

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 20549**

**FORM 10-Q/A  
(Amendment No. 1)**

(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, 2020

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)

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

**94-3263974**

(I.R.S. Employer Identification No.)

**(650) 340-1888**

(Registrant's Telephone Number Including Area Code)

**None**

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
<b>Common Stock</b>	<b>ACY</b>	<b>NYSE American</b>

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 every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files).

Yes  No 

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

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>

## Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

The number of shares of the registrant's common stock outstanding as of November 12, 2020 was 1,545,884.

## EXPLANATORY NOTE

AeroCentury Corp. (the "**Company**") is filing this Amendment No. 1 on Form 10-Q/A (this "**Amendment**") to amend the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2020 (the "**Original Form 10-Q**"). This Amendment is being filed solely to insert inadvertently omitted dates for the certificates filed as Exhibit 31.1 and 31.2 and furnished as Exhibit 32.1 and 32.2 with the Original Form 10-Q. Nothing in the Form 10-Q is being amended other than the dating of the Exhibits as described above.

As used in this report, unless the context indicates otherwise, "AeroCentury" refers to AeroCentury Corp. and the "Company" refers to AeroCentury together with its consolidated subsidiaries.

*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 the Company's plans and objectives for future operations, the Company's future financial or economic performance (including known or anticipated trends), and the assumptions underlying or related to 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 in this report include statements about the following matters, although this list is not exhaustive:

- The Company's business plans and strategies, including its ability to finance acquisitions in the near term, its continued focus on acquiring used regional aircraft, and any potential for acquiring and managing new types and models of regional aircraft;
- Certain industry trends and their impact on the Company and its performance, including: increasing competition that results in higher acquisition prices for many of the aircraft types that the Company has targeted to buy and, at the same time, downward pressure on lease rates for these aircraft; relatively lower market demand for older aircraft types that are no longer in production, which could cause certain of the Company's aircraft to remain off lease for significant periods of time; and expectations of shakeouts of weaker carriers in economically troubled regions, which could impact the financial condition and viability of certain of the Company's customers, and as a result, their demand for the Company's aircraft and their ability to fulfill their lease commitments and other obligations to the Company under existing leases;
- The effects on the airline industry and the global economy of events such as public health emergencies or natural disasters, such as the ongoing coronavirus (COVID-19) outbreak;
- Expectations about the Company's future liquidity, cash flow and capital requirements;
- The Company's ability to qualify for forgiveness on its PPP loan, or obtain additional debt or equity financing to repay any of its indebtedness;
- The Company's ability to comply with its term loans and other outstanding debt instruments, including making payments of principal and interest thereunder as and when required and complying with the financial and other covenants included in these instruments;
- The Company's ability to reach agreement on repayment terms for the debt obligations of the Company sold to Drake Asset Management Jersey Limited ("Drake");
- The Company's ability to access additional sources of capital in the future as and when needed, in the amounts desired, on terms favorable to the Company, or at all;
- The expected impact of existing or known threatened legal proceedings;
- The effect on the Company and its customers of complying with applicable government and regulatory requirements in the numerous

As used in this report, unless the context indicates otherwise, "AeroCentury" refers to AeroCentury Corp. and the "Company" refers to AeroCentury together with its consolidated subsidiaries.

### *Forward-Looking Statements*

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Forward-looking statements in this report include statements about the following matters, although this list is not exhaustive:

- The Company's business plans and strategies, including its ability to finance acquisitions in the near term, its continued focus on acquiring used regional aircraft, and any potential for acquiring and managing new types and models of regional aircraft;
- Certain industry trends and their impact on the Company and its performance, including: increasing competition that results in higher acquisition prices for many of the aircraft types that the Company has targeted to buy and, at the same time, downward pressure on lease rates for these aircraft; relatively lower market demand for older aircraft types that are no longer in production, which could cause certain of the Company's aircraft to remain off lease for significant periods of time; and expectations of shakeouts of weaker carriers in economically troubled regions, which could impact the financial condition and viability of certain of the Company's customers, and as a result, their demand for the Company's aircraft and their ability to fulfill their lease commitments and other obligations to the Company under existing leases;
- The effects on the airline industry and the global economy of events such as public health emergencies or natural disasters, such as the ongoing coronavirus (COVID-19) outbreak;
- Expectations about the Company's future liquidity, cash flow and capital requirements;
- The Company's ability to qualify for forgiveness on its PPP loan, or obtain additional debt or equity financing to repay any of its indebtedness;
- The Company's ability to comply with its term loans and other outstanding debt instruments, including making payments of principal and interest thereunder as and when required and complying with the financial and other covenants included in these instruments;
- The Company's ability to reach agreement on repayment terms for the debt obligations of the Company sold to Drake Asset Management Jersey Limited ("Drake");
- The Company's ability to access additional sources of capital in the future as and when needed, in the amounts desired, on terms favorable to the Company, or at all;
- The expected impact of existing or known threatened legal proceedings;
- The effect on the Company and its customers of complying with applicable government and regulatory requirements in the numerous jurisdictions in which the Company and its customers operate;
- The Company's cyber-vulnerabilities and the anticipated effects on the Company if a cybersecurity threat or incident were to materialize;
- General economic, market, political and regulatory conditions, including anticipated changes in these conditions and the impact of such changes on customer demand and other facets of the Company's business; and
- The impact of the foregoing on the prevailing market price and trading volume of the Company's common stock.

All of the Company's forward-looking statements involve risks and uncertainties that could cause the Company's actual results to differ materially from those projected or assumed by such forward-looking statements. Among the factors that could cause such differences are: the Company's ability to comply with its debt obligations to Drake; the Company's ability to reach agreement with Drake and regarding repayment terms on the debt purchased by Drake from the MUFG Lenders; the potential impact on the Company's debt obligations of developments regarding LIBOR, including the potential phasing out of this metric; the Company's ability to raise capital on acceptable terms when needed and in desired amounts, or at all; the Company's ability to locate and acquire appropriate and revenue-producing assets; deterioration of the market for or appraised values of aircraft owned by the Company; the Company's ability to retain its existing customers, or attract replacement customers or prospective purchasers for off-lease aircraft if and when existing customers are lost or become unable to maintain lease compliance; a surge in interest rates; any noncompliance by the Company's lessees with obligations under their respective leases, including payment obligations; any economic downturn or other financial crisis; the timing, rate and amount of maintenance expenses for the Company's asset portfolio, as well as the distribution of these expenses among the assets in the portfolio; limited trading volume in AeroCentury's common stock; the duration and continuing impact of the COVID-19 pandemic, including a potential resurgence in COVID-19 cases; and the other factors detailed under "*Factors That May Affect Future Results and Liquidity*" in Item 2 of this report. In addition, the Company operates in a competitive and evolving industry in which new risks emerge from time to time, and it is not possible for the Company to predict all of the risks it may face, nor can it assess the impact of all factors on its business or the extent to which any factor or combination of factors could cause actual results to differ from expectations. As a result of these and other potential risks and uncertainties, the Company's forward-looking statements should not be relied on or viewed as predictions of future events.

This cautionary statement should be read as qualifying all forward-looking statements included in this report, wherever they appear. All forward-looking statements and descriptions of risks included in this report are made as of the date hereof based on information available to the Company as of the date hereof, and except as required by applicable law, the Company assumes no obligation to update any such forward-looking statement or risk for any reason. You should, however, consult the risks and other disclosures described in the reports the Company files from time to time with the United States Securities and Exchange Commission (“SEC”) after the date of this report for updated information.

## Table of Contents

### [PART I – FINANCIAL INFORMATION 4](#)

[Item 1. Financial Statements. 4](#)

[Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations. 15](#)

[Item 3. Quantitative and Qualitative Disclosures About Market Risk. 18](#)

[Item 4. Controls and Procedures. 18](#)

### [PART II – OTHER INFORMATION 18](#)

[Item 2. Unregistered Sales of Equity Securities and Use of Proceeds. 18](#)

[Item 6. Exhibits. 18](#)

## PART I – FINANCIAL INFORMATION

### Item 1. Financial Statements.

AeroCentury Corp.  
Condensed Consolidated Balance Sheets  
(Unaudited)

ASSETS

	September 30, 2020	December 31, 2019
Assets:		
Cash and cash equivalents	\$4,863,800	\$2,350,200
Restricted cash	50,000	1,076,900
Accounts receivable, including deferred rent of \$0 and \$828,000 at September 30, 2020 and December 31, 2019, respectively	123,100	1,139,700
Finance leases receivable, net of allowance for doubtful accounts of \$1,170,000 and \$2,908,600 at September 30, 2020 and December 31, 2019, respectively	2,880,000	8,802,100
Aircraft and aircraft engines held for lease, net of accumulated depreciation of \$36,848,500 and \$31,338,700 at September 30, 2020 and December 31, 2019, respectively	96,052,100	108,368,600
Assets held for sale	15,331,500	26,036,600
Property, equipment and furnishings, net of accumulated depreciation of \$14,700 and \$9,600 at September 30, 2020 and December 31, 2019, respectively	14,600	62,900
Office lease right of use, net of accumulated amortization of \$11,000 and \$524,500 at September 30, 2020 and December 31, 2019, respectively	158,900	948,300
Deferred tax asset	1,185,300	517,700
Prepaid expenses and other assets	361,400	292,800
<b>Total assets</b>	<b>\$21,020,700</b>	<b>\$49,595,800</b>

## PART I – FINANCIAL INFORMATION

## Item 1. Financial Statements.

AeroCentury Corp.  
Condensed Consolidated Balance Sheets  
(Unaudited)

	<u>September 30, 2020</u>	<u>December 31, 2019</u>
ASSETS		
Assets:		
Cash and cash equivalents	\$4,863,800	\$2,350,200
Restricted cash	50,000	1,076,900
Accounts receivable, including deferred rent of \$0 and \$828,000 at September 30, 2020 and December 31, 2019, respectively	123,100	1,139,700
Finance leases receivable, net of allowance for doubtful accounts of \$1,170,000 and \$2,908,600 at September 30, 2020 and December 31, 2019, respectively	2,880,000	8,802,100
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Deferred tax asset	1,185,300	517,700
Prepaid expenses and other assets	361,400	292,800
<b>Total assets</b>	<b><u>\$21,020,700</u></b>	<b><u>\$49,595,800</u></b>
LIABILITIES AND STOCKHOLDERS' (DEFICIT)/EQUITY		
Liabilities:		
Accounts payable and accrued expenses	\$1,081,900	\$ 736,000
Accrued payroll	172,300	164,200
Notes payable and accrued interest, net of unamortized debt issuance costs of \$1,906,500 and \$3,825,700 at September 30, 2020 and December 31, 2019, respectively	111,575,400	111,638,400
Derivative liability	874,700	1,824,500
Derivative termination liability	3,075,300	-
Lease liability	170,700	336,400
Maintenance reserves	1,804,700	4,413,100
Accrued maintenance costs	121,800	446,300
Security deposits	4,159,900	1,034,300
Unearned revenues	1,578,300	3,039,200
Deferred income taxes	-	2,529,800
Income taxes payable	36,300	175,000
<b>Total liabilities</b>	<b><u>124,651,300</u></b>	<b><u>126,337,200</u></b>
Commitments and contingencies (Note 8)		
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, 1,545,884 shares outstanding at September 30, 2020 and December 31, 2019	1,800	1,800
Paid-in capital	16,782,800	16,782,800
(Accumulated deficit)/retained earnings	(16,895,100)	10,882,100
Accumulated other comprehensive loss	(482,800)	(1,370,800)
	<u>(593,300)</u>	<u>26,295,900</u>
Treasury stock at cost, 213,332 shares at September 30, 2020 and December 31, 2019, respectively	(3,037,300)	(3,037,300)
<b>Total stockholders' (deficit)/equity</b>	<b><u>(3,630,600)</u></b>	<b><u>23,258,600</u></b>

<b>Total liabilities and stockholders' (deficit)/equity</b>	<b><u>\$21,020,700</u></b>	<b><u>\$49,595,800</u></b>
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The accompanying notes are an integral part of these condensed consolidated financial statements.

AeroCentury Corp.				
Condensed Consolidated Statements of Operations				
(Unaudited)				
	For the Nine Months		For the Three Months	
	Ended		Ended	
	September 30,		September 30,	
	<u>2020</u>	<u>2019</u>	<u>2020</u>	<u>2019</u>
Revenues and other income:				
Operating lease revenue	\$2,395,800	\$20,820,100	\$3,249,100	\$6,705,900
Maintenance reserves revenue, net	221,400	16,968,400	221,400	16,968,400
Finance lease revenue	56,300	764,800	-	268,600
Net gain on disposal of assets	8,700	322,000	19,800	44,000
Net loss on sales-type leases	-	(170,600)	-	-
Other (loss)/income	(23,200)	11,200	-	400
	<u>12,659,000</u>	<u>38,715,900</u>	<u>3,490,300</u>	<u>23,987,300</u>
Expenses:				
Interest	13,492,700	7,745,000	3,020,100	2,347,600
Impairment in value of aircraft	16,820,500	24,923,000	439,000	23,354,600
Depreciation	5,514,900	9,140,700	1,342,100	2,970,000
Professional fees, general and administrative and other	4,368,900	2,627,300	1,370,600	944,900
Bad debt expense	1,170,000	3,918,000	-	3,918,000
Salaries and employee benefits	1,533,500	1,749,000	498,800	529,200
Insurance	602,900	409,600	191,400	130,200
Maintenance	246,400	373,100	78,000	255,900
Other taxes	77,600	88,700	26,500	25,600
	<u>43,827,400</u>	<u>50,974,400</u>	<u>6,966,500</u>	<u>34,476,000</u>
Loss before income tax (benefit)/provision	(31,168,400)	(12,258,500)	(3,476,200)	(10,488,700)
Income tax (benefit)/provision	(3,391,200)	(2,641,400)	604,900	(2,257,300)
Net loss	<u>\$27,777,200</u>	<u>\$9,617,100</u>	<u>\$4,081,100</u>	<u>\$8,231,400</u>
Loss per share:				
Basic	<u>\$ (17.97)</u>	<u>\$ (6.22)</u>	<u>\$ (2.64)</u>	<u>\$ (5.32)</u>
Diluted	<u>\$ (17.97)</u>	<u>\$ (6.22)</u>	<u>\$ (2.64)</u>	<u>\$ (5.32)</u>
Weighted average shares used in loss per share computations:				
Basic	<u>1,545,884</u>	<u>1,545,884</u>	<u>1,545,884</u>	<u>1,545,884</u>
Diluted	<u>1,545,884</u>	<u>1,545,884</u>	<u>1,545,884</u>	<u>1,545,884</u>

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

AeroCentury Corp.  
Condensed Consolidated Statements of Comprehensive Loss  
(Unaudited)

For the Nine Months

For the Three Months

AeroCentury Corp.  
Condensed Consolidated Statements of Comprehensive Loss  
(Unaudited)

	For the Nine Months Ended September 30,		For the Three Months Ended September 30,	
	2020	2019	2020	2019
	Net loss	<u>\$27,777,200</u>	<u>\$9,617,100</u>	<u>\$4,081,100</u>
Other comprehensive loss:				
Unrealized losses on derivative instruments	(575,000)	(1,985,100)	-	(174,500)
Reclassification of net unrealized losses on derivative instruments to interest expense	1,706,200	5,900	149,100	28,000
Tax benefit/(expense) related to items of other comprehensive loss	(243,200)	425,100	(32,400)	31,500
Other comprehensive income/(loss)	888,000	(1,554,100)	116,700	(115,000)
Total comprehensive loss	<u>\$26,889,200</u>	<u>\$11,171,200</u>	<u>\$3,964,400</u>	<u>\$8,346,400</u>

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

AeroCentury Corp.  
Condensed Consolidated Statements of Stockholders' Equity/(Deficit)  
For the Three Months and Nine Months Ended September 30, 2019 and September 30, 2020  
(Unaudited)

	Number of Common Stock Shares Outstanding	Common Stock	Paid-in Capital	Retained Earnings/ (Deficit)	Treasury Stock	Accumulated Other Comprehensive Loss	Total
Balance, December 31, 2018	1,545,884	\$ 1,800	\$6,782,800	\$27,540,600	\$(3,037,300)	\$ -	\$1,287,900
Net loss	-	-	-	(1,308,200)	-	-	(1,308,200)
Accumulated other comprehensive loss	-	-	-	-	-	(427,800)	(427,800)
Balance, March 31, 2019	1,545,884	1,800	16,782,800	26,232,400	(3,037,300)	(427,800)	39,551,900
Net loss	-	-	-	(77,600)	-	-	(77,600)
Accumulated other comprehensive loss	-	-	-	-	-	(1,011,300)	(1,011,300)
Balance, June 30, 2019	1,545,884	1,800	16,782,800	26,154,800	(3,037,300)	(1,439,100)	38,463,000
Net loss	-	-	-	(8,231,400)	-	-	(8,231,400)
Accumulated other comprehensive loss	-	-	-	-	-	(115,000)	(115,000)
Balance, September 30, 2019	<u>1,545,884</u>	<u>\$ 1,800</u>	<u>\$6,782,800</u>	<u>\$17,923,400</u>	<u>\$(3,037,300)</u>	<u>\$(1,554,100)</u>	<u>\$0,116,600</u>
Balance, December 31, 2019	1,545,884	\$ 1,800	\$6,782,800	\$10,882,100	\$(3,037,300)	\$(1,370,800)	\$2,258,600
Net loss	-	-	-	(10,178,400)	-	-	(10,178,400)
Accumulated other comprehensive income	-	-	-	-	-	583,700	583,700
Balance, March 31, 2020	1,545,884	1,800	16,782,800	703,700	(3,037,300)	(787,100)	13,663,900
Net loss	-	-	-	(13,517,700)	-	-	(13,517,700)

AeroCentury Corp.  
Condensed Consolidated Statements of Stockholders' Equity/(Deficit)  
For the Three Months and Nine Months Ended September 30, 2019 and September 30, 2020  
(Unaudited)

	Number of Common Stock Shares Outstanding	Common Stock	Paid-in Capital	Retained Earnings/ (Deficit)	Treasury Stock	Accumulated Other Comprehensive Loss	Total
Balance, December 31, 2018	1,545,884	\$ 1,800	\$6,782,800	\$27,540,600	\$(3,037,300)	\$ -	\$1,287,900
Net loss	-	-	-	(1,308,200)	-	-	(1,308,200)
Accumulated other comprehensive loss	-	-	-	-	-	(427,800)	(427,800)
Balance, March 31, 2019	1,545,884	1,800	16,782,800	26,232,400	(3,037,300)	(427,800)	39,551,900
Net loss	-	-	-	(77,600)	-	-	(77,600)
Accumulated other comprehensive loss	-	-	-	-	-	(1,011,300)	(1,011,300)
Balance, June 30, 2019	1,545,884	1,800	16,782,800	26,154,800	(3,037,300)	(1,439,100)	38,463,000
Net loss	-	-	-	(8,231,400)	-	-	(8,231,400)
Accumulated other comprehensive loss	-	-	-	-	-	(115,000)	(115,000)
Balance, September 30, 2019	<u>1,545,884</u>	<u>\$ 1,800</u>	<u>\$6,782,800</u>	<u>\$7,923,400</u>	<u>\$(3,037,300)</u>	<u>\$(1,554,100)</u>	<u>\$0,116,600</u>
Balance, December 31, 2019	1,545,884	\$ 1,800	\$6,782,800	\$10,882,100	\$(3,037,300)	\$(1,370,800)	\$23,258,600
Net loss	-	-	-	(10,178,400)	-	-	(10,178,400)
Accumulated other comprehensive income	-	-	-	-	-	583,700	583,700
Balance, March 31, 2020	1,545,884	1,800	16,782,800	703,700	(3,037,300)	(787,100)	13,663,900
Net loss	-	-	-	(13,517,700)	-	-	(13,517,700)
Accumulated other comprehensive income	-	-	-	-	-	187,600	187,600
Balance, June 30, 2020	<u>1,545,884</u>	<u>1,800</u>	<u>16,782,800</u>	<u>(12,814,000)</u>	<u>(3,037,300)</u>	<u>(599,500)</u>	<u>333,800</u>
Net loss	-	-	-	(4,081,100)	-	-	(4,081,100)
Accumulated other comprehensive income	-	-	-	-	-	116,700	116,700
Balance, September 30, 2020	<u>1,545,884</u>	<u>\$ 1,800</u>	<u>\$6,782,800</u>	<u>\$16,895,100</u>	<u>\$(3,037,300)</u>	<u>\$(482,800)</u>	<u>\$3,630,600</u>

