Aircastle LTD
Form 10-Q
November 05, 2010

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

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

For the quarterly period ended September 30, 2010

OR

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

For the transition period from to

Commission File number 001-32959

AIRCASTLE LIMITED

(Exact name of registrant as specified in its charter)

Bermuda	**98-0444035**
(State or other jurisdiction of incorporation or organization)	*(IRS Employer Identification No.)*

c/o Aircastle Advisor LLC **300 First Stamford Place, 5th Floor, Stamford, CT**	**06902**
(Address of principal executive offices)	*(Zip Code)*

Registrant s telephone number, including area code **(203) 504-1020**

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 þ NO o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES o NO o

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

Large accelerated filer o	Accelerated filer þ	Non-accelerated filero (Do not check if a smaller reporting company)	Smaller reporting company o

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

As of October 29, 2010, there were 79,471,068 outstanding shares of the registrant s common shares, par value $0.01 per share.

Aircastle Limited and Subsidiaries
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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Aircastle Limited and Subsidiaries
Consolidated Balance Sheets
(Dollars in thousands, except share data)

	December 31, 2009	September 30, 2010 (Unaudited)
ASSETS		
Cash and cash equivalents	$ 142,666	$ 310,881
Accounts receivable	2,941	1,900
Restricted cash and cash equivalents	207,834	190,331
Restricted liquidity facility collateral	81,000	77,000
Flight equipment held for lease, net of accumulated depreciation of $586,537 and $740,786	3,812,970	3,871,054
Aircraft purchase deposits and progress payments	141,144	228,023
Leasehold improvements, furnishings and equipment, net of accumulated depreciation of $2,455 and $2,746	802	534
Other assets	65,155	71,569
Total assets	$ 4,454,512	$ 4,751,292
LIABILITIES AND SHAREHOLDERS EQUITY		
LIABILITIES		
Borrowings from secured and unsecured debt financings (including borrowings of ACS Ireland VIEs of $331,856 and $318,736, respectively)	$ 2,464,560	$ 2,679,909
Accounts payable, accrued expenses and other liabilities	60,392	68,738
Dividends payable	7,955	7,947
Lease rentals received in advance	34,381	38,049
Liquidity facility	81,000	77,000
Security deposits	82,533	77,610
Maintenance payments	253,175	299,519
Fair value of derivative liabilities	179,279	217,089
Total liabilities	3,163,275	3,465,861
Commitments and Contingencies		
SHAREHOLDERS EQUITY		
Preference shares, $.01 par value, 50,000,000 shares authorized, no shares issued and outstanding		
Common shares, $.01 par value, 250,000,000 shares authorized, 79,550,421 shares issued and outstanding at December 31, 2009; and 79,471,068 shares issued and outstanding at September 30, 2010	796	795
Additional paid-in capital	1,479,995	1,483,577

Retained earnings		70,294		92,036
Accumulated other comprehensive loss		(259,848)		(290,977)
Total shareholders equity		1,291,237		1,285,431
Total liabilities and shareholders equity	$	4,454,512	$	4,751,292

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

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Aircastle Limited and Subsidiaries
Consolidated Statements of Income
(Dollars in thousands, except per share amounts)
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2010	2009	2010
Revenues:				
Lease rental revenue	$ 128,283	$ 133,486	$ 383,683	$ 391,741
Amortization of net lease discounts and lease incentives	(3,992)	(4,203)	(7,919)	(13,957)
Maintenance revenue	31,376	2,540	47,616	14,630
Total lease rentals	155,667	131,823	423,380	392,414
Interest income	556		1,783	
Other revenue	9,517	424	9,628	578
Total revenues	165,740	132,247	434,791	392,992
Expenses:				
Depreciation	53,130	55,703	156,379	164,272
Interest, net	43,032	47,453	127,925	128,578
Selling, general and administrative (including non-cash share based payment expense of $1,742 and $1,532 for the three months ended, and $5,129 and $5,243 for the nine months ended, September 30, 2009 and 2010, respectively)	11,074	11,334	33,291	34,043
Impairment of aircraft	18,211	7,342	18,211	7,342
Maintenance and other costs	4,836	1,192	15,114	6,829
Total expenses	130,283	123,024	350,920	341,064
Other income (expense):				
Gain (loss) on sale of aircraft	162		162	(1,291)
Other income (expense)	(738)	(501)	855	(1,047)
Total other income (expense)	(576)	(501)	1,017	(2,338)
Income from continuing operations before income taxes	34,881	8,722	84,888	49,590
Income tax provision	1,423	153	5,388	4,003
Net income	$ 33,458	$ 8,569	$ 79,500	$ 45,587

Earnings per common share	Basic	$ 0.42	$ 0.11	$ 1.00	$ 0.57
Earnings per common share	Diluted	$ 0.42	$ 0.11	$ 1.00	$ 0.57
Dividends declared per share		$ 0.10	$ 0.10	$ 0.30	$ 0.30

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

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Aircastle Limited and Subsidiaries
Consolidated Statements of Cash Flows
(Dollars in thousands)
(Unaudited)

	Nine Months Ended September 30, 2009	Nine Months Ended September 30, 2010
Cash flows from operating activities:		
Net income	$ 79,500	$ 45,587
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	156,379	164,272
Amortization of deferred financing costs	8,808	11,494
Amortization of net lease discounts and lease incentives	7,919	13,957
Deferred income taxes	4,560	2,957
Accretion of purchase discounts on debt investments	(430)	
Non-cash share based payment expense	5,129	5,243
Cash flow hedges reclassified into earnings	10,932	6,412
Ineffective portion of cash flow hedges	(116)	2,533
(Gain) loss on sale of flight equipment	(162)	1,291
Security deposits and maintenance payments included in earnings	(36,982)	(13,026)
Loss on sale of investments	131	
Impairment of aircraft	18,211	7,342
Other	(556)	990
Changes in certain assets and liabilities:		
Accounts receivable	(909)	15
Restricted cash and cash equivalents	(35,456)	17,503
Other assets	(1,975)	(4,288)
Accounts payable, accrued expenses and other liabilities	(8,397)	3,137
Lease rentals received in advance	(537)	3,298
Net cash provided by operating activities	206,049	268,717
Cash flows from investing activities:		
Acquisition and improvement of flight equipment and lease incentives	(124,082)	(230,450)
Proceeds from sale of flight equipment	10,601	34,832
Aircraft purchase deposits and progress payments, net of returned deposits	(41,912)	(124,994)
Proceeds from sale of debt investments	5,423	
Principal repayments on debt investments	3,787	
Leasehold improvements, furnishings and equipment	(82)	(23)
Net cash used in investing activities	(146,265)	(320,635)
Cash flows from financing activities:		
Repurchase of shares from directors and employees	(247)	(1,662)
Proceeds from debt financings	70,916	472,682
Debt repayments	(111,619)	(257,418)

