

AEROCENTURY CORP  
Form 10-Q  
November 14, 2014

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2014

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: 001-13387

AeroCentury Corp.  
(Exact Name of Registrant as Specified in Its Charter)

Delaware  
(State or Other Jurisdiction of Incorporation or  
Organization)

94-3263974  
(I.R.S. Employer Identification No.)

1440 Chapin Avenue, Suite 310  
Burlingame, California 94010  
(Address of Principal Executive Offices)

(650) 340-1888  
(Registrant's Telephone Number Including Area Code)

None  
(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required submit and post such files).

Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting

company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer   
Non-accelerated filer  Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practicable date: As of November 14, 2014 the issuer had 1,606,557 shares of common stock, par value \$0.001 per share, issued, of which 63,300 are held as treasury stock.

PART I  
FINANCIAL INFORMATION

Forward-Looking Statements

This Quarterly Report on Form 10-Q includes "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"). All statements in this Report other than statements of historical fact are "forward-looking statements" for purposes of these provisions, including any statements of plans and objectives for future operations and any statements of assumptions underlying any of the foregoing. Statements that include the use of terminology such as "may," "will," "expects," "plans," "anticipates," "estimates," "potential," or "continue," or the negative thereof, or other comparable terminology are forward-looking statements. Forward-looking statements include these statements: (i) in Part 1, Item 1, "Notes to Financial Statements," that the Company expects to deliver a Saab 340B in November 2014; and that the Company will be in compliance with all of its credit facility covenants at future calculation dates; (ii) in Part 1, Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations – Liquidity and Capital Resources – Credit Facility" that the Company will be in compliance with all of its credit facility covenants at future calculation dates; (iii) in Part I, Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations – Cash Flow," that the Company will have adequate cash flow to meet its ongoing operational needs; (iv) in Part I, Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations — Outlook," that the Company could experience a delay in remarketing its off-lease assets; that the customers for several of the leases that expire in 2015 will choose to return the assets; that additional customers may choose to return leased assets in the future; that an engine on lease may be returned at lease expiration; that the Company will be in compliance with all of its credit facility covenants at future calculation dates; and that the available borrowings under the Credit Facility will be sufficient to meet the Company's continuing obligations and fund anticipated acquisitions; (v) in Part I, Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations – Factors that May Affect Future Results," that the Company will be in compliance with all of its credit facility covenants at future calculation dates; that the Company will have sufficient cash funds to make any required principal repayment that arise due to borrowing base limitations; that most of the Company's growth will be outside the United States; that the overall industry experience of JMC's personnel and its technical resources should permit the Company to effectively manage new aircraft types and engines; that effective mitigating factors exist against undue compensation-incented risk-taking by JMC; that it is contemplated that the burden and cost of complying with regulatory requirements will fall primarily upon lessees of equipment or the Company as owner of the equipment; that the costs of complying with environmental regulations will not have a material adverse effect on the Company; that the Company has sufficient cyber-security measures in place; and that sufficient replacement mechanisms exist in the event of an interruption in its internet communications ability that there would not be a material adverse financial impact on the Company's business.

These forward-looking statements involve risks and uncertainties, and it is important to note that the Company's actual results could differ materially from those projected or assumed in such forward-looking statements. Among the factors that could cause actual results to differ materially are the factors detailed under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations — Factors That May Affect Future Results," including the lack of any unexpected lessee defaults or insolvency; a deterioration of the market values of aircraft types owned by the Company; compliance by the Company's lessees with obligations under their respective leases; no sudden current economic downturn or unanticipated future financial crises; the continued availability of financing for acquisitions under the Credit Facility; the Company's success in finding appropriate assets to acquire with such financing; deviations from the assumption that future major maintenance expenses will be relatively evenly spaced over the entire portfolio; and future trends and results which cannot be predicted with certainty. The cautionary statements made in this Report should be read as being applicable to all related forward-looking statements wherever they appear herein. All forward-looking statements and risk factors included in this document are made as of the date

hereof, based on information available to the Company as of the date hereof, and the Company assumes no obligation to update any forward-looking statement or risk factor. You should consult the risk factors listed from time to time in the Company's filings with the Securities and Exchange Commission.

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## Item 1. Financial Statements.

AeroCentury Corp.  
Balance Sheets  
(Unaudited)

ASSETS		
	September 30, 2014	December 31, 2013
Assets:		
Cash and cash equivalents	\$2,588,100	\$2,112,700
Accounts receivable, including deferred rent of \$32,100 and \$217,200 at September 30, 2014 and December 31, 2013, respectively	2,726,300	3,303,800
Finance leases receivable	945,400	1,895,200
Aircraft and aircraft engines held for lease, net of accumulated depreciation of \$37,665,700 and \$50,679,300 at September 30, 2014 and December 31, 2013, respectively	159,408,600	152,954,600
Assets held for sale	6,561,200	735,000
Prepaid expenses and other	4,296,700	3,633,000
<b>Total assets</b>	<b>\$ 176,526,300</b>	<b>\$ 164,634,300</b>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities:		
Accounts payable and accrued expenses	\$2,239,700	\$1,202,700
Notes payable and accrued interest	108,352,400	77,527,300
Maintenance reserves	13,777,200	16,671,800
Accrued maintenance costs	1,778,400	1,612,100
Security deposits	5,579,300	6,265,000
Unearned revenues	2,121,400	646,700
Deferred income taxes	7,540,700	14,573,800
Taxes payable	800,100	-
<b>Total liabilities</b>	<b>142,189,200</b>	<b>118,499,400</b>
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$0.001 par value, 2,000,000 shares authorized, no shares issued and outstanding	-	-
Common stock, \$0.001 par value, 10,000,000 shares authorized, 1,606,557 shares issued and outstanding	1,600	1,600
Paid-in capital	14,780,100	14,780,100
Retained earnings	20,059,500	31,857,300
	34,841,200	46,639,000
Treasury stock at cost, 63,300 shares	(504,100 )	(504,100 )
<b>Total stockholders' equity</b>	<b>34,337,100</b>	<b>46,134,900</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 176,526,300</b>	<b>\$ 164,634,300</b>

The accompanying notes are an integral part of these statements.



AeroCentury Corp.  
Statements of Operations  
(Unaudited)

	For the Nine Months Ended September 30,		For the Three Months Ended September 30,	
	2014	2013	2014	2013
<b>Revenues and other income:</b>				
Operating lease revenue, net	\$15,998,500	\$13,941,200	\$4,815,400	\$4,368,200
Maintenance reserves revenue, net	3,393,600	13,866,000	-	6,146,000
Net gain on disposal of assets	2,963,900	4,147,700	1,809,400	1,985,200
Other income	151,800	644,500	700	37,800
	22,507,800	32,599,400	6,625,500	12,537,200
<b>Expenses:</b>				
Provision for impairment in value of aircraft	18,518,700	-	11,718,700	-
Maintenance	5,819,800	4,883,700	2,173,200	1,413,800
Depreciation	5,609,900	5,376,600	1,731,500	1,803,600
Management fees	3,864,900	3,231,000	1,205,000	1,058,400
Interest	3,793,000	3,034,300	1,225,000	966,200
Professional fees, general and administrative and other	1,488,000	881,000	360,200	256,400
Insurance	1,034,100	827,900	413,600	276,300
Other taxes	407,600	67,600	362,500	22,500
Bad debt expense	-	357,600	-	357,600
	40,536,000	18,659,700	19,189,700	6,154,800
(Loss)/income before income tax provision	(18,028,200)	13,939,700	(12,564,200)	6,382,400
Income tax (benefit)/provision	(6,230,400 )	4,764,300	(4,317,200 )	2,361,200
Net (loss)/income	\$(11,797,800)	\$9,175,400	\$(8,247,000 )	\$4,021,200
<b>(Loss)/earnings per share:</b>				
Basic	\$(7.64 )	\$5.95	\$(5.34 )	\$2.61
Diluted	\$(7.64 )	\$5.78	\$(5.34 )	\$2.53
<b>Weighted average shares used in (loss)/earnings per share computations:</b>				
Basic	1,543,257	1,543,257	1,543,257	1,543,257
Diluted	1,543,257	1,587,329	1,543,257	1,590,164

The accompanying notes are an integral part of these statements.

AeroCentury Corp.  
Statements of Cash Flows  
(Unaudited)

	For the Nine Months Ended September 30,	
	2014	2013
Net cash provided by operating activities	\$3,478,000	\$7,222,400
Investing activities:		
Proceeds from sale of aircraft and aircraft engines held for lease, net of re-sale fees	15,723,700	8,173,800
Proceeds from sale of assets held for sale, net of re-sale fees	273,800	73,600
Purchases of aircraft and aircraft engines	(47,254,600)	(6,634,300)
Net cash (used in)/provided by investing activities	(31,257,100)	1,613,100
Financing activities:		
Borrowings under Credit Facility	43,900,000	4,000,000
Repayments of Credit Facility	(13,200,000)	(7,300,000)
Debt issuance costs	(2,445,500)	(2,055,000)
Net cash provided by/(used in) financing activities	28,254,500	(5,355,000)
Net increase in cash and cash equivalents	475,400	3,480,500
Cash and cash equivalents, beginning of period	2,112,700	1,596,800
Cash and cash equivalents, end of period	\$2,588,100	\$5,077,300

During the nine months ended September 30, 2014 and 2013, the Company paid interest totaling \$3,029,900 and \$2,260,100, respectively. The Company paid income taxes of \$800 and \$800 during the nine months ended September 30, 2014 and 2013, respectively.

The accompanying notes are an integral part of these statements.



AeroCentury Corp.  
Notes to Financial Statements (Unaudited)  
September 30, 2014

1. Organization and Summary of Significant Accounting Policies

(a) The Company and Basis of Presentation

AeroCentury Corp., a Delaware corporation incorporated in 1997, acquires used regional aircraft and engines for lease to foreign and domestic regional carriers.

The condensed financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial information, the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three-month and nine-month periods ended September 30, 2014 are not necessarily indicative of the results that may be expected for the year ending December 31, 2014.

