AEROCENTURY CORP
Form 10-K
March 12, 2015

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2014

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

For the transition period from ____________ to ____________

Commission File Number: 001-13387

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

Delaware	94-3263974
(State or Other Jurisdiction of Incorporation or Organization)	(IRS Employer Identification No.)

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

Registrant's telephone number, including area code: (650) 340-1888

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, par value $0.001 per share	NYSE MKT Exchange

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes o No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.
Yes o No x

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

Yes x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate 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 to submit and post such files).
Yes x No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

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 o Accelerated filer o
Non-accelerated filer o Smaller reporting company x

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates (based upon the closing price as of June 30, 2014) was $15,332,400.

The number of shares of the Registrant's Common Stock outstanding as of March 12, 2015 was 1,543,257.

DOCUMENTS INCORPORATED BY REFERENCE

Part III of this Annual Report on Form 10-K incorporates information by reference from the Registrant's Proxy Statement for its 2015 Annual Meeting of Stockholders. Except as expressly incorporated by reference, the Registrant's Proxy Statement shall not be deemed to be a part of this Annual Report on Form 10-K.

PART I
FINANCIAL INFORMATION

Forward Looking Statements

This Annual Report on Form 10-K 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 I, Item 1, "Business of the Company," that the Company can purchase assets at an appropriate price and maintain an acceptable overall on-lease rate for the Company's assets; and that it is able and willing to enter into transactions with a wider range of lessees than would be possible for traditional, large lending institutions and leasing companies; (ii) in Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations – Liquidity and Capital Resources" that the Company will be in compliance with all of its credit facility covenants at future calculation dates; and 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; (iii) in Part II, Item 7, "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 under several of the leases that expire in 2015 will choose to return the assets; that three of the Company's aircraft will be returned at lease-end in 2015 after meeting the return conditions of the leases; that the leases for the remaining four aircraft will be extended; and that the Company will be in compliance with all of its Credit Facility covenants at future calculation dates; that available borrowings under the Credit Facility will be sufficient to meet its continuing obligations and, if it is expanded to the maximum of $180 million, to fund anticipated acquisitions; (v) in Part II, Item 7, "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 arises due to borrowing base limitations; that most of the Company's growth will be outside North America; 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 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; that its main vulnerability would be interruption to email communication, loss of archives and loss of document sharing; and that sufficient replacement mechanisms exist such 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.

Item 1.Business.

Business of the Company

AeroCentury Corp., a Delaware corporation incorporated in 1997 (the “Company”), typically acquires used regional aircraft and aircraft engines for lease to regional carriers worldwide.

The business of the Company is managed by JetFleet Management Corp. ("JMC"), pursuant to a management agreement (the “Management Agreement”) with JMC. JMC 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.

Since its formation, the Company has been engaged in the business of investing in used regional aircraft equipment leased to foreign and domestic regional air carriers. The Company’s principal business objective is to increase stockholder value by acquiring aircraft assets and managing those assets in order to provide a return on investment through lease revenue and, eventually, sale proceeds. The Company strives to achieve its business objective by reinvesting cash flow and using short-term and long-term debt and/or equity financing.

The Company’s success in achieving its objective depends in large part on its success in three areas: asset selection, lessee selection and obtaining financing for acquisition of aircraft and engines.

The Company typically acquires assets in one of three ways. The Company may purchase an asset already subject to a lease and assume the rights and obligations of the seller, as lessor under the existing lease. Additionally, the Company may purchase an asset from an air carrier and lease it back to the air carrier. Finally, the Company may purchase an asset from a seller and then immediately enter into a new lease for the aircraft with a third party lessee. In this last case, the Company typically does not purchase an asset unless a potential lessee has been identified and has committed to lease the asset. Occasionally, the Company may also acquire an asset for which it does not have a potential lessee.

Although the Company has generally targeted used regional aircraft and engines with purchase prices between $3 million and $10 million, and lease terms of less than five years, in 2013 and 2014, the Company acquired six regional jets and a new ATR 42-600 aircraft with purchase prices and lease terms exceeding those of previously-acquired aircraft. In determining assets for acquisition, the Company evaluates, among other things, the type of asset, its current price and projected future value, its versatility or specialized uses, the current and projected availability of and demand for that asset, and the type and number of future potential lessees. Because JMC has extensive experience in purchasing, leasing and selling used regional aircraft and engines, the Company believes it can purchase these assets at an appropriate price and maintain an acceptable overall on-lease rate for the Company’s assets.