Deferred financing costs	(3,588)	(11,974)
Restricted secured liquidity facility collateral	(81,000)	4,000
Secured liquidity facility collateral	81,000	(4,000)
Security deposits received	39,554	6,675
Security deposits returned	(11,541)	(10,255)
Maintenance payments received	56,608	89,035
Maintenance payments returned	(21,938)	(39,511)
Payments for terminated hedges	(2,758)	(3,586)
Dividends paid	(23,710)	(23,853)
Net cash provided by (used in) financing activities	(8,323)	220,133
Net increase in cash and cash equivalents	51,461	168,215
Cash and cash equivalents at beginning of period	80,947	142,666
Cash and cash equivalents at end of period	$ 132,408	$ 310,881
Supplemental disclosures of cash flow information:		
Cash paid for interest, net of capitalized interest	$ 109,525	$ 103,895
Cash paid for income taxes	$ 2,304	$ 3,121
Supplemental disclosures of non-cash investing activities:		
Security deposits, maintenance payment liabilities and other liabilities settled in sale of flight equipment	$ 2,556	$ 100
Advance lease rentals and security deposits assumed in asset acquisitions	$	$ 4,330
Supplemental disclosures of non-cash financing activities:		
Advance lease rentals converted to maintenance reserves	$	$ 1,750
Security deposits converted to advance lease rentals	$	$ 730
Security deposits converted to maintenance payment liabilities	$ 11,110	$

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

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Aircastle Limited and Subsidiaries
Notes to Unaudited Consolidated Financial Statements
(Dollars in thousands, except per share amounts)
September 30, 2010

Note 1. Summary of Significant Accounting Policies

Organization

Aircastle Limited (Aircastle, the Company, we, us or our) is a Bermuda exempted company that was incorpo on October 29, 2004 by Fortress Investment Group LLC and certain of its affiliates (together, the Fortress Shareholders or Fortress) under the provisions of Section 14 of the Companies Act of 1981 of Bermuda. Aircastle s business is investing in aviation assets, including leasing, managing and selling commercial jet aircraft to airlines throughout the world and investing in aircraft related debt investments.

Basis of Presentation

Aircastle is a holding company that conducts its business through subsidiaries. Aircastle directly or indirectly owns all of the outstanding common shares of its subsidiaries. The consolidated financial statements presented are prepared in accordance with U.S. generally accepted accounting principles (US GAAP). We operate in a single segment.

The accompanying consolidated financial statements are unaudited and have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC) for interim financial reporting and, in our opinion, reflect all adjustments, including normal recurring items, which are necessary to present fairly the results for interim periods. Operating results for the periods presented are not necessarily indicative of the results that may be expected for the entire year. Certain information and footnote disclosures normally included in consolidated financial statements prepared in accordance with US GAAP have been omitted in accordance with the rules and regulations of the SEC; however, we believe that the disclosures are adequate to make information presented not misleading. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2009. The Company s management has reviewed and evaluated all events or transactions for potential recognition and/or disclosure since the balance sheet date of September 30, 2010 through the date on which the consolidated financial statements included in this Form 10-Q were issued.

Principles of Consolidation

The consolidated financial statements include the accounts of Aircastle and all of its subsidiaries. Aircastle consolidates six Variable Interest Entities (VIEs) of which Aircastle is the primary beneficiary. All intercompany transactions and balances have been eliminated in consolidation.

We consolidate VIEs in which we have determined that we are the primary beneficiary. We use judgment when deciding (a) whether an entity is subject to consolidation as a VIE, (b) who the variable interest holders are, (c) the potential expected losses and residual returns of the variable interest holders, and (d) which variable interest holder is the primary beneficiary. When determining which enterprise is the primary beneficiary, we consider (1) the entity s purpose and design, (2) which variable interest holder has the power to direct the activities that most significantly impact the entity s economic performance, and (3) the obligation to absorb losses of the entity or the right to receive benefits from the entity that could potentially be significant to the VIE. When certain events occur, we reconsider whether we are the primary beneficiary of VIEs. We do not reconsider whether we are a primary beneficiary solely because of operating losses incurred by an entity.

Recent Accounting Pronouncements

Effective January 1, 2010, the Company adopted Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) 2009-17 (ASU 2009-17), *Consolidations (Topic 810): Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities*, which requires an enterprise to perform an analysis to determine whether the enterprise s variable interest, or interests, give it a controlling financial interest in a variable

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interest entity. The determination of whether a reporting entity is required to consolidate another entity is based on, among other things, the other entity s purpose and design and the reporting entity s ability to direct the activities of the other entity that most significantly impact the other entity s economic performance. This ASU amends certain guidance for determining whether an entity is a variable interest entity and requires ongoing reassessments of whether an enterprise is the primary beneficiary of a variable interest entity. ASU 2009-17 requires a reporting entity to provide additional disclosures about its involvement with variable interest entities and any significant changes in risk exposure due to that involvement. The adoption of ASU 2009-17 did not have a material impact on the Company s consolidated financial statements. See Note 4 ¯ Variable Interest Entities.

In January 2010, the FASB issued ASU 2010-06 (ASU 2010-06), *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements*, which requires new disclosures (1) to disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and to describe the reasons for the transfers, and (2) in the reconciliation for fair value measurements using significant unobservable inputs (Level 3), to present separately information about purchases, sales issuances, and settlements on a gross basis rather than as one net number. ASU 2010-06 is effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The adoption of ASU 2010-06 did not have a material impact on our consolidated financial statements.

Note 2. Fair Value Measurements

Fair value measurements and disclosures require the use of valuation techniques to measure fair value that maximize the use of observable inputs and minimize use of unobservable inputs. These inputs are prioritized as follows:

Level 1: Observable inputs such as quoted prices in active markets for identical assets or liabilities.

Level 2: Inputs other than quoted prices included within Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities or market corroborated inputs.

Level 3: Unobservable inputs for which there is little or no market data and which require us to develop our own assumptions about how market participants price the asset or liability.

The valuation techniques that may be used to measure fair value are as follows:

Market approach Uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities.

Income approach Uses valuation techniques to convert future amounts to a single present amount based on current market expectation about those future amounts.

Cost approach Based on the amount that currently would be required to replace the service capacity of an asset (replacement cost).

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The following tables set forth our financial assets and liabilities as of December 31, 2009 and September 30, 2010 that we measure at fair value on a recurring basis by level within the fair value hierarchy. 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.

		Fair Value Measurements at December 31, 2009 Using Fair Value Hierarchy			
	Fair Value as of December 31, 2009	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Valuation Technique
Assets:					
Cash and cash equivalents	$ 142,666	$ 142,666	$	$	Market
Restricted cash and cash equivalents	207,834	207,834			Market
Total	$ 350,500	$ 350,500	$	$	
Liabilities:					
Derivative liabilities	$ 179,279	$	$ 140,372	$ 38,907	Income

		Fair Value Measurements at September 30, 2010 Using Fair Value Hierarchy			
	Fair Value as of September 30, 2010	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Valuation Technique
Assets:					
Cash and cash equivalents	$ 310,881	$ 310,881	$	$	Market
Restricted cash and cash equivalents	190,331	190,331			Market
Total	$ 501,212	$ 501,212	$	$	

Liabilities:									
Derivative liabilities	$	217,089	$		$	150,649	$	66,440	Income

Our cash and cash equivalents, along with our restricted cash and cash equivalents balances, consist largely of money market securities that are considered to be highly liquid and easily tradable. These securities are valued using inputs observable in active markets for identical securities and are therefore classified as Level 1 within our fair value hierarchy. Our interest rate derivatives included in Level 2 consist of United States dollar denominated interest rate derivatives, and their fair values are determined by applying standard modeling techniques under the income approach to relevant market interest rates (cash rates, futures rates, swap rates) in effect at the period close to determine appropriate reset and discount rates and incorporates an assessment of the risk of non-performance by the interest rate derivative counterparty in valuing derivative assets and an evaluation of the Company s credit risk in valuing derivative liabilities.

