tangible net worth	$1,252,954	$1,777,443	Yes

The unsecured revolving credit facility contains customary covenants, including limitations on liens, investment, distributions, debt, fundamental changes, and transactions with affiliates, and requires certain customary financial reports.

The unsecured revolving credit facility contains customary events of default (subject in certain cases to specified cure periods), including but not limited to non-payment, breach of covenants, representations or warranties, cross defaults, bankruptcy or other insolvency events, judgments, ERISA events, invalidity of loan documents, loss of real estate investment trust qualification, and occurrence of a change of control (as defined in the agreement for the unsecured credit facility).

Leverage Policies

We expect to employ leverage in our capital structure in amounts determined from time to time by our board of directors. Although our board of directors has not adopted a policy that limits the total amount of indebtedness that we may incur, we anticipate that our board of directors will consider a number of factors in evaluating our level of indebtedness from time to time, as well as the amount of such indebtedness that will be either fixed or floating rate. Our charter and bylaws do not limit the amount or percentage of indebtedness that we may incur nor do they restrict the form in which our indebtedness will be taken (including, but not limited to, recourse or non-recourse debt and cross-collateralized debt). Our overall leverage will depend on our mix of investments and the cost of leverage, however, we initially intend to maintain a level of indebtedness consistent with our plan to seek an investment grade credit rating. Our board of directors may from time to time modify our leverage policies in light of the then-current economic conditions, relative costs of debt and equity capital, market values of our properties, general market conditions for debt and equity securities, fluctuations in the market price of our common stock, growth and acquisition opportunities and other factors.

Capital Expenditures

The following tables summarize our leasing commission costs, tenant improvement costs and our capital expenditures for each of the periods presented (dollars in thousands, except per square foot amounts).

Office Properties[1]

	Nine Months Ended September 30,	
Total New Leases, Expansions, and Renewals	2018	2017
Number of leases signed[2]	117	106
Total square feet	749,598	946,096
Leasing commission costs[3]	$ 13,223	$ 18,931
Tenant improvement costs[3]	48,774	65,884
Total leasing commissions and tenant improvement costs[3]	$ 61,997	$ 84,815
Leasing commission costs per square foot[3]	$ 17.64	$ 20.01
Tenant improvement costs per square foot[3]	65.07	69.64
Total leasing commissions and tenant improvement costs per square foot[3]	$ 82.71	$ 89.65

Retail Properties[4]

	Nine Months Ended September 30,	
Total New Leases, Expansions, and Renewals	2018	2017
Number of leases signed[2]	4	6
Total square feet	7,448	72,616
Leasing commission costs[3]	$198	$3,355
Tenant improvement costs[3]	206	2,021
Total leasing commissions and tenant improvement costs[3]	$404	$5,376
Leasing commission costs per square foot[3]	$26.51	$46.20
Tenant improvement costs per square foot[3]	27.70	27.83
Total leasing commissions and tenant improvement costs per square foot[3]	$54.21	$74.03

(1) Excludes an aggregate of 513,437 and 494,935 rentable square feet of retail space in our Manhattan office properties in 2018 and 2017, respectively. Includes the Empire State Building broadcasting licenses and observatory operations.

(2) Presents a renewed and expansion lease as one lease signed.

(3) Presents all tenant improvement and leasing commission costs as if they were incurred in the period in which the lease was signed, which may be different than the period in which they were actually paid.

(4) Includes an aggregate of 513,437 and 494,935 rentable square feet of retail space in our Manhattan office properties in 2018 and 2017, respectively. Excludes the Empire State Building broadcasting licenses and

observatory operations.

	Nine Months Ended September 30,	
	2018	2017
Total Portfolio		
Capital expenditures [1]	$102,920	$86,682

(1) Excludes tenant improvements and leasing commission costs.

As of September 30, 2018, we expect to incur additional costs relating to obligations under existing lease agreements of approximately $91.5 million for tenant improvements and leasing commissions. We intend to fund the tenant improvements and leasing commission costs through a combination of operating cash flow, cash on hand, additional property level mortgage financings and borrowings under the unsecured revolving credit facility.