As discussed in Note 2, the Company has adopted an alternate method of accounting for non-refundable maintenance reserves and certain lessor maintenance obligations. The Company has applied this change in accounting principle retrospectively in accordance with ASC 250, Accounting Changes and Error Corrections (“ASC 250”).

For further information, refer to the financial statements and footnotes thereto included in the Company’s annual report on Form 10-K for the year ended December 31, 2013.

(b) Use of Estimates

The Company’s financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”). The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable for making judgments that are not readily apparent from other sources.

The most significant estimates with regard to these financial statements are the residual values and useful lives of the assets, the amount and timing of cash flows associated with each asset that are used to evaluate whether assets are impaired, accrued maintenance costs, accounting for income taxes, and the amounts recorded as allowances for doubtful accounts.

(c) Fair Value Measurements

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs, to the extent possible. The fair value hierarchy under GAAP is based on three levels of inputs.

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

Level 2 - Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

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AeroCentury Corp.  
Notes to Financial Statements (Unaudited)  
September 30, 2014

1. Organization and Summary of Significant Accounting Policies (continued)

(c) Fair Value Measurements (continued)

Level 3 - Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

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

The following table shows by level, within the fair value hierarchy, the fair value of the Company's assets that are measured and recorded at fair value on a recurring basis:

	September 30, 2014				December 31, 2013			
	Total	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3
Money market funds included in cash and cash equivalents	\$443,700	\$443,700	\$-	\$-	\$1,842,000	\$1,842,000	\$-	\$-
Total	\$443,700	\$443,700	\$-	\$-	\$1,842,000	\$1,842,000	\$-	\$-

As of September 30, 2014 and December 31, 2013, there were no liabilities that were required to be measured and recorded at fair value on a recurring basis.

Assets Measured and Recorded at Fair Value on a Nonrecurring Basis

The Company determines fair value of long-lived assets held and used, such as aircraft and aircraft engines held for lease and held for sale, by reference to independent appraisals, quoted market prices (e.g., offers to purchase) and other factors. An impairment charge is recorded when the Company believes that the carrying value of an asset will not be recovered through future net cash flows and that the carrying value exceeds its fair value.

During the third quarter ended September 30, 2014, the Company determined that the carrying values of its seven Fokker 100 aircraft were not recoverable and consequently recorded an impairment charge of \$11,385,300 based on the appraised values and management's estimate of realizable value of those aircraft, in addition to the \$6,800,000 impairment charge recorded for five of these aircraft during the second quarter ended June 30, 2014. During the third quarter of 2014, the Company also recorded an impairment charge of \$333,400 for one of its Fokker 50 aircraft. Of these aircraft, five Fokker 100 aircraft and the Fokker 50 aircraft were reclassified as held for sale at September 30, 2014, in addition to two Saab 340B airframes that were previously classified as held for sale. The Company's other two Fokker 100 aircraft are held for lease.

Fair Value of Other Financial Instruments

The Company's financial instruments, other than cash and cash equivalents, consist principally of finance leases receivable and amounts borrowed under its credit facility (the "Credit Facility," as defined in Note 5). The fair value of accounts receivable, finance leases receivable, accounts payable and the Company's maintenance reserves and accrued maintenance costs approximates the carrying value of these financial instruments.



AeroCentury Corp.  
Notes to Financial Statements (Unaudited)  
September 30, 2014

1. Organization and Summary of Significant Accounting Policies (continued)

(c) Fair Value Measurements (continued)

Borrowings under the Company's Credit Facility bear floating rates of interest that reset periodically to a market benchmark rate plus a credit margin. The Company believes the effective interest rate of this debt agreement approximates current market rates for such indebtedness at the balance sheet date, and therefore that the carrying amount of its floating rate debt at the balance sheet dates approximates its fair value. The fair value of the Company's outstanding balance of its Credit Facility would be categorized as Level 3 under the GAAP fair value hierarchy.

(d) Finance Leases

The lease for one of the Company's aircraft contains a lessee purchase option at a price substantially below the assets' estimated residual values at the exercise date for the option. Consequently, the Company considers the purchase option to be a "bargain purchase option" and has classified the lease as a finance lease for financial accounting purposes. The Company does not include the value, purchase price or accumulated depreciation of finance lease assets on its balance sheet. Instead, the discounted present value of (i) future minimum lease payments (including the bargain purchase option) and (ii) any residual value not subject to a bargain purchase option are reported as a finance lease receivable. Rental revenue and depreciation expense are not recognized on finance leases. Rather, the Company accrues interest on the balance of the finance lease receivable based on the interest rate inherent in the applicable lease.

Two engines that were previously subject to finance leases were returned to the Company during the second quarter of 2014 and the finance lease receivable balances were reclassified to aircraft and aircraft engines held for lease on the Company's balance sheet.

The Company recognized interest earned on finance leases as "other income" in the amount of \$0 and \$37,100 in the quarters ended September 30, 2014 and 2013, respectively, and \$150,000 and \$102,100 in the nine months ended September 30, 2014 and 2013, respectively.

(e) Recent Accounting Pronouncements

On May 28, 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update No. 2014-09 (the "ASU") that created the new Topic 606 in the Accounting Standards Codification ("ASC"). The ASU also included numerous conforming additions and amendments to other Topics within the ASC. Topic 606 establishes new rules that affect the amount and timing of revenue recognition for contracts with customers, but does not affect lease accounting and reporting. As such, adoption of these provisions will not affect the Company's lease revenues but may affect the reporting of other of the Company's revenues. The provisions included in the ASU are effective for years commencing after December 15, 2016, cannot be adopted early, and may be reflected using either a full retrospective method or a simplified method that does not recast prior periods but does disclose the effect of the adoption on the current period financial statements. The Company has not determined either the potential impact on its financial statements nor the method it will elect to use in connection with the adoption of the changes included in the ASU.



AeroCentury Corp.  
Notes to Financial Statements (Unaudited)  
September 30, 2014

1. Organization and Summary of Significant Accounting Policies (continued)

(e) Recent Accounting Pronouncements (continued)

On August 27, 2014, the FASB issued ASU 2014-15, "Presentation of Financial Statements - Going Concern," which added Subtopic 205-40 to the ASC (the "Subtopic"). This Subtopic requires management to determine whether substantial doubt exists concerning the reporting entity's ability to continue as a going concern, in which case certain disclosures will be required. The Subtopic affects financial statement presentation but not methods of accounting, and is effective on a prospective basis for annual periods ending after December 2016 and each reporting period thereafter, although early adoption is permitted. The Company has not currently early adopted the Subtopic.

2. Adjustment of Previously Reported Financial Information

The Company adopted the direct expensing method under Financial Accounting Standards Board ("FASB") Staff Position AUG AIR-1, Accounting for Planned Major Maintenance Activities ("FSP AUG AIR-1") on January 1, 2007. Under FSP AUG AIR-1, non-refundable maintenance reserves were recorded as maintenance reserves revenue (assuming cash was received or collection was reasonably assured), and associated maintenance work was recorded as maintenance expense when the work was performed. The Company evaluated its method of accounting for maintenance reserves and lessor maintenance obligations and elected to change its method of accounting, effective January 1, 2014, to:

- (i) Recognize non-refundable maintenance reserves as liabilities for deposits against future maintenance reimbursements of maintenance reserves received in the normal course of ongoing leases;
- (ii) Recognize reimbursements from such collected reserves as disbursements against the liability when claims are submitted for payment against previously collected maintenance reserves;
- (iii) Reflect as liabilities non-refundable reserves received by the prior lessor upon acquisition of an aircraft, which are claimable by the lessee when maintenance is performed;
- (iv) Recognize as income non-refundable reserves not refunded to lessees upon termination of the lease and return of the aircraft to the Company in accordance with all lease return requirements; and
- (v) Record lessor maintenance obligations as liabilities upon acquisition of an aircraft subject to a lease under which the Company assumes the prior lessor's obligation to pay a portion of a first-time maintenance event.

In management's judgment, the change to this accounting method is preferable in that it will provide the user of the Company's financial statements a better understanding of the underlying business terms of the Company's leasing transactions and provide additional clarity with respect to the Company's sources of income, its non-refundable reserve obligations, and its lessor maintenance obligations. The change in accounting method resulted in a cumulative net decrease of \$8,088,200 in stockholders' equity as of January 1, 2013.

AeroCentury Corp.  
Notes to Financial Statements (Unaudited)  
September 30, 2014

## 2.Adjustment of Previously Reported Financial Information (continued)

The effects on the Company's December 31, 2013 balance sheet as a result of the retroactive application of the change in accounting principle in accordance with ASC 250 were as follows:

	December 31, 2013		
	As reported previously	As adjusted	Effect of change
Cash and cash equivalents	\$2,112,700	\$2,112,700	\$-
Accounts receivable, net	3,313,700	3,303,800	(9,900 )
Finance leases receivable	1,895,200	1,895,200	-
Aircraft and aircraft engines held for lease, net	152,375,200	152,954,600	579,400
Assets held for sale	735,000	735,000	-
Prepaid expenses and other	3,633,000	3,633,000	-
<b>Total assets</b>	<b>\$164,064,800</b>	<b>\$164,634,300</b>	<b>\$569,500</b>
Accounts payable and accrued expenses	\$1,175,300	\$1,202,700	\$27,400
Notes payable and accrued interest	77,527,300	77,527,300	-
Maintenance reserves and accrued maintenance costs	13,254,100	18,283,900	5,029,800
Security deposits	6,265,000	6,265,000	-
Unearned revenues	646,700	646,700	-
Deferred income taxes	16,099,700	14,573,800	(1,525,900)
<b>Total liabilities</b>	<b>114,968,100</b>	<b>118,499,400</b>	<b>3,531,300</b>
Preferred stock	-	-	-
Common stock	1,600	1,600	-
Paid-in capital	14,780,100	14,780,100	-
Retained earnings	34,819,100	31,857,300	(2,961,800)
Treasury stock	(504,100 )	(504,100 )	-
<b>Total stockholders' equity</b>	<b>49,096,700</b>	<b>46,134,900</b>	<b>(2,961,800)</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$164,064,800</b>	<b>\$164,634,300</b>	<b>\$569,500</b>



AeroCentury Corp.  
Notes to Financial Statements (Unaudited)  
September 30, 2014