In order to improve the remarketability of an aircraft after expiration of a lease, the Company’s leases generally contain provisions that require lessees to return the aircraft in a condition that allows the Company to expediently re-lease or sell the aircraft, or pay sufficient amounts based on usage under the lease to cover any maintenance or overhaul of the aircraft required to bring the aircraft to such a state.

When considering whether to enter into transactions with a lessee, the Company generally reviews the lessee’s creditworthiness, growth prospects, financial status and backing; the experience of its management; and the impact of legal and regulatory matters in the lessee's market, all of which are weighed in determining the lease terms offered to the lessee. In addition, it is the Company’s policy to monitor the lessee’s business and financial performance closely throughout the term of the lease, and, if requested, provide assistance drawn from the experience of the Company’s management in many areas of the air carrier industry. Because of its “hands-on” approach to portfolio management, the Company believes it is able and willing to enter into transactions with a wider range of lessees than would be possible for traditional, large lending institutions and leasing companies.

The Company has funded its asset acquisitions primarily through debt financing supplemented by free cash flow. The Company’s primary source of debt financing has been a secured credit facility. The Company's current credit facility ("Credit Facility") is provided by a syndicate of banks, with MUFG Union Bank, N.A. as agent, and in May 2014, the term was extended to May 31, 2019.

Working Capital Needs

The Company’s portfolio of assets has historically generated revenues that have exceeded the Company’s cash expenses, which consist mainly of management fees, maintenance costs, principal and interest payments on debt, professional fees, and insurance premiums.

The management fees paid by the Company to JMC are based upon the size of the Company’s asset pool. Maintenance costs for off-lease aircraft are recognized as expenses as incurred, while reimbursement of lessee maintenance costs from previously collected maintenance reserves reduce the Company's maintenance reserves liability. Interest expense is dependent on both the balance of the Company’s indebtedness and applicable interest rates. Professional fees are paid to third parties for expenses not covered by JMC under the Management Agreement. Insurance expense includes amounts paid for directors and officers insurance, as well as product liability insurance and aircraft hull insurance for periods when an aircraft is off lease.

So long as the Company succeeds in keeping the majority of its assets on lease and interest rates do not rise significantly and rapidly, the Company’s cash flow should continue to be sufficient to cover its expenses and provide excess cash flow. If the Company incurs unusually large maintenance costs or reimbursements for maintenance in any given period, the Company expects it will have sufficient cash flow or borrowing availability under its credit facility to fund such maintenance.

Competition

The Company competes with other leasing companies, banks, financial institutions, and aircraft leasing partnerships for customers that generally are regional commercial aircraft operators seeking to lease aircraft under operating leases. Competition has increased as competitors who have traditionally neglected the regional air carrier market have begun to focus on that market. Because competition is largely based on price and lease terms, the entry of new competitors into the market, and/or the entry of traditional large aircraft lessors into the regional aircraft niche, particularly those with greater access to capital markets than the Company, could lead to fewer acquisition opportunities for the Company and/or lease terms less favorable to the Company on acquisitions, as well as fewer renewals of existing leases or new leases of existing aircraft, all of which could lead to lower revenues, profitability and cash flow for the Company.

The Company, however, believes that it has a competitive advantage due to its experience and operational efficiency in financing the transaction sizes that are desired by many in the regional air carrier market. Management believes that the Company also continues to have a competitive advantage because JMC has developed a presence as a global participant in the regional aircraft leasing market.

Dependence on Significant Customers

For the year ended December 31, 2014, the Company’s four largest customers accounted for 20%, 18%, 14% and 11% of lease revenue. For the year ended December 31, 2013, the Company’s four largest customers accounted for 23%, 19%, 11% and 10% of lease revenue. Concentration of credit risk with respect to lease receivables will diminish in the future only if the Company is able to re-lease assets currently on lease to significant customers to new customers and/or acquire assets for lease to new customers.