Capital expenditures are considered part of both our short-term and long-term liquidity requirements. We intend to fund capital improvements through a combination of operating cash flow, cash on hand and borrowings under the unsecured revolving credit facility.

Contractual Obligations

Refer to our Annual Report on Form 10-K for the year ended December 31, 2017 for a discussion of our contractual obligations. There have been no material changes, outside the ordinary course of business, to these contractual obligations during the nine months ended September 30, 2018.

Off-Balance Sheet Arrangements

As of September 30, 2018, we did not have any off-balance sheet arrangements.

Distribution Policy

In order to qualify as a REIT, we must distribute to our securityholders, on an annual basis, at least 90% of our REIT taxable income, determined without regard to the deduction for dividends paid and excluding net capital gains. In addition, we will be subject to U.S. federal income tax at regular corporate rates to the extent that we distribute less than 100% of our net taxable income (including net capital gains) and will be subject to a 4% nondeductible excise tax on the amount, if any, by which our distributions in any calendar year are less than a minimum amount specified under U.S. federal income tax laws. We intend to distribute our net income to our securityholders in a manner intended to satisfy the REIT 90% distribution requirement and to avoid U.S. federal income tax liability on our income and the 4% nondeductible excise tax.

Before we pay any distribution, whether for U.S. federal income tax purposes or otherwise, we must first meet both our operating requirements and obligations to make payments of principal and interest, if any. However, under some circumstances, we may be required to use cash reserves, incur debt or liquidate assets at rates or times that we regard as unfavorable or make a taxable distribution of our shares in order to satisfy the REIT 90% distribution requirement and to avoid U.S. federal income tax and the 4% nondeductible excise tax in that year.

Distributions to Securityholders

Distributions and dividends amounting to $96.0 million and $95.2 million have been made to securityholders for the nine months ended September 30, 2018 and 2017, respectively.

Stock and Publicly Traded Operating Partnership Unit Repurchase Program

Our Board of Directors authorized the repurchase of up to $500 million of our Class A common stock (“Common Stock”) and Empire State Realty OP, L.P.’s Series ES, Series 250 and Series 60 operating partnership units (NYSE Arca: ESBA, FISK and OGCP, respectively; collectively with the Common Stock, the “Securities”) through December 31, 2019.

Under the program, we may purchase our Securities in accordance with applicable securities laws from time to time in the open market or in privately negotiated transactions. The timing, manner, price and amount of any repurchases will be determined by us at our discretion and will be subject to stock price, availability, trading volume and general market conditions. The authorization does not obligate us to acquire any particular amount of Securities, and the program may be suspended or discontinued at our discretion without prior notice.

Cash Flows

Comparison of Nine Months Ended September 30, 2018 to the Nine Months Ended September 30, 2017

Net cash. Cash and cash equivalents and restricted cash were $284.1 million and $496.1 million, respectively, as of September 30, 2018 and 2017. The decrease was primarily attributable to investments in short-term time deposits and capital improvements and expenditures offset by net proceeds from the issuance of debt during the nine months ended September 30, 2018.

Operating activities. Net cash provided by operating activities increased by $12.6 million, to $187.4 million, for the nine months ended September 30, 2018 compared to $174.8 million for the nine months ended September 30, 2017, primarily due to changes in working capital.

Investing activities. Net cash used in investing activities increased by $412.0 million, to $569.6 million, for the nine months ended September 30, 2018 compared to $157.6 million for the nine months ended September 30, 2017, due to

investments in short-term time deposits made during the second quarter 2018.

Financing activities. Net cash provided by financing activities increased by $273.1 million, to $136.1 million provided by financing activities for the nine months ended September 30, 2018 compared to $137.0 million used in financing activities for the nine months ended September 30, 2017, primarily due to net proceeds on issuance of debt in the nine months ended September 30, 2018.