## 2.Adjustment of Previously Reported Financial Information (continued)

The effects on the Company's statements of operations for the nine months and three months ended September 30, 2013 as a result of the retroactive application of the change in accounting principle in accordance with ASC 250 were as follows:

	For the Nine Months Ended September 30, 2013			For the Three Months Ended September 30, 2013		
	As reported previously	As adjusted	Effect of change	As reported previously	As adjusted	Effect of change
Operating lease revenue, net	\$ 13,941,200	\$ 13,941,200	\$-	\$ 4,368,200	\$ 4,368,200	\$-
Maintenance reserves income, net	8,260,500	13,866,000	5,605,500	556,900	6,146,000	5,589,100
Gain on disposal of assets and other income	4,792,200	4,792,200	-	2,023,000	2,023,000	-
	26,993,900	32,599,400	5,605,500	6,948,100	12,537,200	5,589,100
Maintenance	6,239,900	4,883,700	(1,356,200)	2,451,100	1,413,800	(1,037,300)
Depreciation	5,339,700	5,376,600	36,900	1,790,300	1,803,600	13,300
Management fees	3,218,500	3,231,000	12,500	1,054,000	1,058,400	4,400
Interest	3,034,300	3,034,300	-	966,200	966,200	-
Professional fees, general and administrative and other	948,600	948,600	-	278,900	278,900	-
Insurance	827,900	827,900	-	276,300	276,300	-
Bad debt expense	357,600	357,600	-	357,600	357,600	-
	19,966,500	18,659,700	(1,306,800)	7,174,400	6,154,800	(1,019,600)
Income before taxes	7,027,400	13,939,700	6,912,300	(226,300 )	6,382,400	6,608,700
Tax provision	2,414,100	4,764,300	2,350,200	114,300	2,361,200	2,246,900
Net income	\$ 4,613,300	\$ 9,175,400	\$ 4,562,100	\$ (340,600 )	\$ 4,021,200	\$ 4,361,800
Earnings per share:						
Basic	\$ 2.99	\$ 5.95	\$ 2.96	\$ (0.22 )	\$ 2.61	\$ 2.83
Diluted	\$ 2.91	\$ 5.78	\$ 2.87	\$ (0.22 )	\$ 2.53	\$ 2.75

AeroCentury Corp.  
Notes to Financial Statements (Unaudited)  
September 30, 2014

### 3. Aircraft and Aircraft Engines Held for Lease or Sale

#### (a) Assets Held for Lease

At September 30, 2014 and December 31, 2013, the Company's aircraft and aircraft engines, which were on lease or held for lease, consisted of the following:

Model	September 30, 2014			December 31, 2013		
	Number owned	% of net book value		Number owned	% of net book value	
Bombardier Dash-8-300	8	20 %		9	23 %	
Bombardier CRJ-700	3	19 %		-	-	
Bombardier Dash-8-Q400	3	16 %		3	17 %	
ATR 42-600	1	11 %		-	-	
Bombardier CRJ-705	1	11 %		1	12 %	
Saab 340B Plus	6	7 %		6	8 %	
Fokker 50	6	6 %		10	10 %	
Fokker 100	2	3 %		7	19 %	
General Electric CF34-8E5 engine	2	4 %		3	6 %	
Saab 340B	1	1 %		4	4 %	
Tay 650-15 engine	1	1 %		1	1 %	
General Electric CT7-9B engine	2	1 %		2	-	
Saab 340A	1	-		1	-	

Assets subject to finance leases are not included in the net book value of assets held for lease. Therefore, the Company's single Saab 340A aircraft, which is subject to a finance lease, is not included in the net book value calculations as of September 30, 2014 and December 31, 2013, and the Company's two General Electric CT7-9B engines, which were subject to finance leases, are not included in the net book value calculation as of December 31, 2013.

During the third quarter ended September 30, 2014, the Company recorded an impairment charge of \$2,906,400 on its two Fokker 100 aircraft that are held for lease based on appraised values.

During the third quarters of 2014 and 2013, the Company used cash of \$15,020,600 and \$2,545,400 for the purchase and capital improvement of aircraft and engines.

During the third quarter of 2014, the Company recorded net gains totaling \$1,809,400 related to the sale of two Fokker 50 and one Bombardier Dash-8-300 aircraft. During the third quarter of 2013, the Company recorded gains of \$1,985,200 upon the sale of a deHavilland DHC-6 aircraft and a Fokker 50 aircraft.

During the third quarter of 2014, the Company extended the leases for three of its assets and re-leased a Fokker 100 aircraft and a Saab 340B Plus aircraft that were off lease on June 30, 2014.



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3. Aircraft and Aircraft Engines Held for Lease or Sale (continued)

(a) Assets Held for Lease (continued)

At September 30, 2014, eleven of the Company's assets that were off lease, representing 14% of the net book value of the Company's aircraft and engines, were held for lease and were comprised of one Fokker 100 aircraft, five Saab 340B Plus aircraft, two General Electric CF34-8E5 engines, two General Electric CT7-9B engines and one Tay 650-15 engine.

As discussed in Note 8, in October 2014, the Company sold a Saab 340A aircraft and a Saab 340B aircraft and delivered a Fokker 100 aircraft to the same customer that took delivery of another Fokker 100 aircraft in the third quarter of 2014. The Company has a signed letter of intent and deposit for the lease of a Saab 340B Plus aircraft and expects to deliver the aircraft in November 2014. The Company is seeking re-lease opportunities for its other off-lease assets that are held for lease, other than the Tay 650-15 engine that is being held as a spare and used in connection with required maintenance on the Company's Fokker 100 aircraft.

(b) Assets Held for Sale

Assets held for sale include two Saab 340B airframes as well as five Fokker 100 aircraft and a Fokker 50 aircraft.

During the three months ended September 30, 2014 and 2013, the Company received \$48,100 and \$73,600, respectively, from the sale of parts belonging to the two airframes, which proceeds reduced their carrying value.

As discussed in Note 1, during the second quarter of 2014, the Company recorded a \$6,800,000 impairment charge related to five Fokker 100 aircraft. During the third quarter, the Company recorded an additional impairment charge of \$8,478,900 related to these aircraft, as well as a \$333,400 impairment charge related to a Fokker 50 aircraft, which are recorded at their estimated realizable value net of disposal costs. At September 30, 2014, these aircraft were reclassified as held for sale on the Company's balance sheet.

4. Maintenance Reserves and Accrued Maintenance Costs

Maintenance costs under the Company's triple net leases are generally the responsibility of the lessees. Most of the Company's leases require payment of maintenance reserves, which are based upon lessee-reported usage and billed monthly, and are intended to accumulate and be applied by the Company toward reimbursement of most or all of the cost of the lessees' performance of certain maintenance obligations under the leases. Maintenance reserves are characterized as either refundable or non-refundable depending on their disposition at lease end. The Company retains non-refundable maintenance reserves at lease-end, even if the lessee has met all of its obligations under the lease, including any return conditions applicable to the leased asset, while refundable reserves are returned to the lessee under such circumstances.

Maintenance reserves in the accompanying balance sheets include refundable and non-refundable maintenance reserves payments billed to lessees, which are paid out as related maintenance is performed and, in the case of refundable reserves, at the end of the lease. Accrued maintenance costs include (i) maintenance for work performed for off-lease aircraft, which is not related to the release of reserves received from lessees and (ii) lessor maintenance obligations assumed upon acquisition of aircraft subject to a lease with such provisions.

Maintenance reserves received by the Company are accounted for as a liability, which is reduced when maintenance work is performed during the lease and reimbursement to the lessee is paid. Any reserves retained by the Company at lease end are recorded as revenue at that time.

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### 5. Notes Payable and Accrued Interest

At September 30, 2014 and December 31, 2013, the Company's notes payable and accrued interest consisted of the following:

	September 30, 2014	December 31, 2013
Credit Facility principal	\$108,200,000	\$77,500,000
Credit Facility accrued interest	152,400	27,300
	\$108,352,400	\$77,527,300

During May 2014, the Company's \$130 million Credit Facility (the "Credit Facility"), which is provided by a syndicate of banks, was increased to \$180 million and extended through May 31, 2019. The Credit Facility is secured by all of the assets of the Company, including its aircraft and engine portfolio.

In November 2013, the Company obtained a waiver of compliance with a customer concentration covenant at the September 30, 2013 and December 31, 2013 calculation dates. The Company was in compliance with all covenants other than the waived covenant under the Credit Facility agreement at December 31, 2013.

As of June 30, 2014, the Company was out of compliance with a profitability covenant. The non-compliance resulted primarily from the Company recording aircraft impairment charges on aircraft totaling \$6,800,000 during the second quarter ended June 30, 2014. In August 2014, the Company and the Credit Facility banks agreed to an amendment to the profitability covenant, which cured the June 30, 2014 non-compliance.

As of September 30, 2014, the Company was out of compliance with several covenants. The non-compliance resulted primarily from the Company recording additional aircraft impairment charges on aircraft totaling \$11,718,700 during the third quarter of 2014. In November 2014, the Company and the Credit Facility banks agreed to an amendment to the Credit Facility, which cured the September 30, 2014 non-compliance, revised the compliance requirements through September 30, 2015, decreased the amount of the Credit Facility to \$150 million due to the departure of two participant lenders, and decreased the maximum amount to which the Credit Facility can be expanded from \$200 million to \$180 million.

Based on its current projections, the Company believes that it will be in compliance with all of its Credit Facility covenants at future calculation dates. However, there can be no assurance the Company's beliefs will prove to be correct.

The unused amount of the Credit Facility was \$71,800,000 and \$52,500,000 as of September 30, 2014 and December 31, 2013, respectively.

The weighted average interest rate on the Credit Facility was 3.59% and 3.94% at September 30, 2014 and December 31, 2013, respectively.