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

AeroCentury Corp.  
Condensed Consolidated Statements of Cash Flows  
(Unaudited)

	For the Nine Months Ended September 30,	
	2020	2019
Net cash provided by operating activities	<u>\$5,983,900</u>	<u>\$8,146,400</u>
Investing activities:		

AeroCentury Corp.  
Condensed Consolidated Statements of Cash Flows  
(Unaudited)

	For the Nine Months Ended September 30,	
	2020	2019
Net cash provided by operating activities	<u>\$ 5,983,900</u>	<u>\$ 8,146,400</u>
Investing activities:		
Proceeds from sale of aircraft and aircraft engines held for lease, net of re-sale fees	-	1,702,500
Proceeds from sale of assets held for sale, net of re-sale fees	3,229,900	5,505,400
Investment in aircraft parts and acquisition costs	-	(150,000)
Net cash provided by investing activities	<u>3,229,900</u>	<u>7,057,900</u>
Financing activities:		
Issuance of notes payable – MUFG Credit Facility and MUFG Loan	-	5,100,000
Repayment of notes payable – MUFG Credit Facility and MUFG Loan	(1,165,000)	(44,300,000)
Issuance of notes payable – Nord Loans	-	44,310,000
Repayment of notes payable – UK LLC SPE Financing	-	(9,211,100)
Repayment of notes payable – Nord Loans	(5,131,500)	(5,513,000)
Issuance of notes payable – PPP Loan	276,400	-
Debt issuance costs	(1,707,000)	(5,074,200)
Net cash used in financing activities	<u>(7,727,100)</u>	<u>(14,688,300)</u>
Net increase in cash, cash equivalents and restricted cash	1,486,700	516,000
Cash, cash equivalents and restricted cash, beginning of period	<u>3,427,100</u>	<u>1,542,500</u>
Cash, cash equivalents and restricted cash, end of period	<u>\$ 4,913,800</u>	<u>\$ 2,058,500</u>
Non-cash financing activities:		
Non-cash issuance of notes payable – Credit Facility \$ 2,150,000		<u>\$ -</u>

The components of cash and cash equivalents and restricted cash at the end of each of the periods presented consisted of:

	September 30,	
	2020	2019
Cash and cash equivalents	<u>\$ 4,863,800</u>	<u>\$ 2,058,500</u>
Restricted cash	<u>50,000</u>	<u>-</u>
Total cash, cash equivalents and restricted cash shown in the statement of cash flows	<u>\$ 4,913,800</u>	<u>\$ 2,058,500</u>

During the nine months ended September 30, 2020 and 2019, the Company paid interest totaling \$3,250,300 and \$6,141,300, respectively. The Company paid income taxes of \$222,900 and \$536,000 during the nine months ended September 30, 2020 and 2019, respectively.

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

AeroCentury Corp.  
Notes to Condensed Consolidated Financial Statements (Unaudited)  
September 30, 2020

**1. Organization and Summary of Significant Accounting Policies**

*(a) The Company and Basis of Presentation*

AeroCentury Corp.  
Notes to Condensed Consolidated Financial Statements (Unaudited)  
September 30, 2020

## 1. Organization and Summary of Significant Accounting Policies

### *(a) The Company and Basis of Presentation*

AeroCentury Corp. (“AeroCentury”) is a Delaware corporation incorporated in 1997. AeroCentury together with its consolidated subsidiaries is referred to as the “Company.”

In August 2016, AeroCentury formed two wholly-owned subsidiaries, ACY 19002 Limited (“ACY 19002”) and ACY 19003 Limited (“ACY 19003”) for the purpose of acquiring aircraft using a combination of cash and third-party financing (“UK LLC SPE Financing” or “special-purpose financing”) separate from AeroCentury’s credit facility (the “MUFG Credit Facility”). The UK LLC SPE Financing was repaid in full in February 2019 as part of a refinancing involving new non-recourse term loans totaling approximately \$44.3 million (“Nord Loans”) made to ACY 19002, ACY 19003, and two other newly formed special-purpose subsidiaries of AeroCentury, ACY SN 15129 LLC (“ACY 15129”) and ACY E-175 LLC (“ACY E-175”), which were formed for the purpose of refinancing four of the Company’s aircraft using the Nord Loans. See Note 4(b) for more information about the Nord Loans.

Financial information for AeroCentury and its consolidated subsidiaries is presented on a consolidated basis 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 8 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP 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, 2020 are not necessarily indicative of the results that may be expected for the year ending December 31, 2020 or for any other period. All intercompany balances and transactions have been eliminated in consolidation.

### *(b) Going Concern*

As discussed in Note 4, the Company was in default under its MUFG Credit Facility as of December 31, 2019. On May 1, 2020, the Company and the MUFG Credit Facility Lenders (“MUFG Lenders”) executed an amendment to the MUFG Credit Facility (as amended, the “MUFG Loan Agreement”) to convert the MUFG Credit Facility into a term loan facility (as converted, the “MUFG Loan”). The amendment included certain requirements and establishment of deadlines for achievement of milestones toward execution of Company strategic alternatives for the Company and/or its assets acceptable to the MUFG Lenders. The amendment cured the December default, but the Company was in default under the MUFG Loan Agreement due to non-payment of interest due on July 1, 2020, August 3, 2020, September 1, 2020 and October 1, 2020. As discussed in Note 5, the Company was also obligated to pay \$3.1 million related to the termination of the MUFG Swaps in March 2020. On October 30, 2020, the MUFG Lenders sold the MUFG Loan and the obligation of the Company from termination of the MUFG Swaps to Drake Asset Management Jersey Limited (“Drake”), and the Company and Drake entered into an amendment of the loan (as amended, the “Drake Loan Agreement”) under which, among other things, the cash component of interest due for March 2020 and thereafter for the term of the loan will be capitalized and the requirement for execution of a Strategic Alternative and related milestones was deleted (see Note 11 regarding Subsequent Events).

Drake has the right to exercise any and all remedies for default under the Drake Loan Agreement. Such remedies include, but are not limited to, declaring the entire indebtedness immediately due and payable and, if the Company were unable to repay such accelerated indebtedness, foreclosing upon the assets of the Company that secure the indebtedness under the Drake Loan Agreement (the “Drake Loan”) and the indebtedness for the terminated swaps (together, the “Drake Indebtedness”), which consist of substantially all of the Company’s assets except for certain assets held in the Company’s single asset special-purpose financing subsidiaries. As discussed in Note 4, the Company also defaulted on payment under the Nord Loans.

The COVID-19 pandemic has led to significant cash flow issues for airlines, and some airlines, including some of the Company’s customers, have been unable to timely meet their obligations under their lease obligations with the Company unless government financial support is received, of which there can be no assurance. Any additional significant nonpayment or late payment of lease payments by a significant lessee or combination of lessees could in turn impose limits on the Company’s ability to fund its ongoing operations as well as cause the Company to be unable to meet its debt obligations, which in turn could lead to an immediate acceleration of debt and foreclosure upon the Company’s assets.

As a result of these factors, there is substantial doubt regarding the Company’s ability to continue as a going concern. The condensed consolidated financial statements presented in this Quarterly Report on Form 10-Q have been prepared on a going concern basis and do not include any adjustments that might arise as a result of uncertainties about the Company’s ability to continue as a going concern.

*(c) Impact of COVID-19*

In March 2020, the World Health Organization (“WHO”) declared the novel strain of coronavirus (“COVID-19”) a pandemic, and COVID-19 has continued to have wide-ranging impacts as the virus spreads globally (the “COVID-19 Outbreak”). In March 2020, the WHO classified the COVID-19 Outbreak as a pandemic, based on the rapid increase in exposure globally. The ongoing COVID-19 Outbreak has had an overwhelming effect on all forms of transportation globally, but most acutely for the airline industry. The combined effect of fear of infection during air travel and international and domestic travel restrictions has caused a dramatic decrease in passenger loads in all areas of the world, not just in those countries with active clusters of COVID-19, but in airline ticket net bookings (i.e. bookings made less bookings canceled) of flights as well. This has led to significant cash flow issues for airlines, including some of the Company’s customers. Two of the Company’s eight customers did not make operating lease rent payments that were due in March, April, May and June 2020, totaling approximately \$3.5 million. As discussed in Notes 4(b) and 11, one of the customers paid the deferred rent in September 2020 and purchased the aircraft in October 2020. The Company permitted the second customer, which leases two regional turboprop aircraft, to make reduced payments totaling approximately \$0.3 million in April, May and June 2020 and the customer paid the reduced amounts. In addition, two other customers, each of which leases an aircraft subject to a sales-type lease, did not make lease payments totaling approximately \$0.9 million, and the Company and the customers are discussing remedies regarding non-payment of a portion of the lease payments due during the first quarter of 2020 as well as the lease payments due during the second and third quarters. As discussed in Note 3, the Company recorded impairments of \$439,000 and \$16,820,500 during the three months and nine months ended September 30, 2020. The impact of the COVID-19 Outbreak has also lead the Company to determine that there is uncertainty related to rent, interest and debt payments such that, as disclosed in Notes 4 and 5, the Company dedesignated its interest rate swaps as hedges in March 2020 since the payments related to the swaps were deemed not probable to occur.

Furthermore, for the duration of the pandemic and a period of financial recovery thereafter, sale and acquisition transactions are likely to be curtailed entirely or delayed while the industry returns to financial stability, which could impact the Company’s ability to implement a recapitalization plan (“Recapitalization Plan”). The Company has made estimates of the impact of the pandemic within its financial statements and there may be changes to those estimates in future periods. While the Company’s results of operations, cash flows and financial condition would be negatively impacted, the extent of the impact for the remainder of 2020 cannot be reasonably estimated at this time.

*(d) Use of Estimates*

The Company’s condensed consolidated financial statements have been prepared in accordance with GAAP. The preparation of consolidated 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 condensed consolidated 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 condensed consolidated financial statements are the residual values and useful lives of the Company’s long-lived assets, the current value of the Company’s assets held for sale, the amount and timing of future cash flows associated with each asset that are used to evaluate whether assets are impaired, accrued maintenance costs, accounting for income taxes, the assumptions used to value the Company’s derivative instruments, the valuation of the right of use asset and related lease liability associated with the Company’s office, and the amounts recorded as allowances for doubtful accounts.

*(e) Comprehensive Income/(Loss)*

The Company accounts for former interest rate cash flow hedges by reclassifying accumulated other comprehensive income into earnings in the periods in which the expected transactions occur or when it is probable that the hedged transactions will no longer occur, and are included in interest expense.

*(f) Finance Leases*

As of December 31, 2019, the Company had three aircraft subject to sales-type leases and three aircraft subject to direct financing leases. All six leases contain lessee bargain purchase options at prices substantially below the subject asset’s estimated residual value at the exercise date for the option. Consequently, the Company classified each of these six leases as finance leases for financial accounting purposes. For such finance leases, the Company reports 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, as a finance lease receivable on its balance sheet, and accrues interest on the balance of the finance lease receivable based on the interest rate inherent in the applicable lease over the term of the lease. For each of the three sales-type leases, the Company recognized as a gain or loss the amount equal to (i) the net investment in the sales-type lease plus any initial direct costs and lease incentives less (ii) the net book value of the subject aircraft at inception of the applicable lease.

In the first nine months of 2020, the Company sold the underlying aircraft in one of its sales-type leases and all three of its direct finance leases to

the lessees, resulting in net losses totaling \$47,900. The remaining two sales-type leases were substantially modified and, as a result of payment delinquencies by the two customers, the Company recorded a bad debt allowance of \$1,170,000 during the first quarter of 2020. The two leases remain treated as sales-type leases.

*(g) Taxes*

As part of the process of preparing the Company's condensed consolidated financial statements, management estimates income taxes in each of the jurisdictions in which the Company operates. This process involves estimating the Company's current tax exposure under the most recent tax laws and assessing temporary differences resulting from differing treatment of items for tax and GAAP purposes. These differences result in deferred tax assets and liabilities, which are included in the balance sheet. In assessing the valuation of deferred tax assets, the Company considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income or availability to carryback the losses to taxable income during periods in which those temporary differences become deductible. The Company considered several factors when analyzing the need for a valuation allowance including the Company's current five-year cumulative loss through September 30, 2020, the impacts of COVID-19 pandemic on the worldwide airline industry and the need to rapidly refinance its debt or sell its assets in accordance with the provisions of its Drake Indebtedness. Significant management judgment is required in determining the Company's future taxable income for purposes of assessing the Company's ability to realize any benefit from its deferred taxes. Based on its analysis, the Company has concluded that a valuation allowance is necessary for its U.S. deferred tax assets not supported by either future taxable income or availability of future reversals of existing taxable temporary differences and has recorded a valuation allowance of \$1,409,400 and \$4,585,300 for the three months and nine months ended September 30, 2020, respectively. Additionally, the Company has concluded that, based on its analysis, some of its foreign deferred tax assets are not expected to be realized based on limitations on the utilization of its foreign net operating losses, and has therefore recorded a valuation allowance of \$778,000 for the three months and the nine months ended September 30, 2020.

The Company accrues non-income based sales, use, value added and franchise taxes as other tax expense in the condensed consolidated statement of operations.

*(h) Interest Rate Hedging*

During the first quarter of 2019, the Company entered into certain derivative instruments to mitigate its exposure to variable interest rates under the Nord Loan debt and a portion of the MUFG Indebtedness. Hedge accounting is applied to such a transaction only if specific criteria have been met, the transaction is deemed to be "highly effective" and the transaction has been designated as a hedge at its inception. Under hedge accounting treatment, generally, the effects of derivative transactions are recorded in earnings for the period in which the hedge transaction affects earnings. A change in value of a hedging instrument is reported as a component of other comprehensive income/(loss) and is reclassified into earnings in the period in which the transaction being hedged affects earnings.

If at any time after designation of a cash flow hedge, such as those entered into by the Company, it is no longer probable that the forecasted cash flows will occur, hedge accounting is no longer permitted and a hedge is "dedesignated." After dedesignation, if it is still considered reasonably possible that the forecasted cash flows will occur, the amount previously recognized in other comprehensive income/(loss) will continue to be reversed as the forecasted transactions affect earnings. However, if after dedesignation it is probable that the forecasted transactions will not occur, amounts deferred in accumulated other comprehensive income/(loss) will be recognized in earnings immediately.

As noted in Note 5, in October 2019 the Company became aware that, as a result of certain defaults under its MUFG Credit Facility, certain of the forecasted transactions related to its MUFG Credit Facility interest rate swaps were no longer probable of occurring and, hence, those swaps were dedesignated from hedge accounting at that time. The two swaps related to the MUFG Credit Facility were terminated in March 2020 and the Company incurred a \$3.1 million obligation in connection with such termination, payment of which is due no later than the March 31, 2021 maturity of the Drake Loan. As a result of the forecasted transaction being not probable to occur, accumulated other comprehensive loss of \$34,500 and \$1,421,800 related to the MUFG Swaps was recognized as interest expense in the quarter and nine months ended September 30, 2020, respectively.

In March 2020, the Company determined that the future hedged interest payments related to its five remaining Nord Loan interest rate hedges were no longer probable of occurring, and consequently dedesignated all five swaps from hedge accounting.

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*(i) Recent Accounting Pronouncements*

ASU 2016-13

*(i) Recent Accounting Pronouncements*ASU 2016-13

The FASB issued ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326)*, in June 2016 (“ASU 2016-13”). ASU 2016-13 provides that financial assets measured at amortized cost are to be presented as a net amount, reflecting a reduction for a valuation allowance to present the amount expected to be collected (the “current expected credit loss” model of reporting). As such, expected credit losses will be reflected in the carrying value of assets and losses will be recognized before they become probable, as is required under the Company’s present accounting practice. In the case of assets held as available for sale, the amount of the valuation allowance will be limited to an amount that reflects the marketable value of the debt instrument. This amendment to GAAP is effective in the first quarter of 2023 for calendar-year SEC filers that are smaller reporting companies as of the one-time determination date. Early adoption is permitted beginning in 2019. The Company plans to adopt the new guidance on January 1, 2023, and has not determined the impact of this adoption on its consolidated financial statements.

ASU 2019-12

In December 2019, the FASB issued ASU 2019-12, *Income Taxes (Topic 740)*, to simplify the accounting for income taxes. The new guidance removes certain exceptions for recognizing deferred taxes for investments, performing intra-period allocation and calculating income taxes in interim periods. It also adds guidance to reduce complexity in certain areas, including recognizing deferred taxes for tax goodwill and allocating taxes to members of a consolidated group. This guidance will be effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2020. The Company is currently evaluating the impact of the new guidance on its consolidated financial statements and related disclosures.

FASB Staff Guidance on Effects of COVID-19

In April 2020, the FASB staff provided some relief from the unprecedented effect of the COVID-19 pandemic. Under this guidance, lessors may elect to treat lease concessions due to COVID-19 as if they arose from enforceable rights and obligations that existed in the lease contract, with the consequent effect that the concessions would not be treated as a lease modification which could require reclassification and remeasurement of the lease and to either recognize income during the deferral period or to treat deferred rent as variable rent during the period. Other guidance released in April 2020 provides that when hedge accounting is discontinued and it is probable that the forecasted transaction that had been hedged will occur beyond two months after its originally expected date as a result of the effects of COVID-19, the reporting entity may still defer recognizing related AOCI immediately and should defer recognition of such amounts until the forecasted transactions actually occur. The Company has elected to treat certain lease concessions to lessees as if they arose from rights initially in the lease contracts and so did not give rise to modifications of the leases, and to treat deferrals as variable rent during the period of the deferral, reducing income during such period.

*(j) Reclassifications*

Certain prior period amounts have been reclassified to conform with the current period presentation.

**2. Aircraft Lease Assets**

The Company’s leases are normally “triple net leases” under which the lessee is obligated to bear all costs, including tax, maintenance and insurance, on the leased assets during the term of the lease. In most cases, the lessee is obligated to provide a security deposit or letter of credit to secure its performance obligations under the lease, and in some cases, is required to pay maintenance reserves based on utilization of the aircraft, which reserves are available for qualified maintenance costs during the lease term and may or may not be refundable at the end of the lease. Typically, the leases also contain minimum return conditions, as well as an economic adjustment payable by the lessee (and in some instances by the lessor) for amounts by which the various aircraft or engine components are worse or better than a targeted condition set forth in the lease. Some leases contain renewal or purchase options, although the Company’s sales-type leases contain a bargain purchase option at lease end which the Company expects the lessees to exercise or require that the lessee purchase the aircraft at lease-end for a specified price.