Net Operating Income ("NOI")

Our internal financial reports include a discussion of property net operating income. NOI is a non-GAAP financial measure of performance. NOI is used by our management to evaluate and compare the performance of our properties and to determine trends in earnings and to compute the fair value of our properties as it is not affected by: (i) the cost of funds of the property owner, (ii) the impact of depreciation and amortization expenses as well as gains or losses from the sale of operating real estate assets that are included in net income computed in accordance with GAAP, (iii) acquisition expenses, loss on early extinguishment of debt and loss from derivative instruments, or (iv) general and administrative expenses and other gains and losses that are specific to the property owner. The cost of funds is eliminated from net operating income because it is specific to the particular financing capabilities and constraints of the owner. The cost of funds is also eliminated because it is dependent on historical interest rates and other costs of capital as well as past decisions made by us regarding the appropriate mix of capital which may have changed or may change in the future. Depreciation and amortization expenses as well as gains or losses from the sale of operating real estate assets are eliminated because they may not accurately represent the actual change in value in our office or retail properties that result from use of the properties or changes in market conditions. While certain aspects of real property do decline in value over time in a manner that is reasonably captured by depreciation and amortization, the value of the properties as a whole have historically increased or decreased as a result of changes in overall economic conditions instead of from actual use of the property or the passage of time. Gains and losses from the sale of real property vary from property to property and are affected by market conditions at the time of sale which will usually change from period to period. These gains and losses can create distortions when comparing one period to another or when comparing our operating results to the operating results of other real estate companies that have not made similarly-timed purchases or sales. We believe that eliminating these costs from net income is useful because the resulting measure captures the actual revenue, generated and actual expenses incurred in operating our properties as well as trends in occupancy rates, rental rates and operating costs.

However, the usefulness of NOI is limited because it excludes general and administrative costs, interest expense, depreciation and amortization expense and gains or losses from the sale of properties, and other gains and losses as stipulated by GAAP, the level of capital expenditures and leasing costs necessary to maintain the operating performance of our properties, all of which are significant economic costs. NOI may fail to capture significant trends in these components of net income which further limits its usefulness.

NOI is a measure of the operating performance of our properties but does not measure our performance as a whole. NOI is therefore not a substitute for net income as computed in accordance with GAAP. This measure should be analyzed in conjunction with net income computed in accordance with GAAP and discussions elsewhere in this Management’s Discussion and Analysis of Financial Condition and Results of Operations regarding the components of net income that are eliminated in the calculation of NOI. Other companies may use different methods for calculating NOI or similarly titled measures and, accordingly, our NOI may not be comparable to similarly titled measures reported by other companies that do not define the measure exactly as we do.

The following table presents a reconciliation of our net income, the most directly comparable GAAP measure, to NOI for the periods presented (amounts in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
	(unaudited)		(unaudited)	
Net income	$29,230	$35,489	$77,472	$85,993
Add:				
General and administrative expenses	13,148	12,899	39,001	36,566
Depreciation and amortization	42,475	38,490	121,826	119,868
Interest expense	20,658	16,890	58,774	52,109
Loss on early extinguishment of debt	—	2,157	—	2,157
Loss from derivative financial instruments	—	—	—	289
Income tax expense	2,135	2,245	3,330	4,333
Less:				
Third-party management and other fees	(312)	(345)	(1,151)	(1,088)
Interest income	(3,485)	(774)	(7,209)	(2,169)
Net operating income	$103,849	$107,051	$292,043	$298,058
Other Net Operating Income Data				
Straight-line rental revenue	$5,000	$6,861	$16,662	$20,581
Net increase in rental revenue from the amortization of above- and below-market lease assets and liabilities	$1,668	$1,607	$4,387	$4,154
Amortization of acquired below-market ground leases	$1,957	$1,957	$5,873	$5,873

Funds from Operations ("FFO")