Our interest rate derivatives included in Level 3 consist of United States dollar denominated interest rate swaps on Term Financing No. 1 with a guaranteed notional balance. The guaranteed notional balance has an upper notional band that matches the hedged debt and a lower notional band. The notional balance is guaranteed to match the hedged debt balance if the debt balance decreases within the upper and lower notional band. During the nine months ended September 30, 2010, we made supplemental principal payments on Term Financing No. 1 and the notional balance was adjusted to match the debt balance of Term Financing No. 1. The fair value of the interest rate derivative is determined based on the adjusted upper notional band using cash flows discounted at the relevant market interest rates in effect at

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the period close. It incorporates an assessment of the risk of non-performance by the interest rate derivative counterparty in valuing derivative assets and an evaluation of the Company s credit risk in valuing derivative liabilities. The range of the guaranteed notional between the upper and lower band represents an option that may not be exercised independently of the debt notional and is therefore valued based on unobservable market inputs.

The following table reflects the activity for the classes of our assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the three and nine months ended September 30, 2010:

	Three Months Ended September 30, 2010	Nine Months Ended September 30, 2010
	Derivative Liabilities	
Balance at beginning of period	$ (59,416)	$ (38,907)
Transfers into Level 3		
Transfers out of Level 3		
Total gains or (losses):		
Included in interest income		
Included in other income (expense)	(171)	(446)
Included in interest expense	(58)	(180)
Included in other comprehensive income	(6,795)	(26,907)
Balance at end of period	$ (66,440)	$ (66,440)

We measure the fair value of certain assets and liabilities on a non-recurring basis, when US GAAP requires the application of fair value, including events or changes in circumstances that indicate that the carrying amounts of assets may not be recoverable. Assets subject to these measurements include aircraft. We record aircraft at fair value when we determine the carrying value may not be recoverable. Fair value measurements for aircraft in impairment tests are based on an income approach that uses Level 3 inputs, which include the Company s assumptions and appraisal data as to future cash proceeds from leasing and selling aircraft.

In the three and nine months ended September 30, 2009, we recognized an impairment of $18,211 related to two Boeing Model 737-300 aircraft and two Boeing Model 757-200 aircraft, triggered by the early termination of the leases for these aircraft and the change to estimated future cash flows. The Company received $18,176, of which $8,382 represented lease termination payments and $9,794 related to maintenance revenue from the previous lessees of these aircraft. These lease termination payments were recorded as other revenue during the three and nine months ended September 30, 2009.

In the three and nine months ended September 30, 2010, we recognized an impairment of $7,342 related to one Boeing Model 737-300 aircraft and one Boeing Model 737-500 aircraft, triggered by the early termination of the lease for one aircraft, a signed forward sales agreement for the other aircraft and, for each, the change to estimated future cash flows. The Company recorded $4,396 related to maintenance revenue from the previous lessees of the aircraft that is the subject of the forward sales agreement during the three months ended March 31, 2010 and $1,765 related to maintenance revenue from the lessees of one aircraft during the three months ended September 30, 2010.

Our financial instruments, other than cash, consist principally of cash equivalents, restricted cash and cash equivalents, accounts receivable, accounts payable, amounts borrowed under financings and interest rate derivatives. The fair value of cash, cash equivalents, restricted cash and cash equivalents, accounts receivable and accounts payable approximates the carrying value of these financial instruments because of their short term nature.

The fair values of our securitizations which contain third-party credit enhancements are estimated using a discounted cash flow analysis, based on our current incremental borrowing rates of borrowing arrangements that do not

Aircastle Limited and Subsidiaries
Notes to Unaudited Consolidated Financial Statements
(Dollars in thousands, except per share amounts)
September 30, 2010

contain third-party credit enhancements. The fair values of our term debt financings are estimated using a discounted cash flow analysis, based on our current incremental borrowing rates for similar types of borrowing arrangements.

The carrying amounts and fair values of our financial instruments at December 31, 2009 and September 30, 2010 are as follows:

	December 31, 2009		September 30, 2010	
	Carrying Amount of Asset (Liability)	Fair Value of Asset (Liability)	Carrying Amount of Asset (Liability)	Fair Value of Asset (Liability)
Securitizations and term debt financings	$ (2,324,972)	$ (2,037,718)	$ (2,099,525)	$ (1,892,319)
ECA term financings	(139,588)	(140,984)	(201,585)	(207,257)
A330 PDP Facility			(82,778)	(82,778)
2010-1 Notes			(296,021)	(304,500)

Note 3. Lease Rental Revenues and Flight Equipment Held for Lease

Minimum future annual lease rentals contracted to be received under our existing operating leases of flight equipment at September 30, 2010 were as follows:

Year Ending December 31,	Amount
Remainder of 2010	$ 134,788
2011	522,082
2012	458,435
2013	354,419
2014	270,676
2015	216,745
Thereafter	415,130
Total	$ 2,372,275

Geographic concentration of lease rental revenue earned from flight equipment held for lease was as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
Region	2009	2010	2009	2010
Europe	47%	46%	46%	46%
Asia	18%	21%	20%	20%
North America	16%	14%	16%	15%
Latin America	8%	9%	7%	9%
Middle East and Africa	11%	10%	11%	10%
Total	100%	100%	100%	100%

The classification of regions in the tables above and the table and discussion below is determined based on the principal location of the lessee of each aircraft.

For the three months ended September 30, 2009, one customer accounted for 7% of lease rental revenue or, if combined with two companies under common control with it, 11% of lease rental revenue and for the three months ended September 30, 2010, one customer accounted for 7% of lease rental revenue or, if combined with two companies under common control with it, 10% of lease rental revenue. The obligations of these companies under common control are not guaranteed by the controlling entity.

Aircastle Limited and Subsidiaries
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(Dollars in thousands, except per share amounts)
September 30, 2010

For the nine months ended September 30, 2009, one customer accounted for 7% of lease rental revenue or, if combined with two companies under common control with it, 11% of lease rental revenue and for the nine months ended September 30, 2010, one customer accounted for 7% of lease rental revenue or, if combined with two companies under common control with it, 11% of lease rental revenue. The obligations of these companies under common control are not guaranteed by the controlling entity.

The following tables set forth revenue attributable to individual countries representing at least 10% of total revenue based on each lessee s principal place of business:

	Three Months Ended September 30,					
	2009			2010		
Country	**Revenue**	**Percent of Total Revenue**	**Number of Lessees**	**Revenue**	**Percent of Total Revenue**	**Number of Lessees**
United States	$ 16,501	10%	4	$ 16,980	13%	4
China[(a)]				14,714	11%	5
Netherlands	24,001	14%	4	14,015	11%	3
India[(b) (c)]	19,944	12%	3			

(a) Total revenue attributable to China was less than 10% for the three months ended September 30, 2009.

(b) Total revenue attributable to India was less than 10% for the three months ended September 30, 2010.

(c) Includes maintenance revenue of $17.2 million for the three months ended September 30, 2009.

	Nine Months Ended September 30,					
	2009			2010		
Country	Revenue	Percent of Total Revenue	Number of Lessees	Revenue	Percent of Total Revenue	Number of Lessees
United States	$ 48,841	11%	4	$ 50,379	13%	4
China[a]				42,557	11%	5
Netherlands	53,418	12%	4	42,042	11%	3
India[b] [c]	46,318	11%	3			

(a) Total revenue attributable to China was less than 10% for the nine months ended September 30, 2009.

(b) Total revenue attributable to India was less than 10% for the nine months ended September 30, 2010.

