AVIATION CAPITAL GROUP LLC
AND SUBSIDIARIES

Unaudited Condensed Consolidated Financial Statements
as of September 30, 2018 and December 31, 2017 and for the
nine months ended September 30, 2018 and 2017

Aviation Capital Group LLC and Subsidiaries

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

(In Thousands)	September 30, 2018	December 31, 2017
ASSETS		
Cash and cash equivalents	$239,386	$166,875
Restricted cash	197,124	206,168
Flight equipment held for lease, net	8,388,564	7,424,227
Assets held for sale	289,161	410,073
Prepayments on flight equipment	1,298,593	1,174,046
Investment in finance leases, net	260,978	332,648
Equity method investments	1,503	25,622
Other assets, net	133,050	107,217
TOTAL ASSETS	**$10,808,359**	**$9,846,876**
LIABILITIES AND EQUITY		
Liabilities:		
Accounts payable, accrued expenses and other liabilities	$181,093	$139,143
Debt financings, net	6,498,311	5,900,839
Maintenance reserves	713,845	638,122
Security deposits	145,977	129,231
Deferred income	65,567	55,569
Lease incentives	15,505	21,126
Derivative financial instruments at fair value, net	5,667	4,684
Deferred income taxes, net	3,973	1,953
TOTAL LIABILITIES	7,629,938	6,890,667
Commitments and contingencies (Note 11)		
Equity:		
Members' equity	3,180,759	2,961,215
Accumulated other comprehensive loss	(2,338)	(5,006)
TOTAL EQUITY	3,178,421	2,956,209
TOTAL LIABILITIES AND EQUITY	**$10,808,359**	**$9,846,876**

See Notes to Condensed Consolidated Financial Statements

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(In Thousands)	Nine Months Ended September 30, 2018	2017
REVENUES		
Operating lease revenue	$691,450	$652,934
Amortization of lease incentives and premiums, net	(15,384)	(16,076)
Gain on sale of flight equipment	19,480	5,103
Finance lease revenue	16,022	13,909
Maintenance revenue	—	18,539
Other income	27,188	6,914
TOTAL REVENUES	738,756	681,323
EXPENSES		
Depreciation	257,755	238,432
Interest, net	181,076	167,872
Operating lease expense	17,521	17,519
Maintenance and transition expense	5,055	13,603
Asset impairment	3,511	142,099
Selling, general and administrative	55,694	47,063
TOTAL EXPENSES	520,612	626,588
Income before provision for (benefit from) income taxes and earnings from equity method investments	218,144	54,735
Provision for (benefit from) income taxes	2,310	(886,305)
Earnings from equity method investments	3,710	2,759
NET INCOME	**$219,544**	**$943,799**

See Notes to Condensed Consolidated Financial Statements

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

(In Thousands)	Nine Months Ended September 30, 2018	2017
NET INCOME	$219,544	$943,799
Other comprehensive income:		
Unrealized gain on interest rate swap contracts, net of taxes of $72 and $595	2,191	2,065
Reclassification into earnings from accumulated other comprehensive loss for de-designated hedges (included in interest, net)	477	620
COMPREHENSIVE INCOME	**$222,212**	**$946,484**

See Notes to Condensed Consolidated Financial Statements

CONDENSED CONSOLIDATED STATEMENTS OF EQUITY

(Unaudited)

(In Thousands)	Members' Equity	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive (Loss) Income	Total Equity
BALANCES, JANUARY 1, 2017	**—**	**$1**	**$773,385**	**$1,143,556**	**($9,005)**	**$1,907,937**
Net loss prior to organizational transactions	—	—	—	(61,050)	—	(61,050)
Effect of organizational transactions	$2,746,797	(1)	(773,385)	(1,082,506)	—	890,905
Net income subsequent to organizational transactions	113,943	—	—	—	—	113,943
Other comprehensive income	—	—	—	—	2,685	2,685
BALANCES, SEPTEMBER 30, 2017	**$2,860,740**	**—**	**—**	**—**	**($6,320)**	**$2,854,420**
BALANCES, JANUARY 1, 2018	**$2,961,215**	**—**	**—**	**—**	**($5,006)**	**$2,956,209**
Net income	219,544	—	—	—	—	219,544
Other comprehensive income	—	—	—	—	2,668	2,668
BALANCES, SEPTEMBER 30, 2018	**$3,180,759**	**—**	**—**	**—**	**($2,338)**	**$3,178,421**