Because all of the Company’s leases transfer use and possession of the asset to the lessee and contain no other substantial undertakings by the Company, the Company has concluded that all of its lease contracts qualify for lease accounting. Certain lessee payments of what would otherwise be lessor costs (such as insurance and property taxes) are excluded from both revenue and expense.

The Company evaluates the expected return on its leased assets by considering both the rents receivable over the lease term, any expected additional consideration at lease end, and the residual value of the asset at the end of the lease. In some cases, the Company depreciates the asset to the expected residual value because it expects to sell the asset at lease end; in other cases, it may expect to re-lease the asset to the same or another lessee and the depreciation term and related residual value will differ from the initial lease term and initial residual value. Residual value is

estimated by considering future estimates provided by independent appraisers, although it may be adjusted by the Company based on expected return conditions or location, specific lessee considerations, or other market information.

Three of the Company's operating lease assets are subject to manufacturer residual value guarantees totaling approximately \$16 million at the end of their lease terms in the second quarter of 2025. The Company considers the best market for re-leasing and/or selling its assets at the end of its leases, although it does not expect to retain ownership of the assets under sales-type leases given the lessees' bargain purchase options or required purchase.

During the third quarter of 2020, the Company recorded impairment losses totaling \$300,000 for two of its aircraft held for lease, which were written down based on estimated future cash flow. The Company also recorded an impairment loss of \$139,000 on an aircraft that is held for sale, which was written down based on its estimated sales price, less cost of sale.

*(a) Assets Held for Lease*

At September 30, 2020 and December 31, 2019, the Company's aircraft held for lease consisted of the following:

Type	September 30, 2020		December 31, 2019	
	Number Owned	% of net book value	Number owned	% of net book value
Regional jet aircraft	9	79%	9	80%
Turboprop aircraft	2	21%	2	20%

The Company did not purchase or sell any aircraft held for lease during the first nine months of 2020. None of the Company's aircraft held for lease were off lease at September 30, 2020.

As of September 30, 2020, minimum future lease revenue payments receivable under non-cancelable operating leases were as follows:

Years ending December 31

Remainder of 2020	\$ 3,234,500
2021	10,512,500
2022	8,760,100
2023	8,760,100
2024	6,931,400
Thereafter	1,683,300
	<u>\$9,881,900</u>

The remaining weighted average lease term of the Company's assets under operating leases was 35 months and 41 months at September 30, 2020 and December 31, 2019, respectively.

*(b) Sales-Type and Finance Leases*

In January 2020, the Company amended the leases for three of its assets that were subject to sales-type leases. The amendments provided for (i) the sale of one aircraft to the customer in January 2020, which resulted in a gain of \$12,700, (ii) application of collected maintenance reserves and a security deposit held by the Company to past due amounts for the other two aircraft, (iii) payments totaling \$585,000 in January for two of the leases and (iv) the reduction of future payments due under the two leases. As a result of payment delinquencies by the two customers of these aircraft, the Company recorded a bad debt allowance of \$1,170,000 during the first quarter.

In January 2020, the lessee for an aircraft leased pursuant to a direct financing lease notified the Company of its intention to exercise the lease-end purchase option for the aircraft in March 2020. In February 2020, the Company and the same lessee agreed to the early exercise of lease-end purchase options for direct financing leases that were to expire in March 2021 and March 2022. All three aircraft were sold to the lessee in March 2020, resulting in a loss of \$52,000. During the second and third quarters of 2020, the Company recorded additional legal expenses totaling \$8,600 related to the sale.

At September 30, 2020 and December 31, 2019, the net investment included in sales-type leases and direct financing leases receivable were as follows:

At September 30, 2020 and December 31, 2019, the net investment included in sales-type leases and direct financing leases receivable were as follows:

	September 30, 2020	December 31, 2019
Gross minimum lease payments receivable	\$4,138,000	\$2,772,300
Less unearned interest	(88,000)	(1,053,900)
Allowance for doubtful accounts	(1,170,000)	(2,908,600)
Difference between minimum lease payments receivable and collateral value of leases	-	(7,700)
Finance leases receivable	<u>\$2,880,000</u>	<u>\$8,802,100</u>

As of September 30, 2020, minimum future payments receivable under finance leases were as follows:

Years ending December 31

Remainder of 2020	\$1,013,000
2021	1,284,000
2022	1,284,000
2023	557,000
	<u>\$4,138,000</u>

The remaining weighted average lease term of the Company's assets under sales-type and finance leases was 28 months and 20 months at September 30, 2020 and December 31, 2019, respectively.

The following is a roll forward of the Company's finance lease receivable allowance for doubtful accounts from December 31, 2019 to September 30, 2020:

Balance, December 31, 2019	\$2,908,600
Deductions upon sale of assets	(735,200)
Deductions upon lease amendments	(2,173,400)
Additions charged to expense	1,170,000
Balance, September 30, 2020	<u>\$1,170,000</u>

### 3. Assets Held for Sale

Assets held for sale at September 30, 2020 included three regional jet aircraft, one turboprop aircraft, which is subject to a short-term operating lease, and airframe parts from two turboprop aircraft.

During the third quarter of 2020, the Company recorded a loss of \$139,000 on an aircraft that is held for sale, which was written down to its estimated sales price, less cost of sale.

During the third quarter of 2020, the Company received \$69,400 in cash and accrued \$25,500 in receivables for parts sales. These amounts were accounted for as follows: \$30,100 reduced accounts receivable for parts sales accrued in the second quarter of 2020; \$43,600 reduced the carrying value of the parts; and \$21,200 was recorded as gains in excess of the carrying value of the parts. During the third quarter of 2019, the Company received \$220,500 in cash and accrued \$77,000 in receivables for parts sales. These amounts were accounted for as follows: \$142,100 reduced accounts receivable for parts sales accrued in the second quarter of 2019; \$131,900 reduced the carrying value of the parts; and \$23,500 was recorded as gains in excess of the carrying value of the parts.

### 4. Notes Payable and Accrued Interest

#### 4. Notes Payable and Accrued Interest

At September 30, 2020 and December 31, 2019, the Company's notes payable and accrued interest consisted of the following:

	September 30, 2020	December 31, 2019
MUFG Credit Facility and MUFG Loan:		
Principal	\$5,069,100	\$4,084,100
Unamortized debt issuance costs	(1,558,000)	(3,084,200)
Accrued interest	2,280,000	376,200
Nord Loans:		
Principal	25,783,000	30,914,500
Unamortized debt issuance costs	(348,500)	(741,500)
Accrued interest	72,400	89,300
Paycheck Protection Program Loan:		
Principal	276,400	-
Accrued interest	1,000	-
	<u>\$11,575,400</u>	<u>\$11,638,400</u>

##### (a) MUFG Credit Facility

In February 2019, the MUFG Credit Facility, which was to expire on May 31, 2019, was extended to February 19, 2023, and was amended in certain other respects. Also, four aircraft that previously served as collateral under the MUFG Credit Facility and two aircraft that previously served as collateral under special-purpose subsidiary financings were refinanced in February 2019 using non-recourse term loans (the "Nord Loans") with an aggregate principal of \$44.3 million.

In addition to payment obligations (including principal and interest payments on outstanding borrowings and commitment fees based on the amount of any unused portion of the MUFG Credit Facility), the MUFG Credit Facility agreement contained financial covenants with which the Company must comply, including, but not limited to, positive earnings requirements, minimum net worth standards and certain ratios, such as debt to equity ratios.

The Company was not in compliance with various covenants contained in the MUFG Credit Facility agreement, including those related to interest coverage and debt service coverage ratios and a no-net-loss requirement under the MUFG Credit Facility, beginning in the third quarter of 2019.

On October 15, 2019, the agent bank for the MUFG Lenders delivered a Reservation of Rights Letter to the Company which contained notice of the Borrowing Base Default and a demand for repayment of the amount of the Borrowing Base Deficit by January 13, 2020, and also contained formal notices of default under the MUFG Credit Facility relating to the alleged material adverse effects on the Company's business as a result of the early termination of leases for three aircraft and potential financial covenant noncompliance based on the Company's financial projections provided to the MUFG Lenders (the Borrowing Base Default and such other defaults referred to as the "Specified Defaults"). The Reservation of Rights Letter also informed the Company that further advances under the MUFG Credit Facility agreement would no longer be permitted due to the existence of such defaults.

In October, November and December 2019, the Company, agent bank and the MUFG Lenders entered into a Forbearance Agreement and amendments extending the Forbearance Agreement with respect to the Specified Defaults under the MUFG Credit Facility. The Forbearance Agreement (i) provided that the MUFG Lenders temporarily forbear from exercising default remedies under the MUFG Credit Facility agreement for the Specified Defaults, (ii) reduced the maximum availability under the MUFG Credit Facility to \$85 million and (iii) extended the cure period for the Borrowing Base Deficit from January 13, 2020 to February 12, 2020. The Forbearance Agreement also allowed the Company to continue to use LIBOR as its benchmark interest rate, but increased the margin on the Company's LIBOR-based loans under the MUFG Credit Facility from a maximum of 3.75% to 6.00% and set the margin on the Company's prime rate-based loans at 2.75%, as well as added a provision for paid-in-kind interest ("PIK Interest) of 2.5% to be added to the outstanding balance of the MUFG Credit Facility debt in lieu of a cash payment. The Company paid cash fees of \$406,250 in connection with the Forbearance Agreement and amendments, as well as a fee of \$832,100, which was added to the outstanding balance of the MUFG Credit Facility debt in lieu of a cash payment. The Forbearance Agreement was in effect until December 30, 2019, after which the Company and the MUFG Lenders agreed not to further amend the Forbearance Agreement. On February 12, 2020, the agent bank for the MUFG Lenders delivered a Reservation of Rights Letter to the Company which contained notice of the failure to cure the Borrowing Base Default by February 12, 2020.

The unused amount of the MUFG Credit Facility was \$915,900 as of December 31, 2019. The weighted average interest rate on the MUFG Credit Facility was 10.23% at December 31, 2019.

On May 1, 2020, the Company and the MUFG Lenders entered into a Fourth Amended and Restated Loan and Security Agreement, which amended and restated the existing agreement regarding the Company's indebtedness to the MUFG Lenders and effected the following changes to the terms and provisions of such indebtedness:

- A forbearance of the existing defaults and events of default under the MUFG Loan Agreement until May 10, 2020, with a provision to extend such forbearance to July 1, 2020 and August 15, 2020, if the Company is still in compliance with the agreement at May 10, 2020 and July 1, 2020, respectively;
- Elimination of the borrowing base collateral value covenant under the MUFG Loan Agreement, and of the existing event of default under the Loan Agreement for a borrowing base deficiency, along with cessation of the default interest accrual on the outstanding loan amount;
- Conversion of the revolving MUFG Credit Facility structure to a term loan structure with an initial principal balance of \$83,689,900.86 and a final maturity date of March 31, 2021;
- Interest accrual on the indebtedness based on the Base Rate (defined as the greater of (i) the rate of interest most recently announced by MUFG as to its U.S. dollar "Reference Rate", or (ii) the Federal Funds Rate plus one-half of one percent (0.50%)), according to the following schedule: (a) Base Rate + 525 bps (0 bps as cash interest and 525 bps as payment in kind ("PIK")) until June 30, 2020, and (b) Base Rate + 525 bps (100 bps as cash interest and 425 bps as PIK) from and after July 1, 2020, subject to a Base Rate floor at 325 bps for both time periods;
- Deferral of the cash component of the interest payments (on the loan indebtedness and swap termination payment obligation) that was due on April 1, 2020 and May 1, 2020, until the earlier of (i) the date of receipt of net proceeds into the Company's restricted account held at MUFG to hold sales proceeds (the "Restricted Account") from the sale of certain enumerated aircraft assets and (ii) July 1, 2020;
- Required sweep of any unrestricted cash in the Company's bank accounts in excess of \$1,000,000 at the end of each fiscal quarter;
- Addition of certain default provisions triggered by certain defaults or other events with respect to the Company's aircraft leases for the Company's aircraft that are collateral for the MUFG Loan Agreement ("Aircraft Collateral");
- Provision for certain payments from the Restricted Account to (i) the Company's investment banking advisor; (ii) payments due under the agreement and for interest on the swap termination indebtedness owed by the Company; and (iii) Lenders' outside counsel and consultants;
- Addition of a requirement for the Company's engagement of a Financial Advisor/Consultant, at the Company's expense, with a specific scope of work as prescribed by the MUFG Loan Agreement;
- Revisions to the Company's required appraisal process for the Aircraft Collateral; and
- Establishment of deadlines for achievement of milestones toward execution of Company strategic alternatives for the Company and/or its assets with respect to the MUFG Loan Agreement indebtedness ("Strategic Alternatives") as follows: (a) obtaining indications of interest for Strategic Alternatives by May 6, 2020, which was subsequently extended to May 20, 2020 and was met by the Company at that time; (b) obtaining a fully-executed (tentative or generally non-binding) agreement on the terms and conditions for a Strategic Alternative by June 29, 2020, which milestone has been met, and (c) consummation of the selected strategic Alternative by August 15, 2020.

On July 8, 2020, the agent bank for the MUFG Lenders delivered a Reservation of Rights Letter to the Company which contained notice of defaults with respect to failure to deliver a lessee acknowledgment of the MUFG Lender's mortgage from one of the Company's lessees (which was delayed due to extended negotiations between MUFG and the lessee relating to form of such acknowledgment) and (ii) the failure to make a deferred interest payment as required under the Loan Agreement that was due and payable on the earlier of July 1, 2020 or the date of the sale of a certain aircraft scheduled to be sold upon its return from its lessee (the closing of which sale was delayed beyond July 1, 2020).

The Company has engaged B. Riley FBR as an investment banking advisor to help (i) formulate a Recapitalization Plan and analyze various strategic financial alternatives to address the Company's capital structure, strategic and financing needs, as well as corporate level transactions aimed at achieving maximum value for the Company's stockholders; and (ii) locate and negotiate with the Company's lenders, potential new lenders, investors or transaction partners who would play a role in the Company's Recapitalization Plan. The Company's ability to develop, obtain approval for and achieve its Recapitalization Plan is subject to a variety of factors. If the Company is not able to satisfy the requirements under the Recapitalization Plan, maintain compliance with its MUFG Indebtedness or raise sufficient capital to repay all amounts owed under the MUFG Indebtedness, the Company's financial condition and liquidity would be materially adversely affected and its ability to continue operations could be materially jeopardized.

As discussed in Note 11, in October 2020, all indebtedness under the MUFG loan was sold to Drake and the Loan Agreement was amended to modify certain provisions.

*(b) Nord Loans*

On February 8, 2019, the Company, through four wholly-owned subsidiary limited liability companies (“LLC Borrowers”), entered into a term loan agreement NordDeutsche Landesbank Girozentrale, New York Branch (“Nord”) that provides for six separate term loans (“Nord Loans”) with an aggregate principal amount of \$44.3 million. Each of the Nord Loans is secured by a first priority security interest in a specific aircraft (“Nord Loan Collateral Aircraft”) owned by an LLC Borrower, the lease for such aircraft, and a pledge by the Company of its membership interest in each of the LLC Borrowers, pursuant to a Security Agreement among the LLC Borrowers and a security trustee, and certain pledge agreements. Two of the Nord Loan Collateral Aircraft that are owned by the Company’s two UK special-purpose entities were previously financed using special-purpose financing. The interest rates payable under the Nord Loans vary by aircraft, and are based on a fixed margin above either 30-day or 3-month LIBOR. The proceeds of the Nord Loans were used to pay down the MUFG Credit Facility and pay off the UK LLC SPE Financing. The maturity of each Nord Loan varies by aircraft, with the first Nord Loan maturing in October 2020 and the last Nord Loan maturing in May 2025. The debt under the Nord Loans is expected to be fully amortized by rental payments received by the LLC Borrowers from the lessees of the Nord Loan Collateral Aircraft during the terms of their respective leases and remarketing proceeds.

The Nord Loans include covenants that impose various restrictions and obligations on the LLC Borrowers, including covenants that require the LLC Borrowers to obtain Nord consent before they can take certain specified actions, and certain events of default. If an event of default occurs, subject to certain cure periods for certain events of default, Nord would have the right to terminate its obligations under the Nord Loans, declare all or any portion of the amounts then outstanding under the Nord Loans to be accelerated and due and payable, and/or exercise any other rights or remedies it may have under applicable law, including foreclosing on the assets that serve as security for the Nord Loans. The Company was in compliance with all covenants under the Nord Loans at December 31, 2019 but, as discussed below, was in default of its obligation to make its quarterly payments due on March 24, 2020 and June 24, 2020.

As a result of the COVID-19 Outbreak, in March and June 2020, one of the Company’s customers, which leases two regional jet aircraft subject to Nord Loan financing, did not make its quarterly rent payments totaling approximately \$2.8 million. The nonpayment led to corresponding Nord Loan financing payment events of default under the Nord Loans for each of the LLC Borrowers. In May 2020, with Nord’s consent, the Company collected on the customer’s security letters of credit and paid a portion of the March and June financing payments due under the Nord Loans, and entered into an agreement with the customer to defer payment of the remaining balance of the March rent to June 2020. In June 2020, the Company agreed with the customer to defer payment of the March and June rent to September 2020, and entered into an agreement with Nord to defer until September 24, 2020 (i) payment of the principal amount due under the respective Nord Loans for the two aircraft due in March and June 2020 and (ii) payment of past due interest at the default interest rate on the March and June 2020 overdue payments. The lease arrearage was repaid by the lessee in late September, which permitted the special-purpose subsidiaries to come back into compliance with their Nord Loan indebtedness. The lessee also paid deposits totaling approximately \$3,444,000 for purchase of the aircraft. As discussed in Note 11, in October 2020, the Company sold the two aircraft to the lessee, and fully repaid the term loan indebtedness on such aircraft with the proceeds of the sale. The excess proceeds from the purchase were applied to the remaining Nord Term Loan indebtedness owed by a special-purpose subsidiary of the Company secured by three regional jets on lease to a U.S. regional airline. The lessee of those aircraft is in compliance and current in its lease obligations, and the special-purpose subsidiary is in full compliance with its loan repayment obligations.

As a result of the customer’s non-payments in March and June 2020 and potential consequent uncertainty concerning future interest payments under the related Nord Loans, the Company dedesignated the two related derivative instruments from hedge accounting during the first quarter of 2020 since the swapped interest was not deemed as probable to occur.

After discussions with the lessee for the remaining three swaps related to the Nord Loans, the Company determined that there was sufficient uncertainty related to rent payments and related debt payments, and that the Company could not conclude that the payments related to the swaps were probable of occurring, so that the Company dedesignated those swaps from hedge accounting in March 2020 as well.

*(c) Paycheck Protection Program Loan*

On May 20, 2020, JetFleet Management Corp. (the “PPP Borrower”), a subsidiary of AeroCentury Corp., was granted a loan (the “PPP Loan”) from American Express National Bank in the aggregate amount of \$276,353, pursuant to the Paycheck Protection Program (the “PPP”) under Division A, Title I of the CARES Act, which was enacted March 27, 2020. The application for these funds required the Company to, in good faith, certify that the current economic uncertainty made the loan request necessary to support the ongoing operations of the Company. This certification further required the Company to take into account its current business activity and its ability to access other sources of liquidity sufficient to support ongoing operations in a manner that is not significantly detrimental to the business. The receipt of these funds, and the forgiveness of the loan attendant to these funds, is dependent on the Company having initially qualified for the loan and qualifying for the forgiveness of such loan based on its future adherence to the forgiveness criteria.