(c) Includes maintenance revenue of $31.9 million for the nine months ended September 30, 2009.

Geographic concentration of net book value of flight equipment held for lease was as follows:

	December 31, 2009		September 30, 2010	
Region	Number of Aircraft	Net Book Value %	Number of Aircraft	Net Book Value %
Europe	58	46%	62	46%
Asia	30(1)	20%	33	23%
North America	15	12%	14	11%
Latin America	10	9%	11	9%
Middle East and Africa	13	12%	11	11%
Off-lease	3(2)	1%	1(3)	%

Total	129	100%	132	100%

(1) Includes one Boeing Model 737-400 aircraft which was being converted to freighter configuration and for which we had an executed lease with a carrier in Asia post-conversion and which we delivered in the first quarter of 2010.

(2) Includes one Boeing Model 737-300 aircraft which was returned to us on a consensual early lease termination in the third quarter of 2009 and which was delivered to a customer on lease in the second quarter of 2010 and two Boeing Model 757-200 aircraft which were returned to us early on a consensual basis in the third quarter of 2009, one of which was sold in the second quarter of 2010 and the other which was

sold in the third quarter of 2010.

(3) Represents one Boeing Model 737-300 aircraft which was returned to us late in the third quarter of 2010 when a customer ceased operations. We are currently marketing this aircraft for lease or sale.

Aircastle Limited and Subsidiaries
Notes to Unaudited Consolidated Financial Statements
(Dollars in thousands, except per share amounts)
September 30, 2010

The following table sets forth net book value of flight equipment attributable to individual countries representing at least 10% of total assets based on each lessee s principal place of business as of:

	December 31, 2009			September 30, 2010		
Country	**Net Book Value**	**Net Book Value %**	**Number of Lessees**	**Net Book Value**	**Net Book Value %**	**Number of Lessees**
China	$			$ 444,396	11%	5
Netherlands	435,796	11%	3	416,539	11%	3

(a) The net book value of flight equipment attributable to China was less than 10% as of December 31, 2009.

At December 31, 2009 and September 30, 2010, the amounts of lease incentive liabilities recorded in maintenance payments on the consolidated balance sheets were $14,859 and $19,011, respectively.

At December 31, 2009 and September 30, 2010, the amounts of prepaid lease incentives, net of amortization, recorded in other assets on the consolidated balance sheets were $9,560 and $8,668 respectively.

Note 4. Variable Interest Entities

As described in Note 1 Summary of Significant Accounting Policies, effective January 1, 2010 ASU 2009-17 provided additional guidance for determining when to consolidate certain entities in which the investors do not have the characteristics of a controlling financial interest or the total equity investment at risk is not sufficient to permit the legal entity to finance its activities without additional subordinated financial support by any parties, including equity holders.

Aircastle consolidates six VIEs of which it is the primary beneficiary. ACS Aircraft Finance Ireland plc (ACS Ireland), ACS Aircraft Finance Ireland 2 Limited (ACS Ireland 2), ACS Ireland 3 Limited (ACS Ireland 3), Air Knight 1 Leasing Limited (Air Knight 1), Air Knight 2 Leasing Limited (Air Knight 2) and Air Knight 3 Leasing Limited (Air Knight 3). The operating activities of these VIEs are limited to acquiring, owning, leasing, maintaining, operating and, under certain circumstances, selling the eighteen aircraft discussed below.

Securitizations and Term Financing

In connection with Securitization No. 1, two of our subsidiaries, ACS Ireland and ACS Aircraft Finance Bermuda Limited (ACS Bermuda) issued Class A-1 notes and each has fully and unconditionally guaranteed the other s obligations under the notes. In connection with Securitization No. 2, two of our subsidiaries, ACS Ireland 2 and ACS 2007-1 Limited (ACS Bermuda 2) issued Class A-1 notes and each has fully and unconditionally guaranteed the other s obligations under the notes. In connection with Term Financing No. 1, two of our subsidiaries, ACS Ireland 3 and ACS 2008-1 Limited (ACS Bermuda 3) entered into a seven year term debt facility and each has fully and unconditionally guaranteed the other s obligations under the term debt facility. ACS Bermuda, ACS Bermuda 2 and ACS Bermuda 3 are collectively referred to as the ACS Bermuda Group . At September 30, 2010, the assets of the three VIEs include fifteen aircraft transferred into the VIEs at historical cost basis in connection with Securitization No. 1, Securitization No. 2 and Term Financing No. 1.

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Aircastle is the primary beneficiary of ACS Ireland, ACS Ireland 2 and ACS Ireland 3 (collectively, the ACS Ireland VIEs) as we have both the power to direct the activities of the VIEs that most significantly impact the economic performance of such VIEs and we bear the significant risk of loss and participate in gains through Class E-1 Securities. Although Aircastle has not guaranteed the ACS Ireland VIEs debt, Aircastle wholly owns the ACS Bermuda Group which has fully and unconditionally guaranteed the ACS Ireland VIEs obligations. The activity that most significantly impacts the economic performance is the leasing of aircraft. Aircastle Advisor (Ireland) Limited (Aircastle s wholly owned subsidiary) is the Remarketing Servicer and is responsible for the leasing of the aircraft. An Irish charitable trust owns 95% of the common shares of the ACS Ireland VIEs. The Irish charitable trust s risk is limited to its annual dividend of $2 per VIE.

The combined assets of the ACS Ireland VIEs as of September 30, 2010 are $474,142. The combined liabilities of the ACS Ireland VIEs, net of $96,016 Class E-1 Securities held by the Company which is eliminated in consolidation, as of September 30, 2010 are $425,800.

ECA Term Financings

Air Knight 1, Air Knight 2, and Air Knight 3 (collectively, the Air Knight VIEs) entered into three different twelve-year term loans, two with Citibank International Plc, and one with Calyon, all of which are supported by a guarantee from Compagnie Francaise d Assurance pour le Commerce Exterieur, (COFACE), the French government sponsored export credit agency (ECA), for the financing of three new Airbus Model A330-200 aircraft. The Air Knight VIEs are owned by a charitable trust. We refer to these COFACE-supported financings as ECA Term Financings.

Aircastle is the primary beneficiary of the Air Knight VIEs as we have the power to direct the activities of the VIEs that most significantly impact the economic performance of such VIEs and we bear the significant risk of loss and participate in gains through a finance lease. The activity that most significantly impacts the economic performance is the leasing of aircraft of which Aircastle Advisor LLC (Aircastle s wholly owned subsidiary) is the Servicer and is responsible for the leasing of the aircraft. There is a cross collateralization guarantee between the Air Knight VIEs. In addition, Aircastle guarantees the debt of the Air Knight VIEs.

The only assets that the Air Knight VIEs have on their books are financing leases that are eliminated in the consolidated financial statements. The related aircraft are included in our flight equipment held for lease balance. The consolidated liabilities of the Air Knight VIEs as of September 30, 2010 are $219,256.

