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Easier Said Than Done: *Liability protection planning for business aircraft.*

Corporations that form separate entities to operate their business aircraft must beware of limitations imposed by the Federal Aviation Administration, cautions attorney Chris Younger.

An owner of a large cabin business aircraft recently contacted me to request some advice concerning sales tax. The owner had formed a special purpose entity (SPE) to acquire his aircraft, and that SPE had leased the aircraft to another SPE that operated the aircraft. I asked the owner if, aside from the sales tax issues he mentioned he had considered any other legal and tax ramifications of his aircraft ownership and operating structure. He stated that the structure was designed to

provide him with maximum liability protection regarding his ownership and operation of the aircraft and that he always used separate entities to own and operate his business and real estate ventures.

Unfortunately, as described in the example above, many business aircraft owners and their advisors do not recognize that typical practices in the real estate or business world are not standard operating procedure in the context of business aircraft operations. The owner who contacted me clearly had not engaged counsel familiar with the "flight department company" rule.

The Federal Aviation Administration (FAA) requires a company that provides transportation by air for compensation (which is defined very broadly to include any kind of economic benefit) or hire to have an FAA air carrier operating certificate and to operate its aircraft in accordance with more stringent rules applicable to air carriers. However, the FAA has adopted certain limited exceptions to this general rule. These exceptions are contained in Section 91.501 of the FAR and permit the provision of air transportation for compensation to be operated under FAR Part 91 without an FAA air carrier or operating certificate in limited and narrowly defined circumstances.

SPECIFIC REQUIREMENTS

FAA policy requires that any operation of aircraft under the limited exceptions of Section 91.501 of the FAR must be "incidental to and within the scope" of some business other than the provision of air transportation (i.e., an operating business). An SPE that operates an aircraft under FAR Part 91 conducts no business other than the provision of air transportation services, which by its very nature is not allowed by the FAA.

There is no legally permissible way to fund the operations of an aircraft by an SPE if it is operated under FAR Part 91 because the term "compensation" >



What the Boardroom needs to know about Business Aviation



can be defined broadly to include amounts contributed to the SPE as compensation received for the provision of air transportation services.

This requirement presents a paradox. On the one hand, most business aircraft owners recognize the inherent liability risks associated with owning and operating a business aircraft. They want to isolate that liability risk and shield their other assets from it. On the other hand, the FAA requires that the business aircraft operator have some "skin in the game" if it is going to operate an aircraft pursuant to FAR Part 91 rules. The aircraft must be operated as an industrial aid in support of the owner's primary business, which cannot be air transportation.

INSURANCE, AND LOTS OF IT!

First and foremost, regardless of the characteristics of an entity that is legally permitted to operate a business aircraft under FAR Part 91, it is imperative that a Board recognize the benefit of comprehensive and adequate liability insurance for the company aircraft. Typical liability limits in the business aircraft arena exceed US\$100,000,000 of coverage and, recently, US\$500,000,000 or even \$1,000,000,000 of coverage have become available and more common. This is the primary mechanism for mitigating the risks associated with business aircraft operations.

It is imperative that the Board closely review and scrutinize their company's organizational chart to ensure that the aircraft will be operated by an entity that is eligible to do so, but has a smaller footprint in terms of balance sheet exposure. If such an entity is available, then it would usually be preferable to make that entity the aircraft operator.

THE CHARTER OPTION

A third alternative is to have the aircraft operated solely by an FAR Part 135 charter operator. This alternative, however, is often unpalatable because of restrictions specific to FAR Part 135 regarding flight crew duty time, airports and weather. Also, there are often negative income, excise and sales tax consequences emanating from such a structure. If such issues can be satisfactorily resolved, this solution can be an excellent means for achieving liability protection.

The name of the game is to recognize that there is no "one size fits all" approach to planning for business aircraft ownership and operations. Instead, each situation must be analyzed in its own context to design the best structure from the standpoint of liability protection while ensuring that the proposed operation also complies with FAA and other legal requirements and meets the company's business and tax objectives.

If these issues are not considered, the Board runs the risk of creating additional liability rather than successfully avoiding it!

Note: This article should not be construed as legal advice or legal opinion on any specific facts or circumstances. The reader is urged to consult legal counsel or other advisors concerning his/her own situation and specific legal questions.

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