The PPP Loan, which was in the form of a Note dated May 18, 2020 issued by the PPP Borrower and is included in the Company’s notes payable

and accrued interest, matures on April 22, 2022 and bears interest at a rate of 1.00% per annum, payable in 18 monthly payments commencing on November 20, 2020. The Note may be prepaid by the PPP Borrower at any time prior to maturity with no prepayment penalties. Funds from the PPP Loan may only be used for payroll costs and any payments of certain covered interest, lease and utility payments. The Company intends to use the entire PPP Loan amount for qualifying expenses. Under the terms of the PPP, certain amounts of the Loan may be forgiven if they are used for qualifying expenses as described in the CARES Act. Although the Company expects that all or a significant portion of the PPP loan will be forgiven, no assurance can be provided that the Company will obtain such forgiveness.

## 5. Derivative Instruments

In the first quarter of 2019, the Company entered into eight fixed pay/receive variable interest rate swaps. The Company entered into the interest rate swaps in order to reduce its exposure to the risk of increased interest rates. With respect to the six interest rate swaps entered into by the LLC Borrowers, the swaps were deemed necessary so that the anticipated cash flows of such entities, which arise entirely from the lease rents for the aircraft owned by such entities, would be sufficient to make the required Nord Loan principal and interest payments, thereby preventing default so long as the lessees met their lease rent payment obligations. The two interest rate swaps entered into by AeroCentury were intended to protect against the exposure to interest rate increases on \$50 million of the Company's MUFG Credit Facility debt.

The Company estimates the fair value of derivative instruments using a discounted cash flow technique and uses creditworthiness inputs that corroborate observable market data evaluating the Company's and counterparties' risk of non-performance. Valuation of the derivative instruments requires certain assumptions for underlying variables and the use of different assumptions would result in a different valuation. Management believes it has applied assumptions consistently during the period.

The Company designated seven of its interest rate swaps as cash flow hedges. Changes in the fair value of the hedged swaps are included in other comprehensive income/(loss), which amounts are reclassified into earnings in the period in which the transaction being hedged affects earnings (i.e., with future settlements of the interest rate swaps). One of the interest rate swaps was not eligible under its terms for hedge treatment and was terminated in 2019 when the associated asset was sold and the related debt was paid off. Changes in fair value of non-hedge derivatives are reflected in earnings in the periods in which they occur.

Six of the interest rate swaps were entered into by the LLC Borrowers and provided for reduced notional amounts that mirror the amortization under the Nord Loans entered into by the LLC Borrowers, effectively converting each of the six Nord Loans from a variable to a fixed interest rate, ranging from 5.38% to 6.30%. Each of these six interest rate swaps extended for the duration of the corresponding Nord Loan. Two of the swaps have maturities in 2020 and three have maturities in 2025. The sixth swap was terminated in the fourth quarter of 2019 in connection with the sale of the related aircraft,

As discussed in Note 4, in March, the Company determined that the future hedged interest payments related to its five remaining Nord Loan interest rate hedges were no longer probable of occurring, and consequently dedesignated all five swaps as hedges. As a result of dedesignation, future changes in market value will be recognized in ordinary income and AOCI will be reclassified to ordinary income as the forecasted transactions occur. Accumulated other comprehensive loss of \$114,600 and \$284,500 related to the Nord Swaps was recognized as an expense in the third quarter and first nine months of 2020, respectively.

The other two interest rate swaps (the "MUFG Swaps"), related to the Company's MUFG Credit Facility, were entered into by AeroCentury and had notional amounts totaling \$50 million and were to extend through the maturity of the MUFG Credit Facility in February 2023. Under the ISDA agreement for these interest rate swaps, defaults under the MUFG Credit Facility give the swap counterparty the right to terminate the interest rate swaps with any breakage costs being the liability of the Company.

In October 2019, the Company determined that it was no longer probable that forecasted cash flows for its two interest rate swaps with a nominal value of \$50 million would occur as scheduled as a result of the Company's defaults under the MUFG Credit Facility. Therefore, those swaps were no longer subject to hedge accounting and changes in fair market value thereafter were recognized in earnings as they occurred. As a result of the forecasted transaction being not probable to occur, accumulated other comprehensive loss of \$34,500 and \$1,421,800 related to the MUFG Swaps was recognized as interest expense in the third quarter and first nine months of 2020, respectively. The two swaps related to the MUFG Credit Facility were terminated in March 2020 and the Company incurred a \$3.1 million obligation in connection with such termination, payment of which is due no later than the March 31, 2021 maturity of the Drake Indebtedness.

The Company has reflected the following amounts in its net loss:

For the Nine Months  
Ended

For the Three Months  
Ended

The Company has reflected the following amounts in its net loss:

	For the Nine Months Ended September 30,		For the Three Months Ended September 30,	
	2020	2019	2020	2019
Change in value of interest rate swaps	\$ 1,980,500	\$ 455,100	\$ (10,000)	\$ 3,700
Reclassification from other comprehensive income	538,500	5,900	149,100	28,000
Reclassification from other comprehensive income – forecasted transaction not probable to occur	1,167,700	-	-	-
Included in interest expense	<u>\$ 3,686,700</u>	<u>\$ 461,000</u>	<u>\$ 139,100</u>	<u>\$ 31,700</u>

The following amount was included in other comprehensive income/(loss), before tax:

Unrealized gain/(loss) on derivative instruments	\$ (575,000)	\$ 1,985,100	\$ -	\$ (174,500)
Reclassification from other comprehensive income	538,500	5,900	149,100	28,000
Reclassification from other comprehensive income – forecasted transaction not probable to occur	1,167,700	-	-	-
Change in value of interest rate swaps	<u>\$ 1,131,200</u>	<u>\$ (1,979,200)</u>	<u>\$ 149,100</u>	<u>\$ (146,500)</u>

Approximately \$232,800 of the current balance of accumulated other comprehensive loss is expected to be reclassified in the next twelve months.

At September 30, 2020, the fair value of the Company's interest rate swaps was \$874,700.

The Company evaluates the creditworthiness of the counterparties under its hedging agreements. The swap counterparties for the Company's interest rate swaps are large financial institutions in the United States that possess an investment grade credit rating. Based on this rating, the Company believes that the counterparties are creditworthy and that their continuing performance under the hedging agreements is probable.

## 6. Lease Right of Use Asset and Liability

The Company was a lessee under a lease of the office space it occupies in Burlingame, California, which expired in June 2020. The lease also provided for two, successive one-year lease extension options for amounts that were substantially below the market rent for the property. The lease provided for monthly rental payments according to a fixed schedule of increasing rent payments. As a result of the below-market extension options, the Company determined that it was reasonably certain that it would extend the lease and, therefore, included such extended term in its calculation of the right of use asset ("ROU Asset") and lease liability recognized in connection with the lease.

In addition to a fixed monthly payment schedule, the office lease also included an obligation for the Company to make future variable payments for certain common areas and building operating and lessor costs, which have been and will be recognized as expense in the periods in which they are incurred. As a direct pass-through of applicable expense, such costs were not allocated as a component of the lease.

Effective January 1, 2020, the Company reduced both the size of the office space leased and the amount of rent payable in the future. As such, the Company recognized a reduction in both the capitalized amount related to the surrendered office space and a proportionate amount of the liability associated with its future lease obligations. In January 2020, the Company recorded a loss of \$160,000 related to the reduction in its ROU Asset, net of the reduction in its operating lease liability, and expected to recognize amortization of \$308,100, \$317,600 and \$162,600 in 2020, 2021 and the first half of 2022, respectively.

In March 2020, the Company elected not to exercise the extension options for its office lease. The lease liability associated with the office lease was calculated at March 31, 2020 and December 31, 2019 by discounting the fixed, minimum lease payments over the remaining lease term, including the below-market extension periods, at a discount rate of 7.25%, which represents the Company's estimate of the incremental borrowing rate for a collateralized loan for the type of underlying asset that was the subject of the office lease at the time the lease liability was evaluated. As a result of non-exercise of its extension option, the Company reduced the lease liability to reflect only the three remaining rent payments in the second quarter of 2020.

In July 2020, the lease for the Company's office lease was extended for one month to July 31, 2020 at a rate of \$10,000. The Company has signed a lease for a smaller office suite in the same building effective August 1, 2020. The lease provides for a term of 30 months expiring on January 31, 2023, at a monthly base rate of approximately \$7,400, with no rent due during the first six months. The Company recognized an ROU asset and lease liability of \$169,800, both of which were non-cash items and are not reflected in the condensed consolidated statement of cash flows. No cash

was paid at the inception of the lease, and a discount rate of 3% was used, based on the interest rates available on secured commercial real estate loans available at the time. At September 30, 2020, the weighted average discount rate was 3% and the weighted average remaining lease term was 28 months.

The Company estimates that the maturities of operating lease base rent of its office space were as follows as of September 30, 2020 and December 31, 2019:

	September 30, 2020	December 31, 2019
2020	\$ -	\$ 145,000
2021	88,700	147,200
2022	88,700	74,700
	<u>177,400</u>	<u>366,900</u>
Discount	(6,700)	(30,500)
Lease liability	<u>\$ 170,700</u>	<u>\$ 336,400</u>

During the quarter ended September 30, 2020, the Company recognized amortization, finance costs and other expense related to the office lease as follows:

Fixed rental expense during the quarter	\$ 11,800
Variable lease expense	(1,200)
Total lease expense during the quarter	<u>\$ 10,600</u>

Variable rent for the quarter ended September 30, 2020 reflects a refund of previously charged and accrued common area maintenance charges for the Company's office space.

## 7. 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.

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

As of September 30, 2020, the Company measured the fair value of its interest rate swaps of \$25,783,000 (notional amount) based on Level 2 inputs, due to the usage of inputs that can be corroborated by observable market data. The Company estimates the fair value of derivative instruments using a discounted cash flow technique and has used creditworthiness inputs that corroborate observable market data evaluating the Company's and counterparties' risk of non-performance. The interest rate swaps had a net fair value liability of \$874,700 as of September 30, 2020. In the quarter and nine months ended September 30, 2020, \$(10,000) and \$1,980,500 was realized through the income statement as a (decrease)/increase in interest expense.

As of December 31, 2019, the Company measured the fair value of its interest rate swaps of \$80,914,500 (notional amount) based on Level 2 inputs, due to the usage of inputs that can be corroborated by observable market data. The Company estimates the fair value of derivative instruments using a discounted cash flow technique and has used creditworthiness inputs that corroborate observable market data evaluating the Company's and counterparties' risk of non-performance. The interest rate swaps had a net fair value liability of \$1,824,500 as of December 31, 2019. In the year ended December 31, 2019, \$255,200 was realized through the income statement as an increase in interest expense.

The following table shows, by level within the fair value hierarchy, the Company's assets and liabilities at fair value on a recurring basis as of September 30, 2020 and December 31, 2019:

	September 30, 2020				December 31, 2019			
	Total	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3
Money market funds	\$ -	\$ -	\$ -	\$ -	\$ 400	\$ 400	\$ -	\$ -
Derivatives	(874,700)	-	(874,700)	-	(1,824,500)	-	(1,824,500)	-
<b>Total</b>	<b>\$ (874,700)</b>	<b>\$ -</b>	<b>\$ (874,700)</b>	<b>\$ -</b>	<b>\$ (1,824,100)</b>	<b>\$ 400</b>	<b>\$ (1,824,500)</b>	<b>\$ -</b>

There were no transfers between Level 1 and Level 2 during the third quarters or nine months ended September 30, 2020 or 2019, and there were no transfers into or out of Level 3 during the same periods.

#### 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 these and other assets held for sale, by reference to independent appraisals, quoted market prices (e.g., offers to purchase) and other factors. These are considered Level 3 within the fair value hierarchy. 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 asset's carrying value exceeds its fair value. During the third quarter of 2020, the Company recorded impairment losses totaling \$300,000 for two of its aircraft held for lease, which were written down to their estimated sales prices, less cost of sale. The Company also recorded a losses of \$139,000 for a turboprop aircraft that was written down its estimated sales price, less cost of sale. The Company recorded impairment charges totaling \$23,354,600 on two of its assets held for lease and three of its assets held for sale in the third quarter of 2019, which had a fair value of \$36,256,500.

The following table shows, by level within the fair value hierarchy, the Company's assets at fair value on a nonrecurring basis as of September 30, 2020 and December 31, 2019:

	Assets Written Down to Fair Value								Total Losses	
	September 30, 2020				December 31, 2019				For the Nine Months Ended September 30,	
	Total	Level			Total	Level			2020	2019
Assets held for lease	\$7,000,000	\$ -	\$ -	\$7,000,000	\$ -	\$ -	\$ -	\$ -	\$7,006,600	\$ -
Assets held for sale	12,970,000	-	-	12,970,000	25,880,700	-	\$ -	25,880,700	9,813,900	11,424,900
<b>Total</b>	<b>\$29,970,000</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$29,970,000</b>	<b>\$25,880,700</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$25,880,700</b>	<b>\$16,820,500</b>	<b>\$11,424,900</b>

There were no transfers between Level 1 and Level 2 and no transfers into or out of Level 3 in either of the third quarters or nine-month periods ended September 30, 2020 or 2019.

#### Fair Value of Other Financial Instruments

The Company's financial instruments, other than cash and cash equivalents, consist principally of finance leases receivable, amounts borrowed under the MUFG Credit Facility, notes payable under special-purpose financing, its derivative termination liability and its derivative instruments. The fair value of accounts receivable, accounts payable and the Company's maintenance reserves and accrued maintenance costs approximates the carrying value of these financial instruments because of their short-term maturity. The fair value of finance lease receivables approximates the carrying value as discussed in Note 1(f). The fair value of the Company's derivative instruments is discussed in Note 5 and in this note above in "Assets and Liabilities Measured and Recorded at Fair Value on a Recurring Basis."

Borrowings under the Company's MUFG Credit Facility bore floating rates of interest that reset periodically to a market benchmark rate plus a credit margin. The same is true of the MUFG Loan. The Company believes the effective interest rate under the MUFG Credit Facility approximated then current market rates for such indebtedness at December 31, 2019 and, under the MUFG Loan, approximates current market rates, and therefore that the outstanding principal and accrued interest of \$87,349,100 and \$84,460,300 at September 30, 2020 and December 31, 2019, respectively, approximate their fair values on such dates. The fair value of the Company's outstanding balance of its MUFG Credit Facility and MUFG Loan are categorized as a Level 3 input under the GAAP fair value hierarchy.

Before their repayment in February 2019 in connection with the Nord Loans refinancing, the amounts payable under the UK LLC SPE Financing were payable through the fourth quarter of 2020 and bore a fixed rate of interest. As discussed above, during February 2019, the UK LLC SPE Financing and four assets that previously served as collateral under the MUFG Credit Facility were refinanced using the Nord Loans. The Company believes the effective interest rate under the special-purpose financings approximates current market rates for such indebtedness at the dates of the condensed consolidated balance sheets, and therefore that the outstanding principal and accrued interest of \$25,855,400 and \$31,003,800 approximate their fair values at September 30, 2020 and December 31, 2019, respectively. Such fair value is categorized as a Level 3 input under the GAAP fair value hierarchy.

There were no transfers in or out of assets or liabilities measured at fair value under Level 3 during the third quarters or nine months ended September 2020 or 2019.

## 8. Commitments and Contingencies

In the ordinary course of the Company's business, the Company may be subject to lawsuits, arbitrations and administrative proceedings from time to time. The Company believes that the outcome of any existing or known threatened proceedings, even if determined adversely, should not have a material adverse effect on the Company's business, financial condition, liquidity or results of operations.

## 9. Income Taxes

The Company recorded income tax expense of \$604,900 in the third quarter of 2020, or negative 17.4% of pre-tax loss, compared to \$2.3 million income tax benefit, or 21.5% of pre-tax loss in the third quarter of 2019. The difference in the effective federal income tax rate from the normal statutory rate was primarily related to the recording of a valuation allowance of \$1.4 million in the third quarter on U.S. and foreign deferred tax assets.

The Company recorded income tax benefit of \$3.4 million for the nine months ended September 30, 2020, or 10.9% of pre-tax loss, compared to \$2.6 million income tax benefit, or 21.5% of pre-tax loss, for the nine months ended September 30, 2019. The difference in the effective federal income tax rate from the normal statutory rate was primarily related to the recording of a valuation allowance of \$4.6 million for the nine months ended September 30, 2020 on U.S. and foreign deferred tax assets.

In March of 2020, the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act") became law. The CARES Act included tax provisions under which net operating losses from 2018, 2019 and 2020 can be carried back for five years, modifying the law that had previously not permitted any carryback, and also increased the amount of deductible interest from 30% to 50% of adjusted taxable income for the 2019 and 2020 years. These changes have not had any effect on the Company's expected cash tax expenditures or income tax expense. The CARES Act also accelerated the ability to receive refunds of AMT credits from prior year, which allowed the Company to accelerate \$11,400 of the refund of such credit into its 2019 return.

## 10. Computation of Loss Per Share

Basic and diluted loss per share are calculated as follows:

	For the Nine Months Ended September 30,		For the Three Months Ended September 30,	
	2020	2019	2020	2019
Net loss	<u>\$27,777,200</u>	<u>\$9,617,100</u>	<u>\$4,081,100</u>	<u>\$8,231,400</u>
Weighted average shares outstanding for the period	1,545,884	1,545,884	1,545,884	1,545,884
Basic loss per share	<u>\$ (17.97)</u>	<u>\$ (6.22)</u>	<u>\$ (2.64)</u>	<u>\$ (5.32)</u>
Diluted loss per share	<u>\$ (17.97)</u>	<u>\$ (6.22)</u>	<u>\$ (2.64)</u>	<u>\$ (5.32)</u>

Basic loss per common share is computed using net loss and the weighted average number of common shares outstanding during the period. Diluted loss per common share is computed using net (loss)/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. There were no anti-dilutive shares outstanding during the three months or nine months ended September 30, 2020 or 2019.

## 11. Subsequent Events

### (a) MUFG's Sale of Indebtedness to Drake

On October 30, 2020, Drake Asset Management Jersey Limited ("Drake"), purchased from the MUFG Lenders all of the outstanding indebtedness of the Company under such loan, totaling approximately \$87.9 million as well as all of the Company's indebtedness to MUFG Bank, Ltd. of

approximately \$3.1 million for termination of interest rate swaps entered into with respect to such Loan Agreement indebtedness (such total indebtedness with Drake as Lender referred to as the “Drake Indebtedness”). The purchase and sale was consented to by the Company pursuant to a Consent and Release Agreement of Borrower Parties, entered into by the Company and its subsidiaries. The closing of this debt purchase transaction satisfied the requirement under the Loan Agreement for execution of a Strategic Alternative with respect to the MUFG Loan indebtedness satisfactory to the MUFG Lenders.