See Notes to Condensed Consolidated Financial Statements

Aviation Capital Group LLC and Subsidiaries

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(In Thousands)	Nine Months Ended September 30, 2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$219,544	$943,799
Adjustments to reconcile net income to net cash flows provided by operating activities:		
Depreciation	257,755	238,432
Amortization of lease incentives and premiums, net	15,384	16,076
Amortization of debt acquisition costs and original issuance discounts	14,197	14,507
Unrealized (gain) loss on foreign currency adjustment of debt financings	(4,278)	7,176
Non-hedging derivative financial instrument settlements	4,849	3,808
Gain on sale of flight equipment	(19,480)	(5,103)
Earnings from equity method investments	(3,710)	(2,759)
Unrealized loss (gain) on non-hedging derivative financial instruments	3,247	(7,095)
Deferred income taxes, net	1,948	(876,488)
Asset impairment	3,511	142,099
Maintenance reserves, security deposits and lease incentives included in earnings	(583)	(18,336)
Other operating activities, net	(1,219)	(4,592)
Changes in operating assets and liabilities:		
Other assets, net	(37,887)	(16,264)
Accounts payable, accrued expenses and other liabilities	27,397	12,284
Equity method investments	13,684	4,833
Deferred income	10,909	2,495
Lease incentives	(4,468)	(4,294)
NET CASH FLOWS PROVIDED BY OPERATING ACTIVITIES	500,800	450,578
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of flight equipment and related assets	(1,032,974)	(1,022,736)
Prepayments on flight equipment	(452,835)	(528,428)
Proceeds from sale of flight equipment and related assets	348,486	387,678
Capitalized interest on prepayments on flight equipment	(30,373)	(24,342)
Distributions from equity method investments	15,236	38,124
Collections on investment in finance leases, net	16,788	10,559
Payments on non-hedging derivative financial instruments	(5,902)	(4,867)
Receipts from non-hedging derivative financial instruments	1,053	1,059
Other investing activities, net	—	3,802
NET CASH FLOWS USED IN INVESTING ACTIVITIES	(1,140,521)	(1,139,151)

(Continued)

See Notes to Condensed Consolidated Financial Statements

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Nine Months Ended September 30,	
(In Thousands)	2018	2017
(Continued)		
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from debt financings	$1,732,492	$996,842
Repayment of debt financings	(1,259,990)	(232,825)
Proceeds from commercial paper, net	335,000	—
Repayment of Revolving Credit Facilities, net	(215,000)	(145,000)
Receipts of maintenance reserves	139,131	125,216
Payments of maintenance reserves	(36,407)	(29,239)
Receipts of security deposits	21,084	26,322
Payments of security deposits	(8,143)	(9,787)
Other financing activities, net	(4,979)	(3,347)
NET CASH FLOWS PROVIDED BY FINANCING ACTIVITIES	703,188	728,182
Net change in cash and cash equivalents and restricted cash	63,467	39,609
Cash and cash equivalents and restricted cash, beginning of period	373,043	313,427
CASH AND CASH EQUIVALENTS AND RESTRICTED CASH, END OF PERIOD	**$436,510**	**$353,036**
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Interest paid, net of capitalized interest	$127,966	$113,891
Non-cash transfer from prepayments on flight equipment to flight equipment held for lease, net	$359,680	$144,071
Security deposits and maintenance reserves settled in sale of flight equipment	$33,288	$59,738
Non-cash transfer from flight equipment held for lease, net to investment in finance leases, net	—	$29,195
Security deposits and maintenance reserves assumed in purchase of flight equipment	—	$25,992

See Notes to Condensed Consolidated Financial Statements

1. ORGANIZATION

Aviation Capital Group LLC, a Delaware limited liability company (ACG LLC), together with its subsidiaries (collectively, ACG, we, us, our) is a full service aircraft asset manager. Our business consists primarily of the acquisition, disposition and leasing of commercial jet aircraft, and our principal activity is to act as an owner and lessor of commercial jet aircraft subject to operating leases. We also provide certain asset management services for third parties. Our lessee customers are primarily commercial airlines operating across the globe.

ACG LLC is an indirect subsidiary of Pacific Life Insurance Company (Pacific Life), a wholly owned subsidiary of Pacific LifeCorp (LifeCorp). Pacific Life Aviation Holdings LLC (PLAH), a wholly owned subsidiary of Pacific Life, owns 79% of the membership interests in ACG LLC. TC Skyward Aviation U.S., Inc. (TCSA), a Delaware corporation and direct subsidiary of Tokyo Century Corporation (Tokyo Century), a Japanese corporation, owns 20% of the membership interests in ACG LLC. Aviation Capital Group Holdings, Inc. (ACGHI), a wholly owned subsidiary of PLAH, owns 1% of the membership interests in ACG LLC and is the managing member of ACG LLC. TCSA owns one share of the outstanding common stock of ACGHI.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION AND PRINCIPLES OF CONSOLIDATION

The accompanying condensed consolidated financial statements (consolidated financial statements) have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) for interim reporting. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. The information presented reflects all adjustments, consisting of normal recurring adjustments, that in the opinion of management, are necessary to fairly state the consolidated financial statements for the periods indicated. Results of operations for the interim periods presented are not necessarily indicative of the results of operations for the full year. The condensed consolidated balance sheet as of December 31, 2017 was derived from the audited consolidated financial statements as of December 31, 2017. Therefore, the information included in these consolidated financial statements should be read in conjunction with our audited consolidated financial statements as of and for the year ended December 31, 2017.

Our consolidated financial statements include the accounts of all entities in which we have a controlling financial interest, including the accounts of any variable interest entity (VIE) where we are the primary beneficiary.

All intercompany transactions and balances have been eliminated in consolidation.

We manage, operate and present our business as a single segment.

Certain reclassifications have been made in the presentation of the 2017 condensed consolidated statements of cash flows to conform to the 2018 presentation.

We have evaluated events subsequent to September 30, 2018 and through November 7, 2018, the date these consolidated financial statements were available to be issued, and have concluded that no events or transactions have occurred subsequent to September 30, 2018 that require consideration as adjustments to, or disclosures in, the consolidated financial statements.