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Note 5. Borrowings from Secured and Unsecured Debt Financings

The outstanding amounts of our secured and unsecured term debt financings were as follows:

	At December 31, 2009	At September 30, 2010		
	Outstanding	Outstanding		Final Stated
Debt Obligation	**Borrowings**	**Borrowings**	**Interest Rate[1]**	**Maturity[2]**
Secured Debt Financings:				
Securitization No. 1	$ 436,091	$ 420,444	0.53%	6/20/31
Securitization No. 2	1,061,566	1,012,961	0.52%	6/14/37
Term Financing No. 1	708,710	666,120	2.01%	5/02/15
Term Financing No. 2	118,605		N/A	N/A
ECA Term Financings	139,588	201,585	2.65% to 4.48%	5/27/21 to 08/31/22
A330 PDP Facility		82,778	2.76%	12/1/11[3]
Total secured debt financings	2,464,560	2,383,888		
Unsecured Debt Financings:				
2010-1 Notes		296,021	9.75%	8/01/18
2010 Revolving Credit Facility			N/A	9/28/13
Total unsecured debt financings		296,021		
Total secured and unsecured debt financings	$ 2,464,560	$2,679,909		

(1) Reflects floating rate in effect at the applicable reset date except for the ECA Term Financings, which are fixed rate.

(2) For Securitization No. 1,

Securitization No. 2 and Term Financing No. 1, all cash flows available after expenses and interest will be applied to debt amortization, if the debt is not refinanced by June 2011, June 2012, and May 2013, respectively.

(3) Reflects the last scheduled delivery month for the six relevant new Airbus A330-200 delivery positions. The final maturity date is the earlier of the aircraft delivery date or nine months after the scheduled delivery month for the last scheduled delivery position.

The following securitizations and term debt financing structures include liquidity facility commitments described in the table below:

Facility	Liquidity Facility Provider	Available Liquidity December 31, 2009	Available Liquidity September 30, 2010	Unused Fee	Interest Rate on any Advances
Securitization No. 1	Calyon	$ 42,000	$ 42,000	0.45%	1M Libor + 1.00%
Securitization No. 2	HSH Nordbank AG[1]	79,617	75,972	0.50%	1M Libor + 0.75%

Term Financing No. 1	Calyon	14,174	13,222	0.60%	1M Libor + 1.20%

(1) Following a ratings downgrade with respect to the liquidity facility provider in May 2009, the liquidity facility was drawn and the proceeds, or permitted investments thereof, remain available to provide liquidity if required. Amounts drawn following a ratings downgrade with respect to the liquidity facility provider do not bear interest; however, net investment earnings will be paid to the liquidity facility provider and the unused fee continues to apply.

Secured Debt Financings:

Term Financing No. 1

A maintenance-adjusted appraisal of Term Financing No. 1 Portfolio must be completed each year before a date in early May by a specified appraiser. To determine the maintenance-adjusted values, the appraiser applies upward or downward, adjustments of half-life current market values for the aircraft in the Term Financing No. 1 Portfolio based upon the maintenance status of the airframe, engines, landing gear and auxiliary power unit (APU), and applies certain other upward or downward adjustments for equipment, capabilities and utilization. Compliance with the loan to value ratio is measured each month by comparing the 75% minimum ratio against the most recently completed maintenance-adjusted appraised value, less 0.5% for each month since such appraisal was provided to the lenders, plus 75% of the cash maintenance reserve balance held on deposit for the Term Financing No. 1 Portfolio. Noncompliance

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with the loan to value ratio will require us to make supplemental principal payments but will not by itself result in a default under Term Financing No. 1.

In March 2010, we completed the maintenance-adjusted appraisal for the Term Financing No. 1 Portfolio and determined that our loan to value ratio on the April 2010 payment date was approximately 78%. During the second quarter of 2010, we made supplemental principal payments of $11,496. In June 2010, we amended the loan documents for Term Financing No. 1 so that 75% of the stated amount of qualifying letters of credit held for maintenance events would be taken into account in the loan to value test. Based on this amendment and the supplemental principal payments previously made, we were in compliance with the loan to value ratio as of October 12, 2010.

Term Financing No. 2

The outstanding principal balance of Term Financing No. 2 in the amount of $103,196, plus accrued interest, loan breakage fees, interest rate derivative breakage fees of $3,586, and accrued interest on the terminated interest rate derivative, was repaid in full, and no further amounts may be drawn thereunder, from the proceeds of the 2010-1 Notes on August 12, 2010. During the third quarter of 2010, we wrote-off $1,859 of deferred financing fees, which is reflected in interest expense on the consolidated statement of income.

ECA Term Financings

In August 2010, we entered into a twelve-year $68,967 term loan with Citibank N.A. which is supported by a guarantee from Compagnie Francaise d Assurance pour le Commerce Exterieur, or COFACE, the French government sponsored export credit agency, or ECA, for the financing of a new Airbus Model A330-200F freighter aircraft. The borrowing under this financing bears a fixed rate of interest equal to 2.645%. We refer to these COFACE-supported financings as ECA Term Financings .

The obligations outstanding under the ECA Term Financings are secured by, among other things, a mortgage over the aircraft and a pledge of our ownership interest in our subsidiary company that leases the aircraft to the operator. The ECA Term Financings documents contain a $500,000 minimum net worth covenant for Aircastle Limited, as well as a material adverse change default, a cross default to any other recourse obligation of Aircastle Limited, and other terms and conditions customary for ECA-supported financings being completed at this time. In addition, Aircastle Limited has guaranteed the repayment of the ECA Term Financings.

A330 PDP Facility

In June 2010, one of our subsidiaries entered into a $108,500 loan facility to finance a portion of the pre-delivery payments (PDP) on six new Airbus Model A330-200 aircraft to be acquired under the Airbus A330 acquisition agreement (the Airbus A330 Agreement). See Note 10 Commitments and Contingencies. We refer to this loan facility as the A330 PDP Facility . The loans are secured by, among other things, an assignment of certain rights under the Airbus A330 Agreement and an assignment of the lease agreement for each aircraft and are guaranteed by Aircastle Limited.

Loans under the A330 PDP Facility bear interest on a floating rate basis of one-month Libor plus 2.50% per annum and are payable monthly in arrears following the initial drawdown on the outstanding balance of the facility. The loans are subject to a commitment fee of 0.25% per annum, payable quarterly in arrears, on the undrawn portion of the facility. The facility may be prepaid without penalty, subject to certain customary conditions. Each loan is payable in full on the delivery date of the relevant aircraft. There are no financial covenants associated with this facility.

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A330 SLB Facility

In July 2010, one of our subsidiaries entered into a $75,000 secured credit facility, which we refer to as the A330 SLB Facility, with Citicorp North America Inc., to finance the acquisition of three used Airbus Model A330-200 passenger configuration aircraft during the third quarter of 2010 from Sri Lankan Airlines in a sale-leaseback transaction. On July 26, 2010, the first of the three sale-leaseback transactions closed and we borrowed $25,000 under the facility. The outstanding balance in the amount of $25,000 plus accrued interest was repaid in full from the proceeds of the 2010-1 Notes on August 3, 2010 and no further amounts may be drawn thereunder. During the third quarter of 2010, we wrote-off $612 of deferred financing fees which is reflected in interest expense on the consolidated statement of income.

Unsecured Debt Financings:

2010-1 Notes

On July 30, 2010, Aircastle Limited issued $300,000 aggregate principal amount of 9.75% Senior Notes due 2018, which we refer to as the 2010-1 Notes, pursuant to an Indenture, dated as of July 30, 2010, between Aircastle Limited and Wells Fargo Bank, National Association, as trustee. The 2010-1 Notes were issued at 98.645% of par and were offered only to qualified institutional buyers and buyers outside the United States in accordance with Rule 144A and Regulation S, respectively, under the Securities Act of 1933. The 2010-1 Notes will mature on August 1, 2018 and bear interest at the rate of 9.75% per annum, payable semi-annually in arrears on February 1 and August 1, commencing on February 1, 2011 to holders of record on the immediately preceding January 15 and July 15.