We present below a discussion of FFO. We compute FFO in accordance with the “White Paper” on FFO published by the National Association of Real Estate Investment Trusts, or NAREIT, which defines FFO as net income (loss) (determined in accordance with GAAP), excluding impairment write-downs of investments in depreciable real estate and investments in in-substance real estate investments, gains or losses from debt restructurings and sales of depreciable operating properties, plus real estate-related depreciation and amortization (excluding amortization of deferred financing costs), less distributions to non-controlling interests and gains/losses from discontinued operations and after adjustments for unconsolidated partnerships and joint ventures. FFO is a widely recognized non-GAAP financial measure for REITs that we believe, when considered with financial statements determined in accordance with GAAP, is useful to investors in understanding financial performance and providing a relevant basis for comparison among REITs. In addition, FFO is useful to investors as it captures features particular to real estate performance by recognizing that real estate has generally appreciated over time or maintains residual value to a much greater extent than do other depreciable assets. Investors should review FFO, along with GAAP net income, when trying to understand an equity REIT’s operating performance. We present FFO because we consider it an important supplemental measure of our operating performance and believe that it is frequently used by securities analysts, investors and other interested parties in the evaluation of REITs. However, because FFO excludes depreciation and amortization and captures neither the changes in the value of our properties that result from use or market conditions nor the level of capital expenditures and leasing commissions necessary to maintain the operating performance of our properties, all of which have real economic effect and could materially impact our results of operations, the utility of FFO as a measure of performance is limited. There can be no assurance that FFO presented by us is comparable to similarly titled measures of other REITs. FFO does not represent cash generated from operating activities and should not be considered as an alternative to net income (loss) determined in accordance with GAAP or to cash flow from operating activities determined in accordance with GAAP. FFO is not indicative of cash available to fund ongoing cash needs, including the ability to make cash distributions. Although FFO is a measure used for comparability in assessing the performance of REITs, as the NAREIT White Paper only provides guidelines for computing FFO, the

computation of FFO may vary from one company to another.

Modified Funds From Operations ("Modified FFO")

Modified FFO adds back an adjustment for any above or below-market ground lease amortization to traditionally defined FFO. We consider this a useful supplemental measure in evaluating our operating performance due to the non-cash accounting treatment under GAAP, which stems from the third quarter 2014 acquisition of two option properties as they carry significantly below market ground leases, the amortization of which is material to our overall results. We present Modified FFO because we consider it an important supplemental measure of our operating performance in that it adds back the non-cash amortization of below-market ground leases. There can be no assurance that Modified FFO presented by us is comparable to similarly titled measures of other REITs. Modified FFO does not represent cash generated from operating activities and should not be considered as an alternative to net income (loss) determined in accordance with GAAP or to cash flow from operating activities determined in accordance with GAAP. Modified FFO is not indicative of cash available to fund ongoing cash needs, including the ability to make cash distributions.

Core Funds From Operations ("Core FFO")

Core FFO adds back to Modified FFO the following items: deferred tax asset write-off, loss on early extinguishment of debt and acquisition expenses. The Company presents Core FFO because it considers it an important supplemental measure of its operating performance in that it excludes non-recurring items. There can be no assurance that Core FFO presented by the Company is comparable to similarly titled measures of other REITs. Core FFO does not represent cash generated from operating activities and should not be considered as an alternative to net income (loss) determined in accordance with GAAP or to cash flow from operating activities determined in accordance with GAAP. Core FFO is not indicative of cash available to fund ongoing cash needs, including the ability to make cash distributions. In future periods, we may also exclude other items from Core FFO that we believe may help investors compare our results.

The following table presents a reconciliation of our net income, the most directly comparable GAAP measure, to FFO, Modified FFO and Core FFO for the periods presented (amounts in thousands, except per share amounts):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
	(unaudited)		(unaudited)	
Net income	$29,230	$35,489	$77,472	$85,993
Private perpetual preferred unit distributions	(234)	(234)	(702)	(702)
Real estate depreciation and amortization	42,004	38,134	120,521	118,690
FFO attributable to common stockholders and non-controlled interests	71,000	73,389	197,291	203,981
Amortization of below-market ground leases	1,957	1,957	5,873	5,873
Modified FFO attributable to common stockholders and non-controlled interests	72,957	75,346	203,164	209,854
Loss on early extinguishment of debt	—	2,157	—	2,157
Core FFO attributable to common stockholders and non-controlled interests	$72,957	$77,503	$203,164	$212,011
Weighted average shares and Operating Partnership Units				
Basic	297,478	296,389	297,180	296,389
Diluted	297,478	297,871	297,181	298,089

Factors That May Influence Future Results of Operations

Leasing

We signed 1.3 million rentable square feet of new leases, expansions and lease renewals for the year ended December 31, 2017. During the nine months ended September 30, 2018, we signed 0.8 million rentable square feet of new leases, expansions and renewals.