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### 6. Computation of Earnings Per Share

Basic and diluted earnings per share are calculated as follows:

	For the Nine Months Ended September 30,		For the Three Months Ended September 30,	
	2014	2013	2014	2013
Net (loss)/income	\$(11,797,800)	\$9,175,400	\$(8,247,000)	\$4,021,200
Weighted average shares outstanding for the period	1,543,257	1,543,257	1,543,257	1,543,257
Dilutive effect of warrants	-	44,072	-	46,907
Weighted average diluted shares used in calculation of diluted (loss)/earnings per share	1,543,257	1,587,329	1,543,257	1,590,164
Basic (loss)/earnings per share	\$(7.64 )	\$5.95	\$(5.34 )	\$2.61
Diluted (loss)/earnings per share	\$(7.64 )	\$5.78	\$(5.34 )	\$2.53

Basic earnings per common share is computed using net income and the weighted average number of common shares outstanding during the period. Diluted earnings per common share are computed using net income and the weighted average number of common shares outstanding, assuming dilution. Weighted average common shares outstanding, assuming dilution, include potentially dilutive common shares outstanding during the period. Potentially dilutive common shares include the assumed exercise of warrants using the treasury stock method. For the three months and nine months ended September 30, 2014, the dilutive effect of outstanding warrants was 28,927 and 36,497 potentially outstanding shares issuable upon the assumed exercise of all outstanding warrants, respectively. However, the effect of these potentially outstanding shares was not included in the calculation of diluted loss per share for the applicable period because the effect would have been anti-dilutive.

### 7. Related Party Transactions

The Company's portfolio of leased aircraft assets is managed and administered under the terms of a management agreement with JetFleet Management Corp. ("JMC"), which is an integrated aircraft management, marketing and financing business and a subsidiary of JetFleet Holding Corp. ("JHC"). Certain officers of the Company are also officers of JHC and JMC and hold significant ownership positions in both JHC and the Company.

Under the management agreement, JMC receives a monthly management fee based on the net asset value of the assets under management. JMC also receives an acquisition fee for locating assets for the Company. Acquisition fees are included in the cost basis of the asset purchased. JMC may receive a remarketing fee in connection with the re-lease or sale of the Company's assets. Remarketing fees are amortized over the applicable lease term or included in the gain or loss on sale.

Fees incurred during the three months and nine months ended September 30, 2014 and 2013 were as follows:

	For the Nine Months Ended September 30,		For the Three Months Ended September 30,	
	2014	2013	2014	2013
Management fees	\$3,864,900	\$3,231,000	\$1,205,000	\$1,058,400



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Acquisition fees	1,400,000	236,000	420,000	88,000
Remarketing fees	64,000	485,300	-	244,300

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8. Subsequent Events

In October 2014, the Company sold a Saab 340A and a Saab 340B aircraft to the customer that had been leasing them and recorded a gain of approximately \$192,000. As part of the sale, the Company took ownership of another Saab 340B aircraft that had previously been owned by the customer. The Company is seeking remarketing opportunities for that aircraft.

In October 2014, the Company delivered a second Fokker 100 aircraft that had been off lease at September 30, 2014 to a customer in Australia.

In November 2014, the Company and the Credit Facility banks agreed to an amendment to the Credit Facility, which cured the September 30, 2014 non-compliance, revised the compliance requirements through September 30, 2015, decreased the amount of the Credit Facility to \$150 million due to the departure of two participant lenders, and decreased the maximum amount to which the Credit Facility can be expanded from \$200 million to \$180 million.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion should be read in conjunction with the Company's Form 10-K for the year ended December 31, 2013 and the unaudited financial statements and related notes that appear elsewhere in this report.

### Critical Accounting Policies, Judgments and Estimates

The Company's discussion and analysis of its financial condition and results of operations are based upon the financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets and liabilities, revenues and expenses, and the related disclosure of contingent assets and liabilities at the date of the financial statements. In the event that actual results differ from these estimates or the Company adjusts these estimates in future periods, the Company's operating results and financial position could be materially affected. For a discussion of Critical Accounting Policies, Judgments and Estimates, refer to Note 1 to the Company's financial statements in Item 1 of this Quarterly Report on Form 10-Q.

For a discussion of the Company's accounting policies regarding maintenance reserves, refer to Note 4 to the Company's financial statements in Item 1 of this Quarterly Report on Form 10-Q. For a discussion of the Company's change in method of accounting for certain maintenance reserves and lessor maintenance obligations and its application to prior periods, refer to Note 2 to the Company's financial statements in Item 1 of this Quarterly Report on Form 10-Q.

### Results of Operations

Quarter ended September 30, 2014 compared to the quarter ended September 30, 2013

The Company recorded a net loss of \$8.2 million in the quarter ended September 30, 2014 compared to net income of \$4.0 million in the same period of 2013, primarily because the Company recorded approximately \$11.4 million of impairment charges on its seven Fokker 100 aircraft and an impairment charge of approximately \$0.3 million on one of its Fokker 50 aircraft in the third quarter of 2014. There were no recorded impairment charges of long-lived assets during the third quarter of 2013.

Quarterly operating lease revenue increased 10% from \$4.4 million in the quarter ended September 30, 2013 to \$4.8 million in the third quarter of 2014, primarily as a result of increases in operating lease revenue from assets purchased during 2013 and 2014. These increases were partially offset by the effect of assets on lease in the 2013 period but off lease in the 2014 period and asset sales during 2013 and 2014.

Maintenance reserves revenue represents maintenance reserves retained at lease-end during the relevant period. The Company had no maintenance reserves revenue in the third quarter of 2014, as compared to \$6.1 million in the quarter ended September 30, 2013. The amount recorded in the 2013 period was related to maintenance reserves retained at lease end for three aircraft.

During the third quarter of 2014, the Company recorded net gains totaling approximately \$1.8 million related to the sale of two Fokker 50 and one Bombardier Dash-8-300 aircraft. During the quarter ended September 30, 2013, the Company sold a Fokker 50 aircraft and a deHavilland DHC-6 aircraft and recorded gains totaling approximately \$2.0 million.

During the third quarters of 2014 and 2013, the Company added equipment to its lease portfolio of approximately \$17.2 million and \$2.3 million, respectively. The Company sold equipment with a book value of approximately \$5.2 million and \$1.9 million during the third quarters of 2014 and 2013, respectively. As a result of the amount and timing of these asset acquisitions and sales, depreciation was approximately the same in the third quarters of both years, and management fees in the third quarter of 2014 increased by 14% over the previous year.

The average net book value of assets held for lease during the third quarters of 2014 and 2013 was approximately \$162.8 million and \$138.8 million, respectively, representing an increase of 17%. The average portfolio utilization during the quarters ended September 30, 2014 and 2013 was 80% and 75%, respectively.

The Company's maintenance expense increased by 54% from \$1.4 million in the third quarter of 2013 to \$2.2 million in the third quarter of 2014, primarily as a result of an increase in maintenance performed by the Company on off-lease aircraft.

The Company's interest expense increased by 27% from \$1.0 million in the third quarter of 2013 to \$1.2 million in the third quarter of 2014, primarily as a result of a higher average Credit Facility balance.

The Company's professional fees, general and administrative and other expenses increased from \$0.3 million in the third quarter of 2013 to \$0.4 million in the third quarter of 2014, primarily as a result of expenses incurred in connection with the return of six aircraft and two General Electric CT7-9B engines by one of the Company's customers when it ceased operations in 2014.

The Company's other taxes expense increased by \$0.3 million in the third quarter of 2014 compared to the same period in 2013 as a result of the accrual of goods and services tax related to four of the Company's aircraft that are leased to a customer in Papua New Guinea.

Nine months ended September 30, 2014 compared to the nine months ended September 30, 2013

The Company recorded a net loss of \$11.8 million in the nine months ended September 30, 2014 compared to net income of \$9.2 million in the same period of 2013, primarily as a result of recording impairment charges totaling \$18.2 million for its seven Fokker 100 aircraft, as well as an impairment charge of \$0.3 million for one of its Fokker 50 aircraft in the 2014 period. There were no recorded impairment charges of long-lived assets during the first nine months of 2013.

Quarterly operating lease revenue increased 15% from \$13.9 million in the first nine months of 2013 to \$16.0 million in the first nine months of 2014, primarily as a result of increases in operating lease revenue from assets purchased during 2013 and 2014. The effect of these increases was partially offset by the effect of assets that were on lease in the 2013 period but off lease in the 2014 period and asset sales during 2013 and 2014.

Maintenance reserves revenue decreased 76% from \$13.9 million in the first nine months of 2013 to \$3.4 million in the first nine months of 2014. The amount recorded in the 2013 period was received from the prior lessee of two of the Company's aircraft when the leases were assigned to a new lessee in 2012 and recognized as maintenance reserves revenue upon termination of those leases in the first quarter of 2013, and from maintenance reserves retained at lease end for three other aircraft. The amount recorded in the 2014 period represents maintenance reserves retained at lease end when seven aircraft were returned to the Company.

During the first nine months of 2014, the Company recorded net gains totaling \$3.0 million related to the sale of seven aircraft and an aircraft engine, as compared to the nine months ended September 30, 2013, when the Company recorded net gains of \$4.1 million related to the sale of four aircraft and the finance lease of an engine.

During the nine months ended September 30, 2014 and 2013, the Company added equipment to its lease portfolio of approximately \$50.3 million and \$6.6 million, respectively. The Company sold equipment with a book value of approximately \$19.2 million and \$6.3 million during the nine months ended September 30, 2014 and 2013, respectively. As a result of the timing of these asset acquisitions and sales, as well as changes in residual value assumptions from year to year, depreciation and management fees in the first nine months of 2014 increased by 4% and 20%, respectively, over the previous year.

The average net book value of assets held for lease during the nine months ended September 30, 2014 and 2013 was approximately \$172.9 million and \$141.5 million, respectively, representing an increase of 22%. The average portfolio utilization during the nine months ended September 30, 2014 and 2013 was 80% and 76%, respectively.

The Company's maintenance expense increased by 19% from \$4.9 million in the first nine months of 2013 to \$5.8 million in the same period of 2014, primarily as a result of an increase in maintenance performed by the Company on off-lease aircraft.

The Company's interest expense increased by 25% from \$3.0 million in the first nine months of 2013 to \$3.8 million in the same period of 2014, primarily as a result of a higher average Credit Facility balance.

The Company's professional fees, general and administrative and other expenses increased from \$0.9 million in the first nine months of 2013 to \$1.5 million in the first nine months of 2014, primarily as a result of expenses incurred in connection with the return of six aircraft and two General Electric CT7-9B engines by one of the Company's customers when it ceased operations in the 2014 period.