USE OF ESTIMATES

The preparation of financial statements in conformity with U.S. GAAP requires that we make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. While we believe that the estimates and related assumptions used in the preparation of the consolidated financial statements are reasonable, actual results could differ from those estimates. The use of estimates is or could be a significant factor affecting the reported carrying values of flight equipment, acquired contractual rights, lease incentives, deferred income taxes, accruals and reserves. In developing these estimates, we are required to make subjective and complex decisions that are inherently uncertain and subject to material changes as facts and circumstances change.

RECENT ACCOUNTING PRONOUNCEMENTS ADOPTED

In 2017, the Financial Accounting Standards Board (FASB) issued new guidance on business combinations, Accounting Standards Update (ASU) 2017-01. The guidance clarifies the definition of a business and provides guidance to determine when a set of assets and activities is a business. We adopted this ASU on January 1, 2018 and it did not have an impact on our consolidated financial statements.

In 2016, the FASB issued ASU 2016-15 and ASU 2016-18 (together the Cash Flow ASUs). ASU 2016-15 provides guidance on how certain cash receipts and payments are to be presented and classified in the condensed consolidated statements of cash flows. ASU 2016-18 requires restricted cash to be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the condensed consolidated statements of cash flows. We adopted the Cash Flow ASUs retrospectively on January 1, 2018 which resulted in an increase of $27.0 million in net cash flows provided by financing activities for the nine months ended September 30, 2017, related to reclassifying the changes in our restricted cash balance from financing activities within the condensed consolidated statements of cash flows.

FUTURE ADOPTION OF ACCOUNTING PRONOUNCEMENTS

In 2018, the FASB issued disclosure framework changes to the disclosure requirements for fair value measurement, ASU 2018-13. The objective of this amendment is to modify the disclosure requirements on fair value measurements in the Codification's Fair Value Measurement and Disclosures Topic. The amendments in this guidance are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. Early adoption is permitted. We are currently evaluating the impact of this guidance on our consolidated financial statements.

In 2017, the FASB issued ASU 2017-12, which targeted improvements to accounting for hedging activities. The objective of the amended guidance is to improve the financial reporting of hedging relationships to better portray the economic results of a company’s risk management activities in its financial statements and make certain targeted improvements to simplify the application of the hedge accounting guidance. Upon adoption, cash flow and net investment hedges will require a cumulative-effect adjustment related to eliminating the separate measurement of ineffectiveness to accumulated other comprehensive income with a corresponding adjustment to the beginning balance of retained earnings. The amendments in this guidance are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. The amended presentations and disclosure guidance are required prospectively. Early adoption is permitted. We are currently evaluating the impact of this guidance on our consolidated financial statements.

In 2016, the FASB issued ASU 2016-13, which provides guidance on the measurement of credit losses for certain financial assets. The new guidance replaces the incurred loss impairment methodology with one that reflects expected credit losses. The measurement of expected credit losses should be based on historical loss information, current conditions, and reasonable and supportable forecasts. The guidance also requires enhanced disclosures. The amendments in this guidance are effective for fiscal years beginning after December 15, 2020 and interim periods within those fiscal years with a cumulative-effect adjustment to retained earnings under a modified-retrospective approach. Early adoption is permitted. We are currently evaluating the impact of this guidance on our consolidated financial statements.

In 2016, the FASB issued ASU 2016-02, which, together with all subsequent amendments, primarily amends existing leasing guidance related to a lessee’s accounting for operating leases. The new guidance requires a lessee to recognize assets and liabilities for leases with lease terms of more than 12 months. Consistent with current guidance, leases would be classified as finance or operating leases. However, unlike current guidance, the new guidance will require both types of leases to be recognized on the condensed consolidated statements of financial condition by the lessee. Lessor accounting will remain largely unchanged from current guidance except for certain targeted changes. The amendments in this guidance are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. We are currently evaluating the impact of this guidance on our consolidated financial statements. We do not expect the amendments in this guidance to have a material impact on our consolidated financial statements.

In 2016, the FASB issued ASU 2016-01, which amends certain aspects of recognition, measurement, presentation and disclosure of financial instruments. The new guidance changes the current accounting guidance related to (i) the classification and measurement of certain equity investments, (ii) the presentation of changes in the fair value of financial liabilities measured under the fair value option that are due to instrument-specific credit risk, and (iii) certain disclosures associated with the fair value of financial instruments. The amendments in this guidance are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. We are currently evaluating the impact of this guidance on our consolidated financial statements.

In 2014, the FASB issued ASU 2014-09, which supersedes most of the current revenue recognition requirements. The guidance requires entities to recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration that the entity expects to be entitled to in exchange for those goods or services. The amendments in this guidance are effective for fiscal years,

and interim periods within those fiscal years, beginning after December 15, 2019. The amendment should be applied using a modified retrospective basis through a cumulative-effect adjustment directly to retained earnings as of the beginning of the period of adoption. We are currently evaluating the impact of this guidance on our consolidated financial statements. We do not expect the amendments in this guidance to have a material impact on our consolidated financial statements.

3. FLIGHT EQUIPMENT HELD FOR LEASE, NET

The following table presents the components of flight equipment held for lease, net *(In Thousands)*:

	September 30, 2018	December 31, 2017
Flight equipment held for lease	$10,281,881	$9,088,012
Less: accumulated depreciation	(1,893,317)	(1,663,785)
Flight equipment held for lease, net	$8,388,564	$7,424,227

As of September 30, 2018 and December 31, 2017, maintenance right assets of $166.7 million and $164.3 million, respectively, were included in flight equipment held for lease, net.