Due to the relatively small number of leases that are signed in any particular quarter, one or more larger leases may have a disproportionately positive or negative impact on average rent, tenant improvement and leasing commission costs for that period. As a result, we believe it is more appropriate when analyzing trends in average rent and tenant improvement and leasing commission costs to review activity over multiple quarters or years. Tenant improvement costs include expenditures for general improvements occurring concurrently with, but that are not directly related to, the cost of installing a new tenant. Leasing commission costs are similarly subject to significant fluctuations depending upon the length of leases being signed and the mix of tenants from quarter to quarter.

As of September 30, 2018, there were approximately 0.8 million rentable square feet of space in our portfolio available to lease (excluding leases signed but not yet commenced) representing 7.9% of the net rentable square footage of the properties in our portfolio. In addition, leases representing 2.3% and 7.0% of net rentable square footage of the properties in our portfolio will expire in 2018 and in 2019, respectively. These leases are expected to represent approximately 2.3% and 7.1%, respectively, of our annualized rent for such periods. Our revenues and results of operations can be impacted by expiring leases that are not renewed or re-leased or that are renewed or re-leased at base rental rates equal to, above or below the current average base rental rates. Further, our revenues and results of operations can also be affected by the costs we incur to re-lease available space, including payment of leasing commissions, redevelopments and build-to-suit remodeling that may not be borne by the tenant.

We believe that as we complete the redevelopment and repositioning of our properties we will, over the long-term, experience increased occupancy levels and rents. Over the short term, as we renovate and reposition our properties, which includes aggregating smaller spaces to offer large blocks of space, we may experience lower occupancy levels as a result of having to relocate tenants to alternative space and the strategic expiration of existing leases. We believe that despite the short-term lower occupancy levels we may experience, we will continue to experience increased rental revenues as a result of the increased rents which we expect to obtain following the redevelopment and repositioning of our properties.

Observatory and Broadcasting Operations

The Empire State Building Observatory revenue for the third quarter 2018 was $40.2 million, a 2.4% increase from $39.3 million for the third quarter 2017. The Observatory hosted approximately 1,168,000 visitors in the third quarter 2018 versus 1,237,000 visitors in the third quarter 2017, a decrease of 5.6%. In the third quarter 2018, there were 11 bad weather days compared to 14 bad weather days in the third quarter 2017.

Observatory revenue was $96.7 million for the nine months ended September 30, 2018, a 2.6% increase from $94.2 million for the nine months ended September 30, 2017. The 102nd floor Observatory was closed during the first quarter 2018 for replacement of original elevator machinery with a new, higher speed glass elevator. For the nine months ended September 30, 2018, the Observatory hosted approximately 2,860,000 visitors, compared to 2,949,000 visitors for the same period in 2017, a decrease of 3.0%. For the nine months ended September 30, 2018, there were 37 bad weather days compared to 51 bad weather days in the nine months ended September 30, 2017.

Observatory revenues and admissions are dependent upon the following: (i) the number of tourists (domestic and international) that come to New York City and visit the observatory, as well as any related tourism trends; (ii) the prices per admission that can be charged; (iii) seasonal trends affecting the number of visitors to the observatory; (iv) competition, in particular from other new and existing observatories; and (v) weather trends.

We license the use of the Empire State Building mast to third party television and radio broadcasters and providers of data communications. We also lease space in the upper floors of the building to such licensees to house their transmission equipment and related facilities. During the nine months ended September 30, 2018 and 2017, we derived $15.9 million and $14.5 million of revenue, respectively, and $2.6 million and $5.1 million of expense reimbursements, respectively, from the Empire State Building’s broadcasting licenses and related leases. During the remainder of 2018, licenses and related leases totaling $2.3 million are expected to expire.

Critical Accounting Estimates

Refer to our Annual Report on Form 10-K for the year ended December 31, 2017 for a discussion of our critical accounting estimates. There were no material changes to our critical accounting estimates disclosed in our Annual

Report on Form 10-K for the year ended December 31, 2017.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our future income, cash flows and fair values relevant to financial instruments are dependent upon prevalent market interest rates. Market risk refers to the risk of loss from adverse changes in market prices and interest rates. One of the principal market risks facing us is interest rate risk on our variable rate indebtedness. As of September 30, 2018, we had no variable rate debt as the LIBOR rate on our unsecured term loan facility of $265.0 million was fixed at 2.1485% under a variable to fixed interest rate swap agreement.