Environmental Matters

Neither compliance with federal, state and local provisions regulating discharge of greenhouse gas emissions (including carbon dioxide (CO_2)) in the environment and/or aircraft noise regulations, nor remedial agreements or other actions relating to the environment, has had, or is expected to have, a material effect on the Company's capital expenditures, financial condition, results of operations or competitive position.

Employees

Under the Company's Management Agreement with JMC, JMC is responsible for all administration and management of the Company. Consequently, the Company does not have any employees.

Available Information

The headquarters of AeroCentury Corp. is located at 1440 Chapin Avenue, Suite 310, Burlingame, California 94010. The main telephone number is (650) 340-1888. The Company's website is located at: http://www.aerocentury.com.

The Company is subject to the reporting requirements of the Securities Exchange Act (the "Exchange Act"). Therefore, the Company files periodic reports, proxy statements and other information with the Securities and Exchange Commission (the "SEC"). Copies of these materials, filed by us with the SEC, are available free of charge on our website at www.aerocentury.com through the Investor Relations link (SEC Filings). The public may read and copy any materials the Company files with the SEC at the SEC's Public Reference Room of the SEC at 100 F Street N.E., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. In addition, the SEC maintains an Internet site (http://www.sec.gov) that contains reports, proxy and information statements and other information regarding issuers that file electronically with the SEC.

Item 1A.Risk Factors.

Smaller reporting companies are not required to provide this information.

Item 1B.Unresolved Staff Comments.

None.

Item 2.Properties.

As of December 31, 2014, the Company did not own or lease any real property, plant or materially important physical properties. The Company maintains its principal office at 1440 Chapin Avenue, Suite 310, Burlingame, California 94010. However, since the Company has no employees and the Company's portfolio of leased aircraft assets is managed and administered under the terms of the Management Agreement with JMC, all office facilities are provided by JMC.

For information regarding the aircraft and aircraft engines owned by the Company, refer to Note 3 to the Company's financial statements in Item 8 of this Annual Report on Form 10-K.

Item 3.Legal Proceedings.

The Company from time to time engages in ordinary course litigation relating to lease collection matters against defaulting lessees and mechanic's lien claims by vendors hired by lessees. None of the current litigation, if resolved adverse to the Company, is anticipated to have a material adverse effect on the Company's financial condition or results of operations.

Item 4.Mine Safety Disclosures.

Not applicable.

PART II

Item 5.Market for Registrant's Common Equity, Related Stockholder Matters and
Issuer Purchases of Equity Securities.

The shares of the Company's Common Stock are traded on the NYSE MKT exchange ("NYSE MKT") under the symbol "ACY."

Market Information

The Company's Common Stock has been traded on the NYSE MKT since January 16, 1998. The following table sets forth the high and low sales prices reported on the NYSE MKT for the Company's Common Stock for the periods indicated:

Period	High	Low
Fiscal year ended December 31, 2014:		
Fourth Quarter	$11.82	$8.05
Third Quarter	16.40	10.90
Second Quarter	18.90	15.25
First Quarter	19.00	15.03
Fiscal year ended December 31, 2013:		
Fourth Quarter	20.60	14.65
Third Quarter	22.30	19.10
Second Quarter	21.50	17.53
First Quarter	18.31	14.20

On March 10, 2015, the closing sale price of the Company's Common Stock on the NYSE MKT exchange was $13.50 per share.

Number of Security Holders

According to the Company's transfer agent, the Company had approximately 1,400 stockholders of record as of March 10, 2015. Because brokers and other institutions on behalf of beneficial stockholders hold many of the Company's shares of Common Stock, the Company is unable to estimate the total number of beneficial stockholders represented by those record holders.

Dividends

No dividends have been declared or paid to date. The Company has no plans at this time to declare or pay dividends, and intends to re-invest any earnings into the acquisition of additional revenue-generating aircraft equipment.

The terms of the Credit Facility prohibit the Company from declaring or paying dividends on its Common Stock, except for cash dividends in an aggregate annual amount not to exceed 50% of the Company's net income in the immediately preceding fiscal year so long as immediately prior to and immediately following such dividend the Company is not in default under the Credit Facility.

Stockholder Rights Plan

For information regarding the Company’s stockholder rights plan, refer to Note 8 to the Company’s financial statements in Item 8 of this Annual Report on Form 10-K.

Item 6.Selected Financial Data.

