

## **BUYING A BUSINESS JET ON THE U.S. MARKET (Step 1)** **Some preliminary thoughts for the Chinese business leader**

By Jim Cooling and Kathleen Breckenridge

The China Daily Asia Weekly for January 21–27, 2011, contained a story by Steve Varsano that there are approximately 19,500 business jets in the world and that approximately 11,000 of them are in the U.S. With the economic downturn, now is an excellent time to buy a business jet from the U.S. market.

There are 93 business jets on the Chinese Mainland and 51 in Hong Kong - and the demand for business jets in China is growing. Steve Varsano asks the question "Will there be 5,000 business jets and turboprops sold in China in the next ten years?"

Whatever the answer, the fact is that demand is growing because more and more Chinese business leaders have recognized that the business jet is a valuable business tool, and a time machine that allows them to pursue aggressively their business goals and arrive anywhere in the world ahead of their competition.

For many Chinese visionaries the dream of owning a business jet and looking down from 45,000 feet at the factories and agricultural land of China is something that they may never have believed possible in their lifetime.

For those entrepreneurs and business leaders who have achieved the level of success that allows them to pursue this dream, the fact is that over one-half of the world aviation market for business jets is in the U.S. - and with the U.S. economic downturn, there has never been a better time to purchase a business jet from the U.S. market.

The purchase of an aircraft in the U.S., while complex, proceeds through a number of predictable steps. In the following article, we have outlined for you important considerations for before you initiate the negotiation process.

### **Preliminary Considerations**

**Operational:** The purchaser's answers to the following questions will influence the type of aircraft to be chosen:

- How will the aircraft be used?
- Will it operate predominantly in international flights, or flights within a single country?
- Will the flights be long-distance, (for example, trans-oceanic) or will they tend to be medium- or short-range distances?
- What number of passengers will typically be on board?
- What budget constraints apply to the expected operating costs?
- Will your aircraft be new or pre-owned?

Whether the aircraft will fly a significant number of international flights may also affect the decision about the country of registration for the aircraft, which in turn affects the most desirable brand or model of aircraft.

Other operational considerations include the location and availability of manufacturer service centers and other maintenance providers. The location of pilot training facilities should also be considered when choosing the aircraft make and model, as well as the country of registration.

**Regulatory:** A purchaser's freedom of usage of its business aircraft may be limited by regulatory issues. Within the U.S. there are few restrictions as to where an aircraft may operate, whether the aircraft is registered in the U.S. or overseas.

More stringent restrictions are in place in other countries. For example, in China the regulatory environment may make Chinese registration advantageous for an aircraft to facilitate operations within the country.

Equally important, before a particular make and model of aircraft can be operated, the purchaser may have to obtain governmental approval, known as type certification, by the local country's regulating authority. If the purchaser selects a type aircraft not yet approved for operation in that country, the initial type certification can be very expensive and time-consuming.

**Financing:** If the purchase will require financing, it is very important to investigate the requirements of the potential lenders. Many lenders require the aircraft to maintain a particular country's registration.

There may also be lender restrictions on the use of the aircraft such as geographical areas, or use for charter operations. A lender's requirement to register the aircraft in a particular country may also result in additional use-restrictions on that aircraft, since some registries only allow operations in the private category, or may not provide type certification for all makes of aircraft.

For U.S. lenders, aircraft based outside the U.S. may be subject to additional undertakings from the borrower, including covenants, security filings, legal opinions, personal guarantees and more. Lenders may also impose restrictions such as minimum maintenance requirements and limited rights of the owner to lease, or sub-lease the aircraft. If the aircraft is leased there may be additional requirements for return of the aircraft at the end of the lease.

The purchaser must rely upon experienced financial advisors and aviation counsel to review loan or financing lease documents and to identify these issues in advance of any negotiations.

**Registration Options and Owner Trusts:** The country of registration for the aircraft needs serious consideration. There may be several countries which seem suitable for registration. Most national registries impose citizenship requirements upon aircraft owners, but in some countries the regulatory authority may have some discretion in granting registrations for owners who do not otherwise meet the citizenship requirements.

Citizenship requirements for registration of aircraft are very stringent in the U.S., to the point that some companies based there do not themselves qualify as U.S. citizens. The FAA has provided a registration vehicle for owners who do not otherwise qualify for U.S. citizenship. This is known as an owner trust.

An owner trust is created with a bank in the U.S. that qualifies as a U.S. citizen. That bank is known as the owner-trustee, and the aircraft is registered in the name of the owner-trustee. The overseas purchaser retains its rights in the aircraft as a "beneficial owner" through the trust. The bank owes its fiduciary duty to the purchaser in accordance with the trust document. In addition, the purchaser executes an Operating Lease Agreement with the bank (owner-trustee), which permits the purchaser to use the aircraft.

Advantages of this structure to an overseas purchaser of a U.S. aircraft include ease of international operation, a wider availability of financing options, anonymity of the purchaser through "beneficial ownership," and avoiding any need to obtain a non-U.S. Certificate of Airworthiness for the aircraft.

At the same time, U.S. registration of the aircraft may present some disadvantages to the purchaser. There may be greater restrictions on operations in the purchaser's home country and there may be some difficulty in obtaining manufacturer-approved maintenance or trained pilots overseas. In addition, a U.S. registration for an overseas-based aircraft may trigger additional tax issues.

With all of the above considered, once the purchaser has identified the type of aircraft that fits its needs, and has located a particular aircraft it wants to acquire from a particular seller, the negotiations begin. This forms the content of the article: **'Step 2: Advanced thoughts for the Chinese business leader'** over the following pages.