



ASSESSING AIRCRAFT OWNERSHIP OPTIONS AVAILABLE TODAY

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Acquiring and owning a private jet or turboprop aircraft is an exciting experience. Aircraft owners enjoy luxury and convenience unknown to most travelers, and experience a pride of ownership available to only a handful of Americans. The decision to purchase an aircraft is, however, one that requires careful consideration and review with tax and legal counsel well versed in the area of corporate aircraft acquisitions and operations.

The benefits of acquiring and owning an aircraft vary depending on many factors, including how the aircraft will be used, how frequently the aircraft will be flown, and the owner's specific tax situation. Of course, there are several alternatives to sole ownership of an aircraft. For some, it makes more sense to share ownership with another person or to buy only an interest in an aircraft operated by a fractional ownership program. For others, it makes more sense to lease an aircraft, while for still others; it makes more sense merely to charter an aircraft on an as needed basis. This article is designed to educate the reader about the aircraft ownership options available today.

1. Deciding to Buy, Lease, or Charter

For a person who makes frequent short-duration trips, or multiple stops during trips, buying or leasing an aircraft may make sense because such a person would benefit both from time-savings over commercial flights, and complete flexibility related to length of stay. For a person who travels infrequently or tends to have long layovers at a single destination, chartering or fractional ownership (discussed below) may be more appropriate. Chartering or fractional ownership provides the convenience of a private flight without the direct expense of employing

a flight crew, and without the capital costs of owning an asset that will be idle more often than not. For business owners who require use of a private aircraft for both business and personal travel, another option is to have the company buy a plane, then treat personal use as a fringe benefit. In this case, the business owner benefits from the conveniences of ownership, while the company takes advantage of the tax deductions for the depreciation and operating expenses associated with a business asset.

The nature of the anticipated aircraft usage is a critical factor to study when considering whether to purchase an aircraft. In other words, does the frequency and duration of travel justify the acquisition? In answering this question, consider the following:

- What are your most frequent points of departure and destination?
- Are commercial or private charter aircraft conveniently available?
- What distances do you travel?
- How often do you travel?
- How long is your average stay?
- How many people will travel with you on the flight?

2. Owning vs. Leasing an Aircraft

Owning. A primary factor in deciding whether to purchase an aircraft is the level of anticipated aircraft usage, i.e., will the aircraft be used enough to justify the acquisition and ownership costs? Ownership may make financial sense when the aircraft is flown at least 300 hours each year. At about 300

hours, the amortized cost of full ownership of the aircraft may become less than the amortized cost of chartering or fractional ownership.

One alternative for owners who do not expect to use an aircraft at least 300 hours a year is joint ownership of a single aircraft by two or more purchasers. Under a joint ownership arrangement, the full cost of acquiring, operating, and maintaining the aircraft is shared among the joint owners. However, joint owners also share use of the aircraft so they must carefully select partners whose anticipated use of the aircraft – in terms of flight hours, scheduling, and geographic location – is compatible with their own.

To reduce the cost of aircraft ownership, owners can hire a company to charter the aircraft to third parties when the aircraft is not otherwise in use. Rarely, if ever, will revenue from third party charter activity cover the full cost of aircraft ownership and operations, so an owner should consider third party charter activity solely as a means to help offset the fixed costs of ownership, and, even then, third party charter activity may not significantly offset the fixed costs if the owner places too many scheduling restrictions on the charter company.

Another advantage of ownership, in the context of business use aircraft, is eligibility for depreciation deductions, although owners must meet very strict IRS regulations on passive activity loss rules.

There are disadvantages to owning an aircraft too: an aircraft owner must commit time and energy to managing the aircraft, including hiring pilots, renting hangar space, scheduling maintenance, and obtaining insurance. Alternatively, owners can hire a management company to perform all necessary management services for a fee. The majority of aircraft management companies in the United States are owned and operated as small businesses by pilots. Aircraft management companies exist at large and small airports all over America and the world, and can serve as a means for an aircraft owner with limited aviation experience to “buy” the necessary experience.

Leasing. Leasing offers the same availability benefit as full ownership without the initial financial commitment required to purchase an aircraft. The

most common lease is the operating lease, in which the lessor retains title to the aircraft, but gives possession of the aircraft to the lessee. Another type of lease is the financing lease. A financing lease provides the lessee with an option to purchase the aircraft at the end of the lease term, and resembles a mortgage or an installment sale in that the purchase price of the aircraft at the end of the lease, when added to the total amount of rent paid during the lease period, will be roughly the same as if the aircraft had been originally purchased on credit. A financing lease is most desirable when the cost of borrowing money is low compared to the return on capital available in other investment media.

When negotiating a lease, a critical issue involves the tax deduction for depreciation of the aircraft. The IRS permits the depreciation of aircraft over a period of six tax years, yielding potentially lucrative tax benefits. However, many lessees cannot benefit from aircraft depreciation deductions because they may be used only to offset the lessee’s income from passive activities or because the lessee does not otherwise generate significant taxable income. Fortunately, a lease may be structured to make these deductions available to the lessor rather than the lessee. The lessee may, therefore, be able to negotiate a lower least rate for the aircraft in exchange for allowing the lessor to enjoy the benefit of the depreciation deductions.