As of September 30, 2018 and December 31, 2017, flight equipment held for lease with carrying value of $1,464.2 million and $1,627.2 million, respectively, were pledged as collateral for certain secured debt financings (Note 10).

The following table presents the future minimum lease rentals we are due under operating leases *(In Thousands)*:

Twelve months ended September 30:	
2019	$959,446
2020	878,423
2021	795,932
2022	707,152
2023	562,160
Thereafter	1,653,286
Total	$5,556,399

Included in the table above are future lease rentals relating to six aircraft that we sold to third parties, then leased back under operating leases (the Head Leases), and subsequently leased to airlines (the Sub Leases). During each of the nine months ended September 30, 2018 and 2017, the operating lease revenue we received from the Sub Leases was $20.3 million. The table above includes future minimum lease rentals related to the Sub Leases of $114.1 million. The Sub Leases have maturity dates ranging from 2021 to 2024.

We hold fixed price purchase options exercisable for each of the six Head Leases. The Head Leases have maturity dates ranging from 2023 to 2025. The following table presents our aggregate minimum future lease commitments on the Head Leases *(In Thousands)*:

Twelve months ended September 30:	
2019	$20,262
2020	29,459
2021	26,751
2022	24,151
2023	16,615
Thereafter	8,289
Total	$125,527

4. ASSETS HELD FOR SALE

Assets held for sale consists of flight equipment and the lease-related assets of the aircraft that are part of a sale transaction. Assets held for sale totaled $289.2 million and $410.1 million as of September 30, 2018 and December 31, 2017, respectively. Assets held for sale are valued at the lower of carrying value or fair value less costs to sell. We cease recognition of depreciation and amortization expense on all related assets upon transfer to assets held for sale.

When we record assets held for sale at fair value less costs to sell and the amount is less than our carrying value, we record an asset impairment in our condensed consolidated statements of income.

5. INVESTMENT IN FINANCE LEASES, NET

As of September 30, 2018, our investment in finance leases, net, represents 18 aircraft on lease to three customers. As of September 30, 2018 and December 31, 2017, approximately 90% and 75%, respectively, of the investment in finance leases, net, by carrying value were operated in the U.S. The following table presents the components of investment in finance leases, net *(In Thousands)*:

	September 30, 2018	December 31, 2017
Total future minimum lease payments	$287,605	$369,111
Less: unearned income	(94,148)	(133,327)
Estimated residual value (unguaranteed)	67,521	96,864
Investment in finance leases, net	$260,978	$332,648

The following table presents the future minimum lease payments we are due under finance leases (*In Thousands*):

Twelve months ended September 30:	
2019	$56,480
2020	33,062
2021	32,942
2022	32,782
2023	32,752
Thereafter	99,587
Total	$287,605

6. GEOGRAPHIC CONCENTRATION

Approximately 89% and 87% of our aircraft portfolio, which consists of flight equipment held for lease, net and assets held for sale, was operated in markets outside the U.S. as of September 30, 2018 and December 31, 2017, respectively. The following table presents the global concentration of our aircraft portfolio, based on the lessee's location (*Dollars in Thousands*):

	September 30, 2018		December 31, 2017	
	Net Book Value	Percent of Total	Net Book Value	Percent of Total
Region:				
Europe	$1,920,458	22.1%	$1,318,133	16.8%
Asia Pacific (excluding China and South Asia)	1,882,171	21.7%	1,986,687	25.4%
Central and South America	1,536,937	17.7%	1,330,815	17.0%
China	1,161,202	13.4%	1,038,411	13.3%
North America	1,113,546	12.8%	1,184,201	15.1%
South Asia	635,993	7.3%	458,028	5.8%
Middle East and Africa	427,418	5.0%	300,834	3.8%
Sub-total	8,677,725	100.0%	7,617,109	97.2%
Aircraft off-lease subject to a signed lease or sales commitment	—	—	217,191	2.8%
Total	$8,677,725	100.0%	$7,834,300	100.0%

The following table presents the global concentration of our operating lease revenue, based on the lessee's location, during the nine months ended September 30, 2018 and 2017 (*Dollars in Thousands*):

	Nine months ended September 30,			
	2018		2017	
	Operating Lease Revenue	Percent of Total	Operating Lease Revenue	Percent of Total
Region:				
Asia Pacific (excluding China and South Asia)	$155,278	22.5%	$144,449	22.1%
Europe	141,659	20.5%	144,279	22.1%
Central and South America	124,451	18.0%	104,448	16.0%
North America	114,891	16.6%	116,724	17.9%
China	82,846	12.0%	76,824	11.8%
South Asia	41,935	6.1%	39,939	6.1%
Middle East and Africa	30,390	4.3%	26,271	4.0%
Operating lease revenue	$691,450	100.0%	$652,934	100.0%

For the nine months ended September 30, 2018 and 2017, no individual lessee accounted for more than 10% of our operating lease revenue. For the nine months ended September 30, 2018 and 2017, no country accounted for more than 10% of our operating lease revenue except the U.S. and China.

7. VARIABLE INTEREST ENTITIES

FINANCING STRUCTURES

In connection with certain of our financing structures, we have participated in the design and formation of certain legal entities that we consolidate into our consolidated financial statements. The purpose of these legal entities is to enable our lenders under these financing structures to perfect their security interest in certain aircraft that secure the related debt financings.