On the same day, the Company entered into an Amendment No. 1 to the Loan Agreement (“Amendment No. 1”) with Drake and UMB Bank, N.A., the replacement Administrative Agent under the Loan Agreement, to amend the Loan Agreement (such Loan Agreement as amended, with Drake as Lender thereunder, referred to as the “Drake Loan Agreement”) as follows:

- Deferral of the cash component of the interest payments due under the Drake Loan Agreement, commencing with the payments due for March 2020, and continuing on each consecutive month thereafter, which deferred interest is to be capitalized and added to the principal balance of the indebtedness on each respective interest payment due date, until such time as the indebtedness is repaid.
- Deletion of the requirement for the Company's execution of a Strategic Alternative and of the milestones therefor;
- Deletion of the requirement for the Company's maintenance of a restricted account held with an MUFG Lender to hold aircraft sales proceeds pending application toward the Drake Indebtedness;
- Replacement of references to “MUFG Union Bank, N.A.,” with “UMB, Bank, N.A.,” the new Administrative Agent under the Loan Agreement;
- Requirement of approval by Drake for any “Material Amendments” to leases for the collateral, defined as any amendment of, or waiver or consent under, any lease involving a modification of lease payments, any reduction in, or waiver or deferral of, Rent, a modification to any residual value guaranty, any modification that adversely affects the collateral or the rights and interests of the lender and/or administrative agent in the collateral, any reduction of any amounts payable to any lender or Agent under any indemnity, or any change to the state of registration of aircraft collateral; and
- Deletion of certain financial reporting requirements and changes to required frequency of certain other surviving reporting requirements.

The Drake Indebtedness is secured by a first priority lien held by Drake, which lien is documented in an amended and restated mortgage and security agreement assigned to Drake, on all of the Company's assets, including the Company's aircraft portfolio, except for two aircraft on lease to Kenyan lessees and five aircraft, two of which were sold in October 2020, that are subject to special purpose financing held by subsidiaries of the Company.

The Company and Drake are currently engaged in discussions regarding the satisfaction and discharge of the Drake Indebtedness.

*(b) Sale of Aircraft*

In October 2020, the Company sold two aircraft to the lessee that were subject to Nord Loans, and fully repaid the indebtedness on such aircraft with the proceeds of the sale. The excess proceeds from the purchase were applied to the remaining Nord Term Loan indebtedness owed by a special-purpose subsidiary of the Company secured by three regional jets on lease to a U.S. regional airline.

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

*The following discussion and analysis should be read together with the Company's annual report on Form 10-K for the fiscal year ended December 31, 2019 and the audited consolidated financial statements and notes included therein (collectively, the “2019 Annual Report”), as well as the Company's unaudited condensed consolidated financial statements and the related notes included in this report. Pursuant to Instruction 2 to paragraph (b) of Item 303 of Regulation S-K promulgated by the SEC, in preparing this discussion and analysis, the Company has presumed that readers have access to and have read the disclosure under the same heading contained in the 2019 Annual Report. This discussion and analysis contains forward-looking statements. Please see the cautionary note regarding these statements at the beginning of this report.*

**Overview**

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

*The following discussion and analysis should be read together with the Company's annual report on Form 10-K for the fiscal year ended December 31, 2019 and the audited consolidated financial statements and notes included therein (collectively, the "2019 Annual Report"), as well as the Company's unaudited condensed consolidated financial statements and the related notes included in this report. Pursuant to Instruction 2 to paragraph (b) of Item 303 of Regulation S-K promulgated by the SEC, in preparing this discussion and analysis, the Company has presumed that readers have access to and have read the disclosure under the same heading contained in the 2019 Annual Report. This discussion and analysis contains forward-looking statements. Please see the cautionary note regarding these statements at the beginning of this report.*

### Overview

The Company provides leasing and finance services to regional airlines worldwide. The Company is principally engaged in leasing its aircraft portfolio, primarily consisting of mid-life regional aircraft, through operating leases and finance leases to its customer base of eight airlines in six countries. In addition to leasing activities, the Company sells aircraft from its operating lease portfolio to third parties, including other leasing companies, financial services companies, and airlines. Its operating performance is driven by the composition of its aircraft portfolio, the terms of its leases, and the interest rate of its debt, as well as asset sales.

The COVID-19 pandemic has led to significant cash flow issues for airlines, and some of the Company's customers were unable to timely meet their obligations under their lease obligations with the Company during the first nine months of 2020. This in turn has caused lessees to make requests for lease payment concessions and/or deferrals from the Company, which requires the Company to reach accommodations with its lenders to allow the Company corresponding concessions under its debt financings. The Company expects these circumstances to continue for the foreseeable future.

The Company did not purchase or sell any aircraft during the third quarter of 2020. The Company ended the quarter with a total of eleven aircraft held for lease, with a net book value of approximately \$96 million. This represents a 11% decrease compared to the net book value of the Company's aircraft and engines held for lease at December 31, 2019. In addition to the aircraft held for lease at quarter-end, the Company held two aircraft subject to finance leases and held four aircraft and airframe parts from two aircraft held for sale. In October 2020, the Company sold two aircraft that had been held for lease.

Average portfolio utilization was approximately 89% and 97% during the third quarters of 2020 and 2019, respectively. The year-to-year decrease was due to aircraft that were on lease in the 2019 period, but off lease in the 2020 period.

Net loss for the third quarters of 2020 and 2019 was \$4.1 million and \$8.2 million, respectively, resulting in basic and diluted loss per share of \$(2.64) and \$(5.32), respectively. Pre-tax profit margin (which the Company calculates as its (loss)/income before income tax (benefit)/provision as a percentage of its revenues and other income) was (100%) in the third quarter of 2020 compared to (44%) for the third quarter of 2019.

As discussed above, the Company is currently in discussions with Drake regarding repayment terms for the Drake Indebtedness. While discussions are ongoing, the Company is not required to make cash payment on the accruing interest on the Drake Indebtedness and such interest is being added to the principal as it accrues. The Company does not have sufficient cash to repay the entire Drake Indebtedness, so the Company may need to raise additional debt or equity funds to meet its debt obligations. If additional cash is not available, it is likely that the value of the assets the Company currently holds is not sufficient to repay the entire indebtedness if the assets are sold in the current market environment or foreclosed upon.

As a result of these factors, there is substantial doubt regarding the Company's ability to continue as a going concern.

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### Fleet Summary

#### (a) Assets Held for Lease

Key portfolio metrics of the Company's aircraft held for lease as of September 30, 2020 and December 31, 2019 were as follows:

September

## Fleet Summary

### (a) Assets Held for Lease

Key portfolio metrics of the Company's aircraft held for lease as of September 30, 2020 and December 31, 2019 were as follows:

	September 30, 2020	December 31, 2019
Number of aircraft and engines held for lease	11	11
Weighted average fleet age	12.7 years	11.8 years
Weighted average remaining lease term	35 months	41 months
Aggregate fleet net book value	\$6,052,100	\$108,368,600

	For the Nine Months Ended September 30,		For the Three Months Ended September 30,	
	2020	2019	2020	2019
Average portfolio utilization	88%	98%	89%	97%

The following table sets forth the net book value and percentage of the net book value, by type, of the Company's assets that were held for lease at September 30, 2020 and December 31, 2019:

Type	September 30, 2020		December 31, 2019	
	Number owned	% of net book value	Number owned	% of net book value
Turboprop aircraft:				
Bombardier Dash-8-400	2	21%	2	20%
Regional jet aircraft:				
Embraer 175	3	29%	3	26%
Canadair CRJ-1000	2	15%	2	21%
Canadair CRJ-700	3	21%	3	20%
Canadair CRJ-900	1	14%	1	13%

During the third quarter and first nine months of 2020, the Company did not purchase or sell any aircraft that are held for lease. During the first nine months of 2020, the Company sold one aircraft that had been held for sale, one aircraft that had been held under a sales-type lease and three aircraft that had been held under direct financing leases, and sold certain aircraft parts that were held for sale. In October 2020, the Company sold two aircraft that had been held for lease.

During the third quarter of 2019, the Company purchased no aircraft, sold one aircraft, an engine and certain aircraft parts that were held for sale and reclassified two aircraft from held for lease to held for sale. During the first nine months of 2019, the Company purchased no aircraft, sold two aircraft, an engine and certain aircraft parts that were held for sale, reclassified two aircraft from held for lease to held for sale and reclassified one aircraft from held for lease to a finance lease receivable.

The following table sets forth the net book value and percentage of the net book value of the Company's assets that were held for lease at September 30, 2020 and December 31, 2019 in the indicated regions (based on the domicile of the lessee):

Region	September 30, 2020		December 31, 2019	
	Net book value	% of net book value	Net book value	% of net book value
North America	\$1,533,300	64%	\$3,799,600	59%
Europe	34,518,800	36%	44,569,000	41%
	<u>\$6,052,100</u>	<u>100%</u>	<u>\$108,368,600</u>	<u>100%</u>

For the three months ended September 30, 2020, approximately 60%, 21% and 18% of the Company's operating lease revenue was derived from customers in the United States, Croatia and Canada, respectively. Operating lease revenue does not include interest income from the Company's finance leases. The following table sets forth geographic information about the Company's operating lease revenue for leased aircraft and aircraft equipment, grouped by domicile of the lessee:

Region	For the Nine Months Ended September 30,				For the Three Months Ended September 30,			
	2020		2019		2020		2019	
	Number of lessees	% of operating lease revenue	Number of lessees	% of operating lease revenue	Number of lessees	% of operating lease revenue	Number of lessees	% of operating lease revenue
Europe	3	39%	4	62%	3	22%	4	62%
North America	3	61%	4	37%	3	78%	3	38%
Asia	-	-%	1	1%	-	-%	-	-%

At September 30, 2020 and December 31, 2019, the Company also had two aircraft and six aircraft, respectively, subject to finance leases. The Company did not record any finance lease revenue during the quarter ended September 30, 2020.

*(b) Assets Held for Sale*

Assets held for sale at September 30, 2020 consisted of three Canadair 900 aircraft, one Bombardier Dash-8-300 aircraft and airframe parts from two turboprop aircraft.

**Results of Operations**

*(a) Quarter ended September 30, 2020 compared to the quarter ended September 30, 2019*

*(i) Revenues and Other Income*

Revenues and other income decreased by 85% to \$3.5 million in the third quarter of 2020 from \$24.0 million in the third quarter of 2019. The decrease was primarily a result of decreased operating lease, finance lease and maintenance reserves revenues in the third quarter of 2020.

Operating lease revenue decreased by 52% to \$3.2 million in the third quarter of 2020 from \$6.7 million in the third quarter of 2019, primarily due to reduced rent income resulting from the early termination of four aircraft leases with one of the Company's customers in the third quarter of 2019.

Maintenance reserves that are retained by the Company at lease end are recorded as revenue at that time. The Company recorded \$0.2 million of such revenue during the third quarter of 2020 when an aircraft that had been on lease was returned to the Company and the lease was terminated. During the third quarter of 2019, the Company recorded \$17.0 million of such revenue, arising from maintenance reserves retained upon the termination of four aircraft leases with one customer.

The Company recorded no finance lease revenue in the third quarter of 2020, compared to \$0.3 million in the third quarter of 2019, as a result of the sale of three assets that were subject to direct finance leases during the first quarter of 2020 and the Company's cash-basis accounting for its two sales-type leases in 2020.

*(ii) Expenses*

Total expenses decreased by 80% to \$7.0 million in the third quarter of 2020 from \$34.5 million in the third quarter of 2019. The decrease was primarily a result of decreases in asset impairment losses, depreciation and bad debt expense, the effects of which were partially offset by increases in interest expense and professional fees and general and administrative expenses.

During the third quarter of 2020, the Company recorded impairment charges of \$0.3 million on two assets held for lease, based on estimated future cash flow and \$0.1 million on an asset held for sale, based on expected net sales proceeds. During the third quarter of 2019, the Company recorded impairment charges totaling \$23.4 million for two assets held for lease and one asset held for sale, based on appraised values, and three assets held for sale, based on expected sales proceeds. As a result of four lease terminations during the quarter, the appraised values were based on the maintenance-adjusted condition of the aircraft, rather than the previous basis, which reflected future cash flows under the leases.

For the three months ended September 30, 2020, approximately 60%, 21% and 18% of the Company's operating lease revenue was derived from customers in the United States, Croatia and Canada, respectively. Operating lease revenue does not include interest income from the Company's finance leases. The following table sets forth geographic information about the Company's operating lease revenue for leased aircraft and aircraft equipment, grouped by domicile of the lessee:

Region	For the Nine Months Ended September 30,		For the Nine Months Ended September 30,		For the Three Months Ended September 30,		For the Three Months Ended September 30,	
	2020	2019	2020	2019	2020	2019	2020	2019
	Number of lessees	% of operating lease revenue	Number of lessees	% of operating lease revenue	Number of lessees	% of operating lease revenue	Number of lessees	% of operating lease revenue
Europe	3	39%	4	62%	3	22%	4	62%
North America	3	61%	4	37%	3	78%	3	38%
Asia	-	-%	1	1%	-	-%	-	-%

At September 30, 2020 and December 31, 2019, the Company also had two aircraft and six aircraft, respectively, subject to finance leases. The Company did not record any finance lease revenue during the quarter ended September 30, 2020.

#### *(b) Assets Held for Sale*

Assets held for sale at September 30, 2020 consisted of three Canadair 900 aircraft, one Bombardier Dash-8-300 aircraft and airframe parts from two turboprop aircraft.

### **Results of Operations**

#### *(a) Quarter ended September 30, 2020 compared to the quarter ended September 30, 2019*

##### *(i) Revenues and Other Income*

Revenues and other income decreased by 85% to \$3.5 million in the third quarter of 2020 from \$24.0 million in the third quarter of 2019. The decrease was primarily a result of decreased operating lease, finance lease and maintenance reserves revenues in the third quarter of 2020.

Operating lease revenue decreased by 52% to \$3.2 million in the third quarter of 2020 from \$6.7 million in the third quarter of 2019, primarily due to reduced rent income resulting from the early termination of four aircraft leases with one of the Company's customers in the third quarter of 2019.

Maintenance reserves that are retained by the Company at lease end are recorded as revenue at that time. The Company recorded \$0.2 million of such revenue during the third quarter of 2020 when an aircraft that had been on lease was returned to the Company and the lease was terminated. During the third quarter of 2019, the Company recorded \$17.0 million of such revenue, arising from maintenance reserves retained upon the termination of four aircraft leases with one customer.

The Company recorded no finance lease revenue in the third quarter of 2020, compared to \$0.3 million in the third quarter of 2019, as a result of the sale of three assets that were subject to direct finance leases during the first quarter of 2020 and the Company's cash-basis accounting for its two sales-type leases in 2020.

##### *(ii) Expenses*

Total expenses decreased by 80% to \$7.0 million in the third quarter of 2020 from \$34.5 million in the third quarter of 2019. The decrease was primarily a result of decreases in asset impairment losses, depreciation and bad debt expense, the effects of which were partially offset by increases in interest expense and professional fees and general and administrative expenses.

During the third quarter of 2020, the Company recorded impairment charges of \$0.3 million on two assets held for lease, based on estimated future cash flow and \$0.1 million on an asset held for sale, based on expected net sales proceeds. During the third quarter of 2019, the Company recorded impairment charges totaling \$23.4 million for two assets held for lease and one asset held for sale, based on appraised values, and three assets held for sale, based on expected sales proceeds. As a result of four lease terminations during the quarter, the appraised values were based on the maintenance-adjusted condition of the aircraft, rather than the previous basis, which reflected future cash flows under the leases.

Depreciation expense decreased 55% to \$1.3 million in the third quarter of 2020 from \$3.0 million in the third quarter of 2019 primarily as a result of the reclassification of four aircraft from held for lease to held for sale during the third quarter of 2019, as well as a decrease in depreciation for

two aircraft that were written down to their estimated sale values during the second quarter of 2020.

As a result of payment delinquencies by two customers that lease three of the Company's aircraft subject to finance leases, during the third quarter of 2019, the Company also recorded a bad debt expense of \$3.9 million.

The Company's interest expense increased by 29% to \$3.0 million in the third quarter of 2020 from \$2.3 million in the third quarter of 2019, primarily as a result of a higher average interest rate, the effect of which were partially offset by a lower average debt balance.

Professional fees, general and administrative and other expenses increased 45% to \$1.4 million in the third quarter of 2020 from \$0.9 million in the third quarter of 2019, primarily due to increased legal fees related to the May 2020 MUFG Indebtedness amendment and litigation brought by an activist shareholder and consulting fees related to the May 2020 MUFG Indebtedness amendment.

The Company had a tax expense of \$604,900 in the third quarter of 2020 compared to tax benefit of \$2.3 million in the third quarter of 2019. The effective tax rate for the third quarter of 2020 was a 17.4% tax expense compared to a 21.6% tax benefit in the third quarter of 2019. The difference in the effective income tax rate from the normal statutory rate was primarily related to the recording of a \$1.4 million valuation allowance in the current period on the Company's U.S. and foreign deferred tax assets after concluding that a valuation allowance is necessary for the Company's net U.S. and foreign deferred tax assets not supported by either future taxable income or availability of future reversals of existing taxable temporary differences.

In March of 2020, the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act") became law. The CARES Act included tax provisions under which net operating losses from 2018, 2019 and 2020 can be carried back for five years, modifying the law that had previously not permitted any carryback, and also increased the amount of deductible interest from 30% to 50% of adjusted taxable income for the 2019 and 2020 years. These changes have not had any effect on the Company's expected cash tax expenditures or income tax expense. The CARES Act also accelerated the ability to receive refunds of alternative minimum tax credits from prior years, which allowed the Company to accelerate \$11,400 of the refund of such credit into its 2019 return.

*(b) Nine months ended September 30, 2020 compared to the nine months ended September 30, 2019*

*(i) Revenues and Other Income*

Revenues and other income decreased by 67% to \$12.7 million in the first nine months of 2020 from \$38.7 million in the same period of 2019. The decrease was primarily a result of decreased operating lease, finance lease and maintenance reserves revenues in the 2020 period.

Operating lease revenue decreased by 40% to \$12.4 million in the first nine months of 2020 from \$20.8 million in the same period of 2019, primarily due to reduced rent income resulting from the early termination of four aircraft leases with one of the Company's customers in the third quarter of 2019 and reduced rent for two assets in the 2020 period as a result of lease amendments related to the COVID-19 Outbreak, as well as the sale of an asset in the first quarter of 2019 that had been on lease until the time of sale.

Maintenance reserves that are retained by the Company at lease end are recorded as revenue at that time. The Company recorded \$0.2 million of such revenue during the first nine months of 2020 when an aircraft that had been on lease was returned to the Company and the lease was terminated. During the nine months ended September 30, 2019, the Company recorded \$17.0 million of such revenue, arising from maintenance reserves retained upon the termination of four aircraft leases with one customer.

Finance lease revenue decreased by 93% to \$0.1 million in the first nine months of 2020, compared to \$0.8 million in the same period of 2019, as a result of the sale of three assets that were subject to direct finance leases during the first quarter of 2020 and the Company's cash-basis accounting for its two sales-type leases, for which it received no payments in the 2020 period.

*(ii) Expenses*

Total expenses decreased by 14% to \$43.8 million in the first nine months of 2020 from \$51.0 million in the same period of 2019. The decrease was primarily a result of decreases in asset impairment losses, depreciation and bad debt expense, the effects of which were partially offset by increases in interest expense and professional fees and general and administrative expenses.

During the nine months ended September 30, 2020, the Company recorded impairment charges of (i) \$7.0 million on two assets held for lease, based on estimated future cash flow and (ii) \$9.8 million on five assets held for sale, based on appraised values or expected sales proceeds. During the nine months ended September 30, 2019, the Company recorded impairment charges totaling \$24.9 million on two assets held for lease and two assets held for sale, based on appraised values, and five assets held for sale, based on expected sales proceeds. As a result of four lease terminations during the third quarter of 2019, the appraised values were based on the maintenance-adjusted condition of the aircraft, rather than the previous basis, which reflected future cash flows under the leases.