This report does not include information described under Item 301 of Regulation S-K pursuant to the rules of the SEC that permit "smaller reporting companies" to omit such information.

Item 7.Management's Discussion and Analysis of Financial Condition and Results of Operations.

Overview

The Company owns regional aircraft and engines, which are typically leased to customers under triple net leases with terms that are less than the useful life of the assets. A "triple net operating lease" is an operating 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. The acquisition of such equipment is generally made using debt financing. The Company's profitability and cash flow are dependent in large part upon its ability to acquire equipment, obtain and maintain favorable lease rates on such equipment, and re-lease or sell equipment that comes off lease. The Company is subject to the credit risk of its lessees, both as to collection of rental payments and as to performance by lessees of their obligations to maintain the equipment. Since lease rates for assets in the Company's portfolio generally decline as assets age, the Company's ability to maintain and grow revenue and earnings is primarily dependent upon the Company's ability to acquire and lease additional assets.

The Company's primary uses of cash are for purchases of aircraft and engines, maintenance, debt service payments, management fees, insurance and professional fees.

The Company's most significant non-cash expenses include aircraft and engine depreciation, amortization of costs associated with the Company's indebtedness, which is included in interest expense, and, in some years, impairment provisions, which are affected by significant estimates.

Critical Accounting Policies, Judgments and Estimates

The Company's discussion and analysis of its financial condition and results of operations are based upon its 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 8 of this Annual Report on Form 10-K.

For a discussion of the Company's accounting policies regarding maintenance reserves, refer to Note 4 to the Company's financial statements in Item 8 of this Annual Report on Form 10-K. 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 8 of this Annual Report on Form 10-K.

Results of Operations

The Company recorded a net loss of $11.3 million in 2014 compared to net income of $8.3 million in 2013, primarily as a result of recording impairment charges totaling $18.2 million for its seven Fokker 100 aircraft, as well as impairment charges of $0.5 million for three of its Fokker 50 aircraft in 2014. There were no recorded impairment charges of long-lived assets during 2013.

Operating lease revenue increased 17% from $18.8 million in 2013 to $21.9 million in 2014, primarily as a result of 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 77% from $14.9 million in 2013 to $3.4 million in 2014. The amount recorded in 2013 period was comprised of $6.5 million, which 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 $8.4 million from maintenance reserves retained at lease end for five other aircraft. The amount recorded in 2014 period includes approximately $1.7 million of maintenance reserves retained at lease end for one aircraft and approximately $1.7 million of maintenance reserves retained when six aircraft were returned to the Company prior to lease expiration.

During 2014, the Company recorded $3.1 million of net gains on the sale of nine aircraft and an aircraft engine, as compared to 2013, when the Company recorded $3.8 million in net gains from the sale of five aircraft and an engine, as well as the disposal of a spare engine.

During 2014, the Company recorded $0.1 million of other income from retention of a non-refundable security deposit when a potential buyer of one of the Company's aircraft did not complete the planned purchase. During 2013, the Company recorded $0.5 million of other income from security deposits retained upon early termination of two leases following the lessee's bankruptcy.

During 2014 and 2013, the Company added equipment to its lease portfolio of approximately $81.0 million and $24.7 million, respectively. The Company sold equipment with book values of approximately $14.5 million and $8.7 million million during 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 decreased by 1% in 2014 over the previous year. Management fees, which are based on the net asset value of the Company's aircraft and engines, increased by 12% in 2014 as compared to 2013. Due to a waiver by JMC of its fourth quarter management fees of approximately $1.2 million, management fees incurred by the Company were less by that amount than they would have been without such waiver.

The average net book value of assets held for lease during 2014 and 2013 was approximately $171.7 million and $143.3 million, respectively, representing an increase of 20%. The average portfolio utilization during 2014 and 2013 was 82% and 76%, respectively.

The Company's maintenance expense increased by 7% from $7.0 million in 2013 to $7.5 million in 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 26% from $4.1 million in 2013 to $5.1 million in 2014, primarily as a result of a higher average Credit Facility balance.

The Company's professional fees, general and administrative and other expenses increased by 46% from $1.2 million in 2013 to $1.7 million in 2014, 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 when it ceased operations in 2014.

The Company's other taxes expense increased by $0.4 million in 2014 compared to 2013 as a result of the accrual of goods and service 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.