Leasing can be as costly as full ownership, both in terms of operating expenses and commitments of time and energy to manage the aircraft, because a lessee generally must arrange for, and pay for, all fuel, maintenance, hangar, pilot employment, and insurance to the same extent as an owner. Of course, lessees may avail themselves of the services of an aircraft management company to the same extent as an owner. The major risks of owning the aircraft – such as legal liability and risk of loss from damage or theft – are also just as applicable to a lessee.

3. Chartering vs. Fractional Ownership of Aircraft

Chartering. Chartering is often the easiest and least expensive way to have an aircraft at your disposal, and does not entail the management burdens of ownership or leasing. However, there are a few

drawbacks to chartering, especially for flyers that frequently use private aircraft. Charter services may not be able to guarantee that an aircraft will be available when needed, and if an aircraft is available, it may not be the type of aircraft best suited to the needs or desires of the charter client. Finally, chartering does not offer the “pride of ownership” to the charter client that is a standard feature of ownership, as any owner will attest.

Fractional Ownership. The latest “style” of aircraft ownership is fractional ownership. In a fractional ownership arrangement, owners purchase a fractional interest in a particular aircraft operated by a fractional aircraft program. A typical fractional aircraft program, or fractional program, will purchase a fleet of aircraft comprised of one or more specific aircraft types, and then will sell off each aircraft in pieces or “fractions.” A fractional interest can be as small as a one-sixteenth ownership of the aircraft. Each such sale is conditioned upon the new owner contracting with the fractional program to manage the aircraft. Each such sale is conditioned upon the new owner contracting with the fractional program to manage the aircraft. The fractional program then operates all the aircraft in the program as a single fleet. In the jet marketplace, there are three new aircraft fractional ownership programs: Executive Jet Aviation offering its owners Cessna, Raytheon, Dassault, Gulfstream and Boeing (737) aircraft; Business Jet Solutions offering Learjet and Canadair Jets; and Raytheon Travel Air offering the Raytheon product line. There are also numerous used aircraft fractional programs now developing.

The key element in a fractional ownership program is an agreement signed by all of the fractional owners, which allows each owner to use any of the aircraft in the program. Although the fractional owner legally owns a portion of one particular aircraft, what the owner actually receives as a member of the program is a specified number of hours of flight time each year on a specific type of aircraft. A fractional owner of one type of aircraft may also have access to other types of aircraft operated by the program. The program agreement permits the manager of the fractional ownership program to base individual aircraft at various airports all over the United States and in selected foreign countries, and to provide any program aircraft in the fleet to any fractional owner

on an as needed basis, thus permitting maximum scheduling flexibility of aircraft all over the world. In practice, a fractional owner simply notifies the program manager when and where an aircraft is needed, and the program manager provides an aircraft. The aircraft provided may or may not be the actual aircraft in which the owner owns a fractional interest.

The benefits of fractional ownership are many:

- Aircraft are available from virtually any location in the United States with minimal notice and depending on the program, all over the world.
- Aircraft management is provided by the program manager.
- A buyer can purchase the fraction of an aircraft that best reflects current or projected annual travel needs, and later increase or decrease the ownership percentage to reflect changing travel needs.
- A fractional owner is entitled to a corresponding depreciation deduction when permitted by IRS regulations.
- Depending on the size of the fractional interest purchased, a fractional owner may use two or more aircraft simultaneously.

A major disadvantage of fractional ownership is that the total cost of aircraft ownership and operations, on a per-hour basis, may exceed the costs of other forms of ownership. The fractional program charges a fixed monthly management fee, plus an hourly rate for all flights. Further, the hourly rate and possibly the management fee are subject to an 8% federal transportation excise tax (commencing October 1, 1998), not so in connection with the ownership or leasing alternatives. Finally, state sales tax may be due at the time of purchase of a fractional ownership interest, whereas the ownership and leasing options may often be structured to avoid state sales tax on the purchase or lease. There is also the very personal issue of developing a sense of ownership, which must be assessed.

4. Find the Right Fit

There are several options available today for acquir-

ing a private aircraft. Chartering is the simplest and perhaps least costly way to gain access to a private aircraft on an infrequent basis. Full ownership or leasing may be most cost effective when the owner will use the aircraft at least 300 hours per year. Fractional ownership offers many of the advantages of both chartering and buying: owners of a fraction-

al interest always have an aircraft at their disposal, but avoid the many responsibilities of ownership. Choosing the correct mode of acquiring a private aircraft requires a thorough understanding of your aviation needs, but whatever your aviation needs are, there is a method of acquiring a private aircraft suited to your needs.



Keith G. Swirsky is a partner with Galland, Kharasch, Greenberg, Fellman & Swirsky, P.C., one of the nation's leading aviation law firms. The law firm, and its affiliated consulting firm, employ over thirty aviation lawyers and consultants, and provide a diverse range of services in all sectors of worldwide aviation, representing the needs of businesses, airlines, airports and municipalities. As part of our global transportation practice, the Business Aviation Group provides legal and consulting services to the business aviation industry.

Keith G. Swirsky represents the aviation industry from many perspectives -- the aircraft owner and corporate flight department, the fractional program manager, the aircraft charter and management company, the equipment manufacturer and distributor, the lender, the airline and the airport. Mr. Swirsky and the members of the Business Aviation Group provide legal and consulting services to the business aviation industry.



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