The Company's other taxes expense increased by \$0.3 million in the third quarter of 2014 compared to the same period in 2014 as a result of the accrual of goods and services tax related to four of the Company's aircraft that are leased to a customer in Papua New Guinea.

Liquidity and Capital Resources

The Company is currently financing its assets primarily through debt financing and excess cash flows.

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(a)Credit Facility

During May 2014, the Company's \$130 million Credit Facility (the "Credit Facility") was increased to \$180 million and extended through May 31, 2019. The Credit Facility is provided by a syndicate of banks and is secured by all of the assets of the Company, including its aircraft and engine portfolio.

In November 2013, the Company obtained a waiver of compliance with a lessee concentration covenant under its Credit Facility agreement at the September 30, 2013 and December 31, 2013 calculation dates. The Company was in compliance with all covenants other than the waived covenant under the Credit Facility agreement at December 31, 2013.

Although the Company previously had letters of intent for the lease of five of its Fokker 100 aircraft, the prospective customers decided not to lease the aircraft during the second quarter of 2014. Therefore, at June 30, 2014, the Company reevaluated the recoverability of the net book value of these assets and consequently obtained current market value appraisals, which resulted in aircraft impairment charges totaling \$6.8 million being recorded for these aircraft during the second quarter of 2014. As a result of the impairment charges, the Company was out of compliance with a profitability covenant at June 30, 2014. In August 2014, the Company and the Credit Facility banks agreed to an amendment to the profitability covenant, which cured the June 30, 2014 non-compliance.

During the third quarter of 2014, based on management's assessment of the market for Fokker 100 aircraft and the estimated costs associated with preparing the Company's five off-lease Fokker 100 aircraft for re-lease, the Company recorded additional impairment charges of \$8.5 million for these aircraft to write them down to their estimated liquidation values. The Company also recorded an impairment charge of \$0.3 million for an off-lease Fokker 50 aircraft and reclassified these six aircraft as held for sale. The Company also recorded an impairment charge of \$2.9 million, based on the appraised market values for its two other Fokker 100 aircraft that were leased in September and October 2014.

As a result of the third quarter impairment charges, the Company was out of compliance with several of its Credit Facility covenants at September 30, 2014. In November 2014, the Company and the Credit Facility banks agreed to an amendment to the Credit Facility, which cured the September 30, 2014 non-compliance, revised the compliance requirements through September 30, 2015, decreased the amount of the Credit Facility to \$150 million due to the departure of two participant lenders, and decreased the maximum amount to which the Credit Facility can be expanded from \$200 million to \$180 million.

Based on its current projections, the Company believes that it will be in compliance with all of its Credit Facility covenants at future calculation dates. Although the Company believes that the assumptions it has made in forecasting its compliance with the Credit Facility covenants are reasonable in light of experience, actual results could deviate from such assumptions and there can be no assurance the Company's beliefs will prove to be correct. Among the more significant factors that could have an impact on the accuracy of the Company's covenant compliance forecasts are (i) unanticipated decreases in the market value of the Company's assets, or in the rental rates deemed achievable for such assets that cause the Company to record an impairment charge against earnings; (ii) lessee non-compliance with lease obligations, (iii) inability to locate new lessees for returned equipment within a reasonable remarketing period, or at a rent level consistent with projected rates for the asset, (iv) inability to locate and acquire a sufficient volume of additional assets at prices that will produce acceptable net returns, (v) increases in interest rates, or (vi) inability to timely dispose of off-lease assets at prices commensurate with their market value.

Although the Company believes it will continue to be in compliance with all of the Credit Facility covenants, there can be no assurance of such compliance and, in the event of any non-compliance, the Company will need to seek further waivers or amendment of applicable covenants from its lenders if such compliance failure is not timely cured. Any default under the Credit Facility, if not cured in the time permitted under the facility or waived by the

lenders, could result in foreclosure upon any or all of the assets of the Company.

For additional information regarding the Company's Credit Facility, refer to Note 5 to the Company's financial statements in Item 1 of this Quarterly Report on Form 10-Q.

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(b)Cash flow

The Company's primary sources of cash are (i) rent payments due under the Company's operating and finance leases, (ii) maintenance reserves billed monthly to lessees based on asset usage, and (iii) proceeds from the sale of aircraft and engines.

The Company's primary uses of cash are for purchase of aircraft and engines, maintenance expense and reimbursement to lessees from collected maintenance reserves, management fees, professional fees, insurance, and Credit Facility fees, interest and principal payments. The amount of interest paid by the Company depends on the outstanding balance of its Credit Facility, which carries a floating interest rate as well as an interest rate margin, and is therefore also dependent on changes in prevailing interest rates.

The timing and amount of the Company's payments for maintenance vary, depending on the timing of lessee-performed maintenance that is eligible for reimbursement, the aggregate amount of such claims and the timing and amount of maintenance incurred in connection with preparation of off-lease assets for re-lease to new customers. The Company's maintenance payments typically constitute a large portion of its cash needs, and the Company may from time to time borrow additional funds under the Credit Facility to provide funding for such payments.

Management believes that the Company will have adequate cash flow to meet its ongoing operational needs, including any required repayments under the Credit Facility due to borrowing base limitations, based upon its estimates of future revenues and expenditures, which include assumptions regarding (i) revenues for assets to be re-leased, (ii) required debt payments, (iii) interest rates, (iv) the cost and anticipated timing of maintenance to be performed and (v) timely use of proceeds of unused debt capacity toward additional acquisitions of income producing assets. There can be no assurance, however, that the Company's beliefs will prove to be correct.

Although the Company believes that the assumptions it has made in forecasting its cash flow are reasonable in light of experience, actual results could deviate from such assumptions. As discussed above, in "Liquidity and Capital Resources – (a) Credit Facility" above, there are a number of factors that may cause actual results to deviate from such forecasts.

(i)Operating activities

The Company's cash flow from operations decreased by \$3.7 million in the first nine months of 2014 compared to the same period in 2013. As discussed below, the change in cash flow was primarily a result of an increase in payments received for operating lease revenue as well as a decrease in payments for aircraft insurance, the effects of which were partially offset by decreases in payments received for maintenance reserves and increases in payments for maintenance, interest, management fees and professional fees and general and administrative expenses.

Payments for operating lease revenue and maintenance reserves

Payments received from lessees for rent increased by \$2.5 million in the first nine months of 2014 compared to the first nine months of 2013, primarily due to rent from assets purchased during late 2013 and early 2014. Payments received for maintenance reserves decreased by \$1.5 million in the first nine months of 2014 compared to the same period in 2013, primarily as a result of asset sales and returns, as well as lower utilization of some assets for which the Company collects maintenance reserves.

The Company is receiving no lease revenue for its assets that are currently off lease, which assets are comprised of five Fokker 100 aircraft, four Saab 340B Plus aircraft, one Fokker 50 aircraft, one General Electric CF34-8E5 engines, two General Electric CT7-9B engines and one Tay 650-15 engine. The Tay 650-15 engine is being held as a spare

and used in connection with required maintenance on the Company's Fokker 100 aircraft. The off-lease Fokker 100 and Fokker 50 aircraft are being held for sale and not lease.

Payments for maintenance

Payments for maintenance increased by \$1.7 million in the first nine months of 2014 compared to the first nine months of 2013, primarily as a result of an increase in maintenance costs for off-lease aircraft. The amount of payments for maintenance in future periods will depend on the amount and timing of maintenance paid as reimbursement to lessees for maintenance reserves claims, which are dependent upon utilization and required maintenance intervals, and maintenance paid for off-lease assets.

Payment for interest and management fees

Payments for interest and management fees increased by \$0.8 million and \$0.7 million, respectively, in the first nine months of 2014 compared to the same period of 2013 as a result of a higher Credit Facility balance and asset purchases.

Payment for professional fees, general and administrative and other expenses

Payments for professional fees, general and administrative and other expenses increased by \$0.8 million in the first nine months of 2014 compared to the same period in 2013 primarily as a result of expenses incurred in connection with the return of six aircraft and two engines by one of the Company's customers in the 2014 period when it ceased operations.

(ii) Investing activities

During the nine months ended September 30, 2014 and 2013, the Company received cash of \$16.0 million and \$8.2 million, respectively, from the sale of assets. During the same time periods, the Company used cash of \$47.3 million and \$6.6 million, respectively, for purchases and capital improvement of aircraft.

(iii) Financing activities

The Company borrowed \$43.9 million and \$4.0 million under the Credit Facility during the first nine months of 2014 and 2013, respectively. In these same time periods, the Company repaid \$13.2 million and \$7.3 million, respectively, of its total outstanding debt under the Credit Facility. Such repayments were funded by excess cash flow and the sale of assets. During the first nine months of 2014 and 2013, the Company paid \$2.4 million and \$2.1 million of fees related to the extension and administration of the Company's Credit Facility. Such fees are amortized over the term of the Credit Facility.

Outlook

(a) General

While certain areas of the world air carrier industry are now beginning to experience growth after a period of contraction following the global downturn of recent years, other areas of the world continue to experience slow recovery and failures of weaker air carrier competitors that were unable to survive the aftermath of the global downturn. Overall, the Company continues to experience a reduction in the number of aircraft and aircraft engines needed for operation by carriers in nearly all geographic areas, especially in Western Europe, as compared to periods before the global downturn.

The Company has identified three areas that could challenge the Company's growth and operating results by negatively affecting its collateral base and, therefore, its ability to access sources of financing:

- The Company could experience (i) a delay in remarketing its off-lease assets, as well as (ii) lower rental rates for assets that are remarketed. The Company expects that the customers for several of the leases that expire in 2015 will choose to return the assets rather than renew the leases, notwithstanding that any such customer may incur significant expenses to satisfy return conditions, and, in the future, additional customers may similarly choose to return their leased assets rather than renew the leases.
- Lessees that are located in low- or no- growth areas of the world carry heightened risk of an unanticipated lessee default. A lessee's default and the unscheduled return of an asset to the Company for remarketing could result not only in reduced operating lease revenue but also in unanticipated, unrecoverable expenses arising from the lessee's default on its maintenance and return condition obligations. The Company monitors the performance of all of its customers and has noted that several of the Company's customers continue to experience weakened operating results and have not yet achieved financial stability.
- Competition in the Company's market niche has increased recently as a result of new entrants to the acquisition and leasing market. The increased competition has put downward pressure on lease rates, resulting in lower margins.