(a)Credit Facility

In May 2014, the Company's $130 million 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 lessees 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 impairment charges of $0.3 million for an off-lease Fokker 50 aircraft and reclassified these six aircraft as held for sale. The Company sold the Fokker 50 aircraft in March 2015. 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 the profitability, interest coverage and debt service coverage covenants of its Credit Facility at September 30, 2014. In November 2014, the Company and the Credit Facility banks agreed to an amendment to the Credit Facility that: 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. The Company was in compliance with all covenants at December 31, 2014.

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, (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 7 to the Company's financial statements in Item 1 of this Annual Report on Form 10-K.

(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 assets, 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) the cost and anticipated timing of maintenance to be performed, (iii) required debt payments, (iv) timely use of proceeds of unused debt capacity toward additional acquisitions of income producing assets and (v) interest rates. 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 $1.6 million in 2014 compared to 2013. As discussed below, the change in cash flow was primarily a result of a decrease in payments received for maintenance reserves and increases in payments for maintenance, interest, management fees and professional fees and general and administrative expenses, the effects of which were partially offset by an increase in payments received for operating lease revenue and a decrease in payments for aircraft insurance.

Payments for operating lease revenue and maintenance reserves

Rent receipts from lessees increased by $2.9 million in 2014 compared to 2013, primarily due to rent from assets purchased during late 2013 and early 2014. Receipts from lessees for maintenance reserves decreased by $1.8 million in 2014 compared to 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. In addition, the Company does not collect maintenance reserves for most of the aircraft it acquired in 2013 and 2014.

As of the date of this filing, the Company is receiving no lease revenue for six aircraft and five engines that are off lease, with a total book value of $22.3 million, representing 12% of the Company's total assets held for lease. One of the off-lease engines is being held as a spare and used in connection with required maintenance on the Company’s Fokker 100 aircraft. In addition, five off-lease Fokker 100 aircraft, with a total book value of $5.0 million, are being held for sale and not lease.

Payments for maintenance

Payments for maintenance increased by $0.7 million in 2014 compared to 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, as well as maintenance paid for off-lease assets.

Payment for interest

Payments for interest increased by $1.1 million in 2014 compared to 2013 as a result of a higher Credit Facility balance.

Payments for management fees

Although JMC waived its management fees of approximately $1.2 million for the fourth quarter of 2014, payments for management fees increased by $0.4 million in 2014 compared to 2013 as a result of asset purchases in 2013 and 2014. No assurance can be given that JMC will waive any management fees in the future.

Payment for professional fees, general and administrative and other expenses and aircraft insurance

Payments for professional fees, general and administrative and other expenses increased by $0.6 million in 2014 compared to 2013 primarily as a result of expenses incurred in connection with the early return of six aircraft and two engines by one of the Company's customers in 2014 period when it ceased operations. Payments for aircraft insurance decreased by $0.7 million in 2014 compared to 2013 primarily as a result of a difference in the timing of premium payments that are made on a semi-annual basis.

(ii)Investing activities

During 2014 and 2013, the Company received cash of $16.2 million and $10.9 million, respectively, from the sale of assets. During the same time periods, the Company used cash of $74.5 million and $25.0 million, respectively, for purchases and capital improvement of aircraft.

(iii)Financing activities

The Company borrowed $71.1 million and $19.0 million under the Credit Facility during 2014 and 2013, respectively. In these same time periods, the Company repaid $15.2 million and $9.3 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 2014 and 2013, the Company paid $3.0 million and $2.1 million of fees, respectively, in connection with the extension and administration of the Company's Credit Facility, as well as the waiver obtained from the banks during the fourth quarter of 2014. Such fees are being amortized over the term of the Credit Facility.

Outlook

(a)General

While in certain areas of the world the air carrier industry is 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 and after will choose to return the assets rather than renew the leases, notwithstanding that any such customer may incur significant expenses to satisfy return conditions.

• 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.

At February 28, 2015, 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	17	%
Bombardier CRJ-700	3	16	%
Bombardier CRJ-900	2	16	%
Bombardier Dash-8-Q400	3	13	%

For the month ended February 28, 2015, the Company's sources of operating lease revenue were from the following regions:

Region	Number of lessees	% of operating lease revenue	
Europe	3	29	%