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What Does Our Firm Have in Common with Star Trek®?

We Don't Believe in the No-Win Scenario

If you've seen the new Star Trek movie or are a fan of earlier movies, you may recall that every officer is tested in what is called the "Kobayashi Maru" scenario. This involves the trainee being placed in an untenable position – he or she needs to choose to try to rescue another ship while facing certain death or save his own ship and let hundreds of passengers on the other ship perish. Kirk finds a solution (he cheats the test) but the point is that he doesn't believe in the "no-win" scenario.

While there may not be a perfect solution for every issue encountered in an aircraft transaction, something can typically be done to accommodate fundamental issues that arise, and having a positive mental attitude while dealing with a difficult seller or buyer (or their representatives) is an important part of getting the deal done. Transactions are fluid, can change on a daily basis, and involve give and take. There are times when rigidity is important, but at other times rigidity can result in a busted deal with all parties circling their wagons. Some empathy and a little creativity can make all the difference.

"Bringing Order to Chaos"

I was watching Star Trek First Contact with the kids the other night (actually, they were watching it with me). There's one scene in which the Borg leader is asked whether she is the "brain" of the Borg. She responds "No, I bring order to chaos." What a great phrase to describe the work of an aviation transaction lawyer! We

help clients navigate the issues involved in an aircraft purchase. Some think that the process is as simple as buying or leasing a car. Others believe that they know it all. And yet others are overwhelmed by all of the issues that need to be addressed to have a successful transaction: purchase agreement, deposits, finance, pre-purchase inspection scope, sales tax planning, federal tax planning, FAA compliance, DOT compliance, FAA registration issues, insurance, risk management, management, Part 135, among others.

Many times a client tries to learn about the issues by anecdotal research, information gathered from friends on the golf course, or from web sites that only touch the tip of the iceberg. Learning the ins and outs of all the issues involved in closing an aircraft transaction takes years. The absolute worse time to learn is in the middle of a transaction, although we can guide a client through the maze in an orderly and efficient manner.

In an aircraft transaction, chaos is sometimes intentionally created by people on the other side of the transaction pushing an agenda. Chaos may be created by a client who would rather run the transaction themselves requiring us to "claw back" after a deal has begun. Chaos is also created by the myriad of issues required to be addressed to bring a transaction to a smooth and successful consummation.

So, perhaps the best phrase to describe our job is that we "bring order to chaos." We hope Paramount doesn't mind.

Seller Behavior in this Market

Over the last couple of months we've seen some interesting seller behavior and it raises an interesting question: why are some sellers making it more difficult to negotiate the purchase of their aircraft in this buyer's market? One example was a seller who insisted that the buyer arrange for the shipping to the inspection facility of aircraft parts that the seller had removed from the aircraft during some refurbishment work. Another seller of a large cabin jet received a draft of a purchase agreement the day after the offer to purchase was signed and didn't respond to it until after the date that the offer to purchase terminated. And yet another resisted bringing the aircraft to a bonafide purchaser for a viewing of the aircraft. Are you kidding?

Here we have a market in which inventory of aircraft for sale far exceeds demand, and yet some sellers are making it difficult – and not easy – to purchase their aircraft. What is going on here? One theory is that sellers are behaving like home sellers these days: “If you're going to get my jet for that price, I'm going to make you miserable while you do it.” The purchase of an aircraft is sometimes an emotional purchase, but interjecting emotions into a sale is a recipe for never selling an aircraft. If you're getting the price that you decided that you wanted after a review of the market, you won't gain anything by making the process more difficult than it needs to be. In fact, you're more likely to have a buyer that is more willing to walk away and buy one of the other two dozen similar aircraft being offered for sale.

The Dilemma of Single Purpose Entities

Because of the flexibility given to operators under Part 91 of the Federal Aviation Regulations (“FARs”), most corporate “flight departments” choose this route as opposed to the more restrictive and certainly more costly air carrier certificate “charter” operations under Part 135. A Part 91 operator is generally not permitted to receive compensation in exchange for the provision of transportation unless it falls under the list of exceptions identified in Part 91.501. This regulation applies to large civil aircraft (i.e. a maximum certificated takeoff weight over 12,500 pounds) and turbojet-powered aircraft. Under Part 91.501, an eligible Part 91 operator may receive certain limited reimbursements as long as they are pursuant to an appropriate time-sharing agreement or in the context of an affiliated group chargeback.

Use of Part 91.501 presumes that the operator is eligible to operate the aircraft under Part 91. The provision of an aircraft and crew together for compensation otherwise requires the operator to obtain a 135 charter certificate and the operation of the aircraft is then subject to a variety of restrictive rules under Part 135 of the FARs.

The FAA's primary concern is safety, and it believes that when there is compensation, including mere reimbursement of expenses, operators will focus on compensation at the expense of proper safety precautions.

The threshold question for determining if an aircraft operator is eligible to operate under Part 91 is whether the operation of the aircraft is incidental to the primary business of the operator. An entity that is formed solely to operate an aircraft (i.e., provide aircraft and crew) to carry persons or property, also known as a “flight department company,” would not meet the test for operating an aircraft “incidental” to a primary business because, by definition, the single purpose entity, often a single member LLC, has no other business (other than transportation). At least four FAA interpretations confirm this interpretation. Practically, when an aircraft is operated by a single purpose entity that owns or leases the aircraft and provides the crew (directly or indirectly), the FAA views such an operation as operating for “compensation,” regardless of whether the entity is carrying its owners or any other party and, accordingly, requires the operator to hold a 135 charter certificate. The FAA and Department of Transportation construe “compensation” broadly. For example, because the entity engages in no other business, capital contributions from the operating entity's owner to cover the cost of the operation of the aircraft could be deemed payment in exchange for the provision of transportation to the owner or to any other party. Therefore, under current FAA published interpretations, single purpose entities are not eligible to operate aircraft under Part 91.

We are experienced with helping clients navigate the often counter-intuitive rules of the FAA and other regulatory authorities with respect to the operation of their aircraft.

About Stewart H. Lapayowker, P.A.

Based in Fort Lauderdale, Fla., the law firm of Stewart H. Lapayowker, P.A. focuses its practice on private and corporate aviation transactions worldwide, including throughout the United States, South America, the European Union, Asia and the Middle East. The firm regularly assists clients with a variety of issues related to aviation, including the sale, purchase, regulatory analyses, financing and management of corporate aircraft.