(b) Operating Segments

The Company operates in one business segment, the leasing of regional aircraft to foreign and domestic regional airlines, and therefore does not present separate segment information for lines of business.

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At October 31, 2014, the dominant types of aircraft in the Company's portfolio of assets held for lease were as follows:

Model	Number owned	% of net book value
Bombardier Dash-8-300	8	20 %
Bombardier CRJ-700	3	19 %
Bombardier Dash-8-Q400	3	16 %
Bombardier CRJ-705	1	11 %
ATR 42-600	1	11 %

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For the month ended October 31, 2014, the Company's sources of operating lease revenue were from the following regions:

Region	Number of lessees	% of operating lease revenue
North America	3	32 %
Africa	2	23 %
Asia	3	18 %
Caribbean	1	13 %
Europe	2	11 %
Australia	1	3 %

#### (c) Remarketing Efforts

In October 2014, the Company sold a Saab 340A and a Saab 340B aircraft and re-leased a Saab 340B Plus aircraft and a Fokker 100 aircraft that were off lease as of September 30, 2014.

The Company is seeking remarketing opportunities for four Saab 340B Plus aircraft, a Fokker 50 aircraft, a General Electric CF34-8E5 engines and two General Electric CT7-9B engines.

Five of the Company's Fokker 100 aircraft are off lease. During the third quarter ended September 30, 2014, the Company recorded impairment provisions for these aircraft based on the Company's estimated liquidation value for the aircraft, in addition to impairment charges recorded at June 30, 2014. Additionally, the Company recorded an impairment loss on a Fokker 50 aircraft at September 30, 2014 to reflect its estimated recoverable value from sale. These aircraft were classified as held for sale at September 30, 2014 and the Company is seeking sales opportunities for them.

The Company is considering selling some or all of its other off-lease aircraft. The Company is analyzing the amount and timing of maintenance required to remarket the aircraft, the amount of which may differ significantly if the aircraft are sold rather than re-leased.

The lease for one of the Company's engines will expire during the remainder of 2014 and the Company believes that it is likely that it will be returned at lease-end.

#### (d) Credit Facility

During the second quarter of 2014, leases for five of the Company's Fokker 100 aircraft, for which the Company previously had letters of intent, were not signed, and the Company recorded aircraft impairment charges totaling \$6.8 million for these aircraft based on market value appraisals. As a result of the impairment charges, the Company was out of compliance with a profitability covenant at June 30, 2014. In August 2014, the Company and the Credit Facility banks agreed to an amendment to the profitability covenant, which cured the June 30, 2014 non-compliance.

During the third quarter of 2014, based on management's assessment of the market for Fokker 100 aircraft and the costs associated with preparing the Company's five off-lease Fokker 100 aircraft for re-lease, the Company recorded additional impairment charges of \$8.5 million for these aircraft to write them down to an estimated liquidation value. The Company also recorded an impairment charge of \$0.3 million for an off-lease Fokker 50 aircraft and reclassified these six aircraft as held for sale. The Company also recorded an impairment charge of \$2.9 million for

its two other Fokker 100 aircraft based on the appraised values of the aircraft.

As a result of the third quarter impairment charges, the Company was out of compliance with several of its Credit Facility covenants at September 30, 2014. In November 2014, the Company and the Credit Facility banks agreed to an amendment to the Credit Facility, which cured the September 30, 2014 non-compliance, revised the compliance requirements through September 30, 2015, decreased the amount of the Credit Facility to \$150 million due to the departure of two participant lenders, and decreased the maximum amount to which the Credit Facility can be expanded from \$200 million to \$180 million.

Based on its current projections, the Company believes that it will be in compliance with all of its Credit Facility covenants at future calculation dates. The Company also believes that available borrowings under the Credit Facility will be sufficient to meet its continuing obligations and to fund anticipated acquisitions. However, there can be no assurance the Company's beliefs will prove to be correct.

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## Factors that May Affect Future Results

**Noncompliance with Credit Facility Financial Covenants.** The Company's use of debt as the primary form of acquisition financing subjects the Company to increased risks associated with leveraging. In addition to payment obligations, the Credit Facility agreement includes financial covenants, including some requiring the Company to have positive earnings, meet minimum net worth standards and be in compliance with certain other financial ratios.

As discussed above in "Outlook – Credit Facility," the Company was out of compliance with a number of covenants under its Credit Facility at September 30, 2014 due to impairment charges recorded with respect to its Fokker 100 and Fokker 50 aircraft. In November 2014, the Company and the Credit Facility banks agreed to an amendment to the Credit Facility, which cured the September 30, 2014 non-compliance, revised the compliance requirements through September 30, 2015, decreased the amount of the Credit Facility to \$150 million due to the departure of two participant lenders, and decreased the maximum amount to which the Credit Facility can be expanded from \$200 million to \$180 million.

Although the Company believes it will continue to be in compliance with all of the Credit Facility covenants, there can be no assurance of such compliance, and in the event of any non-compliance, the Company will need to seek further waivers or amendment of applicable covenants from its lenders if such compliance failure is not timely cured. Any default under the Credit Facility, if not cured in the time permitted under the facility or waived by the lenders, could result in foreclosure upon any or all of the assets of the Company.

**Ownership Risks.** The Company's leases are typically less than the entire anticipated remaining useful life of the leased assets. The Company's ability to recover its investment in an asset subject to such a lease is dependent upon the Company's ability to profitably re-lease or sell the asset after the expiration of the lease term. The Company's ability to re-lease or sell the asset is dependent on worldwide economic conditions, general aircraft market conditions, regulatory changes that may make an asset's use more expensive or preclude use due to the age of the aircraft or unless the asset is modified, changes in the supply or cost of aircraft equipment and technological developments that cause the asset to become obsolete. If the Company is unable to remarket its assets on favorable terms when the leases for such assets expire, the Company's financial condition, cash flow, ability to service debt and results of operations could be adversely affected.

The Company acquires used aircraft equipment. The market for used aircraft equipment has been cyclical, and generally reflects economic conditions and the strength of the travel and transportation industry. The demand for and value of many types of used aircraft in the recent past has been depressed by such factors as airline financial difficulties, the number of new aircraft on order and the number of aircraft coming off lease, as well as introduction of new aircraft models and types that may be more technologically advanced, more fuel efficient and/or less costly to maintain and operate. Values may also increase for certain aircraft types that become desirable based on market conditions and changing airline capacity.

In addition, a successful investment in an asset subject to a lease depends in part upon having the asset returned by the lessee in the condition as required under the lease. Each lease typically obligates a customer to return an asset to the Company in a specified condition, which generally requires it be returned in equal or better condition than at delivery to the lessee. If the lessee becomes insolvent during the term of its lease and the Company has to repossess the asset, it is unlikely that the lessee will have the financial ability to meet these return obligations and it is likely that the Company would be required to expend funds in excess of any maintenance reserves collected to return the asset to a remarketable condition. If the lessee files for bankruptcy and rejects the aircraft lease, although the lessee is required to return the aircraft, the lessee is relieved from all further obligations under the lease, including the obligation to return the aircraft in the condition required under the lease. In that case, it is also likely that the Company would be required to expend funds in excess of any maintenance reserves collected to return the asset to a remarketable condition.

Several of the Company's leases do not require payment of monthly maintenance reserves, which serve as the lessee's advance payment for its future repair and maintenance obligations. If repossession due to lessee default or bankruptcy occurs under such a lease, the Company will be left with the costs of unperformed repair and maintenance under the applicable lease and the Company may incur an unanticipated expense in order to re-lease or sell the asset.

Furthermore, the occurrence of unexpected adverse changes that impact the Company's estimates of expected cash flows generated from an asset may result in an asset impairment charge against the Company's earnings. The Company periodically reviews long-term assets for impairment, in particular, when events or changes in circumstances indicate the carrying value of an asset may not be recoverable. An impairment charge is recorded when the carrying amount of an asset is estimated to be not recoverable and exceeds its fair value. The Company recorded impairment charges for some of its aircraft in the second and third quarters of 2014 and may be required to record asset impairment charges in the future as a result of a prolonged weak economic environment, challenging market conditions in the airline industry, events related to particular lessees, assets or asset types or other factors affecting the value of aircraft or engines.

**Lessee Credit Risk.** The Company carefully evaluates the credit risk of each customer and attempts to obtain a third party guaranty, letters of credit or other credit enhancements, if it deems them necessary in addition to customary security deposits. There can be no assurance, however, that such enhancements will be available, or that, if obtained, will fully protect the Company from losses resulting from a lessee default or bankruptcy.

If a lessee that is a certified U.S. airline were in default under a lease and sought protection under Chapter 11 of the United States Bankruptcy Code, Section 1110 of the Bankruptcy Code would automatically prevent the Company from exercising any remedies against such lessee for a period of 60 days. After the 60-day period had passed, the lessee would have to agree to perform the lease obligations and cure any defaults, or the Company would have the right to repossess the equipment. However, this procedure under the Bankruptcy Code has been subject to significant litigation, and it is possible that the Company's enforcement rights may be further adversely affected by a bankruptcy filing by a defaulting lessee.

Several of the Company's customers have experienced significant financial difficulties, become insolvent, or have been declared or have filed for bankruptcy. Such an insolvency or bankruptcy usually discharges all unpaid obligations of the customer existing at the time of the filing, resulting in a total loss of those receivables. The Company closely monitors the performance of all of its lessees and its risk exposure to any lessee that may be facing financial difficulties, in order to guide decisions with respect to such lessee that would mitigate losses in the event the lessee is unable to meet or rejects its lease obligations. There can be no assurance that additional customers will not become insolvent or file for bankruptcy or that the Company will be able to mitigate any of the resultant losses.



