



GKG Law



Unusual Issues In Used Aircraft Import Transactions

-By Keith G. Swirsky-

Our article published in October's issue of World Aircraft Sales Magazine addressed the unusual issues that arise when owners of U.S. registered aircraft sell used aircraft abroad. This month we address the unusual issues that arise when U.S. buyers purchase non-U.S. registered used aircraft.

Historically, the world's corporate jet fleet has consisted primarily of aircraft registered in the United States. Consequently, U.S. companies that purchased corporate jets usually purchased them from other U.S. companies, and it was unusual for a U.S. company to purchase an aircraft that was not already registered in the United States. However, as Bob Dylan once said, "the times, they are a changin'."

Recent years have seen unprecedented numbers of new and used corporate jet aircraft being sold to buyers outside the United States. As more used aircraft are exported from the U.S. to other parts of the world, and as manufacturers deliver increasing numbers of new aircraft to customers outside the U.S., the percentage of aircraft in the worldwide corporate jet fleet that are non-U.S. registered will continue to increase. And, as this percentage of non-U.S. registered aircraft increases, the percentage of non-U.S. registered aircraft that are for sale in the used aircraft market at any point in time will also continue to increase. It is therefore becoming ever more necessary for U.S. buyers (and their brokers) entering the used aircraft market to expand the scope of their search for suitable used aircraft to include non-U.S. registered aircraft. GKG Law has already represented many U.S. buyers in the acquisition and import of non-U.S. registered aircraft, and is well versed in identifying and resolving unusual issues that arise in the course of conducting such a transaction.

Perhaps the most significant concern when representing U.S. buyers of foreign registered aircraft is to be certain that the aircraft will qualify for a U.S. Certificate of Airworthiness (C-of-A) before the deposit becomes nonrefundable. There is a "chicken-or-the-egg" problem involved, because the FAA will not issue a U.S. C-of-A until after the aircraft is registered in the U.S. (which of course typically occurs after the closing), but the U.S. buyer would not be happy to close, take title and register the aircraft in the U.S., only to then discover that some technical issue will prevent obtaining a U.S. C-of-A immediately (and at some additional expense).



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In one transaction we conducted, the U.S. buyer required the foreign seller to obtain a U.S. C-of-A for the aircraft prior to closing. In that case, the foreign seller transferred title to his U.S. broker, who then registered the aircraft in the U.S. and obtained a U.S. C-of-A. At closing, the broker conveyed title to the U.S. buyer.

The more common scenario is to have a Designated Airworthiness Representative (DAR) inspect the aircraft and records prior to the closing. The DAR inspection would typically occur concurrently with the prebuy inspection, and the purchase agreement would have as a condition precedent to the obligation of the buyer to close, that the DAR issue a letter saying that he has inspected the aircraft, is satisfied that the aircraft meets the requirements for a U.S. C-of-A, and that he is prepared to issue the U.S. C-of-A as soon as the aircraft is registered in the U.S. If the pre-purchase inspection occurs outside of the U.S., either the buyer or the seller will incur the travel costs and daily per diem of the DAR to conduct this inspection. Who pays such costs is, of course, negotiable, although most often they are paid by the buyer.

Another important issue that needs to be addressed is the timing of deregistration of the aircraft from the applicable foreign registry. The deregistration process sometimes takes a day or two, and could take longer in some countries. The FAA will not register the aircraft in the U.S. until they receive word directly from the applicable foreign registry that the aircraft has been deregistered. Consequently, the U.S. buyer usually wants the aircraft to be deregistered from the foreign registry and the notice of deregistration to be delivered to the FAA prior to the closing, so that at the time of closing the aircraft can be immediately registered in the U.S.. However, foreign sellers frequently refuse to deregister their aircraft until the purchase price has been paid in full at closing. This is most likely to occur if the seller is concerned that the buyer may default or back out of the deal after the aircraft has been deregistered. If this happens, the seller could be unable to move the aircraft until it is re-registered in their home country, which can take several days, or possibly longer, depending on the country. In such cases, an acceptable compromise could be to have the entire purchase price placed in escrow prior to deregistration, together with an irrevocable escrow instruction letter, jointly executed by buyer and seller, requiring the escrow agent to deliver the purchase price to the seller as soon as the foreign registry delivers a notice of deregistration to the FAA.

Another question that can arise is whether the aircraft and records have been maintained in such a manner as to permit the aircraft on a Part 135 certificate. In the event the U.S. buyer desires the aircraft to be chartered post closing, the buyer should have the Part 135 certificate holder's representative involved in the prebuy inspection to determine that there are no equipment issues or gaps or questionable entries in the aircraft's records that would prevent the aircraft from being placed on the certificate holder's Part 135 certificate.

Several other issues may arise in the course of negotiating the purchase agreement. For example, a significant issue may relate to foreign sellers' customary requirement that buyers insure the seller for some period after closing. In other words, the seller requires the buyer to place the seller on the buyer's insurance policy, as an additional insured, for two or three years post closing, to cover the potential that the buyer's operations post-closing could lead to litigation which names the seller as a defendant. In addition, the amount of coverage may be relevant as well. It is our experience that foreign sellers often want more coverage than U.S. buyers customarily place on their aircraft.



Choice of law may also become an issue, relating to which country's laws govern the purchase agreement, and which courts will have jurisdiction in the event of a dispute. Naturally, each party will want the laws of their own country to apply and each party will want conveniently located courts to have jurisdiction in the event of a dispute. There is no easy resolution to this issue.

Lastly, we have seen currency fluctuation issues affect a transaction. In particular, if the transaction is denominated in U.S. dollars, and U.S. currency weakens relative to the foreign currency, the foreign seller will be yielding a lower purchase price for the aircraft. This provides a significant incentive for the seller to default and refuse to deliver title to the aircraft. As it is most common that a seller's default will only cause the seller to be liable to reimburse the buyer for its out-of-pocket expenses, the seller incurs very little cost in defaulting on a contract. However, if the transaction is denominated in U.S. dollars, and the U.S. currency strengthens against the foreign currency, there will be no added cost to the buyer. Nevertheless, a sophisticated buyer will realize that the seller is yielding a higher purchase price than anticipated, and might desire to "negotiate" the deal further prior to closing. Other variations on this theme are clearly possible.

These are some of the issues that may arise in a used aircraft import transaction. Certainly, there may also be other issues not addressed in this article, and as the used aircraft import (and export) market continues to mature, custom and usage between and among the U.S. and other countries will cause purchase negotiations to evolve into a more homogenous product. Until such time, U.S. buyers will experience these and other difficulties in finalizing a purchase agreement negotiation and coordinating the logistics of inspection and closing. The lawyers at GKG Law are experienced in advising on these transactions and anticipating the unusual business issues. Thus, we can increase the likelihood of a successful closing.

Keith G. Swirsky is a tax specialist concentrating in the areas of corporate aircraft transactions and aviation taxation. The firm's business aircraft practice group, chaired by Mr. Swirsky, provides full-service tax and regulatory planning and counseling services to corporate aircraft owners, operators and managers. The group's services include Section 1031 tax-free exchanges, federal tax and regulatory planning, state sales and use tax planning, and negotiation and preparation of all manner of transactional documents commonly used in the business aviation industry, including aircraft purchase agreements, leases, joint-ownership and joint-use agreements, management and charter agreements, and fractional program documents. Mr. Swirsky may be reached at the firm's Washington, DC office, 1054 31st Street, NW, Suite 200, Washington, DC 20007, Telephone: (202)342-5251, Facsimile: (202)965-5725, E-mail: kswirsky@gkglaw.com.