Depreciation expense decreased 40% to \$5.5 million in the first nine months of 2020 from \$9.1 million in the first nine months of 2019 primarily as a result of the reclassification of four aircraft from held for lease to held for sale during the third quarter of 2019, as well as a decrease in depreciation for two aircraft that were written down to their estimated sale values during the second quarter of 2020.

As a result of payment delinquencies by two of the Company's customers under its two sales-type leases and decreases in the appraised values of the underlying assets, the Company recorded a bad debt expense of \$1.2 million in the first nine months of 2020. As a result of payment delinquencies by two customers that lease three of the Company's aircraft subject to finance leases, during the first nine months of 2019, the Company also recorded a bad debt expense of \$3.9 million.

The Company's interest expense increased by 74% to \$13.5 million in the first nine months of 2020 from \$7.7 million in the same period of 2019, primarily as a result of a higher average interest rate, \$2.0 million of valuation charges related to the Company's interest rate swaps and a \$2.0 million write-off of a portion of the Company unamortized debt issuance costs related to the MUFG Credit Facility, the effects of which were partially offset by a lower average debt balance.

Professional fees, general and administrative and other expenses increased 66% to \$4.4 million in the first nine months of 2020 from \$2.6 million in the first nine months of 2019, primarily due to increased legal fees related to the May 2020 MUFG Indebtedness amendment and litigation relating to an activist shareholder, consulting fees related to the May 2020 MUFG Indebtedness amendment and increased amortization related to the Company's office lease right of use.

The Company had a tax benefit of \$3.4 million for the nine months ended September 30, 2020 compared to a tax benefit of \$2.6 million for the nine months ended September 30, 2019. The effective tax rate for the nine months ended September 30, 2020 was a 10.9% tax benefit compared to a 21.6% tax benefit for the nine months ended September 30, 2019. The difference in the effective income tax rate from the normal statutory rate was primarily related to the recording of a \$4.6 million valuation allowance in the current period on the Company's U.S. and foreign deferred tax assets after concluding that a valuation allowance is necessary for the Company's net U.S. and foreign deferred tax assets not supported by either future taxable income or availability of future reversals of existing taxable temporary differences.

### ***Liquidity and Capital Resources***

As a result of the factors discussed below, there is substantial doubt regarding the Company's ability to continue as a going concern.

#### ***(a) MUFG Credit Facility and Drake Indebtedness***

On May 1, 2020, the Company and the MUFG Lenders entered into a Fourth Amended and Restated Loan and Security Agreement (the "MUFG Loan Agreement"), which, amended and restated the existing agreement regarding the Company's indebtedness to the MUFG Lenders and included the following changes to the terms and provisions of such indebtedness:

- A forbearance of the existing defaults and events of default under the MUFG Loan Agreement until May 10, 2020, with a provision to extend such forbearance to July 1, 2020 and August 15, 2020, if the Company is still in compliance with the agreement at May 10, 2020 and July 1, 2020, respectively;
- Elimination of the borrowing base collateral value covenant under the MUFG Loan Agreement, and of the existing event of default under the Loan Agreement for a borrowing base deficiency, along with cessation of the default interest accrual on the outstanding loan amount;
- Conversion of the revolving MUFG Credit Facility structure to a term loan structure with an initial principal balance of \$83,689,900.86 and a final maturity date of March 31, 2021;
- Interest accrual on the indebtedness based on the Base Rate (defined as the greater of (i) the rate of interest most recently announced by MUFG as to its U.S. dollar "Reference Rate", or (ii) the Federal Funds Rate plus one-half of one percent (0.50%)), according to the following schedule: (a) Base Rate + 525 bps (0 bps as cash interest and 525 bps as payment in kind ("PIK")) until June 30, 2020, and (b) Base Rate + 525 bps (100 bps as cash interest and 425 bps as PIK) from and after July 1, 2020, subject to a Base Rate floor at 325 bps for both time periods;
- Deferral of the cash component of the interest payments (on the loan indebtedness and swap termination payment obligation) that was due on April 1, 2020 and May 1, 2020, until the earlier of (i) the date of receipt of net proceeds into the Company's restricted account held at MUFG to hold sales proceeds (the "Restricted Account") from the sale of certain enumerated aircraft assets and (ii) July 1, 2020;
- Addition of certain default provisions triggered by certain defaults or other events with respect to the Company's aircraft leases for the Company's aircraft that are collateral for the MUFG Loan Agreement ("Aircraft Collateral");
- Provision for certain payments from the Restricted Account to (i) the Company's investment banking advisor; (ii) payments due under the agreement and for interest on the swap termination indebtedness owed by the Company; and (iii) Lenders' outside counsel and consultants;

- Addition of a requirement for the Company's engagement of a Financial Advisor/Consultant, at the Company's expense, with a specific scope of work as prescribed by the MUFG Loan Agreement;
- Revisions to the Company's required appraisal process for the Aircraft Collateral; and
- Establishment of deadlines for achievement of milestones for execution of Company strategic alternatives with respect to the MUFG Indebtedness acceptable to the MUFG Lenders ("Strategic Alternatives") as follows: (a) obtaining indications of interest for Strategic Alternatives by May 20, 2020 and was met by the Company at that time; (b) obtaining a fully-executed (tentative or generally non-binding) agreement on the terms and conditions for a Strategic Alternative by June 29, 2020, which has been met; and (c) consummation of the selected strategic Alternative by August 15, 2020.

On July 8, 2020, the agent bank for the MUFG Lenders delivered a Reservation of Rights Letter to the Company which contained notice of defaults with respect to failure to deliver a lessee acknowledgment of the MUFG Lender's mortgage from one of the Company's lessees (which was delayed due to extended negotiations between MUFG and the lessee relating to form of such acknowledgment) and (ii) the failure to make a deferred interest payment as required under the Loan Agreement that was due and payable on the earlier of July 1, 2020 or the date of the sale of a certain aircraft scheduled to be sold upon its return from its lessee (the closing of which sale has been delayed beyond July 1, 2020).

In March 2019, the Company entered into interest rate swaps (the "MUFG Swaps") with respect to the variable interest rate payment amounts due for \$50 million of the \$84 million of outstanding MUFG Credit Facility debt. On March 12, 2020, MUFG notified the Company that it had terminated the MUFG Swaps. The Company incurred a liability to the swap counterparties of \$3.1 million in connection with such termination, payment of which is due no later than the March 31, 2021 maturity of the MUFG Loan. As a result of the forecasted transaction being not probable to occur, accumulated other comprehensive loss of \$1,167,700 related to the MUFG Swaps was recognized as interest expense in the first quarter of 2020.

The Company has engaged B. Riley FBR as an investment banking advisor to assist in executing the required Strategic Alternative under the MUFG Loan Agreement, as well as assist with the development and execution of a recapitalization plan for the Company.

On October 30, 2020, Drake Asset Management Jersey Limited ("Drake"), purchased all of the indebtedness of the Company under the MUFG Loan, totaling approximately \$87.9 million as well as all of the Company's indebtedness to MUFG Bank, Ltd. of approximately \$3.1 million for termination of interest rate swaps entered into with respect to such Loan Agreement indebtedness. The purchase and sale was consented to by the Company pursuant to a Consent and Release Agreement of Borrower Parties, entered into by the Company and its subsidiaries. The closing of this debt purchase transaction satisfied the requirement under the Loan Agreement for execution of a Strategic Alternative with respect to the MUFG Loan indebtedness satisfactory to the MUFG Lenders.

On the same day, the Company entered into an Amendment No. 1 to the Loan Agreement ("Amendment No. 1") with Drake and UMB Bank, N.A., the replacement Administrative Agent under the Loan Agreement, to amend the Loan Agreement as follows:

- Deferral of the cash component of the interest payments due under the Loan Agreement, commencing with the payments due for March 2020, and continuing on each consecutive month thereafter, which deferred interest is to be capitalized and added to the principal balance of the indebtedness on each respective interest payment due date, until such time as the indebtedness is repaid.
- Deletion of the requirement for the Company's execution of a Strategic Alternative and of the milestones therefor;
- Deletion of the requirement for the Company's maintenance of a restricted account held with an MUFG Lender to hold aircraft sales proceeds pending application toward the Loan Agreement indebtedness;
- Replacement of references to "MUFG Union Bank, N.A.," with "UMB, Bank, N.A.," the new Administrative Agent under the Loan Agreement;
- Requirement of approval by Drake for any "Material Amendments" to leases for the collateral, defined as any amendment of, or waiver or consent under, any lease involving a modification of lease payments, any reduction in, or waiver or deferral of, Rent, a modification to any residual value guaranty, any modification that adversely affects the collateral or the rights and interests of the lender and/or administrative agent in the collateral, any reduction of any amounts payable to any of the lender Agent under any indemnity, or any change to the state of registration of aircraft collateral; and
- Deletion of certain financial reporting requirements and changes to required frequency of certain other surviving reporting requirements.

The borrowings under the Loan Agreement continue to be secured by a first priority lien held by Drake, which lien is documented in an amended and restated mortgage and security agreement assigned to Drake by the MUFG Lenders, on all of the Company's assets, including the Company's

aircraft portfolio, except two aircraft on lease to its Kenyan lessees, and three aircraft that are subject to special purpose financing held by a subsidiary of the Company.

The Company and Drake are currently engaged in discussions regarding the satisfaction and discharge of the Loan Agreement indebtedness. If the Company is not able to maintain compliance with the Drake Loan Agreement, and raise sufficient capital or refinancing debt to repay all amounts owed under the Drake Indebtedness, or reach some settlement on the repayment of the Drake Indebtedness, then the Company's financial condition and liquidity would be materially adversely affected and its ability to continue operations could be materially jeopardized, and Drake and would thereafter have the right to exercise any and all remedies for default under the Drake Loan Agreement. Such remedies include, but are not limited to, declaring the entire indebtedness immediately due and payable, and if the Company were unable to repay such accelerated indebtedness, foreclosing upon the assets of the Company that secure the Drake Indebtedness, which consist of all of the Company's assets except for certain assets held in the Company's special-purpose financing subsidiary.

*(b) Special-purpose Financing and Nord Loans*

In August 2016, the Company acquired, using wholly-owned special-purpose entities, two regional jet aircraft, using cash and third-party financing (referred to as "special-purpose financing" or "UK LLC SPE Financing") separate from the MUFG Credit Facility.

In February 2019, the UK LLC SPE Financing was repaid as part of a refinancing involving the Nord Loans, which were made to special-purpose subsidiaries of AeroCentury (the "LLC Borrowers"). Under the Nord Loans, four aircraft that previously served as collateral under the MUFG Credit Facility were moved into newly formed special-purpose subsidiaries and, along with the aircraft owned by the two existing special-purpose subsidiaries, were pledged as collateral under the Nord Loans.

All of the Nord Loans contain cross-default provisions, so that any default by a lessee of any of the subject aircraft could result in the Nord exercising its remedies under the Nord Loan agreement, including, but not limited to, possession of the aircraft that is subject to a lessee default. Currently, the Nord Loans are fully performing and were unaffected by the Company's default under the MUFG Credit Facility.

Collectively, the LLC Borrowers entered into six interest rate derivatives, or interest rate swaps. Each such interest rate swap has a notional amount that mirrors the amortization under the corresponding Nord Loan entered into by the LLC Borrowers, effectively converting each of the six Nord Loans from a variable to a fixed interest rate. Each of these six interest rate swaps extend for the length of the corresponding Nord Loan, with maturities from 2020 through 2025. One of the aircraft that was subject to Nord Loan financing was sold during the fourth quarter of 2019 and the related Nord Loan and interest rate swap were terminated. Accumulated other comprehensive loss of \$48,100 related to the Nord Swaps was recognized as an expense in the first quarter of 2020.

In March and June 2020, one of the Company's customers, which leases two regional jet aircraft subject to Nord Loan financing, did not timely make its quarterly rent payments. As a result, the special-purpose subsidiary borrowers that hold the aircraft did not have sufficient cash to meet the corresponding quarterly Nord Loan payment installments. The parent corporation was not permitted to fund the special-purpose subsidiary borrower's loan payment obligations due to restrictions under the MUFG Credit Facility. The late payment by the lessee constituted events of default under the Term Loan on March 19 and June 19, 2020, and the Term Loan nonpayment constituted events of default under the Nord Loan for the LLC Borrowers on March 27 and June 27, 2020. The lessee was severely impacted by the COVID-19 pandemic, and was required to cease operations as part of its country's lockdown, but has indicated to the Company that it intends to honor its lease commitments in due course when able. In April 2020, the Company fully drew on the letters of credit that served as security deposits under the leases in order to fund partial repayments of the overdue lease rentals which was then used by the Company to make partial payments on the Nord Loan installment payments. In May 2020, with the consent of Nord, the Company and the customer entered into a deferral agreement whereunder the customer agreed to issue replacement letter of credits as required under its lease, and the Company agreed to waive the default for failing to fully pay the March 2020 quarterly lease payment when due, and to defer the required payment date for the unpaid balance of the March lease rental payment until the June 2020 quarterly payment date so long as no other defaults under the leases arise prior to such date. The Company further agreed not to collect under the newly issued replacement letters of credit during such forbearance period. In June 2020, the Company entered into another agreement with the customer to defer payment of the March and June rent to September 2020, and Nord agreed to defer payment of its corresponding loan installments due in March and June 2020 until the September quarterly payment date. The lease arrearage was repaid by the lessee in late September, which permitted the special-purpose subsidiaries to come back into compliance with their Nord Loan indebtedness. The lessee also paid deposits totaling approximately \$3.4 million for purchase of the aircraft.

On October 29, 2020, the Company sold the two aircraft to the lessee, and fully repaid the term loan indebtedness on such aircraft with the proceeds of the sale. The excess proceeds from the purchase were applied to the remaining Nord Term Loan indebtedness owed by a special-purpose subsidiary of the Company secured by three regional jets on lease to a U.S. regional airline. The lessee of those aircraft is in compliance and current in its lease obligations, and the special-purpose subsidiary is in full compliance with its loan repayment obligations.

*(c) Paycheck Protection Program Loan*

On May 20, 2020, JetFleet Management Corp. (the "PPP Borrower"), a subsidiary of AeroCentury Corp., was granted a loan (the "PPP Loan") from

American Express National Bank in the aggregate amount of \$276,353, pursuant to the Paycheck Protection Program (the “PPP”) under Division A, Title I of the CARES Act, which was enacted March 27, 2020. The application for these funds required the Company to, in good faith, certify that the current economic uncertainty made the loan request necessary to support the ongoing operations of the Company. This certification further required the Company to take into account its current business activity and its ability to access other sources of liquidity sufficient to support ongoing operations in a manner that is not significantly detrimental to the business. The receipt of these funds, and the forgiveness of the loan attendant to these funds, is dependent on the Company having initially qualified for the loan and qualifying for the forgiveness of such loan based on its future adherence to the forgiveness criteria.

The PPP Loan, which was in the form of a Note dated May 18, 2020 issued by the PPP Borrower, matures on April 22, 2022 and bears interest at a rate of 1.00% per annum, payable in 18 monthly payments commencing on November 20, 2020. The Note may be prepaid by the PPP Borrower at any time prior to maturity with no prepayment penalties. Funds from the PPP Loan may only be used for payroll costs and any payments of certain covered interest, lease and utility payments. The Company intends to use the entire PPP Loan amount for qualifying expenses. Under the terms of the PPP, certain amounts of the Loan may be forgiven if they are used for qualifying expenses as described in the CARES Act. Although the Company expects that all or a significant portion of the PPP loan will be forgiven, no assurance can be provided that the Company will obtain such forgiveness.

*(d) Cash Flow*

The Company’s primary sources of cash from operations are payments due under the Company’s operating and finance leases, maintenance reserves, which are billed monthly to lessees based on asset usage, and proceeds from the sale of aircraft and engines.

The Company’s primary uses of cash are for (i) payments due under the Nord Loans, (ii), salaries, employee benefits and general and administrative expenses, (iii) maintenance expense and (iv) reimbursement to lessees from collected maintenance reserves. Until the Drake Indebtedness is repaid, the Company’s cash flow will be subject to monitoring by Drake, and Drake could declare the total indebtedness due and payable at any time if the Company and Drake fail to reach an agreement regarding satisfaction and settlement of the Drake Indebtedness.

The Company has engaged B. Riley as an investment banking advisor to help (i) formulate and analyze various strategic financial alternatives to address the Company’s capital structure, strategic and financing needs, as well as corporate level transactions aimed at achieving maximum value for the Company’s stockholders; and (ii) locate and negotiate with Drake as well as potential lenders, investors or transaction partners who would play a role in recapitalization of the Company.

The Company’s ability to develop, obtain approval for and achieve a recapitalization is subject to a variety of factors, as discussed under *Liquidity and Capital Resources—MUFG Credit Facility*. If the Company is not able to maintain compliance with its Drake Indebtedness or raise sufficient capital to repay all amounts owed under the Drake Indebtedness, then the Company’s financial condition and liquidity would be materially adversely affected and its ability to continue operations could be materially jeopardized.

In that case, the Company may need to incur additional debt or sell equity or certain of its revenue-producing assets in order to raise capital (which it may not be able to do on reasonable terms, or at all), or be forced into bankruptcy or liquidation.

The Company’s payments for maintenance consist of reimbursements to lessees for eligible maintenance costs under their leases and maintenance incurred directly by the Company for preparation of off-lease assets for re-lease to new customers. The timing and amount of such payments may vary widely between quarterly and annual periods, as the required maintenance events can vary greatly in magnitude and cost, and the performance of the required maintenance events by the lessee or the Company, as applicable, are not regularly scheduled calendar events and do not occur at uniform intervals. The Company’s maintenance payments typically constitute a large portion of its cash needs, and the Company has in the past borrowed additional funds under the MUFG Credit Facility to provide funding for these payments. Such funding is no longer available under the Drake Loan Agreement, and the Company will need to use excess cash flow or obtain additional debt or equity financing to fund such expenses.

The entire Nord Loan indebtedness is covered by interest rate swaps, and therefore, the Company has effectively converted the Nord Loan interest payments to fixed rate payments. The swaps were initially treated as interest rate hedges under which changes in market value were reflected in AOCI and were reclassified to ordinary income when the forecasted interest rate payments occurred. The remaining Nord Loan indebtedness swaps were redesignated in March 2020, AOCI already accrued will be reflected in ordinary income as the forecasted transactions occur, and future changes in market value will be reflected in ordinary income.

The Company’s special-purpose indebtedness, as well as related interest rate swaps, use LIBOR as a benchmark for establishing the rates at which interest accrues. LIBOR is the subject of recent national, international and other regulatory guidance and proposals for reform. These reforms and other pressures may cause LIBOR to disappear entirely on or after December 31, 2021, or to perform differently than in the past. Although the consequences of these developments cannot be entirely predicted, they could affect cash flow, as they may require the Company to pay increased costs for its LIBOR debt or even cause an acceleration of maturity of such debt if a suitable replacement index cannot be agreed upon or is not available.

Actual results could deviate substantially from the assumptions management has made in forecasting the Company’s future cash flow. As discussed

in *Liquidity and Capital Resources – (a) Credit Facility* and in *Outlook and Factors that May Affect Future Results and Liquidity*, there are a number of factors that may cause actual results to deviate from these forecasts. If these assumptions prove to be incorrect and the Company's cash requirements exceed its cash flow, the Company would need to pursue additional sources of financing to satisfy these requirements, which may not be available when needed, on acceptable terms or at all. See *Factors that May Affect Future Results and Liquidity* for more information about financing risks and limitations.