These legal entities have entered into loans with various third parties and financial institutions that are primarily guaranteed by ACG and supported by secondary guarantees from either the Export-Import Bank of the United States (Ex-Im) or the export credit agencies (ECA) of the United Kingdom, France and/or Germany (collectively Export Credit Agencies). These legal entities use the proceeds from these loans to purchase aircraft. The aircraft secure the loans and are leased, pursuant to capital leases, to us. The loans are recourse to our general credit through the ACG guarantee that is in place.

These legal entities are considered VIEs because they do not have sufficient equity at risk. Additionally, we bear significant risk of loss and participate in gains through the leases and have the power to direct the activities that most significantly impact the economic performance of these legal entities. Therefore, we have determined we are the primary beneficiary of these VIEs and consolidate them into our consolidated financial statements.

The net book value of the aircraft owned by the legal entities that are considered VIEs as of September 30, 2018 and December 31, 2017, totaled $1,240.4 million and $1,395.7 million, respectively, and is included in flight equipment held for lease, net (Note 3). In addition, as of September 30, 2018 and December 31, 2017, the debt financings associated with these legal entities totaled $565.8 million and $692.6 million, respectively, and are included in debt financings, net (Note 10).

JOINT VENTURES

In February 2016, we established two separate joint ventures, Bauhinia Aviation Capital Limited (BACL) and Bauhinia Aviation Management Limited (BAML). BACL was established with two third-party investors for the purpose of investing in the purchasing, leasing and selling of commercial aircraft. We owned 20% of the equity of BACL and our subsidiary, ACG Aircraft Leasing Ireland Ltd. (AALIL), acted as the servicer for aircraft owned by BACL. BACL was not consolidated because we were not the primary beneficiary since we did not have the obligation to absorb losses/benefits that could potentially be significant to BACL or a controlling financial interest. As of September 30, 2018 and December 31, 2017, the carrying amount and maximum exposure to loss related to BACL was $0 and $14.5 million, respectively, which is included in equity method investments.

BAML was established with a separate third-party investor for the purpose of providing management services for BACL. We own 50% of the equity of BAML. BAML is not consolidated because we are not the primary beneficiary since we do not have the obligation to absorb the losses/benefits that could potentially be significant to BAML or a controlling financial interest. As of September 30, 2018 and December 31, 2017, the carrying amount and maximum exposure to loss related to BAML was $0 and $0.7 million, respectively, which was included in equity method investments.

In January 2018, we sold our equity interest in BACL and AALIL ceased acting as servicer. In connection with the sale of our equity interest in BACL, BAML ceased providing management services for BACL and the liquidation process for BAML has commenced.

8. FAIR VALUE

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. We utilize valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible. We determine fair value based on assumptions that market participants would use in pricing an asset or liability in the principal or most advantageous market. When considering market participant assumptions in fair value measurements, the following fair value hierarchy distinguishes between observable and unobservable inputs, which are categorized in one of the following levels:

Level 1 — Quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity can access at the measurement date.

Level 2 — Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 Unobservable inputs for the asset or liability used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date.

ASSETS AND LIABILITIES MEASURED AT FAIR VALUE ON A RECURRING BASIS

Assets and liabilities measured at fair value are classified in their entirety based on the lowest level of input that is significant to their fair value measurement. As of September 30, 2018 and December 31, 2017, we did not have any Level 3 assets or liabilities that we measured at fair value on a recurring basis. The following table presents the Level 2 assets and liabilities as of September 30, 2018 and December 31, 2017 that we measured at fair value on a recurring basis (*In Thousands*):

	September 30, 2018			December 31, 2017		
	Assets	Liabilities	Total	Assets	Liabilities	Total
Derivative financial instruments at fair value, net	—	($5,667)	($5,667)	$1,006	($5,690)	($4,684)

The fair value of our interest rate swaps, an interest rate cap and foreign currency swap contracts (collectively Derivative Financial Instruments) (Note 9) are determined using market standard valuation methodologies using mid-market inputs that are observable in the market or that can be derived principally from or corroborated by observable market data (Level 2 in the fair value hierarchy) available to us as of September 30, 2018 and December 31, 2017. The pricing models utilize, among other things, interest swap rates, interest rate volatility, and foreign currency forward and spot rates, as applicable. Analysis of the derivative valuations is performed, which includes both quantitative and qualitative analyses. Examples of procedures performed include, but are not limited to, review of internally calculated valuations and comparison to external broker valuations for reasonableness, review of pricing statistics and trends, analysis of the impacts of changes in the market environment and review of changes in the market value for each derivative by risk managers and accountants. Based on the experience and financial strength of our counterparties, we determined nonperformance risk to be immaterial as of September 30, 2018 and December 31, 2017.

ASSETS AND LIABILITIES MEASURED AT FAIR VALUE ON A NON-RECURRING BASIS

We measure the fair value of our aircraft and acquired aircraft contractual rights, when events or changes to circumstances indicate that these carrying amounts of the assets may not be recoverable. The fair value measurements of our aircraft and acquired aircraft contractual rights can be based on the estimated sales price less selling costs (Level 2 inputs), or the present value of the future cash flows (i.e., an income approach) based on Level 3 inputs.