**Risks Related to Regional Air Carriers.** The Company's continued focus on its customer base of regional air carriers subjects the Company to additional risks. Some of the lessees in the regional air carrier market are companies that are start-up, low-capital, and/or low-margin operators. Often, the success of such carriers depends on contractual arrangements with major trunk carriers or franchises from governmental agencies that provide subsidies for operating essential air routes, both of which may be subject to termination or cancellation on short notice. Regional carriers, even if financially strong, that are owned by, or are a sister corporation of, an established major carrier can also be swept into bankruptcy if the major carrier files for bankruptcy or becomes insolvent. Four of the Company's regional air carrier customers filed for bankruptcy in 2012 and 2013, and in May 2014, a Thai regional carrier that leased six aircraft and two engines from the Company ceased operations.

**Credit Facility Debt Limitations.** Under the Credit Facility, the amount available to be borrowed is limited to the total amount of asset-specific advance rates. Lessee arrearages or asset off-lease periods may reduce the advance rate for the related assets and, therefore, the permitted borrowing under the facility. Amounts subject to deferral agreements also reduce the borrowing base. The Company believes it will have sufficient cash funds to make any required principal repayment that arises due to any such borrowing base limitations.

**Availability of Financing.** The Company's continued growth will depend on its ability to continue to obtain capital, either through debt or equity financings. There can be no assurance that the Company will succeed in obtaining capital in the future at terms favorable to the Company.

**General Economic Conditions and Lowered Demand for Travel.** The Company's business is dependent upon general economic conditions and the strength of the travel and transportation industry. The industry is continuing to experience financial difficulty due to the slow recovery in the global economy. The spread of a disease epidemic, the threat or execution of a terrorist attack against aviation, a worsening financial/bank crisis in Europe, a natural event that interrupts air traffic, military conflict, political crises or other events that cause a prolonged spike in fuel prices, or other like events could exacerbate an already weakened condition and lead to widespread failures in the air carrier industry. If lessees experience financial difficulties and are unable to meet lease obligations, this will, in turn, negatively affect the Company's financial performance.

Airline reductions in capacity in response to lower passenger loads have resulted in reduced demand for aircraft and aircraft engines and a corresponding decrease in market lease rental rates and aircraft values for many aircraft types. This reduced market value could affect the Company's results if the market value of an asset or assets in the Company's portfolio falls below carrying value, and the Company determines that a write-down of the value on its balance sheet is appropriate. Furthermore, if older, expiring leases are replaced with leases at decreased lease rates, the lease revenue from the Company's existing portfolio is likely to decline, with the magnitude of the decline dependent on the length of the downturn and the depth of the decline in market rents.

Economic downturns can affect certain regions of the world more than others. As the Company's portfolio is not entirely globally diversified, a localized downturn in one of the key regions in which the Company leases assets could have a significant adverse impact on the Company. The Company's significant sources of operating lease revenue by region are summarized in "Outlook - Operating Segments," above.

Over the last few years, several of the Company's customers have experienced financial difficulties arising from a combination of the weakened air carrier market and their own unique financial circumstances and have requested and been granted deferral of certain overdue and/or future rental or reserve payment obligations. It is possible that the Company may enter into additional deferral agreements if the current weakened air carrier environment continues. When a customer requests a deferral of lease obligations, the Company evaluates the lessee's financial plan, the likelihood that the lessee can remain a viable carrier, and whether the deferral will be repaid according to the agreed schedule. The Company may elect to record the deferred rent and reserve payments from the lessee on a cash basis, which could have a material effect on the Company's financial results in the applicable periods.

**International Risks.** The Company leases assets primarily in overseas markets. Leases with foreign lessees, however, may present different risks than those with domestic lessees. Most of the Company's expected growth is outside of the United States.

A lease with a foreign lessee is subject to risks related to the economy of the country or region in which such lessee is located, which may be weaker than the U.S. economy. An economic downturn in a particular country or region may impact a foreign lessee's ability to make lease payments, even if the U.S. and other foreign economies remain stable.

Foreign lessees are subject to risks related to currency conversion fluctuations. Although the Company's current leases are all payable in U.S. dollars, the Company may agree in the future to leases that permit payment in foreign currency, which would subject such lease revenue to monetary risk due to currency fluctuations. In addition, if the Company undertakes certain obligations under a lease to contribute to a repair or improvement and if the work is performed in a foreign jurisdiction and paid for in foreign currency, currency fluctuations resulting in a weaker dollar between the time such agreement is made and the time payment for the work is made may result in an unanticipated increase in U.S. dollar-denominated cost for the Company.

Even with U.S. dollar-denominated lease payment provisions, the Company could still be affected by a devaluation of the lessee's local currency that would make it more difficult for a lessee to meet its U.S. dollar-denominated payments, increasing the risk of default of that lessee, particularly if its revenue is primarily derived in the local currency.

Foreign lessees that operate internationally may also face restrictions on repatriating foreign revenue to their home country. This could create a cash flow crisis for an otherwise profitable carrier, affecting its ability to meet its lease obligations.

Non-U.S. lessees are not subject to U.S. bankruptcy laws, although there may be debtor protection similar to U.S. bankruptcy laws available in some jurisdictions. Certain countries do not have a central registration or recording system with which to locally establish the Company's interest in equipment and related leases. This could make it more difficult for the Company to recover an aircraft in the event of a default by a foreign lessee. In any event, collection and enforcement may be more difficult and complicated in foreign countries.

Finally, ownership of a leased asset operating in a foreign country and/or by a foreign carrier may subject the Company to additional tax liabilities that are not present with aircraft operated in the United States. Depending on the jurisdiction, laws governing such tax liabilities may be complex, not well formed or not uniformly enforced. In such jurisdictions, the Company may decide to take an uncertain tax position based on the best advice of the local tax experts it engages, which position may be challenged by the taxing authority. If the taxing authority later assesses a liability, the Company may be required to pay penalties and interest on the assessed amount, which penalties and interest would not give rise to a corresponding foreign tax credit on the Company's U.S. tax return.

**Concentration of Lessees and Aircraft Type.** For the month ended October 31, 2014, the Company's five largest customers accounted for a total of approximately 73% of the Company's monthly lease revenue. A lease default by or collection problem with one or a combination of any of these significant customers could have a disproportionate negative impact on the Company's financial results and borrowing base under the Credit Facility, and, therefore, the Company's operating results are especially sensitive to any negative developments with respect to these customers in terms of lease compliance or collection. In addition, if the Company's revenues become overly concentrated in a small number of lessees, the Company could fail to comply with certain financial covenants in its Credit Facility related to customer concentration. In the event of any such failure to be in compliance, the Company will need to seek waivers or amendment of the applicable covenants from its lenders if such compliance failure is not timely cured. Any default under the Credit Facility, if not cured in the time permitted under the Credit Facility or waived by the lenders, could result in foreclosure upon any or all of the assets of the Company.

The dominant types of aircraft in the Company's portfolio are summarized in "Outlook - Operating Segments," above. A change in the desirability and availability of any of these types of aircraft, which would in turn affect valuations of such aircraft, would have a disproportionately significant impact on the Company's portfolio value. Such aircraft type concentration would diminish if the Company acquires additional assets of other types. Conversely, acquisition of these types of aircraft will increase the Company's risks related to its concentration of those aircraft types.

**Investment in New Aircraft Types and Engines.** The Company intends to continue to focus solely on regional aircraft and engines. Although the Company has traditionally invested in a limited number of types of turboprop aircraft and engines, the Company has also acquired several types of regional jet aircraft, as well as regional jet aircraft engines, and may continue to seek acquisition opportunities for new types and models of aircraft and engines used in the Company's targeted customer base of regional air carriers. Acquisition of aircraft types and engines not previously acquired by the Company entails greater ownership risk due to the Company's lack of experience managing those assets. The Company believes, however, that the overall industry experience of JMC's personnel and its technical resources should permit the Company to effectively manage such new aircraft types and engines. Further, the broadening of the asset types in the aircraft portfolio may have a benefit of diversifying the Company's portfolio (see "Factors That May Affect Future Results – Concentration of Lessees and Aircraft Type," above).

**Engine Leasing Risk.** The Company currently has five engines in its portfolio, making up 6% of the Company's total net book value of aircraft and aircraft engines held for lease. The Company may from time to time lease one or more of these engines under industry standard short-term engine leases, which place the risk of an engine failure not caused by lessee negligence or foreign object damage upon the lessor. It is not economically practicable for an engine lessor to insure against that risk. If an engine failure occurs and is not covered by a manufacturer's warranty or is not otherwise caused by circumstances that the lessee is required to cover, the Company's investment in the engine could be a significant loss or the Company might incur a significant maintenance expense.

**Interest Rate Risk.** The Credit Facility carries a floating interest rate based upon short-term interest rate indices. Lease rates typically, but not always, move over time with interest rates, but market demand and numerous other asset-specific factors also affect lease rates. Because the Company's typical lease rates are fixed at lease origination, interest rate changes during the lease term have no effect on existing lease rental payments. Therefore, if interest rates rise significantly and there is relatively little lease origination by the Company following such rate increases, the Company could experience decreased net income as additional interest expense outpaces revenue growth. Further, even if significant lease origination occurs following such rate increases, other contemporaneous aircraft market forces may result in lower or flat rental rates, thereby decreasing net income.

**Reliance on JMC.** All management of the Company is performed by JMC under the twenty-year Management Agreement between the Company and JMC that expires in April of 2018 and provides for an asset-based management fee. JMC is not a fiduciary of the Company or its stockholders. The Company's Board of Directors (the "Board") has ultimate control and supervisory responsibility over all aspects of the Company and owes fiduciary duties to the

Company and its stockholders. The Board has no control over the internal operations of JMC, but the Board does have the ability and responsibility to manage the Company's relationship with JMC and the performance of JMC's obligations to the Company under the Management Agreement, as it would have for any third party service provider to the Company. While JMC may not owe any fiduciary duties to the Company by virtue of the Management Agreement, all of the officers of JMC are also officers of the Company, and in that capacity owe fiduciary duties to the Company and its stockholders. In addition, certain officers of the Company hold significant ownership positions in the Company and JHC, the parent company of JMC.