*(i) Operating activities*

The Company's cash flow from operations decreased by \$2.2 million in the first nine months of 2020 compared to the first nine months of 2019. As discussed below, the decrease in cash flow was primarily a result of decreases in payments received for rent, maintenance reserves and finance lease interest, the effects of which were partially offset by increases in payments received for security deposits and decreases in payments made for interest and income taxes.

(A) Payments for rent

Receipts from lessees for rent decreased by \$5.8 million in the first nine months of 2020 compared to the same period of 2019, primarily due to delinquencies related to one of the Company's customers, the sale of an aircraft during each of the first and fourth quarters of 2019, and the repossession of four aircraft during the third quarter of 2019.

(B) Payments for maintenance reserves

Receipts from lessees for maintenance reserves decreased by \$1.9 million in the first nine months of 2020 compared to the first nine months of 2019, primarily due to the repossession of four aircraft during the third quarter of 2019.

(C) Payments for finance lease interest

Payments received for finance lease interest decreased by \$0.6 million in the first nine months of 2020 compared to the first nine months of 2019 as a result of the sale during the first quarter of 2020 of three aircraft that were subject to finance leases and a decrease in payments received from two lessees which have been impacted by the COVID 19 Outbreak.

(D) Payments for security deposits

Receipts for security deposits increased by \$3.4 million in the first nine months of 2020 compared to the first nine months of 2019, primarily due to deposits received during the third quarter of 2020 for two aircraft that were sold in October 2020.

(E) Payments for interest

Payments made for interest decreased by \$2.9 million in the first nine months of 2020 compared to the first nine months of 2019 as a result the deferral of a portion of the interest due on the Company's MUFG Indebtedness.

(F) Payments for income taxes

Payments made for income taxes decreased by \$0.3 million in the first nine months of 2020 compared to the first nine months of 2019 as a result of lower UK taxes based on the Company's expectation of a loss for UK tax purposes on the sale of two of its assets held for lease.

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*(ii) Investing activities*

The Company did not acquire any aircraft during the first nine months of 2020. During the first nine months of 2019, the Company made a \$0.2 million deposit for the acquisition of an aircraft. The deposit was returned to the Company during the fourth quarter of 2019. During the first nine months of 2020 and 2019, the Company received net cash of \$3.2 million and \$7.1 million, respectively, from asset sales.

*(iii) Financing activities*

During the first nine months of 2020 and 2019, the Company borrowed \$2.1 million, in the form of paid-in-kind interest that was added to the outstanding principal balance, and \$5.1 million, respectively, under the MUFG Indebtedness. During the same periods, the Company repaid \$1.2 million and \$44.3 million, respectively, of its total outstanding debt under the MUFG Credit Facility. Such repayments were funded by excess cash flow, the sale of assets and, in the 2019 period, a portion of the \$44.3 million in proceeds from the Nord Loans. During the first nine months of 2020

*(ii) Investing activities*

The Company did not acquire any aircraft during the first nine months of 2020. During the first nine months of 2019, the Company made a \$0.2 million deposit for the acquisition of an aircraft. The deposit was returned to the Company during the fourth quarter of 2019. During the first nine months of 2020 and 2019, the Company received net cash of \$3.2 million and \$7.1 million, respectively, from asset sales.

*(iii) Financing activities*

During the first nine months of 2020 and 2019, the Company borrowed \$2.1 million, in the form of paid-in-kind interest that was added to the outstanding principal balance, and \$5.1 million, respectively, under the MUFG Indebtedness. During the same periods, the Company repaid \$1.2 million and \$44.3 million, respectively, of its total outstanding debt under the MUFG Credit Facility. Such repayments were funded by excess cash flow, the sale of assets and, in the 2019 period, a portion of the \$44.3 million in proceeds from the Nord Loans. During the first nine months of 2020 and 2019, the Company's special-purpose entities repaid \$5.1 million and \$5.5 million, respectively, of the Nord Loans. During the 2019 period, the Company also repaid \$9.2 million of UK LLC SPE Financing. During the first nine months of 2020 and 2019, the Company paid approximately \$1.7 million and \$5.1 million, respectively, for debt issuance and amendment fees.

*(iv) Off balance sheet arrangements*

The Company has no material off-balance sheet arrangements.

**Critical Accounting Policies, Judgments and Estimates**

*The Company's discussion and analysis of its financial condition and results of operations are based upon the condensed consolidated financial statements included in this report, 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 or during the applicable reporting period. 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 further discussion of Critical Accounting Policies, Judgments and Estimates, refer to Note 1 to the Company's condensed consolidated financial statements in this report and the Company's consolidated financial statements in the 2019 Annual Report.*

**Outlook**

*Drake Indebtedness.* The Company and Drake are currently engaged in discussions regarding the satisfaction and discharge of the Drake Loan Agreement indebtedness. If the Company is not able to maintain compliance with the Drake Loan Agreement, or the Company and Drake are not able to reach agreement regarding such satisfaction and discharge, then Drake could declare the indebtedness due and if the Company was unable to raise sufficient capital or refinancing debt to repay all amounts owed under the Drake Indebtedness, or reach some settlement on the repayment of the Drake Indebtedness, Drake could foreclose upon the assets of the Company that secure the Drake Indebtedness, which consist of nearly all of the Company's significant assets except for certain assets held in the Company's single asset special-purpose financing subsidiaries.

*COVID-19 Pandemic.* As discussed below, in *Factors that May Affect Future Results and Liquidity -- Impact of COVID-19 Pandemic*, the COVID-19 pandemic has had and will continue to have a significant impact on the Company's financial circumstances mainly due to the impact on the Company's primary customers, regional airlines. The COVID-19 pandemic has resulted in a loss of revenue for such customers. This in turn has caused four of the Company's eight customers to make requests for lease payment concessions and/or deferrals from the Company. The Company has so far been able to reach accommodations with its lenders to allow the Company with certain of its lessees to keep its leases with such lessees intact while giving such lessees short-term deferrals on lease obligations. If the financial fallout from the COVID-19 pandemic continues, and the Company receives additional requests from lessees for further concessions, then the Company may not be able to gain the agreement of its lenders for further corresponding concessions under its debt financings. If that occurs, then the Company may be required to terminate such leases and attempt to resell or release such assets, or the lenders themselves may foreclose upon such assets, and take possession of such assets as a remedy for default under the Company's debt agreements. Beyond this short-term effect of the COVID-19 pandemic, there will be a medium-term effect on the Company through the lowered demand for aircraft capacity due to governmental health and safety protocols, shelter-in-place restrictions, passenger appetite for travel and discretionary spending. The onset of the COVID-19 pandemic reduced passenger air travel to a small fraction of what it was in prior years. This in turn has reduced the airlines' need for aircraft capacity, resulting in a current excess supply of aircraft relative to demand for leased aircraft such as those owned by the Company. Some airlines may be forced to cease operations, which will further exacerbate the oversupply of aircraft for lease or sale. Even if the global economy quickly rebounds to pre-COVID-19 levels, the Company anticipates that it may take much longer for passenger air travel and demand for aircraft capacity to return to such levels and then grow beyond such levels that additional aircraft capacity is required, and uncertainties in our industry may prevent us from accessing the equity or debt capital markets on attractive terms or at all for a period of time, which could have an adverse effect on our liquidity position. Further, there is the potential for a widespread resurgence in COVID-19 cases that could prolong the economic recovery. To the extent that the Company is able to retain its aircraft on lease with lessees during

this recovery period, this oversupply in the medium-term may not have a significant impact on the Company's financial circumstances, other than a potential reduction in appraised values of the Company's portfolio when it receives its periodic appraisals. If, however, at the time that the Company is required to repossess an aircraft upon termination or expiration of its lease, demand for aircraft for lease or purchase is still depressed, then the Company may experience substantial difficulty in locating a new lessee or purchaser for such aircraft.

### ***Factors that May Affect Future Results and Liquidity***

The Company's business, financial condition, results of operations, liquidity, prospects and reputation could be affected by a number of factors. In addition to matters discussed elsewhere in this discussion, the Company believes the following are the most significant factors that may impact the Company; however, additional or other factors not presently known to the Company or that management presently deems immaterial could also impact the Company and its performance and liquidity. You should carefully consider the following discussion together with the section titled "Forward-Looking Statements" of this Quarterly Report on Form 10-Q.

***Impact of COVID-19 Pandemic.*** The ongoing COVID-19 pandemic has had an overwhelming adverse effect on the Company during the first nine months of 2020, as it has had on all forms of transportation globally, but most acutely for the airline industry. The combined effect of fear of infection during air travel, quarantines, and international and domestic travel restrictions has caused a dramatic decrease in passenger loads in all areas of the world, not just in those countries with active clusters of COVID-19, as well as in airline ticket net bookings (*i.e.*, bookings made less bookings canceled) of flights. This has led to significant cash flow issues for airlines, including some of the Company's customers, and some airlines have been unable to timely meet their obligations under their lease obligations with the Company. For example, the Company has permitted one customer, which leases two regional jet aircraft, to defer quarterly payment of March and June 2020 rent to September 2020, and the Company has permitted another customer to reduce the amounts due in April, May and June 2020. In addition, the Company and two other customers, each of which leases an aircraft subject to a sales-type lease, are discussing remedies regarding non-payment of a portion of the lease payments due during the first through third quarters of 2020. Since the Company's aircraft are financed with debt, rent payments fund the Company's repayment of debt obligations, and any default under the leases by lessees will generally lead to a default by the Company under its loan obligations, and require the lender and the Company to agree to a financial workout with respect to such debt obligations. The Company has thus far been able to achieve such accommodations from its lenders with respect to lessees that have been unable to remain current in their obligations, but there is no assurance that if such lessees do not return to compliance in the near term, or other lessees who are now current in their obligations fall out of compliance, that the Company will be able to obtain concessions or a workout from its lenders with respect to the Company's obligations under its debt agreements. Any significant nonpayment or late payment of lease payments by a significant lessee or combination of lessees could in turn impose limits on the Company's ability to fund its ongoing operations as well as cause the Company to be unable to meet its debt obligations, which in turn could lead to an immediate acceleration of debt and foreclosure upon the Company's assets. If this were to occur, we may be prevented from accessing the equity or debt capital markets on attractive terms or at all for a period of time, given the volatility in securities and financial markets caused by the COVID-19 pandemic. Furthermore, for the duration of the pandemic and a period of financial recovery thereafter, including the impacts of a potential resurgence in COVID-19 cases, sale transactions are likely to be curtailed entirely or delayed while the industry returns to financial stability, which could impact the Company's ability to implement any aspects of its Recapitalization Plan that require disposition of its assets.

***Resolution of Drake Indebtedness.*** The Company and Drake are currently engaged in discussions regarding the satisfaction and discharge of the Drake Loan Agreement indebtedness. Drake has agreed to not require cash payment of interest accruing on the Drake Indebtedness and to add such interest to the outstanding principal of the loan to be repaid when the final settlement of the Drake Indebtedness is determined. The Company does not currently have sufficient cash to repay the Drake Indebtedness, which has a maturity date of March 31, 2021, and the Company is unlikely to raise sufficient capital through the sale of its portfolio of assets in the current market. If the Company is not able to maintain compliance with the Drake Loan Agreement, and raise sufficient capital or refinancing debt to repay all amounts owed under the Drake Indebtedness, or reach some settlement on the repayment of the Drake Indebtedness, then the Company's financial condition and liquidity would be materially adversely affected and its ability to continue operations could be materially jeopardized, and Drake and would thereafter have the right to exercise any and all remedies for default under the Drake Loan Agreement. Such remedies include, but are not limited to, declaring the entire indebtedness immediately due and payable, and if the Company were unable to repay such accelerated indebtedness, foreclosing upon the assets of the Company that secure the Drake Indebtedness, which consist of all of the Company's assets except for certain assets held in the Company's special-purpose financing subsidiary.

***Listing Compliance Deficiency Notice from NYSE American.*** On September 11, 2020, the Company received a deficiency letter from NYSE American Stock Exchange notifying the Company that it was not in compliance with the continued listing standards as set forth in Section 1003(a) (i) – (iii) of the NYSE American Company Guide (the "Company Guide"). The noncompliance arose from the Company's financial statement showing a stockholders' equity deficiency as of June 30, 2020 and net losses for the most recent fiscal years ended December 31, 2018 and December 31, 2019. The letter has no immediate effect on the listing of the Company's common stock on the NYSE American and the Company's common stock will continue to trade on the NYSE American while the Company takes measures in an attempt to regain compliance with the continued listing standards. As required by Company Guide, the Company has submitted a detailed plan of compliance to the NYSE American, advising the NYSE American of the actions the Company has taken, or plans to take, that would bring it into compliance with the continued listing standards within 18 months of receipt of the Deficiency Letter. There is no assurance that the Company will be able to achieve its plan within the required 18-month period, and if it fails to return to compliance by the end of that period, the NYSE American could de-list the Company's stock. If that occurs, then liquidity of common stock held by the shareholders of the Company could be significantly impacted, as any trading in the

Company's securities would no longer be executed over the NYSE American Exchange but would have to be transacted through over-the-counter exchanges or pink sheets.

*Availability of Financing.* The Company currently has no sources for funding acquisition of aircraft assets. The Company will need to find a new source of acquisition funding, either through equity investment proceeds, a new revolving credit facility, or new asset-specific financing, or a combination of any of the three. Until the final Recapitalization Plan is executed the Company will not have any means to acquire new aircraft assets. There can be no assurance that the Company will be able to obtain such additional capital when needed, in the amounts desired or on favorable terms.

*General Economic Conditions and Lowered Demand for Travel.* Because of the international nature of the Company's business, a downturn in the health of the global economy could have a negative impact on the Company's financial results, as demand for air travel generally decreases during slow or no-growth periods, and thus demand by airlines for aircraft capacity is also decreased. As discussed above, the COVID-19 pandemic has caused significant disruptions to the global supply chain, the stock market and consumer and business-to-business commerce, the effects of which may endure well beyond the current pandemic's life cycle and result in low or negative growth in future periods. According to current reports, scheduled airline flights have been significantly reduced. While lower demand for air travel may actually lead to business opportunities as airlines turn to smaller aircraft to right-size capacity, it also presents potential challenges for the Company as it may impact the values of aircraft in the Company's portfolio, lower market rents for aircraft that are being offered for lease by the Company, cause Company customers to be unable to meet their lease obligations, or reduce demand by airlines that would be potential customers for additional or replacement regional aircraft offered by the Company.

Because the Company's portfolio is not globally diversified and is focused on North America and Europe, a localized downturn in one of these two regions in which the Company leases assets could have a significant adverse impact on the Company. Each of these regions has seen a significant impact from the COVID-19 pandemic and may be heading into recession due to both COVID-19 effects and normal business cycles. The Company's significant sources of operating lease revenue by region are summarized in *Fleet Summary – Assets Held for Lease*.

A downturn in the Chinese domestic or export economy that reduces demand for imported raw materials, such as an extended period of economic slowdown associated with the COVID-19 pandemic, could have a significant negative longer-term impact on the demand for business and regional aircraft in developing countries, including in some of the markets in which the Company seeks to do business.

Furthermore, instability arising from new U.S. sanctions or trade wars against U.S. trading partners, and the global reaction to such sanctions, or due to other factors, could have a negative impact on the Company's customers located in regions affected by such sanctions.

Also, the withdrawal of the United Kingdom ("UK") from the European Union, known as "Brexit," could threaten "open-sky" policies under which UK-based carriers operate throughout the European Union, and European Union-based carriers operate between the UK and other European Union countries. Losing open-sky flight rights could have a significant negative impact on the health of the Company's European lessees and, as a result, the financial performance and condition of the Company.

If international conflicts erupt into military hostilities, heightened visa requirements make international travel more difficult, terrorist attacks involving aircraft or airports occur, or a major flu or pandemic outbreak occurs, passengers may avoid air travel altogether, and global air travel worldwide could be significantly affected. Any such occurrence would have an adverse impact on many of the Company's customers.

Airline reductions in capacity in response to lower passenger loads can result in reduced demand for aircraft and aircraft engines and a corresponding decrease in market lease rental rates and aircraft values. 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 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.

*Nord Loan Risks.* The special-purpose subsidiary that owns the three aircraft serving as collateral for the Nord Loans is the named borrower, and the Nord Loan is secured by the three aircraft are owned by the LLC Borrower. AeroCentury, as the parent corporation of each LLC Borrower, is not a party to the Term Loan agreement, but has entered into an agreement with lessees of the LLC Borrower to guarantee certain obligations to such lessees under each lessee's lease agreement with an LLC Borrower and with Nord to guarantee certain representations, warranties and covenants delivered by the LLC Borrower to the Nord in connection with the refinancing transaction. As a result, although the Term Loans are non-recourse to AeroCentury, AeroCentury could become directly responsible for the LLC Borrower's obligations under the Term Loan and the related lease agreements pursuant to these guaranty arrangements. Moreover, any noncompliance under the Term Loans by any LLC Borrower could negatively affect the liquidity, aircraft portfolio and reputation of the Company as a whole.

The required payments under each Nord Loan are expected to be funded by the operating lease rental revenue received from the lessee of and sales proceeds from the corresponding aircraft, and the LLC Borrower's continued compliance with its Nord Loan will depend upon the lessee's compliance with its lease payment obligations.

*Nord Swap Hedging Dedeignation.* In March 2020, the Company determined that it was no longer probable that the interest payments related to the Nord Loans would occur; consequently, the swaps were dedesignated and no longer were eligible for hedge accounting. As a result of dedesignation, future changes in market value will be recognized in ordinary income and AOCI will be reclassified to ordinary income as the forecasted transactions occur. If a default on the underlying debt related to such swaps were to occur, the counterparty to the swaps could terminate the swaps and demand immediate payment of the termination value of such swaps, which the Company or the related subsidiaries may not have the funds to pay.

*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, they will fully protect the Company from losses resulting from a lessee default or bankruptcy.

If a U.S. lessee defaults under a lease and seeks 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 would be further adversely affected in the event of a bankruptcy filing by a defaulting lessee.

Lessees located in low-growth or no-growth areas of the world carry heightened risk of lessee default. The Company has had customers that have experienced significant financial difficulties, become insolvent, or have entered bankruptcy proceedings, including the European regional airline that ceased operations and declared bankruptcy after the Company terminated its leases and repossessed the four aircraft subject to the leases in the third quarter of 2019. A customer's insolvency or bankruptcy usually results in the Company's total loss of the receivables from that customer, as well as additional costs in order to repossess and, in some cases, repair the aircraft leased by the customer. 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 in an attempt to mitigate losses in the event the lessee is unable to meet or rejects its lease obligations. There can be no assurance, however, that additional customers will not become insolvent, file for bankruptcy or otherwise fail to perform their lease obligations, or that the Company will be able to mitigate any of the resultant losses.

It is possible that the Company may enter into deferral agreements for overdue lessee obligations. 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 is likely to be repaid according to the agreed schedule. The Company may elect to record the deferred rent and reserves payments from the lessee on a cash basis, which could have a material effect on the Company's financial results in the applicable periods.

*Concentration of Lessees.* For the quarter ended September 30, 2020, the Company's two largest customers accounted for approximately 32% and 28% of the Company's monthly operating lease revenue. A lease default by or collection problem with one or a combination of any of the Company's customers could have a disproportionately negative impact on the Company's financial results, and, therefore, the Company's operating results are especially sensitive to any negative developments with respect to these customers in terms of lease compliance.