The Company may redeem all or a portion of the 2010-1 Notes at any time on or after August 1, 2014 at a premium decreasing ratably to zero, plus accrued and unpaid interest. In addition, prior to August 1, 2013 the Company may redeem up to 35% of the aggregate principal amount of the 2010-1 Notes with the net cash proceeds of certain equity offerings at a redemption price equal to 109.75%, plus accrued and unpaid interest. If the Company undergoes a change of control, it must offer to repurchase the 2010-1 Notes at 101% of the principal amount, plus accrued and unpaid interest. The 2010-1 Notes are the Company s unsecured senior obligations and rank equally in right of payment with all of the Company s existing and future senior debt and rank senior in right of payment to all of the Company s existing and future subordinated debt. The 2010-1 Notes are effectively junior in right of payment to all of the Company s existing and future secured debt to the extent of the assets securing such debt, and to any existing and future liabilities of the Company s subsidiaries. The 2010-1 Notes are not guaranteed by any of the Company s subsidiaries or any third party.

We used a portion of the net proceeds from the 2010-1 Notes to repay all of the outstanding indebtedness under our Term Financing No. 2 and our A330 SLB Facility and for general corporate purposes, including the purchase of aviation assets.

On September 24, 2010, the 2010-1 Notes were registered by the Company with the U.S. Securities Exchange Commission and in October 2010 we completed the exchange of all outstanding unregistered 2010-1 Notes. The registered notes have terms that are substantially identical to the privately placed notes.

2010 Revolving Credit Facility

On September 28, 2010, the Company entered into a three-year $50,000 senior unsecured revolving credit facility with a group of banks, which we refer to as the 2010 Revolving Credit Facility. The 2010 Revolving Credit Facility provides loans in amounts up to $50,000 for working capital and other general corporate purposes. We have not drawn on the 2010 Revolving Credit Facility.

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Note 6. Dividends

The following table sets forth the quarterly dividends declared by our Board of Directors for the periods covered in this report:

Declaration Date	Dividend per Common Share	Aggregate Dividend Amount	Record Date	Payment Date
December 22, 2008	$ 0.10	$ 7,862	December 31, 2008	January 15, 2009
March 13, 2009	$ 0.10	7,923	March 31, 2009	April 15, 2009
June 10, 2009	$ 0.10	7,923	June 30, 2009	July 15, 2009
September 10, 2009	$ 0.10	7,925	September 30, 2009	October 15, 2009
December 14, 2009	$ 0.10	7,955	December 31, 2009	January 15, 2010
March 12, 2010	$ 0.10	7,951	March 31, 2010	April 15, 2010
May 25, 2010	$ 0.10	7,947	June 30, 2010	July 15, 2010
September 21, 2010	$ 0.10	7,947	September 30, 2010	October 15, 2010

Note 7. Earnings Per Share

We include all common shares granted under our incentive compensation plan which remain unvested (restricted common shares) and contain non-forfeitable rights to dividends or dividend equivalents, whether paid or unpaid (participating securities), in the number of shares outstanding in our basic and diluted earnings per share calculations using the two-class method. All of our restricted common shares are currently participating securities.

Under the two-class method, earnings per common share are computed by dividing the sum of distributed earnings allocated to common shareholders and undistributed earnings allocated to common shareholders by the weighted average number of common shares outstanding for the period. In applying the two-class method, distributed and undistributed earnings are allocated to both common shares and restricted common shares based on the total weighted average shares outstanding during the period as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2010	2009	2010
Weighted-average shares:				
Common shares outstanding	78,012,914	78,536,704	77,977,089	78,470,237
Restricted common shares	1,352,974	1,048,237	1,309,244	1,137,163
Total weighted-average shares	79,365,888	79,584,941	79,286,333	79,607,400
Percentage of weighted-average shares:				

Common shares outstanding	98.30%	98.68%	98.35%	98.57%
Restricted common shares	1.70%	1.32%	1.65%	1.43%
Total	100.00%	100.00%	100.00%	100.00%

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The calculations of both basic and diluted earnings per share are as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	**2010**	**2009**	**2010**
Earnings per share Basic:				
Net income	$ 33,458	$ 8,569	$ 79,500	$ 45,587
Less: Distributed and undistributed earnings allocated to restricted common shares [a]	(570)	(113)	(1,313)	(651)
Earnings available to common shareholders Basic	$ 32,888	$ 8,456	$ 78,187	$ 44,936
Weighted-average common shares outstanding Basic	78,012,914	78,536,704	77,977,089	78,470,237
Earnings per common share Basic	$ 0.42	$ 0.11	$ 1.00	$ 0.57

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	**2010**	**2009**	**2010**
Earnings per share Diluted:				
Net income	$ 33,458	$ 8,569	$ 79,500	$ 45,587
Less: Distributed and undistributed earnings allocated to restricted common shares	(570)	(113)	(1,313)	(651)
Earnings available to common shareholders Diluted	$ 32,888	$ 8,456	$ 78,187	$ 44,936
Weighted-average common shares outstanding Basic	78,012,914	78,536,704	77,977,089	78,470,237
Effect of dilutive shares	(b)	(b)	(b)	(b)
Weighted-average common shares outstanding Diluted	78,012,914	78,536,704	77,977,089	78,470,237
Earnings per common share Diluted	$ 0.42	$ 0.11	$ 1.00	$ 0.57

(a) For the three months ended September 30, 2009 and 2010, distributed and undistributed earnings to restricted shares is 1.70% and 1.32%, respectively, of net income. For the nine months ended September 30, 2009 and 2010, distributed and undistributed earnings to restricted shares is 1.65% and 1.43%, respectively, of net income. The amount of restricted share forfeitures for all periods present is immaterial to the allocation of distributed and undistributed earnings.

(b) For the three and nine months ended September 30, 2009 and 2010, we have no dilutive shares.

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Note 8. Income Taxes

Income taxes have been provided for based upon the tax laws and rates in countries in which our operations are conducted and income is earned. The Company received an assurance from the Bermuda Minister of Finance that it would be exempted from local income, withholding and capital gains taxes until March 2016. Consequently, the provision for income taxes recorded relates to income earned by certain subsidiaries of the Company which are located in, or earn income in, jurisdictions that impose income taxes, primarily the United States and Ireland.

The sources of income from continuing operations before income taxes for the three and nine months ended September 30, 2009 and 2010 were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	**2010**	**2009**	**2010**
U.S. operations	$ 383	$ 218	$ 1,342	$ 1,240
Non-U.S. operations	34,498	8,504	83,546	48,350
Total	$ 34,881	$ 8,722	$ 84,888	$ 49,590

All of our aircraft-owning subsidiaries that are recognized as corporations for U.S. tax purposes are non-U.S. corporations. These non-U.S. subsidiaries generally earn income from sources outside the United States and typically are not subject to U.S. federal, state or local income taxes unless they operate within the U.S., in which case they may be subject to federal, state and local income taxes. We also have a U.S-based subsidiary which provides management services to our non-U.S. subsidiaries and is subject to U.S. federal, state and local income taxes.