Subject to maintaining our qualification as a REIT for U.S. federal income tax purposes, we may mitigate the risk of interest rate volatility through the use of hedging instruments, such as interest rate swap agreements and interest rate cap agreements. Our primary objectives when undertaking hedging transactions and derivative positions will be to reduce our floating rate exposure and to fix a portion of the interest rate for anticipated financing and refinancing transactions. This in turn will reduce the risk that the variability of cash flows will impose on floating rate debt. However, we can provide no assurances that our efforts to manage interest rate volatility will successfully mitigate the risks of such volatility on our portfolio. We are not subject to foreign currency risk.

We are exposed to interest rate changes primarily on our unsecured revolving credit facility and debt refinancings. Our objectives with respect to interest rate risk are to limit the impact of interest rate changes on operations and cash flows, and to lower our overall borrowing costs. To achieve these objectives, we may borrow at fixed rates and may enter into derivative financial instruments such as interest rate swaps or caps in order to mitigate our interest rate risk on a related floating rate financial instrument. We do not enter into derivative or interest rate transactions for speculative purposes.

We entered into interest rate LIBOR swap agreements with an aggregate notional value of $515.0 million, which fix LIBOR interest rates between 2.1485% and 2.9580% and mature between August 24, 2022 and July 1, 2026. All interest rate swaps as of September 30, 2018 have been designated as cash flow hedges and are deemed highly effective with a fair value of $9.9 million which is included in prepaid expenses and other assets on the condensed consolidated balance sheet.

As of September 30, 2018, the weighted average interest rate on the $1.9 billion of fixed-rate indebtedness outstanding was 3.84% per annum, with maturities at various dates through March 22, 2033.

As of September 30, 2018, the fair value of our outstanding debt was approximately $1.9 billion, which was approximately $54.5 million less than the historical book value as of such date. Interest risk amounts were determined by considering the impact of hypothetical interest rates on our financial instruments. These analyses do not consider the effect of any change in overall economic activity that could occur in that environment. Further, in the event of a change of that magnitude, we may take actions to further mitigate our exposure to the change. However, due to the uncertainty of the specific actions that would be taken and their possible effects, these analyses assume no changes in our financial structure.

Our exposures to market risk have not changed materially since December 31, 2017.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as such term is defined in Rule 13a-15(e) and 15d-15(e) under the Exchange Act) that are designed to ensure that information required to be disclosed in our reports under the Exchange Act is processed, recorded, summarized and reported within the time periods specified in the SEC’s rules and regulations and that such information is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As of September 30, 2018, the end of the period covered by this Report, we carried out an evaluation, under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial

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

Changes in Internal Control over Financial Reporting

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

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

See Note 8 to the Notes to Condensed Consolidated Financial Statements for a description of legal proceedings.

ITEM 1A. RISK FACTORS

There have been no material changes to the risk factors included in the section entitled "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2017.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable

ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS

Exhibit No.	Description
10.45*	First Amendment, dated as of October 5, 2018, to the Amended and Restated Employment Agreement between Empire State Realty Trust, Inc. and Anthony E. Malkin, dated April 5, 2016.
31.1*	Certification of Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certification of Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2*	Certification of Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema Document
101.CAL*	XBRL Taxonomy Extension Calculation Document
101.DEF*	XBRL Taxonomy Extension Definitions Document

101.LAB* XBRL Taxonomy Extension Labels Document
101.PRE* XBRL Taxonomy Extension Presentation Document
Notes:
* Filed herewith.

SIGNATURES

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

EMPIRE STATE REALTY TRUST, INC.

Date: November 6, 2018 By:/s/ David A. Karp
Executive Vice President and Chief Financial Officer
(Principal Financial Officer)

Date: November 6, 2018 By:/s/ Andrew J. Prentice
Senior Vice President, Chief Accounting Officer and Treasurer
(Principal Accounting Officer)