*Ownership Risks.* The Company's leases typically are for a period shorter than the entire, anticipated, remaining useful life of the leased assets. As a result, the Company's recovery of its investment and realization of its expected yield in such a leased asset is dependent upon the Company's ability to profitably re-lease or sell the asset following the expiration of the lease. This ability is affected by worldwide economic conditions, general aircraft market conditions, regulatory changes, changes in the supply or cost of aircraft equipment, and technological developments that may 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 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, airline consolidations, the number of new aircraft on order, an excess supply of newly manufactured aircraft or used 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 or decrease for certain aircraft types that become more or less desirable based on market conditions and changing airline capacity. Declines in the value of the Company's aircraft and any resulting decline in market demand for these aircraft could materially adversely affect the Company's revenues, performance and liquidity.

In addition, a successful investment in an asset subject to an operating lease depends in part upon having the asset returned by the lessee in the condition as required under the lease. Each operating lease obligates a customer to return an asset to the Company in a specified condition, generally in a condition that will allow the aircraft to be readily re-leased to a new lessee, and/or pay an economic settlement for redelivery that is not in compliance with such specified conditions. The Company strives to ensure this result through onsite management during the return process. However, if a lessee becomes insolvent during the term of its lease and the Company has to repossess the asset, it is unlikely that the lessee would have the financial ability to meet these return obligations. In addition, if a lessee files for bankruptcy and rejects the aircraft lease, the lessee would be required to return the aircraft but would be relieved from further lease obligations, including return conditions specified in the lease. In either case, 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.

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 occurred under such a lease, the Company would need to pay the costs of unperformed repair and maintenance under the applicable lease and would likely 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 flow from an asset could result in an asset impairment charge against the Company's earnings. The Company periodically reviews long-term assets for impairment, particularly 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 as recently as the fourth quarter of 2019 and the first nine months of 2020 and may be required to record asset impairment charges in the future as a result of the impact of COVID-19 on the aviation industry, 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.

*Interest Rate Risk.* As a result of the termination of the MUFG Swaps, the amount of interest paid by the Company under the MUFG Indebtedness will fluctuate depending on prevailing interest rates. Consequently, interest rate increases could materially increase the Company's interest payment obligations under its MUFG Indebtedness and thus could have a material adverse effect on the Company's liquidity and financial condition. 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.

*Concentration of Aircraft Type.* Although the Company's aircraft portfolio is currently focused on a small number of aircraft types and models relative to the variety of aircraft used in the commercial air carrier market, most of these types are used extensively by regional airlines. A change in the desirability and availability of any of the particular types and models of aircraft owned by the Company could affect valuations and future rental revenues of such aircraft, and would have a disproportionately significant impact on the Company's portfolio value. In addition, the Company is dependent on the third-party companies that manufacture and provide service for the aircraft types in the Company's portfolio. The Company has no control over these companies, and they could decide to curtail or discontinue production of or service for these aircraft types at any time or significantly increase their costs, which could negatively impact the Company's prospects and performance. These effects would diminish if the Company acquires assets of other types. Conversely, acquisition of additional aircraft of the types currently owned by the Company will increase the Company's risks related to its concentration of those aircraft types.

*Competition.* The aircraft leasing industry is highly competitive. The Company competes with other leasing companies, banks, financial institutions, private equity firms, aircraft leasing syndicates, aircraft manufacturers, distributors, airlines and aircraft operators, equipment managers, equipment leasing programs and other parties engaged in leasing, managing or remarketing aircraft. Many of these competitors have longer operating histories, more experience, larger customer bases, more expansive brand recognition, deeper market penetration and significantly greater financial resources.

Competition in the Company's market niche of regional aircraft has increased significantly recently as a result of increased focus on regional air carriers by competitors who have traditionally neglected this market, new entrants to the acquisition and leasing market and consolidation of certain competitors. This can create upward pressure on acquisition prices for many of the aircraft types that the Company has targeted to buy and, at the same time, create downward pressure on lease rates, resulting in lower revenues and margins for the Company.

Competitors in the niche that have lower costs of capital than the Company could have a significant advantage over the Company. Lower capital costs allow competitors to offer lower lease rates to carriers and/or the prices the competitor is able to pay for a leased asset. Due to the Company's recent defaults under its MUFG Indebtedness, locating debt financing in line with the Company's historical cost of capital in the short term could be difficult thereby exacerbating the competitive disadvantage of the Company with respect to cost of capital, until the Company re-establishes its financial stability following execution of its Recapitalization Plan.

*Risks Related to Regional Air Carriers.* The Company's continued focus on its customer base of regional air carriers subjects the Company to certain risks. Many regional airlines rely heavily or even exclusively on a code-share or other contractual relationship with a major carrier for revenue, and can face financial difficulty or failure if the major carrier terminates or fails to perform under the relationship or files for bankruptcy or becomes insolvent. Some regional carriers may depend on contractual arrangements with industrial customers such as mining or oil companies, or franchises from governmental agencies that provide subsidies for operating essential air routes, which may be subject to termination or cancellation on short notice. Furthermore, many lessees in the regional air carrier market are start-up, low-capital, and/or low-margin operators. A current concern for regional air carriers is the supply of qualified pilots. Due to recently imposed regulations of the U.S. Federal Aviation Administration requiring a higher minimum number of hours to qualify as a commercial passenger pilot, many regional airlines have had difficulty meeting their business plans for expansion. This could in turn affect demand for the aircraft types in the Company's portfolio and the Company's business,

performance and liquidity.

*International Risks.* The Company leases some assets in overseas markets. Leases with foreign lessees, however, may present different risks than those with domestic lessees.

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 or less stable 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 strong and stable.

The Company is subject to certain risks related to currency conversion fluctuations. The Company currently has one customer with rent obligations payable in Euros, and the Company may, from time to time, agree to additional leases that permit payment in foreign currency, which would subject such lease revenue to monetary risk due to currency exchange rate fluctuations. During the periods covered by this report, the Company considers the estimated effect on its revenues of foreign currency exchange rate fluctuations to be immaterial; however, the impact of these fluctuations may increase in future periods if additional rent obligations become payable in foreign currencies.

Even with U.S. dollar-denominated lease payment provisions, the Company could still be negatively affected by a devaluation of a foreign lessee's local currency relative to the U.S. dollar, which would make it more difficult for the lessee to meet its U.S. dollar-denominated payments and increase the risk of default of that lessee, particularly if its revenue is primarily derived in its 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. Foreign lessees may also face restrictions on payment obligations to foreign vendors, including the Company, which may affect their ability to timely meet lease obligations to the Company.

Foreign 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 which can be used to locally record 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.

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. Any such challenge could result in increased tax obligations in these jurisdictions going forward or assessments of liability by the taxing authority, in which case the Company may be required to pay penalties and interest on the assessed amount that would not give rise to a corresponding foreign tax credit on the Company's U.S. tax returns.

The Trump administration and members of the U.S. Congress have made public statements about significant changes in U.S. trade policy and have taken certain actions that materially impact U.S. trade, including terminating, renegotiating or otherwise modifying U.S. trade agreements with countries in various regions and imposing tariffs on certain goods imported into the United States. These changes in U.S. trade policy have triggered and could continue to trigger retaliatory actions by affected countries, including China, resulting in "trade wars" with these countries. These trade wars could generally increase the cost of aircraft, aircraft and engine components and other goods regularly imported by the Company's customers, thereby increasing costs of operations for its air carrier customers that are located in the affected countries. The increased costs could materially and adversely impact the financial health of affected air carriers, which in turn could have a negative impact on the Company's business opportunities, and if the Company's lessees are significantly affected, could have a direct impact on the Company's financial results. Furthermore, the Company often incurs maintenance or repair expenses not covered by lessees in foreign countries, which expenses could increase if such countries are affected by such a trade war.

*Level of Portfolio Diversification.* The Company intends to continue to focus solely on regional aircraft. Assuming a successful implementation of its Recapitalization Plan, the Company may continue to seek acquisition opportunities for new types and models of aircraft used by the Company's targeted customer base of regional air carriers. Acquisition of aircraft types not previously owned by the Company entails greater ownership risk due to the Company's lack of experience managing those assets and the potentially different types of customers that may lease them. Conversely, the Company's focus on a more limited set of aircraft types and solely on regional aircraft subjects the Company to risks that disproportionately impact these aircraft markets, which are described elsewhere in this discussion. As a result, the level of asset and market diversification the Company chooses to pursue could have a significant impact on its performance and results.

*Transition to LIBOR Alternative Reference Rate.* The London Inter-bank Offered Rate ("LIBOR") represents the interest rate at which banks offer to lend funds to one another in the international interbank market for short-term loans, and is the index rate for the Nord Loans of the LLC Borrower subsidiaries. Beginning in 2008, concerns were expressed that some of the member banks surveyed by the British Bankers' Association in connection with the calculation of LIBOR rates may have been under-reporting or otherwise manipulating the interbank lending rates applicable to them. Regulators and law enforcement agencies from a number of governments have conducted investigations relating to the calculation of LIBOR across a range of maturities and currencies. If manipulation of LIBOR or another inter-bank lending rate occurred, it may have resulted in that rate

being artificially lower (or higher) than it otherwise would have been. Responsibility for the calculation of LIBOR was transferred to ICE Benchmark Administration Limited, as independent LIBOR administrator, effective February 1, 2014. On July 27, 2017, the U.K. Financial Conduct Authority announced that it will no longer persuade or compel banks to submit rates for the calculation of LIBOR rates after 2021 (the “July 27th Announcement”). The July 27th Announcement indicates that the continuation of LIBOR on the current basis cannot and will not be guaranteed after 2021. Consequently, at this time, it is not possible to predict whether and to what extent banks will continue to provide LIBOR submissions to the administrator of LIBOR or whether any additional reforms to LIBOR may be enacted in the United Kingdom or elsewhere. Similarly, it is not possible to predict whether LIBOR will continue to be viewed as an acceptable benchmark, what rate or rates may become accepted alternatives to LIBOR or the effect of any such changes in views or alternatives on the value of LIBOR-linked securities.

Although the Financial Stability Oversight Council has recommended a transition to an alternative reference rate in the event LIBOR is no longer available after 2021, which could affect the Company’s indebtedness, such plans are still in development and, if enacted, could present challenges. Moreover, contracts linked to LIBOR are vast in number and value, are intertwined with numerous financial products and services, and have diverse parties. The downstream effect of unwinding or transitioning such contracts could cause instability and negatively impact the financial markets and individual institutions. The uncertainty surrounding the sustainability of LIBOR more generally could undermine market integrity and threaten individual financial institutions and the U.S. financial system more broadly.

With respect to the Company’s indebtedness, if any of its indebtedness remains based on LIBOR when LIBOR is no longer published after 2021 and the Company and its lenders are unable to agree on a mutually acceptable LIBOR alternative for any outstanding debt indexed to LIBOR, the debt agreements could be terminated and repayment of the indebtedness could be accelerated to become immediately due and payable to the lender. This outcome could also lead to substantial breakage fees being payable by the Company in addition to the outstanding principal of such debt. If any of these risks were to occur, the Company could experience material cash shortfalls or be forced into bankruptcy or liquidation.

*Swap Counterparty Credit Risks.* AeroCentury and the LLC Borrower have entered into certain interest rate swaps to hedge the interest rate risk associated with the Nord Loan indebtedness. These interest rate swap agreements effectively convert the variable interest rate payments under the LLC Borrower Term Loan indebtedness to fixed rate payments. If an interest rate swap counterparty cannot perform under the terms of the interest rate swap due to insolvency, bankruptcy or other reasons, the Company would not receive payments due from the counterparty under that interest rate swap agreement, in which case, depending on interest rate conditions at the time of such default, the Company could be unable to meet its variable interest rate debt obligations and may default under one or more loan agreements. In such a case, the debt under the loan agreement could be accelerated and become immediately due and payable, the collateral securing the loan indebtedness could be foreclosed upon, and/or the Company might incur a loss on the fair market value of the interest rate swap agreement. Any such outcome could have a material adverse effect on the Company’s performance, liquidity and ability to continue operations.

*Swap Breakage Fees.* To reduce the amount of interest that accrues under its indebtedness, the Company could choose to prepay certain amounts borrowed under such loans. If the Company has hedged its variable interest rate indebtedness, in addition to prepayment fees that might be payable to the lender of the underlying indebtedness, the Company may also be obligated to pay certain swap breakage fees to the interest rate swap counterparty in order to unwind the interest rate swap related to the indebtedness that is being prepaid. Thus, the Company’s interest rate swaps could reduce the economic benefit that the Company might otherwise achieve through prepayment or could render an otherwise advantageous debt prepayment uneconomical.

*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, there can be no assurance that the cost will not fall on the Company. Additionally, even if lessees are responsible for the costs of complying with these requirements, changes to the requirements to make them more stringent or otherwise increase these costs could negatively impact the Company’s customers’ businesses, which could result in nonperformance under their lease agreements or decreased demand for the Company’s aircraft. Furthermore, future government regulations could cause the value of any noncomplying equipment owned by the Company to decline substantially. Moreover, any failure by the Company to comply with the government regulations applicable to it could result in sanctions, fines or other penalties, which could harm the Company’s reputation and performance.

*Casualties and Insurance Coverage.* The Company, as an 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, because 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 additional 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 its assets that are operated in foreign countries where the provisions of this law 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 has adopted measures designed to ensure these insurance policies continue to be maintained, including

tracking receipt of the insurance certificates, calendaring their expiration dates, and reminding lessees of their obligations to maintain such insurance and provide current insurance certificates to the Company if a replacement certificate is not timely received prior to the expiration of an existing certificate.

Despite these requirements and procedures, there may be certain cases where losses or liabilities are not entirely covered by the lessee or its insurance. Although the Company believes the possibility of such an event is remote, any such uninsured loss or liability, or insured loss or liability for which insurance proceeds are inadequate, might result in a loss of invested capital in and any profits anticipated from the applicable aircraft, as well as potential claims directly against the Company.

*Compliance with Environmental Regulations.* Compliance with 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, including requirements to adopt technology to reduce the amount of carbon emissions or imposing a fee or tax system on carbon emitters. Any such regulation could be directed at the Company's customers, as operators of aircraft, at the Company, as an owner of aircraft, and/or on the manufacturers of aircraft. Under the Company's triple-net lease arrangements, the Company would likely try to shift responsibility for compliance to its lessees; however, it may not be able to do so due to competitive or other market factors, and there might be some compliance costs that the Company could not pass through to its customers 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 liquidity, there is no assurance that the costs of complying with environmental regulations as amended or adopted in the future will not have such an effect.

*Cybersecurity Risks.* The Company believes that its main vulnerabilities to a cyber-attack would be interruption of the Company's email communications internally and with third parties, loss of customer and lease archives, 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 and backup mechanisms exist in the event of such an interruption such that there would not be a material adverse financial impact on the Company's business. A cyber-hacker could also gain access to and release proprietary information of the Company, its customers, suppliers and employees stored on the Company's data network. Such a breach could harm the Company's reputation and result in competitive disadvantages, litigation, lost revenues, additional costs, or liability to third parties. While the Company believes that it has sufficient cybersecurity measures in place commensurate with the risks to the Company of a successful cyber-attack or breach of its data security, its resources and technical sophistication may not be adequate to prevent or adequately respond to and mitigate all types of cyber-attacks.

*Possible Volatility of Stock Price.* The market price of the Company's common stock is subject to fluctuations following developments relating to the Company's operating results, changes in general conditions in the economy, the financial markets or 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 1.55 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. This stock price and trading volume volatility could limit the Company's ability to use its capital stock to raise capital, if and when needed or desired, or as consideration for other types of transactions, including strategic collaborations, investments or acquisitions. Any such limitation could negatively affect the Company's performance, growth prospects and liquidity.

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

Disclosure under this item has been omitted pursuant to the rules of the SEC that permit smaller reporting companies to omit such information.

### **Item 4. Controls and Procedures.**

**CEO and CFO Certifications.** Attached as exhibits to this 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 Item 4 includes information concerning the evaluation of disclosure controls and procedures referred to in the Section 302 Certifications and 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 or submitted under the Exchange Act, such as this report, is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC 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.

In the course of the review of the consolidated financial results of the Company for the three months and nine months ended September 30, 2018, the Company identified a material weakness in its internal control over financial reporting ("Internal Control") at September 30, 2018 related to the Company's incorrect accounting for management fees and acquisition fees associated with the Management Agreement between JetFleet Holding

Corp. (“JHC”) and the Company. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the Company’s annual or interim financial statements will not be prevented or detected on a timely basis. Although the Company implemented controls over identifying the proper accounting treatment for the JHC acquisition and those controls operated as of December 31, 2018, the Company’s tax review control did not identify a complex component of the acquisition accounting, resulting in an adjustment to the Company’s tax expense in 2018. Management has determined that this deficiency continues to constitute a material weakness as of September 30, 2020. Management is in the process of enhancing the tax review control related to unusual transactions the Company may encounter.

The Company’s management, with the participation of the CEO and CFO, evaluated the effectiveness of the Company’s Disclosure Controls as of September 30, 2020. Based on this evaluation, the CEO and CFO concluded that the Company’s Disclosure Controls were not effective as of September 30, 2020 due to the material weakness described above.

**Changes in Internal Control.** No change in the Company’s Internal Control occurred during the fiscal quarter ended September 30, 2020 that has materially affected, or is reasonably likely to materially affect, the Company’s Internal Control.

**Inherent Limitations of Disclosure Controls and Internal Control.** In designing its Disclosure Controls and Internal Control, the Company’s management recognizes that any controls and procedures, no matter how well-designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of the Company’s controls and procedures must reflect the fact that there are resource constraints, and management necessarily applies its judgment in evaluating the benefits of possible controls and procedures relative to their costs. Because of these inherent limitations, the Company’s Disclosure Controls and Internal Control may not prevent or detect all instances of fraud, misstatements or other control issues. In addition, projections of any evaluation of the effectiveness of disclosure or internal controls to future periods are subject to risks, including, among others, that controls may become inadequate because of changes in conditions or that compliance with policies or procedures may deteriorate.

## PART II – OTHER INFORMATION

### Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

Under the Credit Facility agreement, the Company is not permitted to pay dividends on any shares of its capital stock without the consent of the MUFG Lenders.

### Item 6. Exhibits.

Exhibit Number	Description
10.1	<a href="#">Consent and Release Agreement of Borrower Parties, entered into by the Company and its subsidiaries, JetFleet Holding Corp. and JetFleet Management Corp, incorporated by reference to Exhibit 10.1 to the Company’s Report on Form 8-K filed with the Securities Exchange Commission on November 2, 2020.</a>
10.2	<a href="#">First Amendment to Fourth Amended and Restated Loan and Security Agreement, dated as of October 30, 2020, by and between the Company, Drake Asset Management Jersey Limited, and UMB Bank, N.A., incorporated by reference to Exhibit 10.2 to the Company’s Report on Form 8-K filed with the Securities Exchange Commission on November 2, 2020.</a>
31.1	<a href="#">Certification of Michael G. Magnusson, Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</a>
31.2	<a href="#">Certification of Harold M. Lyons, Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</a>
32.1*	<a href="#">Certification of Michael G. Magnusson, Chief Executive Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</a>
32.2*	<a href="#">Certification of Harold M. Lyons, Chief Financial Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</a>
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 SEC.

## SIGNATURES

**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 12, 2020

AEROCENTURY CORP.

By: /s/ Harold M. Lyons

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Name: Harold M. Lyons

Title: Senior Vice President-Finance and  
Chief Financial Officer