Differences between statutory income tax rates and our effective income tax rates applied to pre-tax income consisted of the following:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	**2010**	**2009**	**2010**
Notional U.S. federal income tax expense at the statutory rate	$ 12,209	$ 3,053	$ 29,711	$ 17,357
U.S. state and local income tax, net	19	17	68	78
Non-U.S. operations	(10,972)	(2,925)	(24,878)	(14,318)
Non-deductible expenses in the U.S.	6	135	21	1,025
Other	161	(127)	466	(139)
Provision for income taxes	$ 1,423	$ 153	$ 5,388	$ 4,003

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Note 9. Comprehensive Income

Total comprehensive income includes net income, the changes in the fair value and the reclassification into earnings of amounts previously deferred relating to our derivative financial instruments which qualify for hedge accounting and the change in unrealized fair value of debt securities classified as available-for-sale. Total comprehensive income for the three and nine months ended September 30, 2009 and 2010 was as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	**2010**	**2009**	**2010**
Net income	$ 33,458	$ 8,569	$ 79,500	$ 45,587
Net change in fair value of derivatives, net of tax benefit of $135 and $52 for the three months ended, and tax expense of $1,068 and tax benefit of $332 for the nine months ended, September 30, 2009 and 2010, respectively	(15,696)	(7,716)	63,596	(37,541)
Derivative loss reclassified into earnings	5,894	2,338	13,690	6,412
Net change in unrealized fair value of debt investments	1,836		1,698	
Total comprehensive income	$ 25,492	$ 3,191	$ 158,484	$ 14,458

The following table sets forth the components of accumulated other comprehensive income (loss), net of tax where applicable, at December 31, 2009 and September 30, 2010:

	Accumulated Other Comprehensive Income (Loss)
December 31, 2009, net of tax benefit of $3,057	$ (259,848)
Net change in fair value of derivatives, net of tax benefit of $332	(37,541)
Derivative loss reclassified into earnings	6,412
September 30, 2010	$ (290,977)

Note 10. Commitments and Contingencies

On June 20, 2007, we entered into the Airbus A330 Agreement, under which we agreed to acquire new A330 aircraft (the New A330 Aircraft), from Airbus S.A.S. We currently have nine New A330 Aircraft remaining to be delivered, with one scheduled for delivery in 2010, seven in 2011 and one in 2012. During 2009, we acquired two New A330 Aircraft and in August 2010, we acquired one New A330 Aircraft, configured as an Airbus Model A330-200F freighter aircraft.

Committed amounts to acquire, convert, and modify aircraft including, where applicable, our estimate of adjustments for configuration changes, engine acquisition costs, contractual price escalations and other adjustments, net of amounts already paid, are approximately $265,385 in 2010, $419,492 in 2011 and $61,394 in 2012.

Note 11. Derivatives

The objective of our hedging policy is to adopt a risk averse position with respect to changes in interest rates. Accordingly, we have entered into a number of interest rate derivatives to hedge the current and expected future interest rate payments on our variable rate debt. 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 provide that we make fixed rate payments and receive floating rate payments to convert our floating rate borrowings to fixed rate obligations to better match the largely fixed rate cash flows from our investments in flight equipment.

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We held the following interest rate derivatives as of September 30, 2010:

	Liability Derivatives							
Hedged Item	**Current Notional Amount**	**Effective Date**	**Maturity Date**	**Future Maximum Notional Amount**	**Floating Rate**	**Fixed Rate**	**Balance Sheet Location**	**Fair Value**
Interest rate derivatives designated as cash flow hedges:								
Securitization No. 1	$ 433,368	Jun-06	Jun-16	$ 433,368	1M LIBOR+ 0.27%	5.78%	Fair value of derivative liabilities	$ 71,852
Securitization No. 2	1,004,723	Jun-07	Jun-12	1,004,723	1M LIBOR	5.25 to 5.36%	Fair value of derivative liabilities	78,797
Term Financing No. 1(1)	604,773	Jun-08	May-13	604,773	1M LIBOR	4.04%	Fair value of derivative liabilities	44,824
Term Financing No. 1(1)		May-13	May-15	464,181	1M LIBOR	5.31%	Fair value of derivative liabilities	21,616
Total interest rate derivatives	$ 2,042,864			$ 2,507,045				$ 217,089

(1) The interest payments related to Term Financing No. 1 are being hedged by two consecutive interest rate derivatives. When the first matures in May 2013, the next becomes

effective.

Our interest rate derivatives involve counterparty credit risk. As of September 30, 2010, our interest rate derivatives are held with the following counterparties: JP Morgan Chase Bank NA, Citibank Canada NA and HSH Nordbank AG. All of our counterparties or guarantors of these counterparties are considered investment grade (senior unsecured ratings of A3 or above) by Moody s Investors Service. All are also considered investment grade (long-term foreign issuer ratings of A or above) by Standard and Poor s except HSH Nordbank AG which is not rated. We do not anticipate that any of these counterparties will fail to meet their obligations.

In addition to the derivative liability above, another component of the fair value of our interest rate derivatives is accrued interest. As of September 30, 2010, accrued interest payable included in accounts payable, accrued expenses, and other liabilities on our consolidated balance sheet was $5,555 related to interest rate derivatives designated as cash flow hedges.

Historically, the Company acquired its aircraft using short term credit facilities and equity. The short term credit facilities were refinanced by securitizations or term debt facilities secured by groups of aircraft. The Company completed two securitizations and two term financings during the period 2006 through 2008. The Company entered into interest rate derivatives to hedge interest payments on variable rate debt for acquired aircraft as well as aircraft that it expected to acquire within certain future periods. In conjunction with its financing strategy, the Company used interest rate derivatives for periods ranging from 5 to 10 years to fix the interest rates on the variable rate debt that it incurred to acquire aircraft in anticipation of the expected securitization or term debt re-financings.

At the time of each re-financing, the initial interest rate derivatives were terminated and new interest rate derivatives were executed as required by each specific debt financing. At the time of each interest rate derivative termination, certain interest rate derivatives were in a gain position and others were in a loss position. Since the hedged interest payments for the variable rate debt associated with each terminated interest rate derivative were probable of occurring, the gain or loss was deferred in accumulated other comprehensive income (loss) and is being amortized into interest expense over the relevant period for each interest rate derivative.

Prior to the securitizations and term debt financings, our interest rate derivatives typically required us to post cash collateral to the counterparty when the value of the interest rate derivative exceeded a defined threshold. When the

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interest rate derivatives were terminated and became part of a larger aircraft portfolio financing, there were no cash collateral posting requirements associated with the new interest rate derivative. As of September 30, 2010, we did not have any cash collateral pledged under our interest rate derivatives, nor do we have any existing agreements that require cash collateral postings.

Following is the effect of interest rate derivatives on the statement of financial performance for the nine months ended September 30, 2010:

	Effective Portion			Ineffective Portion	
Derivatives in ASC 815 Cash Flow Hedging Relationships	**Amount of Gain or (Loss) Recognized in OCI on Derivative** (a)	**Location of Gain or (Loss) Reclassified from Accumulated OCI into Income**	**Amount of Gain or (Loss) Reclassified from Accumulated OCI into Income** (b)	**Location of Gain or (Loss) Recognized in Income on Derivative**	**Amount of Gain or (Loss) Recognized in Income on Derivative** (c)
Interest rate derivatives	$ (109,680)	Interest expense	$ (77,786) [1]	Interest expense	$ (2,866) [1]

(a) This represents the change in fair market value of our interest rate derivatives since year end, net of taxes, offset by the amount of actual cash paid related to the net settlements of the interest rate derivatives for the nine months ended September 30, 2010.

(b) This represents the amount of actual cash paid, net of taxes, related to the net settlements of the interest rate derivatives for each month of the nine months ended September 30, 2010 plus any effective amortization of net deferred interest rate derivative losses.

