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Want to Buy a Corporate Jet? Don't Get Grounded Before You leave the Runway

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January 6, 2011

The Dream

Picture this: you are the CEO of a major technology company based in the Research Triangle Park with offices and manufacturing facilities in New York, Silicon Valley, Arizona, and Florida. As CEO, it is imperative that you and your management team travel to the company's various offices and manufacturing facilities to meet with vendors and ensure that company operations are running as smoothly as possible. You also likely need to travel to other cities across the United States and the world to meet with potential acquisition targets and negotiate joint venture projects.

While you certainly could utilize commercial air carriers to travel to these destinations, owning a corporate jet would allow you to get to your destinations much quicker, avoid the hassles associated with busy airports, enable you and your management team to work as a group while you travel to your destination, and make corporate travel much more comfortable and enjoyable. So, being the visionary leader that you are, you have the company purchase a corporate jet, you have your corporate lawyer form a new LLC to own and operate the new corporate jet to insulate your technology company from liability, and you use the jet to efficiently travel across the United States and the globe.

The Dream Becomes a Nightmare

Time (and your travels) passes quickly and one day you land in Florida on the corporate jet's 100th flight. With clipboard in hand, an employee of the Federal Aviation Administration ("FAA") meets you on the tarmac as you are deplaning and informs you that your LLC is subject to the same rules and regulations as Delta Air Lines, U.S. Airways, and the other large commercial air carriers, and that your LLC has violated numerous maintenance and operational rules. Next, the FAA employee hands you a document stating that your company is being fined $1,100,000 for these violations.

The corporate jet that you thought was going to be a mechanism to implement new efficiencies has now cost your company an additional $1,100,000 because you were not aware of the FAA's special rules and regulations regarding the ownership and operation of corporate jets.

If you are contemplating purchasing a corporate jet, it goes without saying that you do not want to find yourself in the position of our hypothetical CEO. Fortunately for you, some advance planning can provide you with certainty that you will not find yourself in this position.

The Primary Issue – Commercial Aviation vs. General Aviation

The FAA has issued voluminous rules and regulations governing the ownership and operation of aircraft in the

United States. Two particular sets of rules must be analyzed carefully when purchasing and operating a corporate jet. Part 91 of the FAA regulations ("General Aviation Rules") applies to personal and incidental business use of aircraft and provides much less restrictive rules than those found in Part 135 of the FAA regulations ("Commercial Aviation Rules"), which apply to aircraft used "for hire." The FAA uses a very broad definition of the term "for hire" and has ruled that a business entity (i.e., your technology company) that owns and operates an aircraft does so "for hire" if the owners of the business receive any benefit whatsoever related to the use of the aircraft.

It is all but impossible for a technology company to comply with the Commercial Aviation Rules, and the penalties for any failure to comply are very severe. Consequently, it is very important to implement the correct ownership and operational structure to ensure that your corporate jet is not deemed to be used "for hire" and, therefore, subject to the strict Commercial Aviation Rules.

The four main reasons to structure the ownership and operation of your corporate jet so that the General Aviation Rules, and not the Commercial Aviation Rules, apply are to avoid:

- The strict maintenance and operational requirements of the Commercial Aviation Rules;
- FAA civil penalties of $11,000 per flight (which can be assessed retroactively) for failing to comply with the Commercial Aviation Rules;
- Voiding the liability and property insurance policies on your jet; and,
- Higher fuel excise taxes.

Option 1 – Buy a Jet in a New Entity and "Dry Lease" it to Your Company

You can form a new LLC or corporation ("NewCo") to purchase and own your corporate jet. However, to avoid the Commercial Aviation Rules, NewCo should not operate the jet. Instead, NewCo should "dry lease" the jet to your technology company ("OldCo").

A "dry lease" is a lease of an aircraft without any captain or crew being provided by the lessor (in your case, NewCo). The lessee (in your case, OldCo) must provide the captain and crew. Even though this structure will allow you to take advantage of the more favorable General Aviation Rules, there are very strict rules on the maximum amount of rent that can be charged under a dry lease. Simply put, the maximum amount of rent that NewCo can charge OldCo for use of the jet is the sum of all of the actual flight-related costs (e.g., gas, hangar costs, and flight-specific insurance) plus an additional amount equal to no more than 100% of such actual flight-related costs.

In addition, if you implement a dry lease structure, you should consult an aviation insurance agent. Under the FAA rules, the individual or entity that has operational control of the aircraft at the time an accident occurs (in your case, OldCo and not NewCo) is the party that is liable if an injured party can prove that the operator or its agents acted negligently. Consequently, OldCo will need a substantial amount of liability and property insurance to cover any claims that may result from its negligent operation of the corporate jet.

There are additional rules, such as rules regarding OldCo's ability to charge any guest for use of the corporate jet, that are beyond the limited scope of this article.

Option 2 – Take Advantage of Fractional Ownership

The FAA rules allow multiple individuals or entities to jointly own a corporate jet, with each participant owning a portion of the jet. This structure is referred to as "fractional ownership." Fractional ownership is roughly analogous to owning a timeshare, in that you own part of the asset but must share the use of the asset. From a business perspective, if you do not need access to the corporate jet 24/7, then it may make sense to look into fractional ownership because it is much cheaper to participate in a fractional ownership program than it is to own a jet outright. However, it is not advisable to partner with other individuals or entities to create your own fractional ownership program unless you consult with an experienced aviation lawyer in advance and ensure that your fractional ownership program complies with the complex FAA rules applicable to such programs.

There are numerous commercial services, such as NetJets, which use the fractional ownership concept and the charter service concept (discussed below) and allow businesses to purchase flight hours. These companies own a large number of corporate jets, so you should have access to a jet any time you need it.

Option 3 – Buy a Jet and Enroll it in a Charter Service

Another option is to purchase the corporate jet outright and then enroll it in a charter service. Under this option, you still form NewCo to own the jet and dry lease it to your technology company. However, in addition, NewCo also will dry lease the jet to a commercial charter service that will use it to transport third parties when you are not using it. This is another option that defrays the ownership costs associated with owning a corporate jet. However, you will not have 24/7 access to the jet if you need it. There are also extensive FAA regulations that govern charter services that must be analyzed before you enroll your corporate jet in a charter service.

There are several additional ownership and operational structures that are beyond the limited scope of this article that can be implemented to resolve any unusual issues that you may encounter.

Summary – The Friendly Skies are not Always so Friendly

There are numerous pitfalls that must be avoided if you purchase a corporate jet or participate in a fractional ownership or charter service program. Failure to comply with the extensive FAA rules can result in severe fines and other penalties. However, a knowledgeable and experienced aviation lawyer can help you traverse the minefield of FAA regulations to implement an ownership and operational structure that will allow you to take advantage of the efficiencies a corporate jet can provide.

For further information regarding the issues described above, please contact Lee C. Hodge .

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