The following table presents assets impaired to fair value (as measured at the time of the adjustment) on a non-recurring basis during the year and still held as of September 30, 2018 and December 31, 2017 (*In Thousands*):

	September 30, 2018		December 31, 2017	
	Level 2	Level 3	Level 2 (a)	Level 3 (b)
Assets held for sale	$109,046	—	$122,720	—
Flight equipment held for lease, net	—	—	18,161	$15,802
Investment in finance leases, net	—	—	52,286	—
Total	$109,046	—	$193,167	$15,802

(a) Included in flight equipment held for lease, net, is $18.2 million measured during the year ended December 31, 2017. Included in investment in finance leases, net, is $52.3 million measured during the year ended December 31, 2017.
(b) Included in flight equipment held for lease, net, is $8.0 million measured during the year ended December 31, 2017.

FLIGHT EQUIPMENT HELD FOR LEASE, NET

The income approach is used to measure the fair value of flight equipment held for lease, net. The key inputs to the income approach include the current contractual lease payments, the projected future lease payments extended to the end of the aircraft's estimated holding period in its highest and best use configuration, estimated disposition value less selling costs, and the discount rate.

The current contractual lease payments are based on in-force lease rates. The projected future lease payments are based on the aircraft's type, age, configuration, current contracted lease rates for similar aircraft, industry trends, and the estimated holding period. We generally assume a 25-year estimated economic useful life for aircraft. Shorter or longer holding periods may be used based on our assessment of the continued marketability of certain aircraft types or when a potential sale of an individual aircraft has been identified, or is likely. In the case of a potential sale, the holding period is based on the estimated sale date. The disposition value reflects an estimated residual value or estimated sales price less selling costs and is generally estimated based on aircraft type and condition. The estimated cash flows are then discounted to present value.

During the nine months ended September 30, 2018, we made no changes to the valuation techniques used in the fair value measurement of the assets and liabilities discussed above.

9. DERIVATIVE FINANCIAL INSTRUMENTS AT FAIR VALUE, NET

The objective of our hedging policy is to adopt a risk averse position with respect to changes in interest rates and foreign currencies.

Our operating lease revenue is generated from rental payments. Rental payments are paid in the United States dollar (USD) and are generally fixed, but may be fixed or floating with respect to leases entered into in the future. In general, an interest rate or foreign currency exposure with respect to our borrowings arises to the extent that our floating interest and foreign currency obligations do not correlate to the mix of fixed and floating rental payments made in USD for different rental periods. We manage the interest rate and foreign currency exposure with respect to our rental payments and borrowings with Derivative Financial Instruments.

We have entered into a number of interest rate derivatives to hedge the current and future interest rate payments on our floating rate debt financings. Interest rate derivatives are agreements in which a series of interest rate cash flows are exchanged with a third party over a prescribed period. The notional amount on an interest rate derivative is not exchanged. Our interest rate derivatives typically allow us to pay fixed amounts based on fixed interest rates and receive floating amounts based on one-month and three-month London Interbank Offered Rate (LIBOR) to convert our floating rate debt to fixed rate obligations to better match the largely fixed rate cash flows from rental payments.

Furthermore, from time to time we enter into foreign currency swaps that limit exposure to foreign currency fluctuations in connection with the issuance of senior unsecured notes denominated in Japanese yen (JPY) (Note 10). The JPY swap exchanges the three-month JPY LIBOR for the three-month USD LIBOR.

CASH FLOW HEDGING DERIVATIVE FINANCIAL INSTRUMENTS

As required for all qualifying and highly effective cash flow hedges, the change in the fair value of the interest rate swap contracts was recorded in accumulated other comprehensive loss (AOCL). During the nine months ended September 30, 2018 and 2017, we recorded a pre-tax unrealized gain of $2.3 million and $2.7 million, respectively. During the nine months ended September 30, 2018 and 2017, all of our hedged forecasted transactions were determined to be probable of occurring. We did not record any ineffectiveness for cash flow hedges during the nine months ended September 30, 2018 and 2017. The maximum length of time over which we are hedging our exposure to variability in future cash flows for forecasted transactions does not exceed three years.

No amounts were reclassified from AOCL to earnings resulting from the discontinuance of cash flow hedges due to forecasted cash flows that were no longer probable of occurring for the nine months ended September 30, 2018 and 2017. Over the next twelve months, we anticipate that $0.6 million of unrealized losses on derivative instruments in AOCL will be reclassified to earnings. There were no additional deferred realized gains or losses in AOCL as of September 30, 2018 and December 31, 2017.

CONSOLIDATED FINANCIAL STATEMENT IMPACT

We determine the fair values (Note 8) of our Derivative Financial Instruments using pricing models and inputs that are observable in the market or can be derived principally from or corroborated by observable market data (Level 2 in the fair value hierarchy) available to us as of September 30, 2018 and December 31, 2017.

Certain Derivative Financial Instruments are subject to master netting agreements, which would allow the netting of derivative assets and liabilities in the case of a default under any one contract.