(c) This represents both realized and unrealized ineffectiveness incurred during the nine months ended September 30, 2010.

(1) Excludes accelerated deferred loss of $766 which was charged to interest expense during the nine months ended September 30, 2010 primarily as a result of changes in projected future debt related to Term Financing No. 1.

Derivatives Not Designated as	Location of Gain or (Loss)	Amount of Gain or (Loss) Recognized in Income on

Hedging Instruments under ASC 815	Recognized in Income On Derivative		Derivative
Interest rate derivatives	Other income (expense)	$	(990)

Generally, our interest rate derivatives are hedging current interest payments on debt and future interest payments on long-term debt. In the past, we have entered into forward-starting interest rate derivatives to hedge the anticipated interest payment on long-term financings. These interest rate derivatives were terminated and new, specifically tailored interest rate derivatives were entered into upon closing of the relevant long-term financing. We have also early terminated interest rate derivatives in an attempt to manage our exposure to collateral calls.

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The following table summarizes the deferred (gains) and losses and related amortization into interest expense for our terminated interest rate derivative contracts for the nine months ended September 30, 2009 and 2010:

Hedged Item	Original Maximum Notional Amount	Effective Date	Maturity Date	Fixed Rate %	Termination Date	Deferred (Gain) or Loss Upon Termination	Unamortized Deferred (Gain) or Loss at September 30, 2010	Amount of Deferred (Gain) or Loss Amortized (including Accelerated Amortization) into Interest Expense for the Nine Months Ended September 30, 2009	2010	Amount of Deferred (Gain) or Loss Expected to be Amortized over the Next Twelve Months
Securitization No. 1	$ 400,000	Dec-05	Aug-10	4.61	Jun-06	$ (13,397)	$	$ (2,321)	$ (1,847)	$
Securitization No. 1	200,000	Dec-05	Dec-10	5.03	Jun-06	(2,541)	(106)	(369)	(191)	(106)
Securitization No. 2	500,000	Mar-06	Mar-11	5.07	Jun-07	(2,687)	(287)	(535)	(511)	(287)
Securitization No. 2	200,000	Jan-07	Aug-12	5.06	Jun-07	(1,850)	(609)	(277)	(264)	(337)
Securitization No. 2	410,000	Feb-07	Apr-17	5.14	Jun-07	(3,119)	(1,743)	(302)	(267)	(345)
Term Financing No. 1	150,000	Jul-07	Dec-17	5.14	Mar-08	15,281	9,951	1,554	1,450	1,813
Term Financing No. 1	440,000	Jun-07	Feb-13	4.88	Partial Mar-08 Full Jun-08	26,281	11,699	4,529	4,229	5,286
Term Financing No. 1	248,000	Aug-07	May-13	5.33	Jun-08	9,888	4,134	1,681	2,233	1,705

Term Financing No. 2	360,000	Jan-08	Feb-19	5.16	Partial Jun-08 Full Oct-08	23,077	10,603	1,991	1,390	1,492
ECA Term Financing for New A330 Aircraft	238,000	Jan-11	Apr-16	5.23	Dec-08	19,430	18,432	940	13	1,781
ECA Term Financing for New A330 Aircraft	231,000	Apr-10	Oct-15	5.17	Partial Jun-08 Full Dec-08	15,310	12,260	1,291	177	2,319
PDP Financing for New A330 Aircraft	203,000	Jun-07	Jan-12	4.89	Dec-08	2,728		1,465		
ECA Term Financing for New A330 Aircraft	238,000	Jul-11	Sep-16	5.27	Dec-08	17,254	15,969	1,285		
Total						$ 105,655	$ 80,303	$ 10,932	$ 6,412	$ 13,321

The amount of loss expected to be reclassified from accumulated other comprehensive income (OCI) into interest expense over the next 12 months consists of net interest settlements on active interest rate derivatives in the amount of $91,583 and the amortization of deferred net losses in the amount of $13,321. Over the next twelve months, we expect the amortization of deferred net losses to increase as certain gains on Securitizations No. 1 and No. 2 fully amortize in the amount of $393 and the losses on the forward starting A330 swaps in the amount of $4,100 begin to amortize as we take delivery of these aircraft. For the nine months ended September 30, 2010, the amount of loss reclassified from OCI into interest expense consisted of net interest settlements on active interest rate derivatives in the amount of $73,391, and the amortization of deferred net losses (including accelerated amortization) in the amount of $6,412 as disclosed below.

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The following table summarizes amounts charged directly to the consolidated statement of income for the three and nine months ended September 30, 2009 and 2010, respectively, related to our interest rate derivatives:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	**2010**	**2009**	**2010**
Interest Expense:				
Hedge ineffectiveness (gains) losses	$ 457	$ 764	$ (116)	$ 2,533
Amortization:				
Accelerated amortization of deferred losses	1,176	313	4,880	766
Amortization of deferred losses	1,960	2,025	6,052	5,646
Total Amortization	3,136	2,338	10,932	6,412
Total charged to interest expense	$ 3,593	$ 3,102	$ 10,816	$ 8,945
Other Income (Expense):				
Mark to market gains (losses) on undesignated interest rate derivatives	$ (608)	$ (444)	$ 556	$ (990)
Total charged to other income (expense)	$ (608)	$ (444)	$ 556	$ (990)

The weighted average interest pay rates of these derivatives at December 31, 2009 and September 30, 2010 were 4.91% and 5.00%, respectively.

Note 12. Interest, Net

The following table shows the components of interest, net:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	**2010**	**2009**	**2010**
Interest on borrowings, net settlements on interest rate derivatives, and other liabilities	$ 36,779	$ 40,144	$ 110,191	$ 111,090
Hedge ineffectiveness (gains) losses	457	764	(116)	2,533
Amortization of interest rate derivatives related to deferred losses	3,136	2,338	10,932	6,412
Amortization of deferred financing fees and notes discount	3,077	5,734	8,808	11,494
Interest Expense	43,449	48,980	129,815	131,529
Less interest income	(57)	(207)	(914)	(247)
Less capitalized interest	(360)	(1,320)	(976)	(2,704)
Interest, net	$ 43,032	$ 47,453	$ 127,925	$ 128,578

Note 13. Shareholders Equity and Share Based Payment

On July 13, 2010, Aircastle Limited entered into an employment agreement with Ron Wainshal, Chief Executive Officer of the Company, which amends and restates Mr. Wainshal s existing employment letter with the Company, dated May 2, 2005, in its entirety. Under the employment agreement, the Company has agreed to amend the restricted share award agreements entered into with Mr. Wainshal in each of December 2007 and January 2009, to provide for an accelerated vesting schedule for certain unvested restricted shares granted to Mr. Wainshal thereunder. The effect of such amendments is to increase the number of common shares of the Company vesting in 2010 and 2011 by approximately 40,000 common shares and consequently reduce the number of common shares vesting in 2012-14 by the same number. For the three and nine months ended September 30, 2010, we recorded an additional $297 of share based payment expense to account for the accelerated vesting.

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Note 14. Subsequent Events

In October 2010, the Company received insurance proceeds in the amount of $29,250 related to an aircraft that suffered a total loss as a consequence of an incident which occurred in the third quarter of 2010. Significant damage to the aircraft occurred when the aircraft exited the runway following landing. No serious injuries resulted and there were no fatalities. In October, the insurers declared the aircraft a total loss.

In November 2010, our counterparty obtained governmental approvals required in connection wi