The Management Agreement may be terminated if JMC defaults on its obligations to the Company. However, the agreement provides for liquidated damages in the event of its wrongful termination by the Company. Certain directors of the Company are also directors of JMC and, as discussed above, the officers of the Company are also officers of JMC and certain officers hold significant ownership positions in both the Company and JHC, the holding company for JMC. Consequently, the directors and officers of JMC may have a conflict of interest in the event of a dispute between the Company and JMC. Although the Company has taken steps to prevent conflicts of interest arising from such dual roles, such conflicts may still occur.

**Management Fee Structure.** All decisions regarding acquisitions and disposal of aircraft from the Company's portfolio are made by JMC. JMC is paid a management fee based on the net asset value of the Company's portfolio. It may also receive a one-time asset acquisition fee upon purchase of an asset by the Company, and a one-time remarketing fee in connection with the sale or re-lease of an asset. Optimization of the results of the Company depends on timing of the acquisition, lease yield on the acquired assets, and re-lease or sale of its portfolio assets. Under the current management fee structure, a larger volume of acquisitions generates acquisition fees and also increases the periodic management fee by increasing the size of the aircraft portfolio. Since the Company's current business strategy involves continued growth of its portfolio and a "buy and hold" strategy, a compensation structure that results in greater compensation with an increased portfolio size is consistent with that strategy. The compensation structure does, nonetheless, create a situation where a decision by JMC for the Company to forego an asset transaction deemed to be an unacceptable business risk due to the lessee or the aircraft type is in conflict with JMC's own pecuniary interest. As a result, the compensation structure could act to incent greater risk-taking by JMC in asset acquisition decision-making. The Company has established objective target guidelines for yields on acquired assets. Further, the Company's Board, including a majority of the outside independent directors, must approve any acquisition that involves a new asset type. While the Company currently believes the foregoing are effective mitigating factors against undue compensation-incented risk-taking by JMC, there is no assurance that such mechanisms can entirely and effectively eliminate such risk.

**Government Regulation.** There are a number of areas in which government regulation may result in costs to the Company. These include aircraft registration safety requirements, required equipment modifications, maximum aircraft age, and aircraft noise requirements. Although it is contemplated that the burden and cost of complying with such requirements will fall primarily upon lessees of equipment, there can be no assurance that the cost will not fall on the Company. Furthermore, future government regulations could cause the value of any non-complying equipment owned by the Company to decline substantially.

**Competition.** The aircraft leasing industry is highly competitive. The Company competes with aircraft manufacturers, distributors, airlines and aircraft operators, equipment managers, leasing companies, equipment leasing programs, financial institutions and other parties engaged in leasing, managing or remarketing aircraft, many of which have significantly greater financial resources. Nevertheless, the Company believes that it is competitive because of JMC's experience and operational efficiency in identifying and obtaining financing for the transaction types desired by regional air carriers. This market segment, which is characterized by transaction sizes of less than \$10 million and in many cases customers that are private companies without well-established third party credit ratings, is not well served by the Company's larger competitors. JMC has developed a reputation as a global participant in this segment of the market, and the Company believes that JMC's reputation benefits the Company. There is, however, no assurance that competition from larger aircraft leasing companies will not increase significantly or that JMC's reputation will continue to be strong in this market segment.

**Casualties, Insurance Coverage.** The Company, as owner of transportation equipment, may be named in a suit claiming damages for injuries or damage to property caused by its assets. As a triple-net lessor, the Company is generally protected against such claims, since the lessee would be responsible for, insure against and indemnify the Company for such claims. A "triple net lease" is a lease under which, in addition to monthly rental payments, the lessee is generally responsible for the taxes, insurance and maintenance and repair of the aircraft arising from the use and operation of the aircraft during the term of the lease. Although the United States Aviation Act may provide some protection with respect to the Company's aircraft assets, it is unclear to what extent such statutory protection would be available to the Company with respect to most of the Company's assets, which are operated in foreign countries where such provisions of the United States Aviation Act may not apply.

The Company's leases generally require a lessee to insure against likely risks of loss or damage to the leased asset, and liability to passengers and third parties pursuant to industry standard insurance policies and require lessees to provide insurance certificates documenting the policy periods and coverage amounts. The Company tracks receipt of the certificates and calendars their expiration dates. Prior to the expiration of an insurance certificate, if a replacement certificate has not been received, the Company reminds the lessee of its obligation to provide current insurance certificates to avoid a default under the lease.

Despite these requirements and procedures, there may be certain cases where the loss is not entirely covered by the lessee or its insurance. The possibility of such an event is remote, but any such uninsured loss with respect to the equipment or insured loss for which insurance proceeds are inadequate might result in a loss of invested capital in and any profits anticipated from, such equipment, as well as a potential claim directly against the Company.

**Compliance with Future Environmental Regulations.** Compliance with future environmental regulations may harm the Company's business. Many aspects of aircraft operations are subject to increasingly stringent environmental regulations, and growing concerns about climate change may result in the imposition by the U.S and foreign governments of additional regulation of carbon emissions, aimed at either requiring adoption of technology to reduce the amount of carbon emissions or putting in place a fee or tax system on carbon emitters. It is likely that any such regulation will be directed at the Company's customers, as operators of aircraft, or at the Company, as owners of aircraft. Under the Company's triple-net lease arrangements, the Company would likely shift responsibility for compliance to its lessees, but there might be some costs of regulation that the Company could not shift and would itself have to bear. Although it is not expected that the costs of complying with current environmental regulations will

have a material adverse effect on the Company's financial position, results of operations, or cash flows, no assurance can be given that the costs of complying with environmental regulations adopted in the future will not have such an effect.

**Cyber-Security Risks.** The Company believes that it has sufficient cyber-security measures in place commensurate with the risks to the Company of a successful cyber-attack or breach of security. The Company's main vulnerability to a cyber-attack would be interruption of the Company's email communications internally and with third parties, and loss of document sharing between the Company's offices and remote workers. Such an attack could temporarily impede the efficiency of the Company's operations; however, the Company believes that sufficient replacement mechanisms exist in the event of such an interruption that there would not be a material adverse financial impact on the Company's business.

**Warrants.** As part of a subordinated debt financing, which was fully repaid in December of 2011, the Company issued warrants to purchase up to 81,224 shares of the Company's common stock that are currently exercisable (and expire on December 31, 2015) and represent approximately 5% of the post-exercise fully diluted capitalization of the Company. The exercise price of the warrants is \$8.75 per share. If the warrants to purchase shares are exercised at a time when the exercise price is less than the market price of the Company's common stock, there will be dilution to the existing holders of common stock. This dilution of the Company's common stock could depress its trading price.

**Possible Volatility of Stock Price.** The market price of the Company's common stock may be subject to fluctuations following developments relating to the Company's operating results, changes in general conditions in the economy, the financial markets, the airline industry, changes in accounting principles or tax laws applicable to the Company or its lessees, or other developments affecting the Company, its customers or its competitors, or arising from other investor sentiment unknown to the Company. Because the Company has a relatively small capitalization of approximately 1.5 million shares outstanding, there is a correspondingly limited amount of trading and float of the Company's shares. Consequently, the Company's stock price is more sensitive to a single large trade or a small number of simultaneous trades along the same trend than a company with larger capitalization and higher trading volume and float.

### Item 3. Quantitative and Qualitative Disclosures About Market Risk.

This report does not include information described under Item 305 of Regulation S-K pursuant to the rules of the Securities and Exchange Commission that permit "smaller reporting companies" to omit such information.

### Item 4. Controls and Procedures.

**CEO and CFO Certifications.** Attached as exhibits to this Quarterly Report on Form 10-Q (the "Report") are certifications of the Company's Chief Executive Officer (the "CEO") and the Company's Chief Financial Officer (the "CFO"), which are required pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (the "Section 302 Certifications"). This section of the Report includes information concerning the evaluation of disclosure controls and procedures referred to in the Section 302 Certifications and this should be read in conjunction with the Section 302 Certifications for a more complete understanding of the topics presented.

**Evaluation of the Company's Disclosure Controls and Procedures.** Disclosure controls and procedures ("Disclosure Controls") are controls and other procedures that are designed to ensure that information required to be disclosed in the Company's reports filed under the Securities Exchange Act of 1934, such as this Report, is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission and that such information is accumulated and communicated to the Company's management, including the CEO and CFO, as appropriate, to allow timely decisions regarding required disclosure.

The Company's management, with the participation of the CEO and CFO, evaluated the effectiveness of the design and operation of the Company's Disclosure Controls and concluded that the Company's Disclosure Controls were effective as of September 30, 2014.

Changes in Internal Control Over Financial Reporting. No change in the Company's internal control over financial reporting occurred during the fiscal quarter ended September 30, 2014 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II  
OTHER INFORMATION

## Item 6.Exhibits

Exhibit Number	Description
10.20	Modification and Limited Waiver to Second Amended and Restated Loan and Security Agreement, dated as of August 26, 2014, among the Company, MUFG Union Bank, N.A., California Bank and Trust, U.S. Bank National Association, Umpqua Bank, First Bank, and Cathay Bank, incorporated by reference to Exhibit 10.1 of the Company's report on Form 8-K filed with the Securities and Exchange Commission on September 2, 2014
10.21	Modification and Limited Waiver to Second Amended and Restated Loan and Security Agreement, dated as of November 13, 2014, among the Company, MUFG Union Bank, N.A., California Bank and Trust, U.S. Bank National Association, Umpqua Bank, First Bank, and Cathay Bank
31.1	Certification of Neal D. Crispin, Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Toni M. Perazzo, Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1*	Certification of Neal D. Crispin, Chief Executive Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2*	Certification of Toni M. Perazzo, Chief Financial Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS	XBRL Instance Document
101.SCH	XBRL Schema Document
101.CAL	XBRL Calculation Linkbase Document
101.LAB	XBRL Label Linkbase Document
101.PRE	XBRL Presentation Linkbase Document
101.DEF	XBRL Definition Linkbase Document

\* These certificates are furnished to, but shall not be deemed to be filed with, the Securities and Exchange Commission.



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.

Date: November 14, 2014

AEROCENTURY CORP.

By: /s/ Toni M. Perazzo  
Name: Toni M. Perazzo  
T i t l e : S e n i o r V i c e  
President-Finance and  
Chief Financial Officer