The following tables present the components of derivative financial instruments at fair value, net *(Dollars in Thousands)*:

	September 30, 2018				
	Fair Value	Maturity Date	Pay Rate	Receive Rate	Notional
Interest rate swaps designated as hedging	($587)	October 2019 - September 2021	2.7% - 3.5%	1M LIBOR or 3M LIBOR	$104,011
Interest rate swaps not designated as hedging	(1,857)	September 2019 - July 2033	4.9% - 5.5%	1M LIBOR	20,000
Foreign currency swaps not designated as hedging	(3,223)	February 2019 - July 2023	3M USD LIBOR	3M JPY LIBOR	300,795
Derivative financial instruments at fair value, net	($5,667)				

	December 31, 2017				
	Fair Value	Maturity Date	Pay Rate	Receive Rate	Notional
Interest rate swaps designated as hedging	($2,850)	October 2019 - September 2021	2.7% - 3.5%	1M LIBOR or 3M LIBOR	$121,104
Interest rate swaps not designated as hedging	(2,840)	September 2019 - July 2033	4.9% - 5.5%	1M LIBOR	20,000
Interest rate cap not designated as hedging	—	January 2018	6.5%	1M LIBOR	217,000
Foreign currency swap not designated as hedging	1,006	February 2019	3M USD LIBOR	3M JPY LIBOR	203,427
Derivative financial instruments at fair value, net	($4,684)				

The following tables present the pre-tax effect of our Derivative Financial Instruments *(In Thousands)*:

	Nine months ended September 30, 2018			
	Gain Recognized In AOCL	Loss Reclassed from AOCL Into Income (a)	Gain (Loss) Recognized In Income Due To Market Adjustments	
Interest rate swaps designated as hedging	$2,263	—	—	
Interest rate swaps not designated as hedging	—	($477)	$982	(b)
Foreign currency swaps not designated as hedging	—	—	(4,229)	
Unrealized gain (loss) on non-hedging derivative financial instruments	$2,263	($477)	($3,247)	

	Nine months ended September 30, 2017			
	Gain Recognized In AOCL	Loss Reclassed from AOCL Into Income (a)	Gain Recognized In Income Due To Market Adjustments	
Interest rate swaps designated as hedging	$2,660	—	—	
Interest rate swaps not designated as hedging	—	($620)	$572	(b)
Foreign currency swaps not designated as hedging	—	—	6,523	
Unrealized gain (loss) on non-hedging derivative financial instruments	$2,660	($620)	$7,095	

(a) Represents the amortization of the loss of de-designated interest rate swaps from AOCL to income.

(b) Represents the mark-to-market adjustments of de-designated interest rate swaps after de-designation.

Credit risk arises from the potential failure of the counterparty to perform according to the terms of the derivative contract. Our exposure to credit risk at any point in time is represented by the fair value of the derivative contract reported as assets. We and the counterparty do not require collateral to support derivative contracts with credit risk. As of September 30, 2018, the counterparties to our derivative contracts were LifeCorp and a third party, both of which were rated investment grade by Standard and Poor's, Moody's, and Fitch Ratings. A credit valuation analysis was performed for all derivative positions to measure the risk that the counterparty to the transaction will be unable to perform under the contractual terms (nonperformance risk) and the risk was determined to be immaterial as of September 30, 2018.

Certain master agreements include a termination event clause associated with a change in ownership and our financial strength ratings assigned by certain independent rating agencies. If there is a change in ownership and our financial strength ratings fall below a specified level, as defined within the master agreement, the counterparty could terminate the master agreement with payment due based on the fair value of the underlying derivatives. As of September 30, 2018, a foreign currency swap not designated as hedging with a fair value liability of $2.9 million had a termination event clause.

10. DEBT FINANCINGS, NET

The following tables present the components of debt financings, net as of September 30, 2018 and December 31, 2017 (*Dollars in Thousands*):

	September 30, 2018					
	Carrying Amount	Maturity Date	Interest Rate	Type	Interest Period	Currency
Unsecured debt obligations:						
Senior Notes	$5,032,000	April 2020 - November 2027	2.9% - 7.2%	Fixed and Floating	Semi-Annual and Quarterly	USD
Commercial paper	335,000	October 2018	2.2% - 2.4%	Floating	Various	USD
Term loans	495,593	February 2019 - July 2023	0.3% - 3.3%	Floating	Quarterly	USD and JPY
Revolving Credit Facilities	20,000	December 2019 - April 2023	3.4%	Floating	Monthly	USD
Secured debt obligations:						
Export Credit Facilities	700,697	September 2019 - November 2024	1.5% - 4.1%	Fixed and Floating	Quarterly	USD
Original issuance discounts	(25,085)					
Debt acquisition costs	(59,894)					
Debt financings, net	$6,498,311					

	December 31, 2017					
	Carrying Amount	Maturity Date	Interest Rate	Type	Interest Period	Currency
Unsecured debt obligations:						
Senior Notes	$4,694,000	January 2018 - November 2027	2.9% - 7.2%	Fixed	Semi-Annual	USD
Revolving Credit Facilities	235,000	December 2019 - April 2022	2.6%	Floating	Monthly	USD
Foreign denominated term loans	205,504	February 2019	0.7%	Floating	Quarterly	JPY
Secured debt obligations:						
Export Credit Facilities	842,832	December 2018 - November 2024	1.5% - 3.9%	Fixed and Floating	Quarterly	USD
Original issuance discounts	(18,735)					
Debt acquisition costs	(57,762)					
Debt financings, net	$5,900,839					

We enter into various senior unsecured financings with third parties. These financings include notes issued in reliance on Rule 144A and Regulation S under the U.S. Securities Act of 1933, as amended, and private placement notes issued to third parties (Senior Notes). In May 2018, we issued $650.0 million of senior unsecured notes due 2023 with a fixed interest rate of 3.875%. In August 2018, we issued (i) $300.0 million of senior unsecured notes due 2021 that bear interest at a floating rate based on three-month LIBOR, and (ii) $500.0 million of senior unsecured notes due 2025 with a fixed interest rate of 4.125%.

In June 2018, we entered into a new dual tranche senior unsecured term loan (2018 Term Loan). The 2018 Term Loan includes a $197.0 million USD tranche, which we drew in full in July 2018, and a 10.8 billion JPY tranche, which we drew in full in August 2018. The USD tranche bears interest at a floating rate based on three-month USD LIBOR and the JPY tranche bears interest at a floating rate based on three-month JPY LIBOR. The USD and JPY tranches both mature in July 2023.

We currently are party to two senior unsecured revolving credit facilities (Revolving Credit Facilities). In April 2018, we increased the capacity of one of our Revolving Credit Facilities from $1.5 billion to $1.6 billion and extended the maturity date from April 2022 to April 2023. As of September 30, 2018, we have drawn $20.0 million of the $1.9 billion aggregate capacity available under the Revolving Credit Facilities.

In May 2018, we established a $1.5 billion commercial paper program under which we may issue notes in minimum denominations of $250.0 thousand for periods ranging from one to 397 days. One of our Revolving Credit Facilities serves as a backstop facility for our commercial paper program.

We enter into various secured loans guaranteed by Export Credit Agencies (Export Credit Facilities) and ACG, some of which are financed through VIEs (Note 7).

As of September 30, 2018, we were in compliance with all applicable debt covenants.

All of our outstanding debt as of September 30, 2018 is recourse only to ACG, and is not guaranteed by any of ACG's equity holders, including Pacific Life, LifeCorp or Tokyo Century.

11. COMMITMENTS AND CONTINGENCIES

CAPITAL COMMITMENTS

As of September 30, 2018, we had commitments to purchase 189 aircraft scheduled for delivery through 2023. In addition, we have a contingent commitment to purchase an additional three aircraft which are not included in the table below. All of these commitments arise from fixed price purchase agreements with Boeing, Airbus and other third parties, and may include escalation provisions. The manufacturers have informed us to expect delivery delays relating to certain aircraft originally scheduled for delivery in 2018 and 2019. The anticipated delays have been reflected in our commitment schedule below; however, there remains potential of further delivery delays not currently reflected in the schedule below.

The following table presents the estimated remaining payments for the purchase of aircraft (including adjustments for certain contractual escalation provisions) *(In Thousands)*:

Twelve months ended September 30:	
2019	$2,148,073
2020	2,568,826
2021	2,104,535
2022	1,591,203
2023	675,990
Thereafter	182,379
Total	$9,271,006

As of September 30, 2018, deposits made related to our purchase agreements totaled $1.2 billion and are included in prepayments on flight equipment.

GENERAL

In the ordinary course of business, as part of contractual agreements, we provide certain indemnifications related to debt financings, aircraft acquisitions, aircraft dispositions, and other transactions. Historically we have not made payments for these types of indemnifications. There are currently no indemnifications from which a probable and reasonably estimable loss could arise. Therefore, as of September 30, 2018 and December 31, 2017, we have no related liabilities to disclose.

In the ordinary course of our business, we are a party to various legal proceedings, claims and litigation we believe are incidental to the operation of our business. Typically, these claims relate to incidents involving our aircraft and claims that involve the existence or breach of a lease, sale, or purchase contract. We regularly review the possible outcome of such legal actions and accrue for such legal actions at the time a loss is probable and the amount of the loss can be estimated. We also review all applicable indemnities and insurance coverage. Based on information currently available, we believe the potential outcome of these claims, and any reasonably possible losses exceeding amounts already recognized on an aggregated basis, are immaterial to our consolidated financial statements.

12. MEMBERS' EQUITY

PLAH owns 79% of our limited liability company interests, TCSA owns 20% of our limited liability company interests and ACGHI owns 1% of our limited liability company interests. In April 2018, we received a payment of $4.8 million from TCSA in connection with TCSA's purchase of 20% of our limited liability company interests, which represented the remaining amount owed to PLAH following the final calculation of the purchase price, and immediately distributed the funds to PLAH.

13. INCOME TAXES

Our 2018 annual effective tax rate is 1.0% based on our expected tax expense and projected income for 2018. As a result of being a limited liability company, we are taxed as a partnership for U.S. income tax purposes, and not subject to U.S. federal or state income taxes. Therefore, our annual effective tax rate is primarily driven by ACG Singapore tax expense, as our Singapore operations continue to be held by entities subject to tax.

The effective tax rate for the nine months ended September 30, 2017 differs from the statutory rate due to the effect of our conversion to a limited liability company, permanent differences and the impact of expected annual foreign income or loss subject to lower statutory rates.

14. RELATED PARTY TRANSACTIONS

For the nine months ended September 30, 2018 and 2017, we reimbursed Pacific Life $41.1 million and $43.6 million, respectively, for expenses Pacific Life incurred on our behalf, predominantly for the payment of employee compensation and benefits, and back office services.

As of September 30, 2018, we had a liability to Pacific Mutual Holding Company, LifeCorp's parent company, and Pacific Life totaling $1.5 million, which is included in accounts payable, accrued expenses and other liabilities.

We make periodic payments to LifeCorp related to our Derivative Financial Instruments.

In February 2018, we entered into a three-year servicing agreement with Tokyo Century to provide certain aircraft related management services for specified aircraft in Tokyo Century's fleet. For the nine months ended September 30, 2018, we have received $2.5 million in fees for these services which is included in other income.